CORPORATE PARTICIPANTS

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CONFERENCE CALL PARTICIPANTS

Andrew Douglas *Jefferies LLC, Research Division - Equity Analyst*

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Mark Lewis Fielding *RBC Capital Markets, Research Division - MD & Head of Capital Goods Research*

PRESENTATION

Operator

Good day ladies and gentlemen and welcome to the Vesuvius plc Trading Update. (Operator Instructions) I would like to remind all participants that this call is being recorded. I will now hand over to the CEO of Vesuvius plc, Patrick Andre, to open the presentation. Please go ahead.

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

Thank you very much. Good morning everyone. So, I'm Patrick Andre, CEO of Vesuvius, and with me this morning is Mark Collis, our Chief Financial Officer.

So, I will give you some update about our trading performance in -- over the past 4 months. So, the most important message is that despite more difficult market conditions than what we saw three, four months ago, we performed quite robustly. And thanks to this, our outlook for the year remains unchanged and in line with expectations.

Starting with markets. Markets have been weaker, softer than what we thought they would be three, four months ago at the time of our last update. This is particularly the case for the foundry end markets outside India and outside of automotive. Automotive has been relatively resilient, but the non-automotive markets outside of India have shown clear signs of higher-than-expected weakness since the end of the summer, and it is continuing as we speak. The area of the strongest weakness is Europe and in particular, the northern part of Europe around Germany and surrounding countries.

Steel markets have also been weaker than what we expected three, four months ago, but much less than the Foundry market. It's more of a softening of this steel market. And the areas where the steel market has been softening more is, of course, EMEA and Europe, where steel markets are quite soft as we speak; and to a lesser extent, Southeast Asia and South America.

In this globally softening environment, India remains an important exception, and it's important for us that India continues to grow quite healthily both in steel and in foundry. And we ourselves, are significantly outperforming what is already a very robust market in India, growing significantly more than the market in India in both divisions and particularly in the steel division.

Globally, worldwide, we have performed robustly and with both market share gains continuing in Flow Control and in Foundry and a very resilient pricing; and this good internal performance enabled us to offset, in fact, the weaker-than-expected external market conditions. And this is the reason why we are maintaining our guidance, and we feel comfortable to maintain this guidance towards our expectations.

From a cash point of view, we are making good progress. We are generating a good cash flow from operations and also starting to make good progress in the reduction and optimisation of our working capital. So, thanks to a positive cash generation, we are expecting our net debt-to-EBITDA ratio to be on or around 1x at the end of the year.

Taking a step back, and even if it is too early at this stage to give any precise guidance on 2024, what is important to note is that we remain convinced that the midterm fundamentals of our market remain positive with, in particular, some expected growth in the steel production outside of China going forward. So, all our strategic initiatives to position us to benefit from these positive trends are fully on track.

First, our R&D effort is continuing to progress well. We have a full pipeline of new products to launch on the market for the next two, four -- two, three, four years. And our investments in new capacity are progressing well, in particular, in India. All of our new capacity investments in Flow Control are now coming online. This is what is enabling us to progress significantly faster than the market in India. This year, our sales in India group-wide will probably grow on or around 15%, which is close to double the growth rate of the underlying market in India, which is very positive. And we expect to continue to outperform the market in India going forward as in the rest of the world.

So globally, we are quite positive about the outlook. But again, we will not give guidance on 2024 today as it would be too early. There are too many moving parts. And we'll do that further when we announce our first-year results in February next year.

So, thank you very much, and I propose now to open the floor for questions.

QUESTION AND ANSWER

Operator

(Operator Instructions) We'll take the first question from Mark Davies Jones of Stifel.

Mark Davies Jones - *Stifel, Nicolaus & Company, Incorporated, Research Division - Associate*

A couple from me, if I may. Firstly, you said your pricing has held up pretty well. Could you comment on general pricing discipline in the market if volumes are weaker? Are you seeing any signs of people losing their discipline there? And then the second one was on the messaging around Foundry. That's obviously a change. You were talking about some recovery coming through in a quite encouraging trend in the first half. Obviously, PMIs in Germany being weak for some time. What has changed there, why do you think we've seen the sort of sudden deterioration?

