Grifols

Q3 2022 Business Update
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Speakers

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Introduction

Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Good day everyone, and welcome to Grifols' business update conference call. We are very pleased to host this call today and thank you for joining.

As we have already explained, we want to increase our engagement with the capital markets and with investors, this is a testament to our commitment to enhance our communication.

The call will last one hour. There will be a presentation of something like 30 minutes, and then we will follow with a Q&A session to complete the hour, or if you have no questions we'll finish earlier.

Today, I am joined by Steve Mayer, our newly appointed Executive Chairman; Raimon Grifols and Victor Grifols, our Co-CEOs; and Alfredo Arroyo, our CFO. The materials of this call are already available on the Investor Relations section of grifols.com.

Then our forward-looking statement disclaimer for this business update. We undertake no obligation to update or revise any of the statements and this is a forward-looking statement that refers to the substantial risk and uncertainties.

With that, I will turn the call over to Steve. Thank you.

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Opening Remarks

Steven F. Mayer, Executive Chairman
Thank you, Nuria and thank you everyone for joining the call today. Since I am new to the Grifols Executive Chairman role, I would like to begin the call by emphasising a few high-level points before we turn to the specifics of our business update.

Many of my friends and acquaintances have asked me why I elected to take on this role at Grifols at this point in my life. The answer is actually pretty simple. Grifols is a great company, with a clear mission and a long history of improving the health and well-being of people around the world. It also has very strong fundamentals in place, irreplaceable assets supporting a long-term strategy and the challenges it has recently faced can and will be overcome.

I have read a few reports that have questioned whether, in light of the fact that I've been on the Grifols Board for several years, there will be any real changes in the offing. In response to that question, on the one hand I can refer you to my long private equity career that was focused on being a change agent and helping companies we owned realise their potential.

On the other hand, I also fully recognise that words are not what matter; our execution and our performance will ultimately tell the true story. I ask that you judge us on our strategic, operational, and financial performance over the coming months, which is how we will be judging ourselves.

If you check out my personal background, you will also know that I am highly competitive and driven to win, with a lot of experience in team sports. While I am now ultimately responsible for delivering, at the same time you should know that this is one team, and we will align as a single unified team behind our goals.

In that regard, we are, as a team, laser focused on our top priorities. First of all, creating an organisation with a performance culture that will be efficient, effective, data-driven, agile, and decisive.

We are already implementing a renewed emphasis on planning and execution. Again, if you look at the investments I led at Cerberus, you will see that in most of them, improved operational performance was at the heart of their success. That improved performance comes from a disciplined approach to planning, project management, and rigorous execution against the plan.

I also believe strongly in the principle of accountability. Everyone in the organisation will be accountable, using measurable indicators, starting with me.

We will also be much leaner and more cost-effective, and while this will improve our margins, just as importantly it will enable us to move faster and serve patients better.

Our next priority is to meaningfully improve our cash flow and expense profile. We have been making, and expect to continue to make, progress on the cost of plasma. Of course there is a six to nine month lag before cost reductions are recognised in our income statement as a result of a long inventory cycle, which as you know is characteristic of our industry.

We are also focused on reducing fixed and semi-fixed cost throughout the organisation from delayering, better spans of control, organisational streamlining, facilities rationalisation and capacity optimisation, outsourcing certain non-core functions, and better use of technology and data.

We are also making further effort to reduce working capital and capex cash use. And, very importantly, we are implementing a zero-based budget process for 2023.

A third and very important priority is debt reduction. Right now, we are evaluating a variety of levers and, although we have nothing to announce today, it is clear that the company has highly valuable assets throughout the world, and therefore, we have a range of attractive deleveraging alternatives under consideration.

We do however believe that the company's stock is meaningfully undervalued today so issuance of equity in today's trading range is not a favoured option

We firmly believe that by year-end 2023, and very possibly before concerns about leverage will be substantially mitigated.

A fourth priority is capturing commercial opportunities with certain of our existing products that we believe are underpenetrated currently. For example, our subcutaneous IG product, which commands a higher price than IVIG, represents only a single-digit percentage of our IG sales, compared to 40% for CSL.

In addition, we continue to see opportunities for our high margin Alpha-1 product, Prolastin, through ongoing efforts in patient identification. We will be mentioning a recent favourable development in that regard later in this call.

Our final top priority to mention today is the effort to unlock the full value of Biotest. We and Biotest are dedicating resources to accelerate integration and the recognition of both cost and revenue synergies.

As you know, we also believe that the approval, commercialisation, and successful launch of the new Biotest proteins are likely to have a substantial impact on Grifols' financial profile.

Of course, any initiative that's dependent on regulatory approval and successful commercialisation and market launch inherently involves uncertainty, but we continue to believe that Fibrinogen and IgM are a matter of when, not if, and that ultimately, they will be very significant and high margin contributors to profitability.

In addition to these five key priorities, we plan to continue improving transparency and enhancing our communications with the capital markets and with investors. Today's call is evidence of this. We also expect to schedule meetings with individual investors once we have progress to report on the priorities I've just walked through. I look forward to meeting many of you in person before too long.

Before turning the call over to Raimon and Victor, I do want to state that it is highly important to me to ensure that we will deliver on all of our goals while remaining true to Grifols' core values and sustainability. Raimon and Victor?

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Key Highlights

Victor Grifols Deu, Co-CEO
Thank you, Steve, and thank you all for being on the call here today with us.

I would like to start by highlighting the two recent leadership appointments, that come out of the recently announced reorganisation. We have appointed Pia D'Urbano to lead Biopharma business unit and Jordi Balsells to lead our Plasma Procurement business unit.

