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Transcription

Spectris Trading Update Call

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22 October 2020

PRESENTATION

Operator

Ladies and gentlemen, welcome to Spectris Trading Update Call. I will now pass the call to Mr Andrew Heath.

Andrew Heath

Thank you, very much, and good morning and welcome, everyone, to this the Spectris Q3 Trading Update. I really do hope that you are all keeping yourselves safe and well at this time. I'm joined today by Derek Harding, our CFO, to discuss our performance in the third quarter. And what we will discuss today is very consistent with the view that we presented at our H1 results back in August.

And before I start, I'd just like to say that we continue to take a balanced, socially responsible approach to managing our business at this time, in line with our culture and our values, very much supporting our people and delivering for our customers. And I'd again just like to start by thanking our people for their commitments and support through what have been some very difficult times.

Let's move on to the update itself. So, I'll start with our performance. We've seen positive progress in a number of our end markets, and I'm very pleased that our like for like sales decline has improved from 18% in quarter two to just 9% in quarter three. So year to date like for like sales were 12% lower. In all regions, there was improvement, most notably in North America and in Asia the improvement was driven by a rebound in activity in China, where like for like sales rose 6% in the period.

So, now just turning to our businesses in turn. In Malvern Panalytical, we had a much improved performance compared with H1 with only a 4% decline in like for like sales. This reflects a resumption in CapEx or [? 00:01:41] from its customers and some revenue from the completion of installations of systems which were delayed from the first half of the year due to customer access restrictions.

There was also good growth in the pharmaceutical and food customers, which was offset by lower like for like sales into academic research institutes, where demand continues to be weak, which really reflects the ongoing closures there. And going into quarter four, we expect sales to be sequentially higher, though the like for like sales performance is not expected to be as strong as in quarter three.

At HBK, Q3 performance was similar to that which we saw in Q2 with like for like sales 13% lower, given its later cycle exposure. We had a strong performance in North America with growth driven by strong sales into aerospace and defence customers, reflecting a number of large projects sales as well as sales into machine manufacturing. Q4 is expected to see like for like sales lower, which reflects the later cycle nature of the HBK business.

At Omega, like for like sales were 16% lower, which was better than quarter two, but still reflects continuing weak demand in its main market in North America. For Q4 we expect to see the like the like sales performance improving, although no growth is expected in North America until the beginning of 21.

In industrial solutions, we saw a noticeable sequential improvement in Q3 with a much improved like for like sales decline of just 9%. There was growth into the pharmaceutical and food industries, while those businesses exposed to automotive and upstream oil and gas saw the weakest performance and here we expect fourth quarter to continue to show a progressive improvement in like for like sales.

Moving onto the balance sheet. During the pandemic, maintaining a strong balance sheet and cash position has been a key priority for us. We remain highly cash generative. At the end of the quarter, we had net cash of 60.2 million pounds, and this is after paying a 50.2 million pounds additional interim dividend, which was in lieu of the 2019 final dividend and before the interim dividend of 26.5 million pounds.

The strength of our balance sheet has put us in a good position to pursue acquisition opportunities that may emerge. With the resumption of activity in the M&A a market, we continue to work on our acquisition opportunity pipeline and have also re-initiated our sale programme to deliver our portfolio optimisation.

As discussed at the H1 results we will be managing the impact of COVID-19 in three phases: React, respond and reset. And we are now firmly in the reset phase, while we continue to support our employees and customers through these times. For our people we have re-instated salaries and also full time working wherever possible, part of the reset to a sustainable business model.

We continue to support our employees with provisional practical guidance and also mental health support and to focus on staying connected with those people, especially who are working remotely. For example, in Europe we have partnered with The Wellbeing Project to offer resilience coaching to employees, and both Derek and I recently participated in workshops on this.

And for our customers, despite the challenges of restrictions of remote working, we've continued to launch new products which enhance our offering to them. For example, HBK have introduced a complete power [ph 00:04:55] metre solution for testing and monitoring solutions around electric drive systems, power supplies and e-grids and VI-grade has recently launched its new product line of cable driven simulators, the DiM400.

In Malvern Panalytical, we launched three new products: the Zetasizer Advance range, the 1Der detectors, and the Empyrean XRD platform, as well as our OmniTrust suite of software tools. And Servomex developed, in record time in just 14 weeks, a variant of the Paracube sensor, called the Mercury, which is designed and approved to work in critical care ventilators.

We also continue to extend our digital offering with a wider emphasis on online sales, virtual engagement, digital workshops and webinars and remote installations and servicing support. Given the benefit to both ourselves and our customers, we continue to enhance our digital offering and that will be a key focus going forward.

As also disclosed in our H1 results, we launched a restructuring programme to further reduce our cost base over the last few months. Work has progressed at each operating company, which confirms the expected benefits of 20 million pounds to come through in 2021.

