

# Chief Executive's review

## Powerful operating model and consistent execution deliver record performance



Steve Foots, Group Chief Executive

“We are building a strong innovation pipeline, supplemented by new technologies and organic investment.”

### Sales

**£2,089.3m**

(2021: £1,889.6m)

Croda achieved another milestone in 2022, exceeding £2 billion of sales and £500 million of adjusted operating profit for the first time. This continues our record of consistent execution. We successfully recovered significant input cost inflation, and navigated challenging economic conditions and continued supply chain disruption. We are building a strong innovation pipeline, supplemented by new technologies and organic investment. Our performance demonstrates the power of our business model, the benefit of our global footprint, greater resilience following recent portfolio change and the increasing importance of our products in a range of niche markets.

We delivered an 11% increase in both sales and adjusted profit before tax, with good sales and profit growth in both core sectors. Consumer Care delivered a solid performance, with sales up 18% and adjusted operating profit 9% higher, albeit with margin diluted by lower volume and change in product mix. Growth remained robust in the second half year across Asia, Europe and Latin America, partly offset by customer destocking that was particularly apparent in North America. Life Sciences built on an exceptional 2021, delivering 19% sales growth and 10% higher adjusted operating profit, despite a reduction in COVID-19 vaccine demand by our principal customers. The balance of the Pharma business, together with Crop Protection and Seed Enhancement, each delivered double digit percentage sales growth.

Adjusted operating profit was also higher in Industrial Specialties, benefitting from strong trading ahead of the divestment of the majority of its Performance Technologies and Industrial Chemicals (PTIC) business midway through the year. Through this divestment, and the acquisitions in recent years, Croda has significantly repositioned to be more closely aligned with the powerful megatrends that are reshaping our markets. We are becoming a pure play company, focused on high value niches in consumer care and life science markets. This is creating a stronger margin, higher return, less cyclical and lower carbon intensive business. We are also more knowledge intensive, with exciting customer and technology innovation pipelines, particularly in sustainable solutions and drug delivery systems. This will translate into more consistent top line growth and increased margins, delivering superior returns in the years ahead.

### Managing a challenging environment

Group sales grew by 11% to £2,089.3m (2021: £1,889.6m). Constant currency sales rose by 5%, driven by our ability to recover input cost inflation, with price/mix up by 24%. The chemical industry experienced a significant impact from inflation and average prices within our raw material basket rose by 23% in 2022, adding to a 17% increase in 2021. Commodity markets remained tight during the year but prices peaked in the third quarter, with signs of modest declines as the year ended. Operating cost inflation increased during 2022, with labour and energy most impacted. The strength of Croda's business model helped manage this challenging environment, ensuring inflation recovery and profit protection.

Group sales volume declined by 20%, with an estimated 13 percentage points of the reduction due to the divestment of much of the industrials business. In addition, after strong consumer demand and customer restocking post-pandemic in 2021, volume declined by 12% in Consumer Care, reflecting capacity constraints and customer reduction of excess inventory levels. Volume in Life Sciences was 8% higher, driven by strong Crop Protection demand, supported by the robust agricultural commodity pricing environment. Across the Group, the challenge of global supply chain constraints began to ease towards the end of the year.

Adjusted operating profit grew by 10% to £515.1m (2021: £468.6m). Over half of this increase was driven by underlying growth across all three sectors, with the balance primarily from favourable currency translation. Return on sales was broadly flat at 24.7% (2021: 24.8%), with an improved margin mix from the reduced share of industrial sales and a lower variable remuneration charge offset by normalisation of the Life Sciences margin, after an exceptional 2021, and a lower Consumer Care margin diluted by lower

volume and weaker mix. Profit before tax (on an IFRS basis) increased to £780.0m (2021: £411.5m), which included a gain on the business disposal of £356.0m. Adjusting for this benefit and one-off exceptional items outlined in the Finance Review, adjusted profit before tax increased by 11% to a record £496.1m (2021: £445.2m).

Inflation and supply chain challenges saw increased working capital during 2021 and the first half of 2022. As expected, this began to moderate in the second half of 2022. Free cash flow increased to £167.4m (2021: £153.6m). Net debt reduced to £295.2m (2021: £823.2m) and debt leverage reduced to 0.5x (2021: 1.4x), due principally to the proceeds from the PTIC divestment.