Patrick Andre - *Vesuvius plc - CEO & Executive Director*

Your first question on pricing. Yes, we have a good and resilient pricing in all three divisions. Regarding our competition, I would say that we see some of our competition trying to put pressure on pricing in Flow Control and in Foundry. There, of course, it's an important phenomenon, but we are relatively comfortable with that because of the technology differentiation of our product. So we are, of course, always offering fair pricing to our customers, but sharing value with them. But the price pressure of some of our peers in Flow Control is not disturbing too much today of our own pricing strategy.

In Advanced Refractories, if you remember well, we have lost some market share in H1 because we have been, I would say, more resilient. We have targeted for more resilient pricing than most of our competitors. And as the technological differentiation is less pronounced in Advanced Refractories than it is in the two other business units, we've lost market share in H1 in Advanced Refractory. We plan to recover. We have started to recover some market share in Advanced Refractory in H2, but less than we were expecting. We have not recovered.

We will not recover fully in H2 what we've lost in H1, which is also an indication of the discipline of other players. And again, you have the very different situation there. You have some players being disciplined, some others less so. But on average, the discipline of the players in Advanced Refractories is a little bit less than what we would like it to be. And as a consequence, prices in the Advanced Refractory world are adapting. And I would say it's also adapting to the decline of raw material prices.

Mark Davies Jones - ***Stifel, Nicolaus & Company, Incorporated, Research Division - Associate***

And on the Foundry question?

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

Regarding Foundry, the -- we see a deterioration in Germany. So independently of the macro indicators that you mentioned, we have clearly seen a deterioration in Germany since the summer. So the mood was already not very good before summer, but the fact on the ground has been deteriorating since earlier in the year. We really see a slowdown in real activity on the ground with the orders received by our customers and the order received by our customers from their own customers on a downward trend since earlier in the year. And clearly, there is a decline in the top line of the Foundry division as compared not only with Q2, but even as compared with Q1. So we -- the downturn in the northern part of Europe is quite important for the Foundry division.

Mark Davies Jones - ***Stifel, Nicolaus & Company, Incorporated, Research Division - Associate***

Okay. Do you think that sort of inventory in their channel is being sorted out? Or is it just underlying weakness in, say, China (inaudible) through the system?

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

As we mentioned, the -- we believe that part of the overall weakness in the Foundry market is due to destocking. It was already true in H1. It continues to be true in H2. We believe that destocking should be mostly over by the end of the year. So it's not making things better on the Foundry side, the destocking. But we think that the destocking movement should be over mostly by the end of the year. In Steel, if you remember, the destocking is over -- was over by midyear. In Foundry, it will be over by the end of the year. So for the year 2024, we should not have any negative impact from destocking any more, both in Steel and Foundry. The uncertainty, in particular, in Foundry relates to the real underlying demand. We feel we are at a low point. And today, it's probably difficult to go much lower than what we are now. But how long will it take for the real demand, especially in Europe for the Foundry product to go back up is a question mark today. That's the reason why we are not giving at this stage guidance on 20'24. We'll do that in two, three months when we announce our full year results.

Operator

The next question we have is from Andrew Douglas of Jefferies.

Andrew Douglas - ***Jefferies LLC, Research Division - Equity Analyst***

You kind of answered my question on risks to destocking in steel, so it's good to hear that. Can I just ask, on the softness that you've seen in both divisions, do you think any of this is structural rather than the cyclical? And does that mean you have to take out costs if you're slightly worried about more structural challenges in your end markets? Or is this just a cyclical phenomenon? And the second question is just on the M&A outlook. Strong balance sheet. I know there's a couple of players out there who just buy anything that moves. What are you seeing on your side? And is this now just an ongoing question of the pricing? Or is it the call to the assets which you're concerned about?

