an NTT Communications Company

Transcription

Title: Compass Group Q3 Trading Call Update

Date: 26.07.2017

Speakers: Richard Cousins and Johnny Thomson

Conference Ref. No: EV00058885

Duration: 20:28

Presentation

Operator

Ladies and gentlemen, welcome to the Compass Group Q3 Trading Update Call. Throughout the call all participants will be in listen-only mode, and afterwards there will be a question and answer session. Just to remind you, this call is being recorded. I am now pleased to present our host, Richard Cousins, Group Chief Executive. Please begin.

Richard Cousins

Thank you. Good morning, ladies and gentlemen, and thanks for dialling in. With me this morning I have our Group Finance Director, Johnny Thomson. Hopefully, you have all had a chance to read the statement, but I will give you a brief overview of the key highlights and our outlook for the rest of the year before opening the call to questions.

Compass continues to have a really good year. The business accelerated, with organic revenue growth in the third quarter of 3.9% and, perhaps more importantly, if we exclude the impact of Easter, it was a very encouraging 5%. The operating margin for the nine-month period was up by 20 basis points. We continue to drive efficiencies, which we are partly reinvesting in exciting growth opportunities around the Group. This year we are also benefiting from the end of the restructuring programme in our offshore and remote business.

Let's look at each of the regions in turn. Our performance in North America remains excellent. Organic revenue in the third quarter grew by 7.1%, or 7.8% if we exclude Easter. Growth continues to be nicely diversified, with all sectors except our oil and gas business performing strongly. Margins for the nine months to 30th June improved modestly. In Europe, organic revenue declined 0.3% in the third quarter, but was up by 2.2% excluding Easter. We continue to drive efficiencies and have improved the margin by around ten basis points in the nine months. Turning now to the rest of the world: organic revenue declined by 1.3% in the third quarter, or 1.1% excluding Easter. Our non-commodity related business grew by 3.6% and, although trading in our offshore and remote business remains challenging, it is improving. The end of the commodity construction cycle in Australia continued to have a modest impact on the operating margin, which declined by ten basis points in the nine months year-to-date.

In summary, Compass had a good third quarter, and our overall expectations for the full year remain positive and unchanged. North America is performing strongly and we anticipate further progress in Europe and the rest of the world in the fourth quarter. We remain focused on driving efficiencies throughout the business, and our margin expectations for the full year are also unchanged. Looking to the longer term, we are excited about the significant structural market opportunity globally and the potential for further revenue growth, margin improvement and continued returns to shareholders. Thank you, and I will now hand back to Mark for your questions.

Q&A

Operator

Thank you. Ladies and gentlemen, if you wish to ask a question please dial 01 on your telephone keypads now to enter the queue. Once your name has been announced, you can ask your question. If you find your question is answered before it is your turn to speak, you can dial 02 to cancel. So once again, that's 01 to ask a question or 02 if you need to cancel.

Our first question comes from Jamie Rollo of Morgan Stanley. Please go ahead, your line is open.

Jamie Rollo

Yeah, thanks, morning everyone. Two questions please. First, just digging in a bit to North America, where clearly you've had a very good performance: could you talk a bit about the healthcare market there, where clearly your two big competitors have faced issues? Are you just simply taking share from them, and do you see any risk to your strong performance given the US Healthcare reform and some of the consolidation referenced in that market?

And then the other question was a bit geeky, and apologies for this, but the nine-month run rate of 3.7%; if we take the calendar-adjusted numbers for Q2 and Q3, it's more like 3.9%. So, is your underlying run rate a bit better than the 3.7% that you are presenting today? Thank you.

Richard Cousins
Okay, let's do those in reverse order, because I didn't understand your second question but Johnny is feeling intelligent this morning.

Johnny Thomson
Yeah, Jamie, thanks. The run rate, as Richard pointed out earlier, in quarter three on an underlying basis is around about 5%. That is broadly what we expect as our carry forward rate through quarter four into next year. I accept the fact there's a little bit of noise around quarters over the last few periods, particularly to do with Easter and the leap year, but I think over the round in the full year that will be immaterial.