These permanent reductions in our cost base will come from a variety of sources, including footprint rationalisation, reduction in discretionary costs, including more productive ways of working digitally, as well as headcount reduction. So, as a result, we anticipate our overhead costs in 2020 be around 50 million pounds lower than in 2019, and that will consist of 20 million of permanent cost savings which was delivered from our profit improvement programme. But also, the 30 million of temporary savings that we talked about at the half year.

And of those 30 million pounds of temporary savings, we expect 20 million of that to turn into permanent savings in 2021. For this programme there will be a 5 million of restructuring costs this year, in addition to the 25 million pounds for the profit improvement programme and an additional 20 million pounds of costs in 2021.

So, in summary, I am really pleased with our improving performance in the third quarter and the sales momentum going into the fourth quarter. Our order book provides confidence in us meeting our full year revenue expectations, although this is subject to no major effects, clearly, from COVID-related restrictions, which may impact our ability to access customer sites for things like product installation and commissioning.

We've also been clear that we remain committed to recognising the sacrifice and dedication of our people during this challenging period. Therefore, any delivery in excess of our expectation will be considered to recognise this sacrifice and commitment. Our cash generation continues to be a strength, and our balance sheet remains robust. As we implement the restructuring, we will emerge from this crisis a stronger and even more resilient business. Our strategic objectives of organic growth and margin expansion remain, as well as optimising our portfolio and making acquisitions to deliver long-term value to our shareholders.

And with that I'll happily open up to questions.

Q&A

Operator

Thank you very much. We will now begin the question and answer session. Participants with questions, please press 01 on your telephone keypad and you will be placed in the queue. To cancel the queue, please press 02.

The first caller we have is from Mark Davies Jones. The floor is yours.

Mark Davies Jones

Morning, Andrew. One or two challenges there. Just a couple of questions if I may. Omega looked a little disappointing given what you were saying overall in terms of momentum in the US. Can you give us some background on what's happening there and when you see the benefit of some of the investments you've put in there?

And then the second question, maybe for Derek, is obviously that today's update is focused on the top line, but in terms of conversion, are you still looking at the sort of drop throughs that you were flagging at the half year, i.e. higher drop through in the second half; 40/50% versus the 32% in the first half? Thanks.

Andrew Heath

Great, thanks for your question, Mark. Nice to hear your voice. So, just in terms of Omega's performance, it really is tracking against the North American IP, industrial production. The business correlates very strongly to that, so we practise statistics quite closely and Omega's performance has been pretty much tracking in line with that over the last few months.

So relative to its core market in North America, which is 70% of its business, we are seeing it sort of track against that. During the height of the lockdown in North America, we definitely saw its digital online business holding up well. That held up better than sort of the direct selling side of the business. And so that gives us confidence in our online model. But in terms of your question around sort of timing of the benefits coming through from the investments we made, clearly we are very much focused on driving scale in that business now, having made that investment.

Omega has done a good job over the last two three years of really sort of leaning its operation out, making itself more efficient, not just on the shop floor, but also in all of their sort of offices and transactional processing in the business. And they've reduced their reduced there headcount there by about 25% over the last two three years, but having at the same time – they also clearly made the investment in e-commerce platform and that sort of added to the fixed costs which we talked about at the half year, we saw that come through in the negative gearing we were seeing impacting the margin.

So, going forward we've brought in a new president, Amit, who joins us from Thermo Fisher with a great background. A lot of relevant experience, not least for his time running Cole-Parmer [? 00:11:53] enthused go and basically turbocharge the top line growth in Omega. And that's really where would be the focus.

Mark Davies Jones

Thank you.

Derek Harding

And Mark, on the question of drop through, the guidance that we gave at the half year hasn't changed and just as a reminder that was that was a full-year answer, if you like. So, depending on where you place your assumptions on the top line, there was a range between 40 to 50% of drop through from sort of the best top line view to the worst top line view. And there's nothing new in this statement in relation to that.

Mark Davies Jones

Great, thank you very much.

Operator

Thank you very much. Next, we have Mr Jonathan Hurn from Barclays. The floor is yours, Mr. Jonathan.

Jonathan Hurn

Good morning, guys. Just – sorry, I should say, a few questions from me. Firstly, just in terms of that sort of 9% decline that you saw in the Q3, can you just give us a little feel of the transition through Q3 just in terms of the sort of performance in July, August and September? That was the first one please.

Andrew Heath

Jonathan, good to hear you. So, I think we – at the half year, we obviously talked about sort of June's performance being a 12% decline, which is clearly a step change from the sort of 20% decline range we saw back in the March/April/May timeframes and really over the last three months of quarter three, typically have seen a similar level of activity. Some months have been better, some a little bit worse. But in terms of what we put in our announcement, given the order intake that we've seen, which has fared even better, that gives us the confidence going into Q4 that we've got momentum and sufficient order cover to meet our expectations revenue-wise over the next three months.

