Bodycote Trading Update Call

May 30, 20254

3:30 AM

Operator: Good morning, ladies and gentlemen, and welcome to the Bodycote Trading update call. At this time, all lines are in a listen only mode. Following the presentation, we will conduct a question and answer session. If at any time during this call you require immediate assistance, please press * 0, for the operator. This call is being recorded on Thursday, May 30, 2024. I would now like to turn the conference over to Mr. Ben Fidler, group CFO. Please go ahead, sir.

Ben Fidler: Thank you very much. And good morning, everybody. Welcome to our AGM trading update, that covers was the first four months of trading for this year. I'm Ben Fidler. I'm the group CFO. I'm afraid my colleague, Jim Fairbairn, who will take over as CEO today, is not able to be with us this morning. He sends his apologies. His father's been taken seriously ill, and is currently in end of life care, up in Scotland. And so we've made the decision, and Jim has made the decision, very rightly, that he needs to be with him and his family this week.

For the call this morning, I'm going to start off with some brief highlights from our trading updates, that I hope you've all read by now. And then, we'll open it up to questions. Overall, we delivered good progress in the first four months of the year. Organic constant currency revenue growth was 2.7%. We were very pleased with that, considering both the mixed end market backdrop that's continued from the end of 2023, and some of the pretty challenging comparators from the same period last year, when you may well recall revenue growth for the first four months of 2023 was up 17%.

Reported revenue is lower, year on year, as you probably saw, at £268 million. You've got to bear in mind that that's solely due to the impact of FX and lower surcharges, as energy prices, and therefore energy input costs, have normalized for us. Surcharges, as I'm sure you recall, were actually at their peak in the first quarter of 2023. And the trend is in line there, with what we had outlined at our full year results in March ,around our expectations for surcharges for this year.

We delivered continued strength in specialist technologies, which was very good to see, Organic revenue growth there was over 10%. Classical heat treatment revenue was marginally lower, year over year. What about end markets? Well, aerospace and defense very much led the charge, and continues to perform very well, up 16%, organically, in this period. And the fundamental demand outlook in aerospace remains very healthy.

We, of course, continue to monitor, closely, the situation with Boeing, on the 737 production rates. But remember we do have a very diversified aerospace business, with a number of platforms that we're on, both on engines and air frames. It won’t surprise you to have seen that automotive and general industrial remain more subdued. Revenue in both of those markets, as you saw, was down 1.8% organically, versus the prior year.

General industrial, as you know, is for us, I guess something of a catch-all term for a variety of markets that don't fall into either the aerospace or automotive sectors. And there were some bright spots in it, most notably energy, which was up 14%, year on year, despite a very challenging comparison from the period last year. For the portion of general industrial that's more linked to industrial production, and also for automotive, the demand environment remained soft in the period.

We have, though, seen some sequential revenue improvement from the lows of the fourth quarter 2023. The Lake City acquisition, which as you may well recall, completed on January the 19th, is going very well. It's been integrated, it's trading well, and it's in line with our expectations. It's continuing to deliver excellent margins, and we're very pleased with it. The balance sheet is strong, net debt at the end of April was £45 million, after we closed the £52 million acquisition of Lake

City in January, and after the almost £11 million pounds that we've spent so far on the share buyback program, which commenced just after our results in mid-March.

So in summary, we've delivered good organic constant currency growth in the first four months, despite some mixed end market backdrops. We were pleased with that. And that growth reflects, I think, the strength of our specialist technologies businesses, with the beneficial effect of our diverse end market exposures. And looking forward, yes, there are still some macroeconomic uncertainties that overhang, but the progress we've delivered to date gives us confidence for the rest of the year.

On the CEO transition. Jim's now completed his handover period with Stephen. He's had the opportunity to visit a large number of our sites, both in the US and in Europe. It's a great shame Jim isn't able to be with us today, for obvious reasons, but I know he very much looks forward to talking more about his impressions and his priorities further down the road, at our half year results in July. With that, I'd like to open it up to any questions that we may have from you guys on the line.

Operator: Thank you, sir. Ladies and gentlemen, we will now begin the question and answer session. Should you have a question, please press *, followed by the number 1 on your touchtone phone. You'll hear a prompt that your hand has been raised. Should you wish to decline from the polling process, please press *, followed by the number 2. If you're using a speakerphone, please lift your handset before pressing any keys.

Our first question comes from the line of Andrew Douglas from Jefferies. Go ahead, please.

Andrew Douglas: Morning, Ben. Morning, Peter. Thanks for that, and please do pass on our best wishes to Jim and his family. Um, the three questions I have, please -- can you go into a bit more detail on the aerospace growth? Is that across all regions or are we seeing stronger outperformance, in America or in Europe or U.K.? And I'm assuming that defense is still strong, so it's not all civil aerospace, it's actually kind of the broader A&D end markets that you serve?