Pia brings with her 29 years of experience in healthcare, particularly biopharmaceuticals, including high responsibility roles in top management in multinational companies like Sanofi and Novo Nordisk in the U.S.

Her experience spans global product launches, new product planning, establishing new businesses, heading marketing and sales, business development activities, strategic planning and alliance development. She is an impressive executive and her broad experience with market launches of new products is expected to be especially helpful as we look forward to launching the Biotest new proteins for example.

We have also named Jordi Balsells for Plasma Procurement business unit. Jordi held various roles during his professional life, with a special focus on retail distribution channels worldwide and global expansion. His experience also includes building local teams in subsidiaries, developing relationships with strategic partners, deploying omnichannel and high-tech projects. All this knowledge and experience in retail businesses will for sure reshape and evolve the way that Grifols has historically approached the management of Plasma Procurement operations. I'm sure that this will move us to a more efficient and efficacious sourcing network.

We are looking forward to working with them.

Now changing gears to the Q3 '22 highlights and the financial performance.

Let me start with revenues and really, I am proud to say that Grifols delivered very strong operational performance in the third quarter leading to a solid Q3 year to date '22 number; while operating all that in a very complex macroeconomic environment.

Compared to Q3 '21, global revenues on a combined basis were up 23% operationally, reaching €1.5bn revenues. On a reported basis, this growth represented a 37% increase due to the foreign exchange tailwind. Underlying excellent operational performance has been the driver, with revenues growing up to 10.7%.

Of these underlying drivers for the quarter it's thanks to higher plasma collections in the first half of this year, 2022, driving volumes of key proteins, especially immunoglobulins, together with pricing upticks, product mix and the Biotest contribution.

Year to date, revenues totalled €4,351m, increasing by 9.5% at constant currency and 18.8% on a reported basis, compared to the same period in 2021. With a standalone operational performance of plus 3.8%.

Regarding Plasma Procurement, following the latest updates, plasma collection volumes grew by 25% in the first 42 weeks of 2022 versus the same period of 2021, which we anticipate will underpin strong sales growth in the second half of the year and onwards. We aim to continue to build on this momentum in the coming future.

Additionally, the lifting of restrictions for Mexican donors in mid-September has also started to contribute notably to further increases in plasma donations, and we expect it to continue to do so.

In terms of EBITDA, volumes, pricing, operational leverage and cost discipline partially offset cost per litre and inflationary pressures to drive reported EBITDA to €927m, representing a 21.3% margin on sales. Excluding Biotest, it stood at 22.2% of sales.

Adjusted EBITDA was €899m, with an adjusted EBITDA margin of 20.7%. Excluding Biotest, it stood at 20.7%.

Paramount in the industry is the balance between volume of plasma and its costs. As plasma collection volumes normalised, we are now focused on driving cost per litre reduction by driving lower donor compensation, and optimisation of labour and the rest of the fixed costs that are impacting the cost per litre.

Donor fee is one of the key components of the cost per litre, accounting for roughly 35% of the fully loaded cost, and therefore the one that has greater impact in the short term. Since its peak in July this year, donor fee declined by more than 15%. Comparing September versus January, it declined by a total of 7%. At the same time since volumes are sequentially increasing, the fixed cost portion of the cost per litre benefits from operating leverage.

We firmly believe that this trend will be sustained, and we are confident on a further reduction from now to year-end that will positively contribute to profitability going forward.

We will continue assessing the trade-off between plasma collections and donor fee and balancing these two components to enhance our performance.

Moreover, as restrictions for Mexican donors were lifted, there is a significant upside to further increase plasma collections, which will certainly determine our decisions on donor fee evolution.

Regarding deleveraging the reported leverage ratio declined from 9.0x in the first half of 2022 to 8.6x in this last 12 months, September 2022. And it is expected to stand below 8x by year end, specifically at 7.9x.

As we are focused on driving donor fee reduction, cost optimisation and operational efficiencies, this is expected to trigger more EBITDA and working capital improvements throughout 2023, leading to a further reduction of the leverage ratio.

After two years of a highlight complex pandemic environment that has severely impacted the plasma industry and now followed by its consequences in the midst of this challenging macroeconomic backdrop, we see it from three different angles. On the one side, inflation and the current challenging context are further driving plasma collections momentum, which can potentially contribute to further cost per litre reduction.

On the other side, macroeconomic backdrop is impacting our labour costs to some extent, especially those in our plasma centres.

And third, our exposure to interest rate hikes so far is limited, as close to 65% of our total debt is tied to a fixed interest rate.

And finalise this highlight section I will move to the innovation pipeline. Certainly, we continue to advance on our most advanced programmes on our innovation pipeline, such as Fibrinogen, IgM, albumin in cirrhosis and ATIII in sepsis, among others.

But in this quarter please, let us highlight that we received FDA clearance for Alpha ID At Home product, the first free service for US adults to screen for their genetic risk of alpha1-antitrypsin deficiency that doesn't need a prescription from a healthcare professional.

And now let me please transition to Alfredo who will give us further details on the financial performance.

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Financial Update

Alfredo Arroyo, CFO
Thanks Victor, hello to everybody, thanks for joining this call. Now let's review our P&L starting with revenues.

Grifols delivered a very strong operational performance during the third quarter. Compared to the third quarter of 2021, global revenues were up by 23% at constant currency, reaching €1.5bn and a 37% growth on a reported basis.

Robust revenue growth was driven mainly by Biopharma's key proteins following increased plasma supply; positive product mix; positive pricing and very positive FX tailwind; as well as a significant contribution from Biotest at five months, circa €200m.

