IMI plc
Interim Management Statement

Thursday, 9th May 2024

Introduction

Roy Twite

CEO, IMI plc

Thank you and good morning everybody. Thanks for taking the time to join us today. I am joined here as usual by Dan, our CFO. Hopefully you have all had a chance to read through the IMS this morning. Now, I am going to take the statement as read so we can get straight into Q&A, but I would just like to highlight that the Group's first quarter performance was in line with expectations with 4% organic growth. So as such, we are reconfirming guidance. We still expect that 2024 full year adjusted EPS will be between 120p and 126p.

So with that, I am going to hand back to the operator who will manage the Q&A session for us. Thank you.

Q&A

Lushanthan Mahendrarajah (JP Morgan): Hi. Morning guys. Thanks for taking my questions. I have got two if that is okay. The first is, if possible, could you give us any colour on April trading please? And I appreciate the Q1 comps in particular are quite tough, just to get an idea of run rate.

And then the second question is on Process Automation. Would it be possible to get some colour on order intakes? Ideally ex that Marine order and just the OE / Aftermarket split there as well, if possible. Thank you.

Roy Twite: Well, good morning, Lush. Yes, so if I start with April, we have got the April sales numbers in. I think probably the variances are Industrial Automation is actually better. So instead of minus 5%, Lush, at the end of April, it was minus 3%. So that is really encouraging. Particularly when I look at some of the comparatives that have been published over the last weeks, it is nice to see us doing pretty well actually in Industrial Automation.

The next bit of good news is that Climate Control, as you know, was minus 4% at the end of the first quarter. It was actually flat now year to date at the end of April, which, when you consider the comparator last year, now the first part of last year, wholesalers were restocking, we had Halo-B, if you remember, our product that we put out to help the German municipalities hit this 19°C target to save energy. So I am actually pretty pleased that that business, as usual, is showing a lot of resilience and obviously very strong in terms of energy savings. So that is good news against, I think everybody appreciates, pretty difficult European construction markets. Yes, so they are probably the two big changes.

Overall, Life Technology, instead of minus 6% at the end of the first quarter was actually minus 2% at the end of the first four months. So again, pretty much in line with where we thought it would be and puts us in a good position, Lush, to really get probably flat this year across Life Technology. So yes, quite encouraged by what has happened in April.

Clearly, Easter moved around a little bit, and always in IMI, for years, we have looked at March and April together. Just as Easter moves, it does have a bit of an impact. So reasonably encouraged on the April situation.

On Process Automation, you are right, so last year we called out this big Marine order, which, as you know, was a multi-year order. So if you strip that out of last year, it would mean that first quarter order intake was actually plus 8% overall. So again, it is going nicely. Against a very strong comparator last year. I mean, very, very strong first quarter last year.

On the Aftermarket side, so again, if we look at year to date April, Aftermarket is plus 7%. So again, that's against a super strong comparator. Actually, I cannot remember, Lush, what the first four months was, but I know that Aftermarket in the first quarter last year was up 49% for Process Automation. So to be ahead of that year to date is encouraging. Does that answer your questions, Lush?

Lushanthan Mahendrarajah: Yes, that was a really, really helpful colour. Thank you very much.

Roy Twite: Thanks Lush.

Christian Hinderaker (Goldman Sachs): Morning Roy. Morning Dan. My first question would be on Climate Control, and you touched on a little bit there in terms of the weakness in construction, but you have also cited strong underlying demand for energy efficient products. Just keen to unpick that a little bit. I mean, what are the assumptions built into the full year guidance for this business? Are you able to comment on dynamics in terms of inventory in the channel? And maybe elaborate on that point of weakness in broad-based demand versus strength in demand for energy efficient products. Thanks.

Roy Twite: Yes, no, nice one. Christian. I think this has traditionally been a very resilient business and you would have heard me, Christian, if we go back to 2009, I think it was down 4%, and actually profits were up. And it is a super resilient business, partly because of the energy saving, partly because of its value equation as well where it is only 2% or 3% of the cost of the system, typically our kit, but it can contribute energy savings up to 30%. So it is really strong, the brands are strong, it is good pull through, and it has always been very resilient on price and good pricing power as well.

So you put all that together and we said pretty much consistently that this year - despite a lot of people saying, well, European construction markets really, really tough place, which they are, we have said consistently we think we will carve out growth this year. And clearly with flat year-to-date April against a very strong comparator, we still think that will be the case.

