

Business Review

After 10 years as Chief Executive, Peter Page left the Board on 28 February 2018. In his final Business Review, written just before he stepped down, he reflects on 2017.



Our priorities at the start of 2017 included sales growth to regain market share and cost reduction in operations. We made strong progress on both objectives, with 8% growth in sales volumes of edible collagen casings and a £7 million reduction in the manufacturing cost base, supporting a significant reduction in net debt.

Markets overview

Devro supplies collagen casings, gel and film to customers in over 100 countries worldwide. Demand for collagen casings is estimated to have increased 7% in 2017, with growth in most markets, including China.

The global food manufacturing sector is dynamic with growing demand for specific casing functionality in traditional sausage applications as well as in emerging categories such as protein snacks and confectionery.

Strategy

Devro's three-part strategy involves revenue growth, manufacturing efficiency and product differentiation. In the last quarter of 2016 the Devro 100 programme was launched to accelerate progress in all three elements of the strategy.

Revenue growth

Devro's sales volumes of edible collagen casings, which represent over 80% of the group's sales, increased 8% worldwide, contributing to a reported revenue increase of 7%, reflecting a mix of markets, products, pricing initiatives and exchange rate variances. Of the total price/mix impact (-4%), approximately half is due to mix, primarily related to the significant increase in volumes in China. Our pricing actions continue to reflect the dynamics of the specific markets in which we operate.

US volumes increased 3% as the protein snack stick segment continued to grow at a faster rate than total food consumption. A 5% reduction in average pricing reflects investment in securing valuable long-term relationships with leading brand owners with significant growth potential.

Latin America volumes declined 25%, with final quarter sales recovering to a level comparable to prior year. The year-on-year volume reduction follows the previously-announced changes in product sourcing in 2016, whilst the reduction in the overall average selling price reflects the resulting changes in country mix. Our technical and product development specialists continue to focus on opportunities to regain business in these markets.

Whilst the UK sausage market overall has shown little growth for several years, 2017 volumes of Devro casings increased 2%, along with a similar increase in average prices, reflecting a changing customer mix, particularly the continuing success of Select Fresh casings in the premium sausage market. Continental European sales recovered well, with 13% volume growth in the second half leading to 6% growth overall, accompanied by price movements related to specific market opportunities.

Volumes sold in Russia and surrounding countries grew 21%, recovering Devro's market share and presence following a period in which a number of specific factors, including currency devaluation and restrictions on EU-sourced pork products, had disrupted sales in the region. The movement in overall average selling price reflects changes in product mix.

Following the successful start-up of Devro's new plant in Nantong during the second half of 2016, and strong sales in the final quarter last year, further activity in China during 2017 led to a 69% volume increase at constant prices in most accounts. As the year progressed, a wider base of customers resulted in higher monthly sales volumes and the development of some specialist opportunities for Devro's differentiated products.

South East Asia sales volumes increased 29%, reflecting a higher level of activity in the region following an increase in capacity availability and product introductions.

Japan continued a 10 year period of sales growth, with volumes increasing 5% in 2017.

Australia and New Zealand are mature markets, with a high proportion of collagen casings principally supplied from Devro's plant in New South Wales. Volumes declined 3%, whilst a 5% reduction in average selling price reflected investments to secure long term global relationships, together with some changes in customer and product mix.

Total volumes of collagen gel sold across the group were marginally lower than prior year. Gel provides a low cost alternative for high volume users of cellulose and volumes grew in previous years as new capacity was added. 2017 was a year of consolidation in this sector.

Manufacturing efficiency

Manufacturing performance progressed well during the past year at most locations, with the new single global supply chain organisation structure enabling the business to improve performance through benchmarking, sharing of best practice, and specialist input to technical development opportunities.

2017 was the first full year of operation of the new plants in China and the US, leading to a greater consistency and standardisation of the process technology in use at all manufacturing locations.

The plant in Nantong performed particularly strongly in 2017, achieving high levels of efficiency and productivity across a range of products. This plant is close to achieving the output levels originally envisaged, with sales matching output in the latter part of the year.

Whilst there has been some good progress at the plant in South Carolina, output volumes in 2017 fell short of projections. As a result, productivity and output efficiencies in the US plant continue to be a matter of priority for the management team, as improvements in this area will support growth ambitions.

Devro 100

A key element of the Devro 100 programme has been to enhance Devro's sales capability through a programme of targeted training and individual development. The benefits of this are reflected in the volume and share gains throughout the year, with further advances expected in 2018.

As a result of the Devro 100 programme, the manufacturing cost base has been reduced by £7 million during the year, which is in addition to the cost savings realised in H1 related to the closure of the old US plant. Following the establishment in late 2016 of a single global supply chain and associated management structure, the group has benefitted from the implementation of new and more effective ways of working and procurement in all areas of activity.

During 2017 a single global team established robust processes for product development and bringing these new products to market. In the final quarter, following extensive commercial scale testing, Devro's Fine Ultra casings were introduced to key customers in Asia and Europe, providing the opportunity for volume growth in future years.

Safety

Over the past 10 years, safety has been a priority at Devro. There has been an improvement in overall performance compared to 2016. Whilst there is more to do to ensure we constantly achieve our safety goals, the move to a single supply chain with global responsibilities is leading to a more rigorous implementation of group standards to the benefit of all.

Devro today

Over the past 10 years, Devro has successfully moved from operating as a series of regional subsidiaries to an efficiently managed single global organisation. Revenue from edible collagen has almost doubled, due to a combination of pricing and volume growth in an increasing variety of markets and applications. Numerous excellent and dedicated colleagues have contributed to the development of the business in many ways, for which I am sincerely grateful.

Growth in demand will continue as the global population increases, consumer spending progresses and tastes become more varied. The business is well positioned for the future.

Peter Page