Gross margin was impacted by a high cost per litre from the plasma collected in the first half of the year due to mainly high donor compensation and labour costs impacted by inflationary pressures.

Additionally, it is noteworthy to mention the negative impact from the high-margin Diagnostic business triggered by the end of the one-off COVID testing and mandatory Zika screening, which largely impacted gross margin by 180 basis points versus Q3 '21 and 250 basis points versus Q3 year to date September '21.

At the EBITDA level we were able to offset the impacts at gross margin level and deliver a sequential EBITDA gradual expansion, which was supported by operational leverage, cost savings and R&D prioritisation. Inflationary pressures were partially offset at opex level as well.

Net income totals €188m profit, which reflects higher financial expenses linked with Biotest acquisition bond, and higher interest rate.

Now moving to the slide 9, the individual performance. A main division Biopharma revenues reached €1.3bn, or €1.2bn excluding Biotest, during the third quarter of 2022, growing by 34% at constant currency and close to 50% on a reported basis thanks to a positive FX impact.

As mentioned, several drivers were behind this strong performance, including robust immunoglobulins underlying demand, larger plasma supply, price increases and product mix. Especially significant were sales of subcutaneous immunoglobulin, thanks to higher demand and a favourable customer mix.

Year to date, Biopharma sales stood at close to €3.6bn or €3.4bn excluding Biotest, this represents a year over year increase of 16% at constant currency and up 26.3% on a reported basis.

Excluding Biotest, Biopharma's revenue grew by 8.7% at constant currency and 19% on a reported basis in the first nine months of 2022 compared to the same period in 2021.

The sales performance reflects sequential accelerated growth of 21.3% at constant currency in the third quarter, compared to 0.1% growth at constant currency in the second quarter and 7.1% growth at constant currency in the first quarter.

The Diagnostic revenues declined by 20.8% at constant currency to €170m in Q3 '22 primarily due to non-recurring sales of our COVID test and the termination of mandatory Zika virus testing, which was partially offset by robust sales of blood typing solutions.

Diagnostic recorded circa €500m in revenues during the first nine months of 2022, down 21% at constant currency compared to the same period of the previous year. Excluding the one off

COVID testing and the Zika-virus screening, the decline was just 3.5% mainly due to country mix and pricing.

Bio Supplies reported significant revenue growth in the third quarter, expanding close to 30% at constant currency reaching €44m, following the acquisition of Access Biologicals. The business unit grew by 5.4% at constant currency during the first nine months of 2022.

Moving to the next slide, to the margins. Gross margin stood at 38.2% representing a slight sequential decline from the 38.9% reported in the first half of 2022. It reflected a high cost per litre incurred in the first half of the year, as a consequence of donor compensation and labour cost inflation.

Grifols continued to expand and enhance its operations despite inflationary pressures. The company's efforts to optimise costs and operational efficiency resulted in a stable cost per litre in the first half of the year, despite the 8 to 10% annual inflation in our regions of operation.

On the back of solid plasma-collection levels, Grifols is focused on balancing volume and cost per litre to drive margin expansion, with an emphasis on reducing donor compensation, and also optimisation of labour and fixed costs. The donor fee, as mentioned that accounts for roughly 35% of the full-loaded cost, it fell by 7% from January to September, and by more than 15% from its peak in July '22.

Additionally, as mentioned, it is important to highlight the impact of Diagnostic into gross margin due to the COVID and once again the Zika screening that impacted by 250 basis points the first nine months of 2022 compared – versus the previous year.

EBITDA grew to €927m in the first nine months of the year at a 22.2% margin, and 21.3% including Biotest. This represents an EBITDA growth versus the previous year of 12.8%.

As I already mentioned, Grifols continues to apply cost discipline through its savings plan and the prioritisation of R&D projects, which partially offset inflationary pressures, as well as higher Biotest expenses, particularly related to the Biotest Next Level project. This accounts for the five-month period where - since the time we acquired Biotest of €35m.

Adjusted EBITDA for the third quarter of the year has proved to be in line with that of the first half of the year, reaching close to €900m with an adjusted EBITDA margin of 20.7%. Here you know the adjustments are basically related to one-off restructuring costs, as well one-off external gains. Excluding Biotest, it stood at similar levels of the standalone company.

Moving to the EBITDA sequential improvement as shown in the slide, in the second half of 2021 the EBITDA was low, especially in the last quarter of 2022, basically since – due to low sales because of lower plasma product, as well as certain restructuring and write offs that took place

in the last quarter of last year. Since then, we have been addressing both the main impacts from COVID, which were lower plasma collections, and a higher cost per litre of plasma.

As mentioned, the impact from the Diagnostic Division has also been significant. We were able to improve EBITDA throughout 2022 through cost control and R&D prioritisation, bringing a contribution of €70m savings in terms of opex.

Also the positive contribution of Access following its integration that includes a one-off capital gain. This bridge also reflects what I've been mentioning so far, mirroring the sequential improvement.

In the next slide as already explained, plasma collections increased by 25% year to date, versus the previous year and to a larger extent in the US, expanding by 28%.

Now that plasma volumes increase normalised, we are focusing on cost per litre reduction, driving donor compensation decrease and optimisation of labour and fixed costs.

There is an ambitious plan to keep reducing cost per litre with the aim to re-base this cost per litre. Donor compensation reduction will continue going forward. In addition, optimisation of labour and fixed costs, including some plasma centres relocation, consolidation and also closing those less efficient. This will support further reductions in terms of cost per litre.

Having said that, we will continue assessing the trade-off between plasma collections and donor fee and balancing these two components to enhance our performance going forward.