Jonathan Hurn

Okay, I was just trying maybe sort of focus on September, just getting a sort of feel for the exit rate for the business overall. I don’t know if you can just give a little bit more colour on September?

Andrew Heath

Yeah, Jonathan, it's always dangerous, I think, to sort of point to a specific month but clearly, sort of July and August are the sort of the heavier holiday months, within the Northern Hemisphere at least, so we were pleased with what we saw in July and August, and September was better. But that's, to some extent, people coming back into work, so we shouldn't draw too many conclusions from that other than certainly the trend over the last four months, we feel that we have good momentum going into the final quarter.

Jonathan Hurn

Great, thank you. Second one just on M&A. Obviously you talk about that in the statement. Both sort of acquisitions and disposals. Just on the acquisition side, can you just sort of remind us of how the structures that could be? Just in terms of the levels of net debt EBITDA that you may go up to. Is it purely all going to be debt? Are you still considering other sources of funding? Just sort of a feel for that please. That would be helpful.

Andrew Heath

Yeah, so clearly the M&A market has come back strongly, overall. It clearly went into a period of paralysis during the height of lockdowns. As we said at the half year, we initiated our disposal programme so we are actively on with that at the moment but on the buy side, to your question, in terms of looking at the landscape and the opportunities, the current situation has clearly created some new opportunities, shall we say, in terms of what we were looking at previously and that varies from relatively small bolt-ons all the way through to acquisitions of potential size of some of our platforms, or indeed even larger than that.

But as we put in our notes, we will absolutely remain disciplined around capital decisions. We've previously guided that a debt range of one to two times is the zone that we would be comfortable operating in and for the right acquisition, but we would go above two times. Now, in the current context, we will be more conservative than that, and therefore we will look at the appropriate structure of debt and equity to suit the size of the transaction and also the opportunities that we see beyond the transaction as well. So, there's a number of factors clearly that we have to consider.

Jonathan Hurn

Great, that's very helpful. And the last one was just on the auto end market. Obviously in your commentary it's one of the weakest, if not the weakest, end markets. I mean, I think the general sort of performance in Q3 auto has been better. Obviously, you guys are late cycle. When do you still feel that the auto market will start to turn for you and improve?

Andrew Heath

Yeah, so I think up until – I think sort of going into more Q3, the auto sales, particularly in North America, have held up quite well for us, but as we've always said, look at HBK, its latest cycle, we've definitely seen that come through. A lot of the customers that we're talking to are certainly trying to sustain or maintain a lot of their R&D programmes, particularly around electric vehicles, hybrid vehicles, battery developments, the whole drive for electrification, and hence, probably one of the new product ranges that I talked about from HBK around their sort of e-power grid solutions. That is getting good traction.

So, I think going into Q4, personally I wouldn't expect for us to see much improvement in automotive because we went into it later, but its – relative to some of the other markets, it will take a little bit longer to come out given the productions been quite a long way down in the last few months, so that inevitably will wash through in terms some of the auto OEM customer sentiment in terms of CapEx spending.

Jonathan Hurn

That's very helpful. Thank you.

Andrew Heath

Pleasure.

Operator

Thank you very much. Next, we have Mr. Andrew Douglas. The floor is yours.

Andrew Douglas

Three questions please, if I may. Can we just talk Malvern? Clearly a strong performance with a bit of catch up from the first half, but still academic research markets are still weak. Do you have any indications from customers when they might be opening up and we can kind of get back to a full run rate?

Secondly on cash, just wondering, Derek, if you can give us a bit a feel for how your cash flow is. I appreciate you got 60 million pounds net cash pre a dividend in November but just in terms of the moving parts there, working capital, et cetera. And then just for the avoidance of any doubt, can you just help us on a bridge for profit as we go into next year? We've got some costs coming in, costs coming out. My working assumption is that we've got 20 million of costs out, but we've got 30 million of costs coming back in. So, is that right? And then, depending on how the analysts think about their operational gearing, that's how we should be modelling next year.

Andrew Heath

Okay, Andy. Thanks for the questions. I'll take the first question. I'll let Derek pick up your other two. So, Malvern Panalytical, clearly we're delighted to see how strongly the business has come back in Malvern Panalytical over the last three months, a lot of that has been helped by a strong pickup in demand from sort of pharma and life sciences side of the business.

So, the orders there have been picking up consistently. And so, whether that's just pent up demand in cash back, we will see, clearly, over the next few months. But certainly, it's come back with a vengeance. And I think is there was quite a lot of disruption in the early days around their own laboratories, research institutes, when lockdown restrictions were imposed where OEMs ended up shutting their own facilities, which clearly didn't help, which feeds through to the argument that quite a bit was pent up demand.