### Reinvesting in the business

The Group successfully completed the divestment of the majority of its PTIC business to Cargill Inc. on 30 June 2022 for gross proceeds of €775m (£665m). The divestment agreement also included a €140m option to sell Croda Sipo in China in which we have a 65% stake; however, this was subject to reaching agreement with our partner to also sell its stake, which now appears unlikely to occur in the near-term.

The divestment has released more capital to invest into a rich seam of growth opportunities in the consumer care and life sciences markets, whilst maintaining our discipline of careful capital allocation to projects which generate superior returns on capital. Our priority is organic capital expenditure, supplemented by targeted acquisitions, in line with our preferred approach to 'buy and build', as exemplified by our recent investments in Life Sciences, where we have secured new technology platforms through modest acquisition spends, then built scale through organic investment.

Our investment in organic capital expenditure was £138.5m (2021: £158.5m). This investment included a new Fragrances and Flavours (F&F) operation in Brazil, expansion in protein technology in Consumer Care and new laboratory capabilities in Life Sciences, together with additional capacity in our Singapore plant and initial work on a new greenfield manufacturing site in India which will together meet fast growing demand in Asia. In addition to our typical capital investment of around 6% of sales, which includes delivering our carbon reduction roadmaps as part of our sustainability commitment, we are investing an extra £175m over the period 2021 to 2024 to broaden our Pharma footprint and capabilities, particularly for nucleic acid drugs. We are investing in our existing GMP sites in Denmark, the UK and Avanti (US), and creating a new Pharma facility in Pennsylvania (US) to meet forecast market demand, with over £90m invested to date under this programme and spend expected to accelerate in 2023. Alongside this investment, the US and UK governments

are co-investing up to an additional £75m, recognising the importance of new generation delivery systems to global pandemic preparedness and drug discovery. This investment will support our innovation pipeline of sales from new product development in the Pharma business.

We expect to supplement our organic plan with selective acquisitions to add adjacent and complementary technologies, particularly those which can accelerate our transition to greater use of natural raw materials or build new technology platforms, enhancing future growth. Shortly after year end, we announced an agreement to acquire Solus Biotech, a leading producer of premium, biotechnology-derived beauty actives based in South Korea. Solus consolidates our position as a global leader in sustainable actives, builds our biotech knowledge base, adds a North Asian manufacturing and innovation facility, and brings rich IP and proprietary know-how that we can leverage globally. Our continued capital deployment will be executed within our consistent capital allocation policy, set out in the Finance Review. Alongside organic and inorganic investment, the policy provides for a regular and increasing ordinary dividend to shareholders, while operating an appropriate balance sheet. As part of this, the Board has recommended an increased full year declared dividend of 8% per share to 108.0p (2021: 100.0p).

### Strong performance in Asia, Western Europe and Latin America

On a geographic basis, all regions saw continuing good growth in sales and profit, other than North America. Asia achieved a record year with strong demand, particularly in Life Sciences, and modest growth in China, despite pandemic lockdowns. Demand in Western Europe remained robust, despite higher prices and energy costs, with strong growth in Crop Protection and Beauty Care. Latin America enjoyed good growth, led by demand in the regional Crop Protection market and supported by Consumer Care demand, including the new F&F operation. EEMEA (Eastern Europe, Middle East and Africa) saw a negative financial impact from the closure of our Russia business (which represented approximately 1% of Group sales in 2021).

In North America, sales peaked in the first quarter before softening in Consumer Care and Pharma, the latter partly reflecting lower COVID-19 demand post-pandemic. Consumer Care was negatively impacted by significant customer destocking, with US customers particularly impacted by lower exports to China following lockdowns.

### Adjusted operating profit

**£515.1m**

(2021: £468.6m)

### IFRS operating profit

**£444.7m**

(2021: £438.2m)

We use a number of Alternative Performance Measures (APMs) to assist in presenting information in this Report in an easily analysable and comparable form. We use such measures consistently at the half year and full year, and reconcile them as appropriate. Whilst the Board believes the APMs used provide a meaningful basis upon which to analyse the Group's financial performance and position, which is helpful to the reader, it notes that APMs have certain limitations, including the exclusion of significant recurring items, and may not be directly comparable with similarly titled measures presented by other companies. APMs are defined in the Finance Review on page 47.