On deleverage, yes, we are laser focused on leverage. And basically the main levers of the organic deleverage are in this order. First, EBITDA improvement, working on margin, plasma cost as well as opex as already mentioned. Optimising working capital, this year we have to build up inventories, whilst last year the inventories were exhausted as a result of the lower plasma collections, but for the next year the inventory increase will be limited, in line with I would say normal times.

Also, limited capex – no meaningful acquisitions, disciplined in capital allocation and since we are well invested this business requires no significant capital moving forward. This is as mentioned by Steve in the opening remarks, this is a top priority. In Q3 we were able to reduce the 9x – that was the peak of the year, down to 8.6%, by the year end it is expected to further decline and will be around 7.9 times.

We will continue to evaluate, also as already mentioned our global wide base of valuable assets for optimisation. Important to mention that Grifols has a strong liquidity position at the end of the quarter, a total of €1.6bn included the cash position of circa €500m. While there are no significant activities until 2025. Victor.

Business Update

Victor Grifols Deu, Co-CEO
Thank you, Alfredo. Now we will enter into more detail about the performance of the business units.

In Biopharma we are optimistic that we are seeing improved momentum evidenced by a strong third quarter across key proteins, especially IG, our flagship, which grew by 12% in Q3 year to date 2022.

As global plasma supply increases, we are anticipating a strong growth with opportunities on core indications of primary such immune deficiencies and CIDP.

Demand has and it is expected to remain robust. Many patients, even in top markets, remain under diagnosed. Furthermore, even though incidences of the diseases are similar across geographies, consumption rates can vary very significantly from one geography to another. Actually, as you see in the US for instance it is still consumed at almost three times the rate per head of population when compared to Europe.

Noteworthy to mention how new products continue increasing its contribution, driven by our plan to boost our subcutaneous franchise, Xembify's to continue the revenues performance going forwards.

In Albumin, as we have already mentioned phasing in the second quarter of the year, sales were flat versus the first nine months of 2021, with lower volumes in China partially offset by low-single-digit price increases. Looking forward, we anticipate volume demand in China to continue to grow at mid-to-high single digits.

Alpha-1 and Specialty proteins delivered a high-single digit growth. Alpha-1 recorded mid-single-digit increase due to favourable customer mix and competitor supply shortage.

Additionally, we delivered robust growth of our latest launches such ..... new formulation hypers and fibrin sealant due to its sustained higher demand, while other more regular products are performing well. All in all offsetting the Factor VIII tender pressures that we are seeing.

Moving to Diagnostic, Diagnostic performance has been impacted due to non-recurring sales of the NAT technology to detect COVID-19 and the termination of mandatory Zika-virus testing, which was partially offset by robust sales of blood typing solutions. Excluding these two items, the business unit declined by 3.5% at constant currency in Q3 year to date 2022.

As already mentioned, these two items impacted consolidated gross margins by 250 basis points in Q3 year to date 2022. These, together with some country mix and pricing, were partially offset by growth in the Chinese market and higher donation volumes, resulting in 35% growth in China year to date 2022.

Blood Typing solutions division recorded a robust growth of 20% supported by solid performance across EMEA and the US region, and stronger GelCard sales in Eastern Europe; as well as growth in China and the rest of Asia Pacific due to increase in donations and sales of GelCards as well as instruments.

Recombinant proteins declined primarily resulting from the joint business collaboration on a new R&D project.

Bio Supplies reported significant revenue growth in the third quarter lead by Bio Supplies Diagnostic supported by plasma for diagnostic, cell media and serum, as well as with the acquisition of Access Biologicals.

Bio Supplies Biopharma declined due to lower sales of NTU albumin and Fraction V, which were partially offset by cell culture media revenue resulting from the acquisition again of Access Biologicals.

And now I give the floor to Steve with his closing remarks. Thank you.

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Closing Remarks

Steven F. Mayer, Executive Chairman
Thank you, Victor. I'd like to conclude by reiterating a few points that we've already made, but that I think bear repeating. And to be clear, my management style is to keep returning to the most important priorities in the business, both those that make us strong, and those that need changing, in order to ensure that our organisational and business priorities are absolutely clear and are driven to and then beyond the finish line.

The Grifols Board of Directors asked me to join the company as Executive Chairman in order to enhance operational execution, financial discipline, business performance, and shareholder value. We are going to do so initially by prioritising operating efficiency and cost reduction throughout the organisation, especially, but not only, in the cost per litre of plasma; by the improvement of cash flow; and by debt reduction.

These initiatives are underway. Standing back from them, though, I am absolutely certain that the fundamentals of our business and our strategy are strong, and that we are well-positioned to capitalise on our highly valuable assets and platform for years to come.

I will be working closely with the entire management team to help Grifols focus on its key priorities and achieve its goals. We are creating a culture of performance and accountability, and to be crystal clear, I will be accountable for delivering. Period.

Recapping what you've heard about our recent business results, plasma collections have grown by 25% over the previous year, which in turn is underpinning strong sales growth in the second half of 2022 and onwards. The market remains strong, and we aim to continue this momentum into the future.

We are laser focused on driving cost per litre down further. Donor compensation per litre has declined by more than 15% since its peak in July 2022 and our objective is to realise further cost per litre decreases through a combination of continued donor fee management, operating leverage as higher volumes absorb fixed costs, and meaningful reductions in fixed and semi-fixed costs per litre such as labour and occupancy costs. A normal characteristic of our industry, these lower costs will in general be recognised in our operating results six to nine months after they are realised.

We are also on track to meet our financial commitments for the full year 2022. We expect global revenues to finish the year in the €5.8bn to €6bn range, including Biotest for about seven months of the year.