But equally it was a lot of investment going into vaccine development, and on the sort of production quality control size of pharmaceuticals, that's an area that Malvern Panalytical is quite strong in, and as such we anticipate that trend to continue. I think if we look at some of the other areas, some of the fine chemicals, semi electronics, that's definitely been coming back to Malvern Panalytical and while sort of mineral mining was tough, we saw a more positive trend in Q3. So, all that's helpful.

But to your point on the sort of research academia side of things, that has been a pretty tough spot for the business. Although September we saw maybe the first sort of green shoots of activity levels starting to come back, which may well tie into the fact that a lot of universities effectively re-commenced operations again in September, so again one month doesn't make a trend, but certainly another positive sign.

So, as we said, we expect the momentum to build albeit they've got a tough comp into Q4 compared to last year, so we don't expect the like for like position to be as good as it was in Q3 and Q4. But momentum all the same.

Derek Harding

And then on your cash question to start with, Andy. Obviously we had a very strong cash performance in the first half, partly a function of the slowing top line and the fact that the first half is always a stronger period for us for cash, so I wouldn't expect the same level of cash conversion in H2 as we saw in H1, and indeed we will see that in the third quarter and again in the fourth quarter. But, notwithstanding that, we still expect to have a very strong cash year overall.

And when you look at that sort of cash conversion metric, likely to be a little bit higher than what we normally achieve given the shape of this year and particularly the reduction in sales. From a CapEx perspective, we're still guiding towards the 50 million for this year, and that will be similar for next year as well.

And working capital, again, because of the reduction in sales if you look at working capital as a percentage of sales, we will probably be near the top end of our range and that range that I've said that we're kind of comfortable with is 11 to 15 and we will be near the top end of that. But I'm not expecting us to be outside of the range when you look at the components of working capital.

And then in terms of the cost bridge. So, your assumption is right. It all depends where your starting point is. If you start on the 2019 cost base then we are confident and still looking towards that 50 million reduction for 2020 compared to 2019. Then of that 50, as we've said before, 30 is temporary, and will reverse, and therefore if we took no action in 2021, the cost base would increase by 30 million compared to 2020.

But we are taking actions which will create another 20 million of permanent and therefore the cost base only increases by 10 million from 2020 to 2021 on a like for like basis. So, that's how that bridge works through. Clearly then there's inflation and activity that comes through in 2021, but that's the sort of core cost base moves in the way I've just described.

Andrew Douglas

And I just want to follow up, if I may. Just going back to your comment Andrew on Omega and your new appointment. I'm working on the assumption that this is now all about him driving growth. There's nothing else kind of on his kind of bucket list or agenda that he needs to kind of fix before growth can come through. It's all about growth and a bit more growth. Is that fair?

Derek Harding

Yeah, yeah, absolutely, Andy. It's number one, two, three priorities about how do we grow the business from here. Scale, we really do need to scale that business up to turn its financial performance around. There's been further work done this year in terms of making further enhancements to the digital offering in terms of improving searchability, product findability, user interface, just continue to refine the platform.

So, we don't foresee the need to do much more beyond what we put in place this year other than just ongoing refinements. So, it is very much now about how to turbo charge the top line, and that's the reason that Amit is coming into the business.

Andrew Douglas

Perfect. Thank you very much.

Operator

Thank you very much. Next, we have a Mr George from Bank of America. The floor is yours, Mr George.

Mr George, you may proceed with your question. Thank you.

George Featherstone

Sorry. Hi. Morning and thanks taking my question. On the orders like for like performance in Q3, how should we think about how that will relate to like for like sales performance in Q4? Is it a case where you expect to do better than that given the commentary?

Andrew Heath

Well, I think we've tried to describe what's going on within each of the businesses, to try and sort of give that sense of how we see things progressing. Clearly, Q3 was in absolute terms an 11% improvement over Q2, so that momentum following through into Q4 we expect to continue. We're not sort of giving any guidance in terms of what the quantum of that is going to be. But clearly, we see a quarter over quarter absolute improvement.

The like for likes, if we look across each of the businesses that we described, I think you then get a reasonable sense of being able to model what that then entails in terms of revenue expectation. I think if you look at consensus at the top end of the sales that some people have got, I would say it's a bit choppy [ph 00:27:39], but in our view clearly we are seeing good momentum going into the next three months.

With absence in further restrictions as I said, that would be my only comments you know coming about from lockdowns with COVID-related social distancing measures. Our order book certainly supports that sort of momentum, but obviously we've still got to deliver and get product to customers, and for a number of businesses we have to install and commission before we can actually recognise the revenue. So, there are some risks there as well as some balance on the upside as well.

George Featherstone

Okay, thanks for that. So maybe just for clarity then. The 8% like for like decline in orders, you shouldn't necessarily read that as being representative of the Q4 performance potential. And then maybe just drilling into the orders a little bit, are there any particular end markets that have exceeded expectations or driven the better performance perhaps than maybe was expected in the order book?