# Chief Executive's review continued

## Consumer Care sales growth

# 18%

## Life Sciences sales growth

# 19%

## Continued growth across sectors

### Consumer Care performance demonstrating increased resilience

Consumer Care achieved record sales and adjusted operating profit in 2022. Sales grew by 18% to £897.8m (2021: £763.0m), with price/mix up 22% as significant inflation was successfully recovered. Adjusted operating profit increased by 9% to £204.7m (2021: £188.5m), resulting in return on sales reducing to 22.8% (2021: 24.7%). This primarily reflected the operating gearing effect of lower volume, alongside a weaker product mix as Beauty Care and F&F grew faster than the higher margin Beauty Actives business. IFRS operating profit declined to £144.5m (2021: £168.0m), which included an impairment charge of £34.6m on goodwill in the Flavours business, where the future value of this business is behind the acquisition case.

After a stand-out performance in Consumer Care in the first half of 2022, growth slowed in the second half year. Full year volume was 12% lower than 2021, driven by two components. Firstly, destocking developed across our customers and the retail supply chain. This followed strong demand in 2021 to meet the post-pandemic recovery, when customers, worried about global supply chain delays and meeting this recovery, restocked significantly; Personal Care sales grew by 20% in the second half of 2021. Slowing consumer sales led to destocking by customers in the second half of 2022, particularly in North America. Secondly, volume was lower due to selective demarketing of lower margin products due to capacity constraints in some Croda sites, together with the closure of our Russia office. It is estimated that customer destocking has accounted for five percentage points of the volume decline, with five points from demarketing and the balance from Russia and other impacts.

Our sector strategy is to Strengthen to Grow and delivery is progressing well, positioning Consumer Care as a more resilient growth platform. Our ingredient transparency programme is supporting a structural shift in behaviour by customers and consumers towards sustainable ingredients, providing product information dossiers and carbon footprint data that includes upstream supply chain emissions. The sector delivered an increase in bio-based ingredients to 56% (2021: 50%), greater use of biotech across the product portfolio and nearly 290,000 tonnes of avoided carbon emissions in 2022. Greater innovation is also being delivered as part of an enhanced formulation capability, with our new Formulation Academies minimising the customer's time to market and giving smaller customers greater access to formulations containing Croda's high

performance ingredients. Consumer demand is growing strongly in Asia and, to deliver fast growth in the China domestic market, we have acquired a new site for a fragrance and botanicals facility.

Encouragingly, sales growth was strongest in Beauty Care and F&F. Beauty Care benefitted from strong pricing, good demand from multinational customers and the move to sustainable ingredients. With strong growth in solar protection for daily wear, Croda's mineral sunscreens had a record year and sales of ECO bio-based surfactants to Personal Care customers increased threefold. In 2020 we added fragrances to Croda's portfolio and 2022 saw the creation of a full formulation service for customers. Sales in fragrances recovered well, after a challenging 2021, with growth in emerging markets, benefits from the integration of 2021's Parfex fine fragrance acquisition and a developing pipeline of sales synergies between Croda and Iberchem. Flavours suffered its worst year for raw materials, with 32% price inflation and shortage of supply, and margin was squeezed as the business did not fully recover input cost inflation. A quieter year for Beauty Actives sales nevertheless saw development into adjacent technologies continue, with the launch of encapsulated retinol and a growing pipeline of biotech-derived actives. The smaller Home Care business continued its roll out of high value proteins for fabric care, extending the life of clothes, with new contracts underpinning future growth.

### Life Sciences building on exceptional prior year

Following an outstanding year for Life Sciences in 2021, with the rapid expansion of Croda Pharma following the Avanti acquisition and exceptional demand for COVID-19 vaccines, 2022 saw further strong progress, driven by an excellent performance in Crop Protection and an extensive pipeline of non-COVID delivery systems in Pharma.