Richard Cousin
And if we look at US healthcare, because it really – we need to talk about the US, I think our US business in general is in terrific shape and it is firing on lots of cylinders. The healthcare market really has been strong for some years now, as hospitals have reacted to Obamacare and have outsourced more, and I think we've naturally won more than our par amount. I don't like to say that we're taking share, I think that we're earning share by the quality of the food and the service that we offer. I think we are in the process of opening about 240 hospitals at this moment, including some truly elite healthcare chains. So, I think the business is in great shape.

I actually remain optimistic about US healthcare. Clearly, there are some uncertainties about the political environment, but whatever happens, cost needs to come out of the system and a way – clearly, there are many others – a way of hospitals taking out cost is to outsource their services to people like us. So, we feel quite bullish and the pipeline is strong.

Jamie Rollo
Thank you very much.

Operator
Thank you. And our next question comes from Vicki Stern at Barclays. Please go ahead, your line is open.

Vicki Stern
Good morning, just a quick one on Europe. Just anything with regards to the macro backdrop, how are European volumes? Is there any shift in trend there? And obviously, clear acceleration coming through within the quarter and expected into next year; just sort of the key countries that are driving that, thanks.

Richard Cousins
When you say volumes, Vicki, do you mean like-for-like volumes?

Vicki Stern
Like-for-like volumes, I do, yes.

Richard Cousins
Okay. I think they are pretty dull, but not bad. I mean, as you know, the protracted European crisis, or the global financial crisis followed by the Euro one, was very difficult for us and others, but clearly there has been some economic stabilisation and, indeed, a little bit of improvement in some parts of the Continent. I can't say we're noticing that. I mean, if you look at our revenue overall, with all the engines of revenue, I would describe the Continent of Europe as okay, really no better. But we are feeling quite positive about the UK, really due to our focus on food, our win rate has improved and our retention rate is much

improved. And we're also feeling quite good about Turkey. So, Europe is sort of three stories: very strong in UK, very strong in Turkey and a bit dull in the middle.

Vicki Stern
Great, thanks very much.

Operator
Thank you. And our next question comes from Sian Marden[?] of Cenkos. Please go ahead, your line is open.

Kean Marden
Hi, I think that might be me. It's Kean Marden from Jefferies.

Richard Cousins
It is now.

Kean Marden
Excellent, thank you very much. I had a quick question regarding margin progression, because at least relative to my model, I think your nine-month margin is a little bit stronger than expected, and therefore Q3 obviously much stronger than expected. If we look to your full-year guidance remaining unchanged, is that because you have a difficult comp particularly in Q4, or are you looking to step up reinvestment, or are there mix factors that you might want to flag up?

Johnny Thomson
To be honest Kean, I don't recognise our Q3 margin being necessarily stronger than the run rate, to be honest with you, so we're still about on track for our 20 basis points through – consistently actually, through the quarters, and that's the same as what we're expecting for quarter four. Margins are – it is tough out there on margins. Labour inflation is particularly difficult, as you know, around US, UK and elsewhere, but we're working hard on it and clearly we're pleased about the fact that we're going to add 20 basis points of improvement this year.

Kean Marden
Okay, thanks for the clarification, thanks.

Operator
Thank you. And our next question comes from Eric Carson[?] of Erdenholme[?]. Please go ahead, your line is open.

Eric Carson
Yeah, thanks for taking my question. You commented on the much-improved retention rate in the UK, and I was wondering if you could also give us an update on what you are seeing in terms of retention in the rest of Europe and also in North America please?

Richard Cousins
Okay. North America remains very strong, halfway between 96% and 97% and, as I am sure you know, we have been delivering that for many, many years in North America. UK, I think is the biggest delta; I think we have got our act together on food and service and process as well, I think, and people, I suppose; retention is a function of all of those things. So, I don't have a number in front of me for the UK, but I'm going to guess it's of the order of 92%. It was round about 88% for some years, and it's now about 92% in the UK. European retention rates are always lower than North America, because the average length of the contract is much shorter. And then on the Continent, we're around about 90–91%, which is also slightly up on where we used to be.