Ben Fidler: Yes. So let me deal with that one, Andy. Thanks for the question. Yes, there was good strength, actually, across both civil aerospace and defense. They were both up nicely, at broadly similar levels actually, in this period of the year. If you look at it, geographically, again, it was very nicely balanced, actually -- similar rates of strong growth in Europe and the U.S., and a continuation, overall, in that nice strength that we saw in aerospace, from the fourth quarter of last year.

Andrew Douglas: Okay, cool. On the automotive market, clearly is a tricky backdrop, can you just remind us when the ramp up of the recent EV contracts kind of kicks in? It's kind of back end of this year, into 2025. And have you had any success on winning new EV contracts?

Ben Fidler: Yeah. Okay. So those programs, in terms of ramp up, and you may well recall, we won, and were down selected on four programs last year. Some of those are now in early stage ramp up. As you know, in automotive, you have to go through a fairly extended PPAP, pre-production approval process, that can take anything up to 12 months or so. And then, obviously, you are ramping, and it doesn't go to full throttle production rates from day zero.

Some of those contracts, particularly a couple of the European ones that we won earlier in the pipeline last year, are now progressing pretty well through that PPAP process, and into early stage production. It's fair to say on some of those, the levels of the rates of ramp up that we've seen, are a little bit lower than certainly the OEMs and the tier one suppliers that we're linking in with there, had originally intended, which I guess won't surprise you. It doesn't really surprise us, in truth, based on the slightly lower rate of EV penetration.

Don't misunderstand me, though, they are in ramp up mode. It's just the steepness of that ramp up curve, in the early periods, is a little bit more subdued. But it will come. And it is coming, anyway. As far as some of the other wins, and certainly the US win that we announced with our full year results, that is still in the far earlier stage, at the moment. And we're only just going through the early stage production of test parts on that contract. Now that's a very ex-sizable contract, when it comes up to full speed. But that is still probably 12, 18 months down the line, before that U.S. one, on the EV, really starts to kick in at meaningful revenue levels.

In terms of other things in the pipeline, other wins -- none to report. If there were at this point, we would have obviously included that in the announcement. But we're in some good discussions, and we're still feeling positive about those discussions, and the potential pipeline of further new contract awards there. And it's not just around EVs, remember. A chunk of these discussions are around hybrids as well, where certainly, as far as the automotive industry is concerned, you know, the expectation that hybrids are probably going to be a more meaningful proportion of production volumes, for longer.

And we're pretty ambivalent to that, right? Both through the nature of our powertrain agnostic exposures in automotive, and through the fact that hybrid vehicles also have, as far as powertrain components and transmission components, they still require a lot of our services and processes.

Andrew Douglas: Okay, cool. And then last one for me, and I'll jump back in the line -- in terms of the Lake City integration, can you explain to us what exactly the integrations involved is? I'm assuming it's HR, payroll, back office stuff. And have you found any interesting things now you are, you know, you're firmly under the bonnet?

Ben Fidler: Yeah, so -- yes, you're right in the first question. The integration has been pretty straightforward. We knew we acquired a good business. It really is around back office elements and rebranding and all of those kind of pieces that you'd naturally expect. Over time, there will be some synergies that we can increasingly drive, from certain elements of procurement around process gases, but we need to wait for their contracts to run their course, which we knew about prior to the acquisition, and was factored into the acquisition business case.

But the integration -- it's back office stuff, straightforward, all being done. Have we found any interesting things? Yeah, I think we've learned some lessons from them, and are learning lessons from them, around customer service, turnaround time, and some elements of their pricing strategy that we can learn some lessons on.

Andrew Douglas: Super. Thank you very much.

Operator: Ladies and gentlemen, just a reminder, should you have a question, please press *, followed by the number 1, on your touchstone phone. We have our next question coming from the line of Harry Philips from Peel Hunt. Go ahead, please.

Harry Philips: Yep. Good morning, everyone. A couple of questions, please. First of all, just on emerging markets, a sort of comment on them, if possible, please, then. There's sort of no reference to them -- to it, rather, in the statement. And obviously, particularly interested in China, where you were sort of talking of being a little softer back in March. And then just coming back to auto, and maybe slightly related -- the sort of sequential comment is very interesting.

Is that sort of -- is it easy to read too much into that, or is it just normal sort of sequencing and progression, and just doing a little bit better than expected? So some context around that would be helpful, as well, please.

Ben Fidler: Yeah. So, let's take your first one on emerging markets. The absence of comment in the statement was more driven, actually, by a desire just to clarify and avoid duplication in some of our communication in the way we talk about the business and describe the business, because we're always conscious, you know, that with emerging markets there's a degree of natural overlap with some of the other segments and markets that we've talked about, through the technologies and process lens, as well as through the end market lens.