Sales grew by 19% to £682.3m (2021: £572.3m) with performance strengthening in the second half of the year. Price/mix grew by 6%, while volume was 8% higher. Adjusted operating profit increased by 10% to £229.4m (2021: £208.5m), as did IFRS operating profit to £220.3m (2021: £201.0m). With Crop Protection a larger proportion of the sales mix and a normalising lipid systems margin, return on sales reduced to 33.6% (2021: 36.4%).

Our strategy to Expand to Grow in Life Sciences sees us empowering biologics delivery in Croda Pharma and reinforcing our existing leadership in sustainable delivery systems for Crop Care. In 2022, this saw the Health Care business repositioned as Croda Pharma, focused on technologies with the fastest growth and innovation needs. The relaunch was accompanied by a new brand, organisational structure and governance for its exciting customer and innovation pipelines. We are investing in innovation, knowledge and capacity, and secured co-investment from national governments. Crop Protection is meeting growing demand for sustainable crop care solutions and emerging delivery systems for crop biologics that are enabling customers to transition to biopesticides.

Encouragingly, 2022's performance was achieved despite the anticipated near 40% decline in sales of lipid systems due to lower demand from our principal COVID-19 vaccine customers. The balance of the Pharma business, Crop Protection and Seed Enhancement all grew sales by double digit percentages. Crop Protection was the standout business, benefitting from a strong agricultural commodity pricing and demand environment. Its strength in sustainability was reflected in Croda's recognition by Syngenta in its 'Reduction in Carbon' supplier award. Seed Enhancement's range of coatings free from microplastics has now been proven in field trials with customers in all major regions and commercial roll out has commenced.

In Pharma, Protein/Small Molecule Delivery grew strongly, providing delivery systems for both the more mature small molecule drugs and the higher growth protein and monoclonal antibody (mAb) applications, with over a thousand customer projects underway. Adjuvant Systems experienced lower demand in COVID-19 applications, offset by growth in its current generation adjuvants, now supplied to over 100 customers, while supporting hundreds of projects to develop new prophylactic vaccines and novel therapeutic vaccines that fight already contracted diseases. These included a respiratory syncytial virus (RSV) vaccine in phase III trials and a personalised cancer vaccine in clinical phase II development.

The Nucleic Acid Delivery systems business is the world's leading innovator of lipid and other components in this new field of drug treatment. The business is developing its portfolio from the blockbuster COVID-19 vaccines, which drove 2021 demand, to new mRNA and gene therapy vaccines, and therapeutic drugs. 2022 sales in this business were approximately US\$170m (2021: \$230m), a little ahead of expectations, mainly due to additional COVID-19 vaccine demand; sales outside the principal COVID-19 vaccine customers already

represent almost 40% of this business and are expected to be the majority of the \$120m sales forecast for 2023, as COVID-19 sales continue to decline. We are supplying delivery systems to customers for close to 100 nucleic acid drugs currently in development, including the world's first human trial of a gene therapy application.

### Industrial Specialties established

With the divesting of the majority of Croda's PTIC business on 30 June 2022, the remaining industrials business, including the Sipo joint venture in China, has become the Industrial Specialties sector. It plays an important role in our manufacturing model, supporting the Consumer Care and Life Sciences sectors on shared sites and operating a medium-term supply contract to the new owner of the divested business. 2022 therefore comprised the full business in the first half year and the retained business in the second half year. Reported sales were £509.2m (2021: £554.3m) and adjusted operating profit was £81.0m (2021: £71.6m). It is estimated that, had the divestment occurred at the start of 2022, sales would have been £191m lower and adjusted operating profit £39m lower in 2022. Reported IFRS profit was £79.9m (2021: £69.2m). After a strong first half year pre-divestment, Industrial Specialties continued to perform well, benefitting from higher commodity prices, with second half sales of £167m and a return on sales of 12.3%.



Our Pharma business is developing delivery systems for biologic drugs which will enable the next generation of vaccines and therapeutics. Recognising the importance of our delivery systems for a wide range of nucleic acid applications, the US Government is supporting a capital expenditure programme, co-investing up to \$75m to establish a lipid facility as part of a new multi-purpose cGMP site in Pennsylvania.