On the inventory side, I think last year there was definitely restocking wholesalers in Q1. We are picking up much less of that. I think generally speaking, Christian, because of where interest rates are, most people are keeping a careful eye on inventories. And so I think there is a general trend to make sure they have only got what they need for customer service, and clearly supply chains are generally better than obviously they were during Covid where they were keeping more safety stock. I think, Christian, when our guys are talking to the wholesalers, most of that Covid situation has unwound, and we are a more normal situation as far as our stocking levels are concerned right now. So from what we can see, no real big change due to stocking, restocking Q1.

Christian Hinderaker: Thanks Roy. Just turning to the divestment of Industrie Mecanique within Life Sciences, should we read that as implying that the pro forma business today is actually 1% better than guided? Am I reading that right?

Roy Twite: I mean, broadly speaking, it is just under 1%, rounds to 1%, but it is not actually a Life Science business. I should just say that. It was on the Fluid Control side of that sector. So I will just be absolutely clear about that. And we actually acquired it, I think it was 2006, something like that, with Orton and with a whole bunch of other assets, and it has got some interesting high-pressure regulation technology, but what we found was it had gone ex-growth apart from hydrogen. So obviously we are applying that technology to hydrogen. So what we were able to do, Christian, is move the products that were applicable to hydrogen into another one of our businesses within Fluid Control. So that is great because that is the bit that is growing, but the rest of it had really gone ex-growth for us. And so being able to move that on with a reasonable multiple on it, was exactly the right thing to do for us. Reduces complexity as well and helps us, again, nudge the mix of the business to higher growth.

So yes, if you look at all of that put together, it rounds to 1%. It is obviously slightly less than 1%, but Dan, I think you are putting half a pence of earnings?

Daniel Shook (Chief Financial Officer, IMI plc): Yes, probably about half a 0.5p of earnings impact. So yes, so embedded in this is a little upgrade to our guidance because we can hold it with the divestiture.

Christian Hinderaker: Very clear. Thanks. And yes, that is very clear. And then thanks for clarifying that is Fluid Control. Maybe just finally, capital allocation. We talked in March about the implications there potentially, but can we touch on the M&A landscape within that framework? You have done four acquisitions I think in the last three years. Just eager to understand where the focus is there in terms of scale, whether there are particular segments where you would prefer to do M&A and what the current pipeline is looking like. Thank you.

Roy Twite: Yes, no, perfect. So scale, as you know, we like bolts-on. So we think anything up to £300 million or slightly beyond that is good for us in terms of scale. We like those bolt-ons because we are always looking to accelerate growth. So we are always looking for us plus the acquisition enables us to grow faster. Heatmiser is the latest one and you know the plans for that, Christian. So we love that sort of scale, nice bolt-on.

In terms of segments, we really like Life Sciences, smart connected buildings, and Automation. That is really the three areas that we really like. Clearly, if there was a nice Automation asset where we could accelerate the Aftermarket growth, like we have done in Process Automation, that sort of thing is very attractive. So again, where us plus them, one plus one equals a lot more than two, that is what we are really after.

Hopefully that gives you a flavour. Pipelines looking pretty good actually, but again we are pretty particular as well. So yes, I would say pipelines look good, opportunities look okay. If we do not get to the point where we can deploy the capital through acquisitions, clearly, you can see how strong our cash flow is becoming, and we will be moving over the next couple of years to £300 million of free cash flow, won't we, Dan? So, at that point, we will obviously look at other means to return money to shareholders.

Dan, do you want to talk about the conversations with shareholders?

Daniel Shook: Yes, and everybody, well by and large shareholders want to keep their own optionality, so share buybacks make the most sense. I think we have talked about it in March. We started the year at 1.3x. If we do not unlock, we will probably do half a turn, so we will be below 1x. And I think that is when we get very comfortable. We have the dry powder for the pipeline and probably a little bit more. So that is when we will start thinking about a share buyback, Roy.

Roy Twite: Yes.

Christian Hinderaker: Understood. Thank you both.

Roy Twite: Brilliant, thanks.

Mark Davies Jones (Stifel): Thank you. Morning Roy. Hi Dan. So at the full year, you talked about the rolling average, I think order intake in Industrial Automation turning gently positive right at the end of the year. I wondered how that had continued through the year to date. Obviously, the macro picture there still seems very mixed, particularly in Germany. So what are you seeing in terms of order flows?

Roy Twite: Yes, so Industrial Automation was slightly positive, as you said, Mark. It is now slightly negative on the 60-day moving average, and US is very slightly down. Europe is slightly more down. So yes, it is probably a bit of a false spring. I have obviously checked all the peers, as I said, and we are probably slightly outperforming, but I think still the industrial landscape is reasonably tough. As I said, the good news on Industrial Automation is that it was minus 3% versus minus 5% by the time we got to the end of April. So some recovery in April. And again that is largely due to working days and Easter moving around and things like that. But in terms of orders, slightly down on that 60-day moving average, Mark.