Andrew Heath

Yes, okay. I think your comment on the orders. The orders this year were consistent with what we've said on all our trading updates is that the order book has held up better than sales all the way through the year, but what we have seen is that the orders have been longer dated than we've typically seen against the history, and that's still the case.

So, it's clearly reassuring that the orders are coming through and great that our sales people are being able to go out there to reach customers and enact business. The orders typically are longer out in time than we'd ordinarily see, so it gives us confidence in terms of that momentum going into Q4, but you shouldn't read being just an 8% decline in orders will translate to an 8% decline in revenue in the next three months.

And then I think the other question was about which markets have surprised on the upside. Clearly it's great to see the pharma, life sciences, food business coming back strongly albeit we always anticipated that the impact – the quite negative decline we saw fairly early on with the pandemic in pharma was going to be a temporary phenomenon and that's proven to be the case.

Even so, it's good to see that coming back. Certainly, into food, food research, food analysis and also food production. HBK provides sensors, weighing sensors, measuring sensors into the food industry. That's proved to be very resilient and continues to grow actually this year so that side of the business has been good and good to see it come back.

On the flipside, we talked automotive. That was to some extent expected being a longer cycle for us and clearly the oil and gas – those businesses that are exposed, particularly upstream in oil and gas have been particularly impacted. But again, that's not a surprise in the current environment.

George Featherstone

Brilliant, thank you.

Operator

Thank you very much. Next, we have Mr Mike Tyndall. The floor is yours.

Mike Tyndall

Morning, gentlemen. Just a couple for me if I can. Just thinking about sticking on the orders for a moment in terms of visibility, how much of Q4 do you have covered as we sit today or is it still a case of based on the actual inflow that we're seeing, we think we can get where we need to get to for the quarter?

And you mentioned about the orders being a bit more long dated, what's happening in terms of ordering behaviour? Are we seeing that stabilise or is it continuing to change because I guess the uncertainty you're seeing, or your customers are seeing as well?

And then the second question for me is North America was relatively strong but Omega was weak. Am I right in assuming that that was MalPan that really kind of bridged the difference there and how much of that is potentially catch up on those delayed installations? Thanks.

Andrew Heath

Okay, great. So, let’s talk about the orders. As I said, they have been typically longer dated than we’ve historically seen through this year. That trend continues. Our concern going back a few months was whether customers were just placing orders maybe speculatively, holding a capacity slot, if you like, and it would decide nearer the time whether they would actually take the order or not. But the very encouraging news is that we have seen very few cancellations.

We have seen some customers delaying taking receipt and part of that is because they haven’t got the people in the right place at the right time to be able to take receipt, but we haven't seen much cancellations at all, certainly nothing material. So, whilst the orders have been longer dated, they've been coming through, which is hugely reassuring.

I think your point in terms of order coverage. It clearly depends by business. But again, I don't want to get too specific. The level of order cover that we have in place because of the state of the order book we are feeling sufficiently confident that we can certainly meet our expectations around our Q4 revenue.

And that's based on history and how much of the book and turn we would expect to see – book and turn business during the period in Q4 we would expect to see historically and now. It is always dangerous given the current time to sort of compare this year to previous years because this year is a totally different year with different buying behaviours and patterns. But relative to what we see in the order book and what we expect and what we understand from our customers and their intentions, that gives us confidence to meet our sales expectations over the next few months.

And then your final point about North America being stronger, yes, I think North America has certainly been strong for Malvern Panalytical. They performed well in North America, particularly in the last quarter. They've actually gone into positive growth territory. HBK has also done well in North America. The automotive has been a bit more resilient for HBK in North America, again, over the last two months, their sales in North American HPK have been positive and similarly within industrial solutions, we've seen an improving trend there as well.

The point around Omega is really that Omega is really exposed to industrial production, particularly in the process industries. And that has not performed to the same extent as the pharma, food, life sciences, auto, certainly, the aerospace defence activity for HBK and some of the sort of medical centre activities that we supplied of ISD [ph 00:35:51].

So, I think that really explains the difference. I fully appreciate on the face of it, it does look a bit anomalous, but hopefully that explains why there's a difference.

Mike Tyndall

Yeah, that's perfect, thank you.

Operator

Thank you very much. Next, we have Mr Andy Wilson from JPMorgan. The floor is yours.

Andy Wilson

Hi. Good morning, everyone. Just a couple of quick, I guess, specific ones thinking about the academia sales which obviously have been under pressure this year for, I guess, obvious reasons. But just thinking about the potential for that to either sort of catch up or bounce back, just trying to get an understanding. Are these sort of sales that are kind of one time cycle sales which won't come back or won't be – there won't be a catch up effect? Or can we stand to have actually quite a good sort of 12 to 18 months when things settle down?