Eric Carson
And a follow-up if I may, as well: where would you see the biggest upside potential in the retention rate globally from current levels?

Richard Cousins

I think North America is pretty optimal, so we wouldn't expect to do much better there. I think we would hope to inch up in both Europe and the rest of the world. I don't think we should get too carried away and expect a massive improvement, because clearly, it's implicit within our spot underlying revenue growth of 5%, which we think is about par for this business. The rest of the world in general, and commodities in particular, clearly has had a tough period with oil and gas and mining and the 'white losses' as we call them – i.e. they are site closures, not our fault – we would expect that to improve as the cycle begins to turn over the next 12 or 18 months. So, I don't want to get too carried away, because we think our spot revenue growth at 5% is impressive and about par.

Eric Carson

Very helpful, thank you very much.

Operator

Thank you and our next question comes from David Phillips of Redburn. Please go ahead, your line is open.

David Phillips

Thanks, and good morning everyone. Can I just ask about the non-commodity growth that you reported in the rest of the world, which is 3.6%? Is it possible to break that down between emerging market countries and developed market countries?

Richard Cousins

It's a fair question. It's an incredibly complicated one, with countries like Japan, Australia and New Zealand on the rich end of the scale, and then obviously you've got India, China, Latin America and so on. Johnny, can you add a little bit of shape to that?

Johnny Thomson

Yeah, I think if you look around the patch, the Japanese growth is around about 1–2%, and the Brazilian growth is still in decline, towards 10% decline, but improving as we go forward. We're pleased, as Richard said, about what we're doing in New Zealand and some of the non-commodities elements of the Australian business, and they're 5%-plus. And then when you look at some of the Asian emerging markets we're in double digit, some of them higher-double-digit growth there. So, it's a bit of a mix, but that gives you I think a broad spectrum of what gets us to our consolidated 3.6%.

David Phillips

Great, that's helpful. Can I ask a follow-up on Brazil and Latin America specifically, and the sort of anticipated timescale of that improvement, given that there's one or two of the macro indicators starting to look a bit better?

Johnny Thomson

Yeah, I mean it's still been tough this year, of course. I mean, unemployment levels are very, very high still, and we have largely B&I business, so that's affected us. We've been working hard on price and costs, increasingly working on retention. Perhaps we've been a bit disappointed with retention in the last few months, but that's starting to get better. So, I indicated a minus 10% for this year; I think that will get better for next year. We'd hope to be closer towards breakeven next year.

David Phillips

Okay. Great, thank you very much.

Richard Cousins

I think it's quite an interesting one, the rest of the world, and incredibly complicated, with all of the trends Johnny just described, plus of course the offshore and remote business. But we do anticipate that the rest of the world will be modest, very modest growth in Q4. So, I think that really is quite encouraging as we look at the next year or two of this business.

David Phillips

Excellent, thank you.

Operator
Thank you, and our next question comes from Jarrod Castle of UBS. Please go ahead, your line is open.

Jarrod Castle
Thank you, good morning. You said you were very positive on the UK: I was just wondering, is that kind of more B2B? Are you seeing any slowdown in the B2C element, or are both areas very strong at the moment?

And then just oil and gas: where overall are we in terms of the organic growth situation in that sub-sector? Thanks.

Richard Cousins
Okay, let's do them in the reverse order. Johnny, oil and gas?

Johnny Thomson
Yeah. I mean, we haven't hit the absolute bottom in dollar terms on oil and gas, but the rate of decline of course is improving. So, if you look at it quarterly, just to give you an indication of the numbers, we were at minus 23% in that business in quarter one, minus 15% in quarter two and we're now at about minus 10%, so you can see the trend as it develops. Richard mentioned that we will be soon into growth in the rest of the world. I think it will be mid-ish 2018 for us by the time we get back into growth in the oil and gas world.