Patrick Andre - *Vesuvius plc - CEO & Executive Director*

Thank you, Andy. First, your question about cyclical versus structural. I think that most of it is cyclical. Especially in the steel sector, we see that as a purely short-term cyclical phenomenon. We believe that the steel position outside of China will structurally grow significantly and not only in India, also outside of India going forward. So, we see the sort of product movement in steel, which, by the way, is not that pronounced. It's softening and mostly cyclical. Regarding Foundry, I think it's -- what we see is cyclical is you talk about Southeast Asia or South America or even North America.

The point where there is more of a structural element, I believe, is the Foundry market in Northern Europe. I believe the weakening, the softening there is probably not only cyclical, there is an element of cycle, but it's not only that. I think that there is clearly a structural decline of the Foundry market in this northern part of Europe. I don't see Germany going back to what they were historically. There are some switches. And -- but you have other areas in Europe or in the rest of world, which are substituting.

You see Turkey, for example, is growing very fast in the Foundry world. So the northern part of Europe is losing, the other parts are gaining. And we have European teams or asset, effort, commercial teams in the Foundry division. As we've done in the Steel division long ago, we are reorienting our efforts towards the fast-growing part of the world and away from the slower growing one.

Regarding M&A, we keep an appetite, that I would say is a disciplined and selective appetite on M&A. So we are looking at a few opportunities. But the only opportunities we are looking at are those which can complement our current portfolio, either from a geographical point of view and/or from a technological point of view. So this is the filter that we are applying to screen opportunities. So we are not interested to buy anything which is potentially on offer. We are very selective. There is no guarantee that something will happen, but we have an appetite, and we have the balance sheet to do it in case there will be opportunities. So we are proactively looking at opportunities, but our main priority remains our organic growth strategy.

Operator

(Operator Instructions) The next question we have is from Lush Mahendrarajah of JPMorgan.

Lushanthan Mahendrarajah - ***JPMorgan Chase & Co, Research Division - Research Analyst***

I've got a couple, I think. Just going back to that Foundry point and from those structural issues, particularly in Northern Europe. I think EMEA was, I think, 40% or so of the Foundry business last year. I mean how big is Northern Europe within that? Is it the majority, or just think about what the impact could be longer term there?

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

Northern Europe is historically the most important part of the EMEA business for the Foundry division. So yes, it's close to the majority of the business. So in fact, Northern Europe is an important business historically for the Foundry division as a whole. So the weakness in Northern Europe is disproportionately impacting the Foundry division. And one of the key strategic pushes of the Foundry division is, of course, to progressively decrease the relative importance of Northern Europe in the overall Foundry business, which has been the case over the past three, four years and will continue in the coming years. So our investments are disproportionately in other areas, in the growing area, not only in the growing area of India, Turkey and so on, but also in the growing other areas in Asia in particular.

Lushanthan Mahendrarajah - ***JPMorgan Chase & Co, Research Division - Research Analyst***

Okay. And the second one, just on pricing in Flow Control and Foundry, presumably raw material have deflations. Is that -- you said prices have been coming down in the second half. Can you sort of give us a rough guide in terms of what you're doing with your pricing and what do you think of your peers today in terms of the numbers?

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

As you know, we have a general policy in terms of pricing that raw material prices are passed through. So we are increasing and decreasing our prices based on fluctuations taking into account fluctuations in raw materials, but also taking into account the value that our products are creating in our customers' processes. So you have two elements. The first one is that raw materials are going down. So this will -- this normally has a normal pass-through to our customers as we have always done, will have a tendency to bring raw material -- to bring prices down. But at the same time, as we are proposing to our customers more and more value-adding solutions, creating values in their processes and we are discussing with our customers the fair sharing of this additional value creation. As a consequence, our prices, because of the value creation sharing components, are declining less than raw materials.

Lushanthan Mahendrarajah - ***JPMorgan Chase & Co, Research Division - Research Analyst***

Okay. Just in terms of are they sort of down low single digits, or is it flat? Just trying an idea of sort of the quantum of the change.

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

Today, prices are, I would say, I'm not talking Advanced Refractories, different, but are very slightly declining.

Operator

The next question we have is from Harry Philips of Peel Hunt.