And secondly on the oil and gas exposure, and I appreciate this is kind of different in different parts of the business, but just any indication from the customers in terms of improving trends. We've seen sort of some better news maybe in oil and gas in some patches. So, just interested on those two specific [? 00:37:02].

Andrew Heath

Yeah, so I think on the academia, Andy, it's too early to tell, but I think there has to be a lot of effectively pent up demand, because we've seen months of pretty low order intake out of that sector. It will clearly depend on the level of government stimulus money that goes in over the coming months and equally which areas governments may put in and how much they can afford to put in. But we would anticipate that academia will recover from here going forward.

If we look at the number of research institutes serving in the pharma area. That's one of the stats that we track. At the height of lockdown half of the world's pharma labs, research labs, both in terms of not just researching [? 00:38:06], OEMs were shut. That stat now is down to I think about 9%, so there's been a much broader reopening of laboratories and research institution in the pharma and life science area over the last weeks and last few months.

So, that's a positive trend. As I said, we've seen sales in September certainly took a tick upwards. It's still down, but the level of decline was much, much lower. So, our expectation is that things will start to build from here. We've seen some green shoots. It's early days, but that's our expectation.

On the oil and gas, really on the upstream side, we have relatively little exposure on the upstream. It's really our ESG business in Canada that does micro seismic analysis for fracking in North America. It's a good chunk of its sales. So, clearly, that's been way down but the more downstream petrochemical refining activity has picked up again and we are again starting to see some signs, certainly within our centre sales, of things picking up.

Andy Wilson

Perfect. Thanks, Andrew.

Operator

Thank you very much. Next, we have Mr Danny Lu from DDS. The floor is yours.

Mr. Danny Lu, you may ask a question. Thank you.

So, next we have Mr Tom Fraine. The floor is yours.

Tom Fraine

Morning. This is regard to something mentioned in the previous update, actually. Regarding the working remotely from employees just been updating how this is going so far. And if you see this as something that's likely to increase across the group in future years, or whether it's likely to be more temporary for large portions of employees? And how's it working, if at all, for engineers and employees that are working on installing products on sites and whether this is having any impact on the service they're delivering and potential cross selling opportunities and new wins?

And then second question on the cost savings. So, some of these potentially including the remote working related cost savings. Why weren't some of these identified in the profit improvement programme? And do you see them as having a bit of an impact potentially on the top line at all?

Andrew Heath

Okay, so let me take the first half of that question. I'll pass you over to Derek about the cost savings and I'll come back and wrap up at the end if there's needed on that. But on the working remotely we have been really pleasantly pleased on the upside at just how well all of our staff have been able to work remotely, work from home, work flexibly.

In terms of our office occupancy, none of our offices anywhere around the world are back to 100% occupancy to where it was pre-pandemic. As part of the profit improvement programme, we were fortunate that as part of our drive there to reduce costs we had upgraded our digital tools for internal working last year and that clearly put us in a very strong position as it turned out when the pandemic unfolded so we were able to quickly move everybody within days to remote working, including the engineers that you touched on.

And that's allowed us to – it's not just sort of operating in a Microsoft Office systems remotely, which people have been doing for years, but in terms of our R&D systems, cash systems, modelling systems, software writing capability, we've got our engineers working very effectively from home at the moment and I think in terms of that as a trend, well, I don't think it's going to increase because we have the majority of people who are doing at the moment. But in terms of our intentions going forward, absolutely, we will maintain remote working.

Maybe not the full extent it is today, but we will certainly be providing people the flexibility to be able to work from home or remotely as well as in our offices. All the surveys that we've done points to the fact that employees, whilst they don't think anybody necessarily wants to – very few people want to work from home five days a week. People recognise that actually working from the office five days a week isn't the most effective either, so they can be more productive in the way that we are working now and in terms of our productivity, we were concerned particularly around the engineers in the early days that this was going to be really difficult, but feedback from our engineering staff consistent with others is that actually people feel – 60% I think is the latest response we did from the survey was 60% of people feel they are significantly or certainly more productive than they were working five days a week in the office.

So, that's something that we are embracing and are building into the cost savings going forward. Your point around installation commissioning service support to customers. That was a bit more challenging in the early days, but again, we moved very quickly, we've been creative, ingenious, using various tools to actually provide customers online support in terms of installation, servicing, that's both in terms of having service engineers, application engineers available online to sort of walk them through it, also providing creative videos, et cetera.

But also we accelerated some of the self-install capabilities on some of our instruments as well that we were working on already but accelerated that so we can make it easier for customers to self-install rather than having to have one of our service engineers necessarily on site to do that.

And then on top of that, things like – we've talked about our digital webinars and things. It's a great opportunity actually to reach out to customers and develop new leads, marketing leads, sales leads, and we're typically getting much higher levels of attendance from customers on those digital channels now than we ever have in the past.