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# Chief Executive's review continued

## 71%

of our people are motivated by our Purpose

### Delivering our strategy

We combine leadership in sustainability with market-leading innovation to deliver consistent top and bottom-line growth, with profit growing ahead of sales, ahead of volume in the medium-term. This is enabling us to help to meet global challenges and capture new opportunities.

### Delivering our sustainability Commitment

Sustainability trends are developing rapidly in our markets as consumers look to make a positive contribution to living more sustainably through the products that they buy. In addition, climate change poses a major risk to the planet which we must all address. We enable customers to realise their sustainability ambitions through the application of our innovation, creating sustainable alternatives that current supply chains cannot offer. We are reinforcing our sustainability leadership by reducing the adverse impact of our operations, by replacing fossil-based ingredients with bio-based materials, reducing emissions, promoting biodiversity and ensuring our sourcing activities make a positive contribution to communities in our supply chains. Our sustainability strategy is built on 23 UN SDG targets grouped around the themes of climate, nature and society, supporting our commitment to be Climate, Land and People Positive by 2030.

To be Climate Positive, our verified carbon reduction target will ensure we contribute to limiting the global temperature rise to no more than 1.5°C above pre-industrial levels, providing customers with an average 35% reduction in carbon emissions associated with our products by 2030, compared to our 2018 baseline. To achieve this Science Based Target (SBT), we have developed externally validated decarbonisation roadmaps for every Croda location and adopted an internal carbon price to ensure investment decisions align with our sustainability ambitions. We have also continued our focus on upstream supply chains, with almost a quarter of suppliers by volume committed to SBTi carbon reduction targets.

Building on our Land Positive commitment, we announced our aspiration to be Net Nature Positive by 2030 and are working to understand our impacts and dependencies on biodiversity. We also joined the World Business Council for Sustainable Development and its Nature programmes, with the aim of being an early adopter of the future Science Based Targets for Nature, when published.

Our People Positive objective addresses the needs of both our communities and our employees. Living our Purpose, Smart science to improve lives™, we have met our target to protect 60 million people from the damaging effects of the sun, seven years ahead of

schedule. Additionally, the Croda Foundation distributed £1 million of funding to 13 projects and another £2 million of grants for health infrastructure projects in South Asia, Africa and Brazil, in total benefitting 15 million people. Our employee engagement surveys show that 71% of our people are motivated by our Purpose and 69% feel involved in delivering our sustainability ambitions. With a target to achieve gender balance in Croda leadership roles by 2030, 2022 saw women occupy 38% of these roles (2021: 36%). Reflecting our absolute commitment to be a safe company for our communities and our employees, we set a stronger safety target to reduce our Total Recordable Incident Rate (TRIR) to 0.3 by 2025, requiring us to more than halve our current rate of 0.74 (2021: 0.76 restated), excluding COVID-19 cases. We conducted a safety culture survey at more than 40 sites, enabling us to identify areas for particular focus.

We have reflected the impact of the PTIC divestment in our sustainability targets. Scope 1 and 2 emissions reduced by 26% as a result of the sale and we have re-baselined our target to maintain the original challenge. The proportion of bio-based organic raw materials reduced to 59% due to the disposal (2021: 69%) but we have retained our original target to achieve 75% by 2030. We have also retained our carbon cover target (where use of our products avoids four times the carbon emissions associated with operating our business) which becomes more stretching as a result of the divestment.

### Driving innovation

Innovation is at the heart of what we do, creating new market and technology niches. We have stepped up our rate of innovation through more resource investment, more external partnerships and a focus on 'big bet' projects. This will support higher growth, improved mix and better margin as we become a more knowledge-intensive company, capturing more intellectual property (IP).

The foundation of our innovation model is internal R&D investment, applying the expertise of our scientists at our global innovation centres to meet customer needs. This is complemented by our open innovation network, which provides access to over 500 universities and SMEs to help develop new intellectual property. We also invest externally in disruptive technologies, the benefits of which can be seen in recent product launches that have leveraged expertise in both biotech and encapsulation to reduce impacts and improve efficacy.