Adjusted EBITDA margin for the full year is expected to remain in the 20 to 21% range. For the reasons we have discussed, and with additional operating leverage, we anticipate margin expansion for 2023.

Our leverage ratio is expected to decline to about 7.9x by year end, a significant drop from the 9x reported just six months ago. Also keep in mind that this leverage ratio does not include any pro forma results relating to the Biotest transaction. As you know, we had forecast about €60m of synergies between Biotest and Grifols; none of these synergies are included in the forecast ratio I just cited. And none of the deleveraging alternatives we are considering are included in that ratio either.

As mentioned, the entire executive team is focused, and I mean focused, on accelerating the execution of the company's operating plan; on operational excellence; on cash flow improvement and debt reduction, and, ultimately, on increasing value for all shareholders.

We look forward to communicating with you more frequently and transparently, including through quarterly earnings reports and calls. Thank you.

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Questions and Answers

Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Thank you, Steven and thank you all for your time. So now let's start, we will be pleased to take questions from the sell-side analysts that follow our company, that follow Grifols. Please press *5 to raise your hand, we will be progressively taking your calls.

Just one thing, be conscious also of your colleagues' time in order to have time for everybody to ask questions.

Let's start with Vineet Agrawal from Citi. Please, Vineet.

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Vineet Agrawal, Citi
Hi, can you hear me?

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Yes.

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Vineet Agrawal, Citi
Great. Thanks. Vineet on behalf of Peter. Two questions. So, first of all, on '23, can you give some preliminary thoughts around '23 and if the trends you're seeing persist can you give us a sense of the scope of margin recovery you hope to see? Could it be 22% to 25% or better?

And, second, how motivated are you to accelerate your deleveraging activities? Could we assume all options are being considered, including collapsing the dual share class structure, monetising your Shanghai RAAS stake and are doing something with Diagnostics? Thank you.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
I think your second question, it was a bit difficult to hear you because maybe you went too close to the microphone, but I think your question was on the Fibrinogen and the timing associated to that. Is that correct?

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Vineet Agrawal, Citi

No, I was just asking if you can, you know, give some preliminary thoughts around the 2023 margin progression. Could we hope to see, you know, 22% to 25% margin?

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Sorry, Vineet. What was your second question?

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Steven F Mayer, Executive Chairman
I think the questions involved margin progression during 2023, which maybe, Alfredo, you can respond to, and the second question half of the question had to do with deleveraging alternatives, which he mentioned a couple which I can respond to.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Okay, thank you, Steve.

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Alfredo Arroyo, CFO
Thanks, Steve. To your first question, the margin progression, my comment is the following, the worst is already behind, so, by focusing on the lower cost per litre, as I already mentioned, we see, you know, a significant decline moving forward, but remember that it will take time to flow to the P&L, based on our long inventory cycle. So that means that we will see meaningful gross margin improvement coming from a lower cost per litre more in the second half of next year, so backloaded.

On the additional opex savings, yes, we will capture those at the beginning of the year, so that will help to improve our gross margin. But also, if I move back to the P&L, by increasing the share of subcu which we'll expect that will be meaningful next year, this will help us to improve the gross margin. Remember that there is a significant price gap between the regular IG and the subcu IG, so this I what I heard, you know, quite a bit about the gross margin also starting next year. So, that's what I'm going to tell you now based on the gross margin as well as EBITDA margins. So, the worst is already behind.

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Steven F Mayer, Executive Chairman
With respect to the deleveraging alternatives, we're going to wait until we have something to announce before we give any details, but I'll just broadly state that Grifols has an extremely

valuable, I would say irreplaceable group of assets globally. We believe that there are opportunities to capitalise on these to reduce the leverage while continuing the overall long-term strategy that Grifols has.

With respect to specifically I think you asked about the consolidation of the two classes of shares, we've already said that we think that the equity is meaningfully undervalued today – that applies to both classes of shares – so, we're not looking to a capital increase or equity issuance in today's trading range, and that also applies to the consolidation of the two classes of shares. As the stock price recovers to what we believe to be a better reflection of the value of Grifols, that, you know, will be one of the alternatives we consider.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Okay, thank you, Steve, and now let's move to James Gordon, JP Morgan. James, please.

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James Gordon, JP Morgan
Hello. Thanks for taking the questions. One question was about the medium-term target. Whilst you're in conjunction with the Biotest deal – can you hear me?

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Victor Grifols Deu, Co-CEO
We can't hear you.

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James Gordon, JP Morgan
Last year, there were targets set in conjunction with the Biotest acquisition for revenues, EBITDA and leverage - more than €7bn revenues, EBITDA, €2.8bn, and leverage below 3.5x. I believe those targets were pushed down to 2025 at the CMD, so should we still think that those targets could be achieved in 2025 or are those targets under review, might it take longer to get to those targets? So, a review on where we are, the revenue, EBITDA and leverage targets in the medium term.

And the other question was just in terms of pipeline, so there were some previous plans in terms of investing in various pipeline projects, things like Alzheimer's disease, etc, are all those plans still going on or might you change some of the pipeline priorities as well, is the second question?

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Alfredo Arroyo, CFO
So, the first question of deleverage, yes, by 2025, either and or it will be a combination of organic and non-organic. Clearly, you know, our target is to be below 4x. Also remember that we need to go to the market, to the debt markets to refinance a portion of our debt, so clearly it's a must to be at a very good, I would say, leverage ratio at that time. So, it will be combination of both.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Thank you. And, James, can you, please, repeat the second one?