Harry Philips - ***Peel Hunt LLP, Research Division - Analyst***

A couple of questions, please. Just -- you gave a statistic on India-Pac, which I missed around sort of the 16% number in there, which sort of caught my ear. And then just secondly, in terms of sort of lines being under recovery, which you were talking about at the half year, how is that playing out current time? And has that sort of lasted longer than you anticipated thinking particularly with reference to your comments around Foundry?

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

First starting with India. Yes, we are growing quite fast in India. And if you remember, our growth strategy in India is not M&A, it's really organic growth. And we have been investing over the past two years now in new capacity in India, both Flow Control -- mostly Flow Control over the past two years and -- but also a little bit in Advanced Refractories, and we are very, very happy to have also because the growth in India is not only more steel, but it's more demanding steel, more sophisticated steel. And the consequence is that thanks to this new investment in capacity which we are starting to use, our isostatic new capacity came on stream in February this year, and we are already using a good part of it.

And this is what enabled us to grow even faster than the underlying steel market in India. And our growth in India this year will be close to -- the year is not over, but probably on or around 15% this year, which is significantly higher than the underlying market growth. And we are also now not only continuing to increase our capacity for control, but we are also -- I was in India myself last week too -- for a first stone laying ceremony for expansion in Advanced Refractories. So we are also increasing our capacity in Advanced Refractories.

We have been increasing our capacity in Foundry with the new filter -- Foundry filter line, which is now fully operational. So we have strong ambitions, both in Steel and Foundry in India. And this year we'll grow nearly double the rate of the market. I will not promise we will grow double the rate of the market every year but clearly, we'll try. And so yes, we are making very good progress in India with a very, very strong team, good products corresponding to what the market is asking for. We have initial discussions now even in India, regarding automation and robotics. And this you can say yes, India is a low-cost country, but even in India now has the level of sophistication of our steel customers, in particular, is driving them as the rest of the world towards robotics and automation solutions. So we are quite optimistic, and if I may, aggressively optimistic about our performance in India going forward.

Regarding the under recovery, we had announced that we were expecting between five million and 10 million under recovery negative impact because we were reducing inventory. We'll probably be closer to five million than to 10 million this year. So we -- which translates to the fact that we are making progress and especially now in the second half, we are making progress. But I would like our progress to be even more than that, together with Mark. And so out of the 10 million, we were and are still planning to do, probably will have five this year, meaning that will be a little bit less for next year.

Harry Philips - ***Peel Hunt LLP, Research Division - Analyst***

Fantastic. And then just maybe a final question. The -- you talked to having new capacity coming on stream in India, and you've outlined that with a whole lot of new capacity coming on around the world, you have that slide in the interim where you talk about potentially adding 40 million of EBITDA by 26, 27 million. That sort of programme is all still on track, and I guess we'll get more on that in a couple of days' time.

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

Yes. The program is completely on track, and I will confirm that later this week. And if I may, we are generating new ideas. But yes, the program is completely on track.

Operator

The next question we have is from Bruno Gjani of BNP Paribas.

Bruno Gjani - ***BNP Paribas Exane, Research Division - Research Analyst***

I just -- could we perhaps talk about the sequential trading profit bridge. It sounds that volume may be lower in the H2 bridge when compared to H1 than previously expected. What's been the positive offset that's giving you the confidence to reiterate the guidance? Is it -- I guess, under absorption is a lower impact, but is there anything else?

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

I think it's -- we have lower volume, you're right, but we have a better pricing. We have better pricing. And the better pricing, the fact that volumes are less than what we were expecting, but less than the market decline and because we are gaining a bit of market share. So -- but still it's lower than what we thought, but price is better than what we thought. So this is offsetting.

Bruno Gjani - ***BNP Paribas Exane, Research Division - Research Analyst***

Understood. That's very clear. And just a clarification on India. Could you remind us of your sales exposure to that country today and give us a rough sense of growth you expect to come in the years ahead.

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

I think it was on or around 9% of our sales last year. It will be on or around 10% this year, and I expect this percentage to continue to grow. We will probably this year, it will be a close tie, but will probably this year for the first time I think, sell more in India than in China.