Mark Davies Jones: Thank you. And then on a slightly more bullish front, the Transport number in Q1 was exceptionally strong in a tough market. I know there is some lumpy stuff going on in Asia, but if you are still looking for flattish for the full year, does that now seem a bit conservative?

Roy Twite: I mean, good operational performance. And Asia was our strongest area, Mark, still and new product coming through, so that was encouraging, 19%. But when you look at all the commentary and you listen to the big OEMs in the US and Europe, they are expecting volumes down. And that varies between minus 5% to minus 15%. So there will be an element of catch-up in our numbers as well as the new products. So we still think for the year, certainly our guidance is based on slightly down sales for the full year. And whereas other markets will obviously improve throughout the year, we think that this is one that is going to go the other way. And particularly when you look at the comps as well, Mark, remember that second half of last year was very strong for Transport for us.

Mark Davies Jones: Okay, great. Thank you very much.

Roy Twite: Thanks Mark.

Harry Philips (Peel Hunt): Good morning everyone. A couple of questions from myself. It is not often you see a 27% positive number in an IMI statement. So it is just really more thinking about the sequencing of how Process Automation evolves through the year. Obviously the order book is there, and we know it is going to have a cracking year, but 27% was certainly more than I thought it was going to be. And just to follow on from Mark's question around the Asian exposure of Transport, I am trying to remember if you have given this number, but just how big is the Asian content within Transport at the current time, particularly with the new contract wins that you have booked in recent times, please?

Roy Twite: Yes, I will let Dan come on to Transport. It is growing substantially, Transport in Asia, Harry, I think last year basically double, but I will let Dan come on to that in a minute. On Process Automation, I have got to say Jackie and the team are doing a fantastic job because the book to bill, Harry, in Q1 was 1.3. So despite 27% growth, now obviously always shipping is a bit lower Q1, and you all know that Q4 is high for Process Automation, but even so, really pleased with that. Really pleased with the 7% Aftermarket bookings growth over the first four months as well given the tough comparator. But the sheer operational excellence in a project-based business to deliver 27% growth is also phenomenal. So I could not be more pleased with Jackie and the team in terms of what they are delivering on Process Automation.

Yes, you know it is a lumpy business, Harry, you know it is project based, so it is not going to run at 27%. We stick with our overall guidance for Process Automation. It is going to be double-digit growth in that, let's say around 12% organic growth for this year in terms of sales. So it will flatten out. Already April flattened out a bit. But yes, I am really encouraged and it is always good, isn't it, Harry, to get it in the books. So it is nice to get a really strong start for Process Automation. So thanks for that.

Harry Philips: Just to follow on, things like pricing in Automation, is there any issue around that or is that a conversation to come down the line?

Roy Twite: No real issue in pricing in Automation. It is pretty much what you expect, which is that we are seeing pricing in the Aftermarket holding up well. As always, Harry, I cannot remember whenever that has been an issue. And then on the Industrial Automation side, strong brands, good market positions, pricing flowing through. So no issue on pricing.

Daniel Shook: Harry, 20% in Asia for Transport, still. About 15% India and China. So those are the big markets, and so it is definitely growing faster than the rest of the business at this stage, but it still rounds to that 20% of the overall Transport business.

Harry Philips: Fantastic, thanks very much indeed.

Roy Twite: Thanks Harry.

Stephan Klepp (HSBC): Morning Roy. Hi again, Dan. Just one, many have been answered already. Book to bill was one of mine as well. So Process Automation again. With its strong growth, I know you are not talking about that in the statement. And I know and I appreciate the project contracts, but should we see, as well, operational leverage coming through? You talked about it. Aftermarket, very stable, very strong, good margins, but should not we see as well now scale effects coming through from that high growth number that you have been executing?

Daniel Shook: Yes, good questions. So we are obviously investing heavily in Process Automation because we are investing in the Growth Hub. Growth Hub orders in the first quarter were almost double the first quarter of last year. So the amount of innovation coming through, particularly in Process Automation frankly is fantastic. So we are investing in that. We are investing in more Aftermarket sales engineers obviously. We have done really well, Jackie has done really well unlocking the code of the upgrade valves, that strategy we presented in quite a lot of detail back in the capital markets presentation. I think Aftermarket growth since then, we targeted 5-7%. I think it is actually running at an 11% CAGR. So obviously we need to invest, we are investing behind that. We need to, it would be crazy not to. So we have always said that once we get to sort of 20% margin overall, through the cycle, that is where we are going to be. We are not just going to rinse this business, we are not just going to keep operational leverage without investment, it cannot work like that. You cannot sustain a 5% growth, which is what we are going to do, industrial company without the investment going into the business. And I think that is what we are going to do.

