

# Chief Executive's Review



**Iain Menneer** Chief Executive Officer

## Introduction

Animalcare has again delivered record sales, up 6.3% to £12.9m, continuing its track record of top line growth.

This result has been achieved against a backdrop of a veterinary market that is very slowly responding to the strengthening economy.

Activities in the period can be split into the following three main areas: revenue delivery, product development pipeline and business infrastructure. I am very pleased with the progress we have made in all these areas.

Animalcare has changed significantly in the last decade and achieved much; as we move into the next stage of the journey the business must change further for it to achieve even more.

The veterinary market is evolving and consolidating; it is imperative therefore that Animalcare develops a new approach too, whilst not losing sight of its core strengths that set it apart from its competitors.

Our objective is to deliver further growth from the current core business and to accelerate that growth with the introduction of enhanced generic veterinary medicines. In response to the number of opportunities available, we have developed a more structured approach for managing and monitoring progress in our development pipeline.

## Market Review

Whilst surveys have shown consumers are generally feeling better off now than a year ago, this nascent confidence has been slow to flow through to veterinary practices. Results from a survey carried out annually show that 37% of UK veterinary practices believe that "things are still the same", with 35% saying things had improved and 29% that they had got worse. (CM Research July 2014)

In contrast, according to the latest available data, the pet medicines market reportedly grew by 10.7% for the year ending December 2013 (National Office of Animal Health [www.noah.co.uk](http://www.noah.co.uk)).

The veterinary industry has seen further consolidation during the period under review on two fronts: veterinary practices and pharmaceutical manufacturers and suppliers.

Listed and private equity backed consolidators have continued to swell their estates with double digit percentage acquisition growth. These key accounts offer an opportunity for Animalcare to negotiate significant revenues and buy-in from the centre; though of course this comes at a cost. Buying groups have also grown during the period, however as this model matures this growth has been mainly in member numbers and inter-group switching rather than number of buying groups. The crowded space has prompted an increasing number of buying groups to seek to differentiate themselves through premium service offerings which gives Animalcare an opportunity to engage more.

There has been a 9% growth in the number of independent small animal practices in the UK over the last three years, with a 25% increase in the number of corporate and charity practices. The number of practices joining a buying group has grown by 74% over the same period (Veterinary Record, January 2014).

The European animal health (AH) sector has experienced unprecedented merger and acquisition activity during the past 12 months, most notably with the sale of Novartis AH to Elanco (Ely Lilly) for \$5.4bn. Within the UK, one competitor, Alstoe AH, was purchased by the French company Sogeval, only for the latter to be purchased itself by Ceva Santé Animale (Fr). There are unlikely to be many product acquisition possibilities from this activity but the industry consolidation and distraction does give Animalcare other opportunities in the marketplace as a result.

# Chief Executive's Review *continued*

## Business Review

### Licensed Veterinary Medicines

Our Licensed Veterinary Medicines product group grew by 9.5% to £7.9m and gross profit by 6.2% to £4.4m representing a strong result against the prior period and in line with the companion animal pharmaceutical market.

The proportion of total Group revenue from veterinary pharmaceuticals has grown again in the year, up almost 2%, to 61.2%. Sales of products from our development pipeline grew in the period and importantly the group of older, lower margin legacy medicines has experienced strong growth too.

The change in sales mix as a result of the strength of our lower gross margin older products has had a modest effect on the gross profit of the product group compared to the prior period. The consolidation in our customer base has also meant that margins are under some pressure from the increased buying power.

Our strategy of progress through new products has continued with three launches in the period.

The first, early in the period, was an extension to the range of Phenoleptil tablets, the epileptic treatment for dogs. The addition of 25mg and 100mg tablet strengths to the existing range launched previously and gives veterinary surgeons a range of options to fine tune the dosing of patients. As expected, Phenoleptil sales have been increasing slowly as patients must be transferred very carefully from other therapies.

**“In response to the number of opportunities available, we have developed a more structured approach for managing and monitoring progress in our development pipeline.”**

In January, Animalcare launched Thiafeline, a treatment for hyperthyroidism in cats, a chronic disease affecting an estimated 12% of the UK cat population. Thiafeline is the first generic to be launched in this therapy area in the UK. Sales are growing steadily and we believe there is good potential for the product as hyperthyroidism is under-diagnosed, which gives Animalcare the opportunity to penetrate the existing market and also grow the total market through education and technical support.

The third launch of the year was Marbocare tablets, the associated in-house development of Marbocare injection launched last period. Marbocare contains an antibiotic for the treatment of infections in dogs and cats. Restrictions on the use of antibiotics in production animals are having an impact on their use in companion animals too. Several other generic products were also launched in the year having an impact on the anticipated growth of Marbocare.

### Companion Animal Identification



#### Cat Health Check

Our Companion Animal Identification group sales and marketing strategy has started to deliver results with revenue growth of 7.8% to £2.4m, and gross profit up by 6.0% to £1.7m, an even more pleasing result against the backdrop of uncertainty over new legislation and the Dogs Trust free microchipping campaign through veterinary practices.

Microchip sales grew by 8.2% whilst our database of pet owners, Anibase, has now grown to 4.0 million. The revenues derived from services sold to these owners also grew in line with microchip sales revenues, at 7.1%.

In February 2013, the English Parliament announced that it would be compulsory for all dogs in England to be implanted with a microchip and have up-to-date owner contact details on a database from April 2016 onwards. This was soon followed by the Welsh Assembly announcing the same legislation would be introduced in March 2015 for dogs in Wales. It is already compulsory in Northern Ireland and the Scottish Parliament is reviewing the situation.