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James Gordon, JP Morgan
Sure, and sorry if I've got a bad line. The second question was are all of the previous pipeline plans, pipeline investment plans, still definitely going ahead or is Grifols also reviewing them? Could there be changes in terms of investment plans in pipeline?

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Sorry if I couldn't understand it, but I think you're asking about the pipeline?

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James Gordon, JP Morgan
That's correct.

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Victor Grifols Deu, Co-CEO
Okay, as we said in our Capital Markets Day back in July, we continue to deliver a strong – in the progress that we are doing in the different projects that we are undergoing, very clear for Biotest products Fibrinogen and IgM. They continue basically on track.

Regarding the Albumin liver disease continues on track as well, second immunodeficiency for our IG products continues on track, and anti-inflammatory and sepsis continues on track. So, overall, everything continues as we said in our last Capital Markets Day.

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James Gordon, JP Morgan
Thank you.

Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Okay, thank you, Victor. Now, Sarita Kapila from Morgan Stanley. Please, Sarita.

Sarita Kapila, Morgan Stanley
Just to understand how we should think about increasing competition in the alpha-1 space, so particularly from Inhibrix following the FDA decision to grant accelerated approval and given that the data we've seen today is quite encouraging. Thank you.

Victor Grifols Deu, Co-CEO
Regarding alpha-1, this is a project that still needs time to arrive to the market, if it is the case. Regarding plasma products, as we have said today, for instance, we are continuously developing tools that can help our franchise to progress – in this case, it's the evolution of our Alpha ID test. Now, in this case, a home profile so that patients can self-test and get the results at home from this new tool. And we continue to develop as well some nice second management formulations for the better convenience of our patients. So, this is regarding Alpha-1, how we see the landscape.

Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Thank you, Victor, and now we Guilherme Sampaio from CaixaBank Equities. Guilherme.

Guilherme Sampaio, CaixaBank Equities
Yes, can you hear me?

Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
We can.

Guilherme Sampaio, CaixaBank Equities

Hello. Yes, okay, perfect. Okay, so one question regarding the process - the defined stake in the GIC environment, how we are on process and whether you are still counting on these for your leverage targets?

And then two small questions on the results, so if you could provide some details on Shanghai RAAS's performance this quarter, and if you could provide some colour on FX impact on quarter-on-quarter?

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Alfredo Arroyo, CFO
Okay, regarding your question of GIC, just to remind you that the aim of both the parties and the rationale has been always and is still that this is the financial instrument which is in equity. So, both parties, this is understanding of the parties at the time of the agreement.

As you know, afterwards, the auditors, KPMG, they havesome, I would say, inside talking, and finally they came up with applying the accounting rule that this is a debt. The agreement is not expected to be modified in the short term, however still the door is open, so this is really where we are. But remember, this is a 20-year, I would say, term, so now it's hard to get, I would say, a debt for 20 years, so, as you can imagine, this is real equity, or quasi equity, so, as I said, debt is not on the table for us.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Yeah, and then on the FX impact?

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Alfredo Arroyo, CFO
The FX impact, overall, yes, this year it's going to be close to €100m at the EBITDA level because there is a significant dollar devaluation, specifically versus Europe, and this is most of our revenues and most of our EBITDA is dollar-driven, we're expecting, and it's already bringing, by the end of September, €74m of positive FX. By the year end, expected to be, if the dollar trend remains the same, around €100m. So, very positive this year and for the next year, if it continues at the similar level, we see also a positive impact, less than this year, but positive indeed.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Thank you, Alfredo. Emily Field from Barclays. Hello, Emily.

Emily Field, Barclays
Hi. Thank you so much for taking my questions. Just a couple. Just on the divestitures point, is there anything that is off the table because, obviously, you know, between Diagnostics and Shanghai RAAS, I know that was kind of asked earlier, but there is some complexity, so I was just, you know, kind of, was wondering is, sort of, anything on the table, you know, if a satisfactory price can be obtained?

And the secondly, you mentioned in the prepared remarks a couple of times about fixed and semi-fixed costs. I believe the company commented a few years ago about the split between fixed and variable costs and how that could be managed in the event of emerging competition. Could you just give us an update on how you see that split between fixed and variable costs and, you know, how much cost you would be able to shift in the event of emerging competition? Thank you.

Alfredo Arroyo, CFO
So, to the proportion of fixed and variable cost, I think a significant component is the labour cost that, you know, overall, accounts for near 50%-45% of our that total cost, and some of the cost, those costs are, I would say, yes, variable because you need certain people to run manufacturing plants, you need certain people to run operations, and some in the back office. But clearly, there is room for improvement.

And then, and the team, up to now and moving forward, is when we keep working on ripping off some of those savings. There are some low-hanging fruit there. And both at the plasma cost sites as well as the rest of the costs across the whole organisation. So, clearly, you know, there are some upsides, not only at the Grifols side but also, as mentioned by Steve, at Biotest level, there are some synergies that can be captured.

Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Yeah, and maybe on the first part of Emily's question, Steve, maybe you can take this one?

Steven F Mayer, Executive Chairman
Well, I think the critical point with respect to what you describe as divestitures, which I'm not sure I would employ that term, but, you know, we think we have this portfolio of irreplaceable assets. We also have a long-term strategy, and obviously, as with any company, we're going to

try to optimise that portfolio of assets in order to achieve both the financial objective of deleveraging but also the long-term strategic goal of driving shareholder value in the long term.

And so, when you ask if you there are sacred cows are if there is any off the table, value aside, what's going to be off the table is something that we think would have a material negative impact on long-term strategic and shareholder value. But we do believe that there are many different ways of achieving our strategic objectives consistent with evaluating these and deleveraging alternatives.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Okay, thank you, Steve. We have next in the line, Tom Jones from Berenberg. Hi, Tom.