So yes, I think what you will see is, again, margin improvement this year in Process Automation, but do not expect us to drop through huge percentages because we are going to keep investing, Stephan.

Stephan Klepp: Okay, super. And then the second one, I think you implicitly answered that, so price volume in Transport and Industrial Automation, that would be just interesting as well.

Roy Twite: Yes, we are not going to break it down quarter by quarter, Stephan, but overall, it is pretty much exactly what we said, Stephan, which is we have got 4% growth in the first quarter, roughly half and half price and volume, pretty much exactly what we planned to do. And I think actually we summed it up pretty well I think at the beginning Stephan. Actually, although markets are moving around, we forecast demand and supply pretty closely, haven't we Dan, compared to our F1 forecast in terms of price and volume. So yes, I think we are in good solid shape.

Stephan Klepp: Super. Thank you so much.

Roy Twite: Great, thanks, Stephan.

Jonathan Hurn (Barclays): Hi guys. Good morning. Just a couple of questions if I can. Firstly, can you talk a little bit about cash generation in the quarter? I was just thinking obviously strong growth in

Process Automation, have you had to increase inventories there? Has that been a little bit of a drag in terms of cash generation in the first quarter? And then obviously going through the rest of the year, how do you see that dynamic playing out? Are you still having to invest in inventory, particularly in Process, to deliver those orders?

Daniel Shook: Yeah, Jonathan, as the order book grows and as we said in March, we expect the order book to be larger at the end of the year versus the beginning, there will be a need for some inventory to go in to manage that order book. The rest of the portfolio, I think we will still see a good evolution. We still have some safety stocks to cover customer service. We think we can pull those down as we go through the back end of the year.

So overall, I think we are going to continue to progress towards that £300 million of free cash flow. We still have the restructuring programme happening in 2024, and that is about £30-40 million of cash outflow in 2024. So that will probably hold us south of that £300 million target, but we are getting very close to it. So yeah, so first quarter, cash was a little bit soft, but that is just normal seasonality and the Process Automation order book growth.

Jonathan Hurn: Okay, that is very clear. And the second one was on profitability, obviously you have touched on that for Process Automation. Can you give us a little bit of colour in terms of profitability across business in Q1 and how you expect that to phase through the year, please?

Roy Twite: Margins in the first period have been pretty similar to last year actually, Jonathan, which I think is really good, because the comparator obviously to last year was tough in the first quarter. So that is why obviously we are sticking with our guidance, we are going to see the benefits of the restructuring coming through as the year progresses. I think we get two-thirds of the benefits of the restructuring in the second half, roughly speaking, Jonathan. So I think you have £15 million coming through this year, another £7 million coming through next year, which lines up nicely, obviously depending on what happens in the macros and stuff, but pushes us towards that 20% margin target. So yes, I think we are in pretty good shape, Dan.

Daniel Shook: Yes, I think mix in the Life Technology sector will probably hold margins back a little bit in the first half because it is more heavily weighted towards Transport. And as that normalises and shifts in the second half, we will see a better margin performance in Life Tech in the second half. But overall, still expectations for margin growth across both platforms.

Jonathan Hurn: Okay, that is very clear, guys. Thanks very much.

Roy Twite: Thanks Jonathan.

Mark Fielding (RBC): Yes, morning, just a quick follow-up on Process Automation, and you have very helpfully provided that book to bill at 1.3 times, but I suppose you mentioned phasing factors. How do you think we are going to end the year in terms of book to bill in that business? It is a slightly longer order book than some, and how do we think about the cycle evolution from here?

And then secondly, could you also provide just a bit more colour on the sequential trends you are seeing in the Life Sciences business, just so we can get a feel for how that is evolving and where that sits versus the full year outlook for that business?

Roy Twite: Yes, brilliant, thanks Mark. Okay, so we think we are going to end the year with the order book up in Process Automation, Mark. So, as we said, double-digit growth on sales this year and actually pretty well placed for some good sales growth next year as well, obviously in current markets. So that is broadly where we see it.