We are pivoting very much now to sort of doing online trade shows, online product launches, online product demos, as the standard way of working. Derek, do you want to pick up just on the cost?

Derek Harding

Yeah, so on the profit improvement plan point, Tom, I guess there's a couple of things. When you think about our original profit improvement programme that we were working through in 2019 and then completing in 2020, we were operating in part in a different world. It was the pre-COVID world and there were, as Andrew said, plans to have more people working remotely and that would result in us being able to reduce our physical footprint.

But I think it's – and we've made the IT investment to facilitate that – but I think it's fair to say that the last six months has educated us all that those plans could go further, and therefore ideas of reducing our physical footprint that we had a year ago, and in certain pockets where we were not sure whether it was possible or not, the events of COVID have proven that it is absolutely impossible and therefore we can push much further on those additional costs.

None of the costs that we're taking out or have taken out in the first wave of the profit improvement plan, or indeed the ones that we're trying to make permanent into 2021, are related to growth, and I think the important thing here is always keeping a balance between taking cost out of activity that you can do in a smarter way and more wisely, having learned from the experiences of the last six months, versus kind of cutting into the bone and in any way damaging the prospects of the group.

So, that's the balance that we're trying to drive and that's the reason for the incremental cost saves that we've identified now, as opposed to the ones that we identified 18 months ago when the world was a very different place.

Tom Fraine

Okay, thanks for that. Just quickly maybe back to Andrew's point on the flexibility of workers working remotely. Will they still have this flexibility though if you're actually looking to shut down a number of facilities?

Andrew Heath

So, yes, because the example that I would use is that where, for example, we might have a city that had two offices or three offices in that city for our various different platform businesses and those officers were fully occupied at all times, where you have a remote working setup with people, some people at home, some people in the office, you can take a more varied, flexible approach and have a smaller physical footprint and still facilitate you know that collaborative working when necessary, have people in the office, have people away from the office.

And I guess that's the sort of thinking that's been going on in many industries for many years, and I think the COVID example has demonstrated that all industries can do that, and that's the type of thing that we will be looking at doing over the coming 12 months.

Tom Fraine

Okay, understood thank you.

Operator

Thank you very much. We have Mr Danny Lu back on the line. Mr Danny Lu, the floor is yours.

Xing Lu

Hi this is Xing Lu from UBS. Can you hear me?

Andrew Heath

Yes, we can.

Xing Lu

Hi, I'm not sure where the name Danny came from, which is why I was a bit confused earlier. Yes. Hi, Andrew. Hi, Derek. A few quick questions from my side. Firstly, just on Omega, you appear to be underperforming IP from a magnitude and recovery perspective. I was just wondering if there's any issues with the new website and customer transfer which was taking a bit longer than before or is that already smoothing out?

Andrew Heath

[? 00:49:04]. What I go back to, as I said earlier, certainly, the stats that we look at relative to the process engineering industrial production space in North America, we feel we are tracking very much in line with the overall market and don't feel that – it's not our proposition or offering that is wrong. Maybe the market is down. There were issues that we were quite public about last year around the transition to the new website and the transition of customers to the new website, et cetera. We feel that the offering has – we've addressed the issues there. Certainly, the customer surveys we've done suggests a lot of that has now been fixed.

But clearly we have brought in a new President of that business, Amit, as I talked about, and he's very much focused on really coming in and assessing the business and making sure that it is really, truly fit for purpose to drive the growth that we're looking for in that business. So, having a new set of eyes in the business, will be, I'm sure, invaluable to us, either to confirm what is working, the strengths of the business, and equally identifying if there are areas that need further work.

We don't know if we've got those, but a new leader coming in with his experience will be invaluable to help either confirm or otherwise our proposition and our offering.

Xing Lu

Got it, thank you very much. And the second question on the M&A market and particularly on your disposals. I guess maybe could you elaborate a bit about any progress there as the activity comes back?

Andrew Heath

On the disposals we've been clear as to what we've said historically, but we won't disclose which businesses that we are in process [ph 00:51:04]. But as I said earlier, we are active. The portfolio rationalisation, optimising our assets is a key plan to our strategy.

We've identified those businesses where we feel we have the strongest growth prospects and likewise where we don't and where we don't think it's sensible for us to invest. We won't be the best owner. My view is that having made that determination, we should push on and tidy up the portfolio sooner rather than later. Clearly, we've got one eye firmly on value and timing around the disposal programme, but we do have some high-quality assets that are of interest to others.

But even in the current environment, it makes sense to be having some discussions. So, we will push on with those and obviously update you as and when we've got something to say.

Xing Lu

Thank you very much. And my last question is just on your outlook. I think you mentioned that you are expecting to meet your full year revenue expectations. I think before you only mentioned that you expect 3Q to be better than 2Q. So, maybe could you maybe help us a little bit there in terms of where exactly you expect for full year revenues if you haven't discussed that before?