At the same time as the English Parliament's announcement the Dogs Trust announced it would fund a million free microchips in a year-long campaign leading up to April 2016.

As a result of this activity the microchip market has seen some price pressure in the short-term.

The lack of clarity and disruption in the market around both announcements has now settled and we better understand how both will be implemented, however uncertainty remains as to what extent owners and veterinary practices will engage in either the legislation or free microchipping campaign respectively.

## Animal Welfare Products

We further rationalised some of our lower margin, commoditised lines in the Animal Welfare Products group resulting in a fall in revenue of 3.6% to £2.6m but gross profit increasing by 0.5% to £1.1m. Approximately half of the revenue from this group is generated from our growing infusions accessories range which complements our intravenous fluids portfolio.

### Vitofyllin



## Operational Overview

As one of the three focus areas over the past twelve months, a lot of work has gone into building a strong foundation to underpin our investment phase over the next three to five years.

These infrastructure improvements outlined below have all been implemented in a planned and measured way, keeping control of our cost base whilst not restricting our growth.

## People

### Sales

Our sales team is a rare asset in the animal health sector and vital for our success. Our new Head of Sales, Samantha Williamson, joined us from a senior sales role in Novartis human health and has had an immediate impact on the shape and culture of the team. The UK sales team has been split into two geographic territories with stronger management support and coaching. In addition, Animalcare has embarked on a long-held plan and is introducing a telesales team. The breadth of products across all three product groups means we need to identify new channels to better address our market. The new structure has allowed our Head of Sales to invigorate our approach to key accounts, the corporate, charity and buying groups mentioned earlier. All three elements of our rejuvenated sales operations will take time to show full effect, however the early signs in all areas are promising.

## Chief Executive's Review continued

### Technical and Business Development

Karolyn Tapper, Director of Business Development, was appointed at the start of August 2013, allowing for a thorough hand over of projects and responsibilities from Stephen Wildridge, Animalcare's previous Director of Strategy and Business Development who left the Company in October 2013. Karolyn joined Animalcare from Catalent, the global pharmaceutical manufacturer, with a wealth of formulation, project management and development experience. At the same time, Torben Orskov was promoted to Director of Technical and Regulatory Affairs. Torben was a practising large and small animal veterinary surgeon for ten years before joining Animalcare in 2007. It became clear that the number of opportunities available to Animalcare meant more resource was required in our Technical and Business Development departments. In the second half of the period both departments were enlarged. These appointments have not only increased the capacity of both teams but this has in turn allowed both senior managers more time to drive our product development strategy.

Moreover, the addition of more veterinary qualified staff across technical, marketing and sales functions means our expertise and service to our customers will improve further still.

### General

Animalcare recognises the dedication and calibre of its employees. The growth in the business has opened up internal promotions and career progression opportunities; hard earned expertise being retained, complemented by the freshness of a 'new' career.

Underpinning our growing business, our suite of personnel systems and policies has been brought up-to-date to further reinforce commitment to our valued team.

### IT

We have carried out upgrades to our computing infrastructure during the period to both the core business and the microchip database, Anibase. Virtualised servers, which provide smooth and uninterrupted operation, have drastically reduced the risk of downtime.

In the second half of the period we started the roll out of a new sales Customer Relationship Management (CRM) software system. This is now implemented and beginning to add value to many areas of the business.

### Inventories

During the period Animalcare increased its inventory levels of certain key products. The increase applied particularly to two product lines, microchips and Buprecare. In the case of the former, this was in readiness for an anticipated surge in demand following the announcement of planned compulsory microchipping by the English Parliament and Welsh Assembly. Now that we understand more of the dynamics of this legislation and the activities of the Dogs Trust we will manage stock levels accordingly. Buprecare ampoules were reintroduced into the market in January 2013 and we have built stock of this key product line to ensure continuity of supply.

We will continue to balance having sufficient stocks to meet demand and contingency to protect us from unexpected eventualities in our supply chain, whilst at the same time, keeping our working capital at an acceptable level. The nature of a highly regulated industry with prescribed batch sizes, and prohibitively expensive regulatory costs to maintain a second supplier, means that this process has to be managed carefully.



Vetasept in use

## Future Developments



### Vet Examines Dog

Animalcare will be launching two new veterinary medicines in the second half of the new financial year on distribution from one of our key European partners. These complement existing products within the range very well. A third distribution product may be launched towards the end of the second half of the current financial year dependent on exact timing of regulatory packaging approvals.

Development of new non-pharmaceutical products and services is still commercially attractive where this can build on our core strengths and improve profitability; where this is not possible we will continue to review and potentially remove more products from our Animal Welfare Products range.

## Outlook

In the short-term there is still great potential in our existing product range and imminent launches to keep our momentum and grow further. Moreover, there is capacity for Animalcare to grow sales through building better relationships with the key account market.

The strength of our business will continue to generate the necessary cash to meet our development and dividend targets, particularly through our investment phase.

I am confident that we can keep our pipeline well stocked with new product candidates into the medium-term.

I have outlined above the dynamics in the European animal health space, leading to a more crowded medicines market and pressure on margins from veterinary channel consolidation. Our strategy to complement (un)differentiated generic medicine launches with enhanced generic product development will enable us to grow market share and protect margin.

Additions we have made to our team and improved structure to our development process will ensure we are on course to meet our objectives.

### Iain Menneer

Chief Executive Officer