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Tom Jones, Berenberg
Hello. Afternoon, everyone. I have two questions, one for Alfredo and one for Steven if that's all right.

Alfredo, just a quick housekeeping one, I was a bit surprised on the drop through in Q3 between EBITDA and net income. Was it just a step up in interest rates that caused that or were there any significant large one-off items that affected Q3? I know the tax rate can bounce around occasionally you get a relatively large FX charge in there as well, so was there anything, kind of, a bit more one-off in nature that meant that the EBITDA number didn't quite drop through to the bottom line?

And then my second question for Steven, it's really a big picture one really, you've obviously been on the Board quite a long time and followed this company in the industry for even longer than that, what would you say, in your words, is it that in Grifols that excites you, that you think we, as investors, miss? You know, investors do love to hate Grifols a bit and, you know, what is it that the market is missing do you think?

And then many be a, sort of, corollary to that is, if you could just click your fingers today and change one thing about Grifols, what would that be?

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Steven F Mayer, Executive Chairman
Well, first, not to be contrary, but we don't take the view that the market's missing anything because we respect all of our shareholders because we think they're owners of the business and the market is probably smarter than any of us individually. So, we're not bemoaning the fact that the market has not rewarded Grifols over the last year or two.

So, our goal is to drive performance and then to make sure that we're transparent and communicative with the market, and we give to the market even more of that performance.

So, if I stood back and look at the biggest picture at Grifols, I think it's a great industry which, over time, has proved to have a lot of resiliency and growth characteristics, and globally, I think that that growth will continue with a high degree of operating leverage and I think the return to the margin structure that prevailed prior to the pandemic.

Clearly, at Grifols, there has been maybe not as much a focus on execution and performance, operational execution and performance as we might have had. I'm not pointing a finger to the past but that's what we're going to be laser-focused on. So, we do have a long-term strategy, but we also have a short to medium-term strategy, and that short to medium strategy is going to be very, very execution-focused.

So, if I could snap my fingers, I would advance two or three years and we would have a highly accountable, highly incented, highly performance-driven organisation that was just really, really focused on execution and on delivering, but I think we need to re-instil that in the organisation a bit. But when you look at the big picture and you look at the platform and the portfolio of assets that Grifols has and the long-term strategy, I'm extremely optimistic, that's why I stepped into this role.

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Alfredo Arroyo, CFO
Tom, to your first question, the drop in the EBITDA margin mainly is driven by lower Biopharma margin associated to higher plasma cost - remember that the time lag between the plasma cost increase and the time that flows through the P&L. So, now in the second half of the of the year, so including Q3 and Q4, we're going to see Biopharma EBITDA margin decline due to the higher plasma cost.

To the net income amount, the drop is due to additional financial expense, which is associated to the interest rate hikes despite the fact that we have 35% only floating debt, we had an impact no doubt, and that impact will, once the interest rate is announced, it takes around two or three months to hit our P&L because we have the quarterly interest rates revisit. So that's why now we see in Q3 and also in Q4, we will see a higher financial expense. So, that explains why the net profit for Q3 is lower.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability

Okay, thank you, Alfredo. Now, we have three more questions, so if you want to stay with us, we'll take these three to complete and to give the possibility to everybody. So, we have Rosie Turner from Jefferies. Rosie, hello.

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Rosie Turner, Jefferies
Hi. Good afternoon. Thank you very much for taking my questions. Three left from me, please. Just thinking about your plasma collection volumes, up 25%, I noticed that's 42 weeks of the year. So, does that include Mexico and the border reopening and, kind of, are you able to approximate, kind of, how much of that is Mexico versus US itself?

Then following up on Alpha-1 competition, can we just recap the level of penetration, I think, is it 70% of patients currently going underdiagnosed?

And then finally, just on that competition theme, just checking we're still not seeing any impact from the anti FcRn competition in myasthenia gravis. Am I correct there? Thank you.

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Victor Grifols Deu, Co-CEO
Okay, I'll take the question on Alpha-1. If I just heard correctly, is the level of diagnosis of the disease, what we think is the rate today, 90% of the potential patients are being underdiagnosed, and we hope with this enhanced tool with the diagnostic of Alpha-1 ID at home test we can improve the level of diagnosis. I think this was the question regarding alpha-1.

And the other one is FcRn competition in myasthenia. Well, for Grifols, myasthenia accounts, only 3% of our revenues today. We are not highly worried about that as we don't depend much on that. We will see the progress of these new products and we will compete with our franchise, but it's not a big threat for Grifols in this indication.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Thank you. And the Mexican...?

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Victor Grifols Deu, Co-CEO
Well, the Mexican border, since September, now we can operate regularly our border centres. We are seeing an accelerated return of these donors to our network and we are seeing a real awake move, progression on the level of volume being collected at those centres and, as you know, in pre-pandemic levels, those centres were roughly collecting around one million litres and

now we are in this ramp up and we are seeing the trend up. As some point, we will hit this level of one million litres for those centres.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Okay, thank you. And Julien Dormois, from BNP. Hi, Julien, I hope you are still with us.

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Julien Dormois, BNP Paribas Exane
I'm still with you, and thanks for squeezing me in, I appreciate it, and I'm sorry I have three questions, one for Steve, one for Victor and one for Alfredo if that's okay.

But one for Steve is that you made it clear during the call that one of your focuses is to return to pre-COVID margin levels, or close to that, but do you plan to plan to provide margin targets for the period 2023 to 2025 because over time there's been some misunderstanding between Grifols and the investment community and some disappointments on profitability, so do you plan to provide clear targets for us to build our models?