Bruno Gjani - ***BNP Paribas Exane, Research Division - Research Analyst***

All right, okay. And just on market share, could you perhaps expand on those market share gains? Is it a particular regional business that's driving that in the trading period and expand on that a little bit, I guess.

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

Yes. In Flow Control, we are continuing to gain market share, we say, across the board. It's interesting to know, for example, that even in China, where, as you know, the steel market is not very good; we are continuing to grow our Flow Control business in China in absolute terms because we are continuing to gain market share there, and we are continuing to have a good business, a quite good business in China for Flow Control. So across the board, worldwide, as there is nearly no exception. We are continuing to grow market share everywhere. And we intend to continue doing that.

We have some very, very promising and very advanced leads to continue to do that in 2024 and the year forward, knowing that we have a full pipeline of new projects, new products -- so the business together with Flow Control is working very, very well, both in terms of pricing resilience and in terms of market share gain, simultaneously.

Regarding Foundry. Foundry, it's a little bit of a pity that the Foundry division is operating in the market, which is not what we would like because they have a good performance also with relatively resilient pricing and at the same time, now some market share gain and -- but with an environment, which is more difficult, but good performance in terms of market share gain on the Foundry division.

Advanced Refractories, as you know, we've lost market share, and if you remember, during the first half -- we -- because we've been, I would say, probably relatively ambitious in terms of pricing, probably a bit overambitious in terms of pricing. We started recovering some of this market share in the second half, but not all because we remain very disciplined in terms of pricing. But I'm confident that even if we will not regain in the second half everything, we lost in the first half, which means that overall, year-on-year, we will lose market share in Advanced Refractories; to be very clear, we believe that has happened already a few years ago, we will continue to recover some market share in 2024. But we want to do it progressively without doing stupid things on prices. So it will take more than one semester to compensate fully the market share we lost in the first half.

Bruno Gjani - ***BNP Paribas Exane, Research Division - Research Analyst***

Got it. That's very clear. And just one final one on market share. In terms of the market share in different regions of your foundry business, is your market positioning stronger in Northern Europe? Do you dominate more of that market than with the other countries or is that not the case.

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

I would never say we dominate the market. This is because we have competitors everywhere in Northern Europe. But historically, yes, the Foundry division is as -- Northern Europe was and is a particular area of strength and presence. This is where we have our biggest plant worldwide, the Borken plant in Germany, a long tradition of close relationships with some of the most important customers in Germany. So this is where we have also -- it's one of the area where we have the strongest area. We have also areas of the world where we have strong presence; in South America, now growing rapidly in India. So -- but yes, it is one of the regions where we have the importance of our presence is above average.

Operator

Thank you. The next question we have is from Mark Fielding of RBC.

Mark Lewis Fielding - ***RBC Capital Markets, Research Division - MD & Head of Capital Goods Research***

Yes. Just actually a quick follow-up to the answer you gave earlier when talking about M&A. I suppose, can you revisit your thoughts on the fact that obviously, your net debt to EBITDA is going to be below your target range at the year-end and just more generally, how you think about future capital allocation?

Patrick Andre - ***Vesuvius plc - CEO & Executive Director***

I think the answer is in the question if you follow me. So we have been, as I said earlier, very disciplined. So we don't want to force ourselves to do M&A. There is no opportunity which fits our criteria. So probably relatively rapidly now, we will make a decision in terms of capital allocation. Depending if there are or not attractive M&A opportunities available, but we will not have to wait forever for this opportunity to be available. So we are probably nearing to the point where -- together with the Board, of course, and we will make sure that it's a choice which we have been preparing for quite some time. And if in the relatively close future no attractive M&A opportunities present themselves, we'll probably think about how to give some money back to our shareholders to bring back our net debt-to-EBITDA ratio a little bit closer to our comfort range.

Operator

There are no further questions on the conference line. I will now hand over to the management for closing remarks.

Patrick Andre - *Vesuvius plc - CEO & Executive Director*

Thank you very much for all of you for your attendance today. As usual, Mark and I remain with Richard at your disposal, would you have any questions. I wish you a very nice day, and I hope to see you all at our Capital Markets Day later this week on Thursday. Thank you very much, and goodbye.