Our 'big bet' projects are reinforcing our leadership in formulation science and harnessing the potential of biotech, alongside our conventional chemical

technologies. In formulation science, we are developing a greater understanding of the impact of our ingredients on wellbeing and self-esteem through neuroscience research, and are sharing our expertise with customers through our new Formulation Academies. We are scaling biotech, with projects to develop more sustainable actives and bio-based fragrance ingredients. R&D here is led by our five biotech laboratories, mostly established through technology acquisitions over the last decade. Candidate technologies are then scaled up at application laboratories in Paris and two UK facilities, before being taken to market by existing business units. Beauty Actives is launching novel anti-ageing and anti-dandruff ingredients developed in this way.

We seek to drive New & Protected Product (NPP) sales growth at least as fast as total sales over the cycle, targeted at mid to high single digit percentage growth. This allows the business to grow through IP-rich NPP and technology acquisitions, while leveraging our rich heritage product portfolio by finding new applications and data for existing products. In 2022, NPP sales grew at 2.6% in constant currency, adjusting for the impact of the PTIC divestment, despite lower lipid systems sales in the year.

### Sector strategies to deliver consistent growth and even stronger margins

Within our strategy to drive sustainability and innovation to deliver profitable growth, each of our seven businesses within the two focus sectors targets superior sales growth, at least one and a half times global GDP, margins of at least 20% and return on invested capital (ROIC) of at least twice our cost of capital over the medium-term.

Our vision for Consumer Care is to be the most sustainable, innovative and responsive solution provider globally through our Strengthen to Grow strategy. Consumer Care targets annual organic sales growth of at least 5%, supplemented by synergies from integrating the recent F&F acquisitions, with a return on sales at or above 25%, over the medium-term.

Our vision for Life Sciences is to empower biologics delivery, enabling our customers to transition to biologic actives which are transforming pharmaceutical and crop science markets. Our Expand to Grow strategy is reinforcing our leadership in sustainable delivery systems in Crop Care and positioning Croda Pharma in drug and vaccine markets which need complex, innovative delivery systems. Life Sciences targets high single digit percentage annual sales growth, with a return on sales over 30% over the medium-term.

Supporting our strategic themes of 'Strengthen to Grow Consumer Care', 'Expand to Grow Life Sciences' and 'Scaling Biotech', as set out above, are three additional strategic initiatives:

**'Fast Grow Asia'**, where we are expanding our technical capabilities and building new manufacturing capacity, to serve rising regional consumption of Consumer Care products and growing opportunities in Pharma and Crop Care. Investment in innovation and sales resource helped deliver a record year for Asia. We are continuing to expand our manufacturing capability in Asia, including commencing construction of a new greenfield site in India, to support the exciting opportunities ahead;

**'Proactive Acquisitions'**, where our global scouting network is identifying potential adjacent technology opportunities in Consumer Care and Life Sciences, such as the Solus Biotech acquisition announced in February 2023; and

**'Doing the Basics Brilliantly'**, which is improving our customer and employee experience through a combination of digital technology, customer insights, new data architectures, enhanced manufacturing capability and employer branding. 2022 saw good results in our customer 'Net Promoter Score' (NPS) and a new customer self-serve ordering online portal developed for global roll-out.

### Outlook

Though early in the year, the Group is trading in line with expectations. We expect the customer destocking that has been particularly apparent in North America to come to an end in the first half year, supporting continued sales growth this year in Consumer Care. In Life Sciences, we expect good sales growth in Crop Care and the non-COVID related Pharma business to offset the previously indicated decline in COVID-19 vaccine demand. Group performance in 2023 will be more second half weighted than in the prior year, reflecting the divestment of the majority of PTIC in June 2022 and the phasing of lipid systems shipments to our principal COVID-19 vaccine customers.

The combination of our differentiated business model, enhanced investment programme and exciting innovation pipelines in sustainable ingredients and drug delivery, will continue to deliver consistent, superior returns.



**Steve Foots**, Group Chief Executive

# 69%

of employees feel involved in delivering our sustainability strategy

The Strategic Report was approved by the Board on 27<sup>th</sup> February 2023 and signed on its behalf by Steve Foots.