For Victor, please, on the penetration for Xembify, could you help us understand what you will do different going forward to move the penetration on this highly profitable product because it's been on the market for three years, so what can you do differently going forward in order to boost the penetration?

And the last question for Alfredo is a housekeeping on net financial costs and following up on Tom's question, I think you had €200m in net financial costs in the first half of this year. Is €400m as a net financial cost for full year 2023 a good run rate or could it be higher than this?

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Steven F Mayer, Executive Chairman
Well, let me just start by addressing the first point which had to do with whether we're going to provide guidance in terms of EBITDA margins. Look, we're obviously in a somewhat turbulent environment, macroeconomically, on top of other the factors that will impact those margins such as synergies with Biotest, such as to continue to drive down cost per litre of plasma and when those costs will be realised through the income statement due to the capitalisation into inventory initially, and the long inventory cycle. Some of the other cost reductions what we're planning, when exactly the new Biotest proteins will be approved and commercialised, even factors like inflation globally.

So, I think, for us to try to provide long-term EBITDA margin guidance would not be prudent right now. I think we'll revisit the question, at least for 2023, in the coming few weeks or months, but,

at the moment, I don't think we'll be giving any kind of precise guidance beyond 2023 and even for 2023, and we would ask you to be a little bit patient because there are a lot of factors that are impacted in it.

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Victor Grifols Deu, Co-CEO
Okay. Thank you, Steve. On the question regarding the Xembify franchise, as you know, unfortunately, the launch of this new product coincided exactly with the pandemic period, so, during the first year of its launch has been very challenging not be able to present at hospitals and meet our customers.

Having said that, it's progressing nicely, the penetration of our product. The main characteristic that probably gives us a competitive advantage is the tolerability of the product for our patients. This is very well-received by doctors and patients, of course. And we are progressing nicely. The weight of our subcutaneous sales over the total IG has continued to grow. Now, we are in the range of 3%, and we are targeting to move that to a 5% proportion of the IG sales.

And the mid future, we are developing the secondary indication for that franchise that will further improve the prospects of this nice product.

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Alfredo Arroyo, CFO
And then regarding the financial expense, I'm talking about the interest because within the financial expense, there are the deferred financial cost, there are FX but let's purely focus on the interest expenses associated to our debt. Our quarterly run rate for this year is around €75m, and expected to grow, as I mentioned, because of the impact in our accounts will be backloaded because the timing of the interest rate hikes, so expected that the quarterly interest expense run rate will be around €100m.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Okay, thank you. And, we have Alvaro Lenze from Alantra. Alvaro?

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Alvaro Lenze, Alantra Equities
Hi. Thanks for hosting this call. I think that having this increased communication from the leadership is very welcome. Three quick questions. The first one is you have announced several management changes over the last couple of months, whether you are now happy with the team as it is right now, or we should expect any additional appointments?

The second question is on cost-cutting, whether you could quantify how much cost-cutting you have identified and how much would you need to invest to achieve this cost-cutting, or if you are still working on these calculations, and, if you are still working, whether you will provide some specific guidance on cost-cutting once you have the plans ready?

And the last question, more philosophically on leverage, you have, historically targeted 4x next debt to EBITDA as your long-term goal, whether this could be - I know that there's still a long way to go to bring leverage down to 4x, but whether you could change this as a long-term target? Thanks.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Okay, Victor?

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Victor Grifols Deu, Co-CEO
Thank you, Alvaro, for your questions. I will probably take the first part of your question and then Alfredo can complement.

During the pandemic, and we have been announcing that and communicating that, we have launched several, kind of, wide range of improvements of the operations with the company. We have closed business units that were not profitable or were not core anymore for us. In the case of Hemostasia business line, in blood bags in the Diagnostic division as well, and certain Hospital division assets now no longer in the hospital division is being reported isolated.

We have closed facilities, we have gone to the fit for growth process across the Board. So, many, many things to improve the operations of the company.

The same for R&D, we have prioritised or stopped and cancelled some R&D projects as well. And subsequent to that, a final move as announced at the last Capital Markets Day was the reorganisation of the company, now, fully, fully accountable business units, and we needed specific presidents to run those business units. Now we have Pia on board and Jordi on board and, with that, we see that all this kind of reorganisation has been completed with those two appointments. And now the organisation is fully at speed with all the structure and all the talent in place to develop further operational improvements and to drive forward with what we've talking during this hour about improving the business overall.

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Alfredo Arroyo, CFO

Okay, to your couple of questions, first cost-cutting, here I will, you know, address Steve's initial comments. Well, basically, we're going to be focused on plasma cost, which is, you know, our main driver, it's where most of the costs are, I would say, in the company, during the company. So, these are various initiatives of driving down the plasma cost , point number one.

Point number two, the opex, basically, lower fixed cost, you know, as well, you know, higher efficiency, delayering and, you know, many, I would say, initiatives now ongoing.

Let me not provide you with some more colour because now Steve just joined and this is one of our top priorities which is in our table, so we are working on this and we will be provide you more colour later on.

Regarding the leverage, as I already mentioned, we will use, you know, whatever it takes, both organic and non-organic levers, to be at the target, I would say, financial discipline level which is 4x but we know, especially, as I said, ahead of the 2025 debt, you know, partial debt refinancing.

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Nuria Pascual, VP, Corporate Treasury & IR & Sustainability
Okay, and now, with that, we come to an end. Thank you, everybody for joining. As always, in the Investor Relations and Sustainability Team, will be happy to take any additional questions or any concerns or anywhere that we can help, and speak to you all soon. Thank you.

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