Andrew Heath

I guess I'll refer you back to what I said in response to, I think, Josh's question earlier really. We've clearly got momentum going from Q2 into Q3. The like for like decline is significantly better than it was to the previous three months. We expect that momentum to carry on into Q4, and the order book gives us that the confidence that we can certainly meet our expectations.

And I'd just refer back to the comment around if you look at the consensus that's out there, there a few that we would say are a choppy [ph 00:53:12] on the outside but you can see that with the momentum that we've got in the business, really, [? 00:53:21] how we can see the next three months panning out.

Xing Lu

Yeah, understood. Thank you very much.

Operator

Thank you very much. Next, we have Mr Robert from Morgan Stanley. Please, sir.

Robert Davies

Yes, morning. Thank you for taking my questions. The first one was just on some of the regional trends. I just wondered within Europe, I think it was down 13, you put in your release this morning. Just maybe if you could [? 00:53:51] some of the end market trends specifically within Europe where you're seeing that weakness. And then also in terms of regional trends. The rest of the world moved quite a lot. I know it's a smaller segment, but I think it went from sort down from 30 to down 14. Perhaps you could give us a little bit colour there in terms of what's changed?

The other questions I had. One was just on pricing dynamics. Just be quite interested to see what you're seeing in terms of pricing and then the final one was around Malvern. I saw you put in a comment about improvement in sequential growth partly being down to CapEx resumption within certain markets versus a sort of catch up of system installations from 2Q that hadn't happened. Just wondering if you can disaggregate those two and particularly, I guess, with a focus around which bits of the sort of CapEx pie have particularly got better. Thank you.

Andrew Heath

Okay, right. So, a number of things there, Robert. Malvern Panalytical, your last question first. I think the cashback in terms of installations that were delayed from Q2 versus the increasing CapEx spend. It is biased much towards the increasing CapEx spend and that's the bigger part of the Delta.

Pricing typically is consistent with what we've said actually in the last two updates, and that we are not seeing any real significant downward pressure on prices, and it's been sort of generally sort of an amnesty in the market almost. The focus has been more on surety of supply, and that still remains. Clearly, we will see how that develops, but there's certainly the pricing increases that we put in as part of our matter of course business at the start of the year.

We've been able to hold right across all our businesses, so that's positive. And then on your points around geography and markets. Maybe I just give you just maybe a little bit of a quick sort of gamble through each of the – by group and by business and by geography. But, clearly as a group in North America and Asia performing the best. We're really pleased to see China come back strongly in Q3. Europe went down quite significantly at the start of lockdown. That's been in that sort of 12 to 14% down over the last three/four months.

Malvern Panalytical, particularly strong in China in Q3 but also in North America. HBK stronger in North America. China is improving. And so, we saw some positive trends in August and September in the Americas and September in China. Europe [? 00:56:47], especially given its European automotive.

And Omega, we talked about. It's very much tracking. That's process engineering, industrial production space against the market in North America, but it has seen some positive signs in Asia. We're up in Asia for mainly driven by semicon demand being up which is helpful.

And then on industrial solutions again, China's been positive over the last two months and North America is improving. So, I hope that gives you a little bit of a flavour for how things are developing.

Robert Davies

Great. Thank you very much.

Operator

Thank you very much. If there's no further question, I would like to pass the call back to Mr Andrew.

Andrew Heath

Okay, thank you very much and apologies. We seem to have a few sort of technical wrinkles there in getting some of you on to ask questions. So, apologies for that, but thank you for all your questions.

So, with that, let me just sort of wrap up. In summary, I'm very pleased as I said at the outset with the improving performance that we are seeing. Clearly, uncertainties do remain, but we believe that we're taking the right steps to weather this period, very much focusing on what we can control, which I think has been very much part of what Spectris has been about since I arrived over the last two years.

We've demonstrated that through our profit improvement programme. We clearly entered this crisis with a net cash on the balance sheet and good liquidity. And since then, we've continued to generate cash and take further cost actions. Pleasing to see that we're well on track to deliver our 50 million of overhead reduction this year. And also, we have commenced our restructuring programme which will deliver sustainable incremental benefits of 20 million next year on top of the 20 million of permanent this year. So, a 40 million reduction in 2021 versus 2019, which then positions us well, I think, to be able to take advantage of the recovery markets coming through in 2021.

As we implement that restructuring, get our cost base to the right place, with the market coming back, with our balance sheet, I'm confident that we will emerge from this crisis an even stronger and more resilient business. So, thank you again for participating in the call today and I just do hope and trust that you and your families continue to stay safe and well. I look forward to talking to you again in the near future. So, thanks very much.

Operator

Ladies and gentlemen, with that, we have come to the end of Spectris Trading Update Call. Thank you for your participation and have a pleasant day ahead.