Emerging markets themselves were modestly down, year over year, in this period. It wasn't actually China related. China was up modestly. China was up low single digit. Eastern Europe was weaker, and drove the deterioration in emerging markets OCC revenues in the period. A chunk of that is tied into the fact that a lot of those eastern European, emerging market demand volumes are coming through on auto and GI, often from the western world, typically from the western world OEMs -- from the German OEMs, etc., from the French OEMs, etc., who are increasingly using supply chains, and therefore, our customers who are based in Eastern Europe.

We're not concerned about that. And we think, certainly, as you go through the second half of the year, the comps get quite a lot easier there. So that will also help. On your question on the sequential performance of automotive -- yeah, I think, look. It is some cause for encouragement, and also the fact that, if you look at the year over year comparators from 2023, probably won't have escaped you that, you know, Q1, when our automotive revenues were up almost 10%, that was the toughest comparative from 2023. And the second half of last year, for our auto business, it was essentially pretty flat. And therefore, we are entering a period where, the year over year comparators start to get increasingly easy in automotive, for us in the second half.

Harry Philips: Lovely. Thank you. And then, just, if you can, a sort of idea on first, second half splits, and stuff like that? Is there anything sort of abnormal, I suppose, is the obvious question?

Ben Fidler: I don't think there is anything abnormal. I mean, you've been covering us for a very long time. You know about our normal revenue shape, which is we are a typically a pretty balanced business, between the first half and the second half. With what we have visibility and line of sight of at the moment, I don't see that there'd be anything out the ordinary for this year, and therefore, I would expect a fairly balanced first half, second half revenue performance. Surcharges, obviously, create a little bit of noise within that, but if you strip out surcharges and you're looking at it on an ex-surcharge basis, I think it will be fairly balanced.

Harry Philips: Great stuff. Many thanks, indeed.

Operator: Ladies and gentlemen, just a reminder, should you have a question, please press *, followed by the number 1, on your touchstone phone. Our next question comes from the line of Thomas Elgar from Deutsche Bank. Go ahead, please.

Thomas Elgar: Thanks. Good morning, all. Two questions from me -- firstly, could you unpack a little bit more, the good spec tech performance? You know, is this end market strength, market share gains, etc.? How should we think about sequential rates here? That's the first question.

Ben Fidler: Yeah, so look. I think it's a combination of -- there is ongoing, end market strength. So if you think about specialist technology, the performance there, from a market sector perspective -- very strong performance in aerospace; strong performance, very strong performance in energy, that helped our specialist technologies business. But it goes beyond just the end markets, because yet again, specialist technologies, consistent with its long-run history, shows the capacity and capability of delivering rates of growth, well ahead of the underlying markets.

So it's growing well ahead of the aerospace market. It's growing well ahead of the auto markets. It’s growing well ahead of the energy markets, which is reflective of the increased adoption of those processes and technologies, which is what makes that element of our business and portfolio so attractive, in our view. The particular process areas that did well in this period - HIP was strong and surface technology was also strong.

Thomas Elgar: Brilliant. Thank you. And then secondly, I guess digging a little bit deeper into the improvement within industrial, within general industrial -- can you add some further color, really to the sequential improvement you've called out in the statement, so your visibility, sitting here today within that market?

Ben Fidler: Yeah, no, visibility, in general industrial, is always more challenging. It's different to an aerospace business, or a medical business, for example, where you have much more forward visibility. If we unpack some of the performance in general industrial, what did we see in this period, within that overall minus 1.8% that we delivered in the period. Geographically, western Europe was weaker than North America, which shouldn't probably surprise you, on the basis of where the industrial production stands, for the first four months of this year, pointing to a very similar trend in the overall macro environment.

There were some encouraging sectors within that. So mining has been good for us. Tooling, which often can be a lead indicator for future automotive production rates, or at least automotive model change; tooling was positive. And actually, it's the first time that we've seen positive revenue growth in tooling since the first quarter of 2023. Industrial machinery is still fairly weak.

Thomas Elgar: Yeah. Brilliant. Thank you, very much.

Operator: Thank you. There seems to be no further questions at this time. I'd now like to turn the call back over to Mr. Fidler for final closing comments.

Ben Fidler: Okay. Well look, thank you everybody. Just to say thanks for your time. Thanks for the questions and participation this morning. Jim and I very much look forward to further updating you at the time of our half year results, which will be on the 30th of July. We may well speak before then. But if not, all the best. Thank you.

Operator: Thank you sir. Ladies and gentlemen, this concludes your conference call for today. We thank you for participating, and ask that you please disconnect your lines. Have a lovely day.