On Life Sciences, sequential orders in the first quarter are slightly up on the fourth quarter of last year, Mark, but there are some scheduled orders in there as always. So I am not getting too excited, but it does look like we have at least bottomed out in terms of Life Sciences orders, which means that sequentially as we go through this year, obviously the comparator gets a lot easier. You will remember, sorry, was it the first four, five months of last year, Dan, was pretty good, and then it fell right off.

Daniel Shook: Yeah, it came off.

Roy Twite: So that is really where we are at the moment in terms of sequentials.

Mark Fielding: Great, thank you very much.

Roy Twite: Thanks Mark.

Rory Smith (UBS): Thanks for taking my question. I think there is still a question to be asked on Process Automation, although I appreciate we have spent a lot of time there already this morning. And that is, you mentioned cracking the code of the valve upgrade work. Is there anything you can add additionally just on how much of the strength in the Aftermarket is underlying strength and how much is IMI taking share in that particular area? Thank you.

Roy Twite: Yes, that is really good point, Rory. Clearly, maintenance budgets are strong right now, so you are absolutely right, and there is no doubt about it, people are running their assets harder since everything has become a lot more scarce following the Russian invasion of Ukraine. So that is definitely helping us. There is no doubt about it. The wind is at our backs on the Aftermarket as well as New Construction. I think what is encouraging is that, and I said this on the last call, Rory, a lot of what we do is obviously replace our old valves in the field. That is our classic upgrade. We have got a lot better at that. We have put in CRM, the IT systems, we have got a lot better understanding of where our assets are. We look at the patterns using data analysis, a level of AI to try and find out exactly what valves are likely to go wrong when, so when are they going to start to wear in what conditions and what sort of valve and all of that. So again, Jackie and the team have done a wonderful job with data analytics and all of that side of things, and that is helping us go to customers and help them upgrade valves. So that is great.

On top of that though, last year, the sales value of our competitor upgrade valve business roughly doubled as well. So that is where obviously we are starting to understand which of our competitor valves are likely to go wrong and when, Rory, and pre-empt that. And then obviously it is tough right, you go to these customers and a lot of the times they will obviously go back to the OEM supplier. If they have had a problem with some sort of service with that OEM supplier, then our brands are super strong. And we have proven that we are able to upgrade some of the competition's valves. And that is what I really mean, that whole ecosystem business system of being able to upgrade both our own and competitor valves has really helped us. And to give you a rough idea, I think Dan, last year our competitor upgrade valve business grew to £35 million.

Daniel Shook: Yes, so it added about, it was three percentage points on the growth for the overall business.

Roy Twite: In the Aftermarket, it was 6-7%. So that gives you a rough idea, Rory, of the sort of self-help now going on within that business.

Rory Smith: Yes, that is great. Thanks very much.

Roy Twite: Thanks Rory.

Alexander Virgo (Bank of America): Thanks very much. Morning Roy. Morning Dan. Sorry, I joined a little bit late so if this has been asked, feel free to tell me so. I wanted to dig a little bit into what you are seeing on the discrete side in Industrial Automation and in particular if you could talk a bit about the end market colour behind, you are down 5% or so in Q1. I appreciate that was in line with what you were expecting, but as you think about how things play out for the rest of the year and in particular what we are seeing around China and the implications of that pulling through for Europe, that would be super helpful. Thank you.

Roy Twite: Yes, thanks Alex. Yes, we did cover some of this. So you are absolutely right. You look at all the other discrete automation prints, I think we have done slightly better. So I am pleased with that. We are actually at minus 3%, Alex, first four months. So by the time we add in April, we are at minus 3%. So again, it was a better April. And as I said earlier, it is partly because of Easter, the number of working days, and in IMI, we also look at March and April together to stop all that sort of movement. So at minus 3% year to date. China is weaker. There is no doubt about it. Asia is weaker for us. I talked about the 60-day moving average earlier on the call and said it was slightly down. Asia is down, and that is being dragged down by China. So we are seeing a similar thing.

And as you say, Alex, that does not just affect China. A lot of our German OEMs and other European OEMs will be exporting into China, and they are feeling it in their order books as well.

So yes, I think at the moment it is slightly down, overall Industrial Automation, and we still think it is going to be a tough year. You saw the American PMI print, was it last week, Alex, and again, it is not exactly filled with confidence at this point. So I think we are perfectly happy with our forecast, which is we think that this year is going to be a resilient year for us, but no great growth. We are not forecasting any great growth in our outlook.

Alexander Virgo: That is great. Thanks Roy.

Roy Twite: Thanks Alex. Well, thanks ever so much for joining the call. It is another period of good progress for IMI, and we certainly look forward to catching up with you at the half year results. Thanks everyone.

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