Richard Cousins
And then if we look at the UK, so the B2B – the MAP 1[?], as we would call it – is very strong for us in the UK. I am delighted with our win rate and our improved retention. The B2C or the MAP 2, as we would call it, is sort of fine, it's dullish really. Now, of course, there are some concerns about the UK economy and the impact of Brexit and so on; we haven't noticed that yet. Whether we will, only time will tell. But I think we shouldn't underestimate the importance of the improvement in the UK to our business. Some of you with a longer memory will recall that our performance in the first decade or so of this century was pretty poor, so we're delighted with the turnaround. The revenue growths in the UK are really exciting. As Johnny said five minutes ago, margin is okay but there are some inflationary pressures in the UK that we need to be aware of. But the top line looks really positive.

Jarrod Castle
Thanks very much.

Operator
Thank you. And our next question comes from Angus Tweedie of Bank of America. Please go ahead, your line is open.

Angus Tweedie
Thanks very much. Two questions, please. Firstly, in your comments, talking about phasing for the fourth quarter, you didn't pull out the US as being stronger. Could you give us some colour around that?

And secondly, on the UK: I don't know if it's possible, but could we get an idea of the delta between 2Q and 3Q in terms of organic performance there? That would be really helpful, thanks.

Richard Cousins
Reverse order, Johnny? I'm struggling with the UK one.

Johnny Thomson
Yeah, I mean, UK obviously came up from a flat quarter one and improved to a couple of percent in quarter two, and we've seen a couple more percent in quarter three. So, we're in the kind of 4–5% in quarter three; we expect it to be a faction better than that in quarter four to carry into next year. So obviously, it pulls the overall European average up and, as Richard just said, we feel very positive about it.

Richard Cousins

And in terms of North America, because Canada is quite tough with the oil and gas trends, in terms of North America we obviously did 7.8% in Q3. I think that is above par, so we would be quite optimistic to assume a repeat of that in Q4, but we will see. All I can say is that the US business is looking very strong.

Angus Tweedie

Perfect, thank you very much.

Operator

Thank you. And our next question comes from Najet El Kassir of Berenberg. Please go ahead, your line is open.

Najet El Kassir

Good morning, everyone. Could you please give us a little bit more colour on price and volume in the US as well as in the rest of the world, please?

Richard Cousins

Okay, well the rest of the world is incredibly complicated. In the DOR world, oil and gas and mining world, volumes are strongly negative. And prices are tough as well, because we have to be competitive when our clients are clearly looking for value for money. So, they are clearly negative. And in the rest of the rest of the world, it is a complex hotchpotch but, by and large, Japanese volumes remain dull. Australia and New Zealand okay; pricing tends to be about the same as inflation or a bit less, and obviously clients expect us to mitigate the rest.

In terms of the US, food inflation is probably slightly below average, but labour inflation is slightly above, and that I think is a trend we are seeing in the US, the UK and other countries as well. So, our pricing trends in the US would be halfway between zero and the rate of inflation, as is usually the case, and volumes fairly steady really; slightly positive, but only slightly.

Najet El Kassir

Thank you.

Operator

Thank you. As a reminder, if you wish to ask a question please dial 01 on your telephone keypad now. We have one further question coming through so far, that is from Julia Pennington of Credit Suisse. Please go ahead, your line is open.

Tim Ramskill

Good morning. It's actually Tim Ramskill here, hi guys. Just a quick question on the US. Richard, I know you've talked in recent months, and really wanted to emphasise to people that sustaining growth above 7% was going to be difficult. I think you talked about sort of 6%-plus-plus. Do you sort of stand by that? I guess again, you know, Q3 was very strong. What are your thoughts on 2018, please?

Richard Cousins

Yeah, it's a great question, Tim. I still think in the medium term – that's a clever phrase isn't it, because that takes out 2018 – in the medium term, 6%-plus-plus is a sensible number when you look at the market, the economy, competitors and so on, but I have to tell you the pipeline in the US is the strongest it's ever been.

Tim Ramskill

Okay. Great stuff, thank you.

Operator

Thank you. Once again, any further questions please dial 01. Okay, there seems to be no further questions on the line, so I will hand back to Richard for the closing comments.

Richard Cousins

Okay, thank you Mark, thank you everyone for joining us. Just wanted to say enjoy the rest of the summer, although looking out of the window I think summer is cancelled. We will see you at the results in November. Thank you very much.

Operator

This now concludes the conference. Thank you all very much for attending, you may now disconnect.