NESTLÉ S.A.

2019 HALF-YEAR RESULTS INVESTOR CALL TRANSCRIPT

26th July, 2019, 14:00 CEST

Speakers:

Mark Schneider, Chief Executive Officer, Nestlé S.A.
François-Xavier Roger, Chief Financial Officer, Nestlé S.A.
Luca Borlini, Head of Investor Relations, Nestlé S.A.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

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Good afternoon and good morning to everyone. Welcome to the Nestlé Half Year 2019 Investor Call. I'm Luca Borlini, Head of Nestlé Investor Relations.

Today, I'm joined by our Chief Executive Officer, Mark Schneider; and our Chief Financial Officer, François Roger. We will begin, as usual, the call with some prepared remarks by Mark. François will then follow with a review of the half year financial figures. We will then open the lines for your questions.

Slide: Disclaimer

Before we begin, please take note of our disclaimer. Now I hand over to Mark.

Mark Schneider, Nestlé S.A. Chief Executive Officer:

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Thank you, Luca, and a warm welcome to our conference call participants today. As always, we appreciate your interest in our company.

Slide: Key Messages

I think it is fair to say that we're looking back on a successful second quarter and first half. I would like to thank team Nestlé, our more than 300,000 associates around the world, for their hard work, sense of urgency and dedication to make this happen.

Many of our initiatives are getting traction, and it clearly shows in our top and bottom lines. Most of all, the balanced pursuit of organic growth on the one hand and operating efficiency on the other is clearly paying off. As we stated in the past, when you see good progress on these two key metrics, wonderful things happen to underlying net income and earnings per share. This is the story of H1 2019.

Our first half results fully support our midterm 2020 targets. They are consistent with the expected 2019 commodity cycle we outlined in February and will allow us some further investments in marketing to strengthen our brands and support innovations.

At the same time, I would like to ensure that your 2019 expectations do not overshoot. The strong year-end in 2018 and the shape of the 2019 commodity cycle create a steeper hill for us in the second half when it comes to organic growth and our margin.

Next, I would like to comment on *Starbucks*. As you know, we have completed the first wave of our launch this spring and have almost a full quarter of data. Our products are now out on the store shelves in fourteen countries with four additional countries following this summer. The second wave, which will involve close to twenty countries, will follow between October and March. In addition, we plan to roll out further SKUs in early 2020.

Earlier this week, we also announced the launch of *Starbucks* coffee creamers in the United States. This will be our fourth product platform and another key opportunity to bring that unique *Starbucks* experience right to the homes of our consumers. In all modesty, the *Starbucks* opportunity is big, really big. We're seeing massive interest in particular in the *Nespresso* and *Nescafé Dolce Gusto* capsule formats. I also have to congratulate our teams on the beautiful in-store shelf presentations, which capture consumer attention and are very consistent with *Starbucks*' premium positioning.

Next, I would like to talk about plant-based foods. This quarter has seen strong investor and media interest in this space. I would like to confirm that we've been working hard to create exciting plant-based food choices for a number of years. Let me clarify in this context that it is about giving choices to consumers to enjoy more flexible and broad-based diets. It is not about advocating a departure from animal-based proteins.

This plant-based arena is ideal to showcase the speed and the depth of our research and development organization. We believe that plant-based products should not only be delicious but that they should also offer a superior nutritional profile. Right for you, right for the planet. This credo summarizes the potential health benefits as well as the lower environmental burden, in particular lower CO_2 emissions and water usage.

I understand that there's a lot of media buzz in this space right now, and at times, it is hard to put all the details in the proper context. I just wanted you to know that we have the ambition and the perseverance to be a major player in this area. Initial results and growth rates are very encouraging, and we see all the elements of a significant long-term trend in the market.

Next, let us turn to portfolio management. We see continued progress here, and we're particularly pleased with the outcome of our Nestlé Skin Health review. I understand that our May press release regarding the sale of Nestlé Skin Health has led to some questions about where exactly this transaction stands and whether the purchase price is agreed. We had to choose this wording in May to satisfy certain regulatory requirements in particular in France. For the avoidance of doubt, I would like to confirm that the transaction is binding with EQT and that the purchase price of CHF 10.2 billion is agreed. We expect closing in the fourth quarter, subject to regulatory approval and completion of the French works council process.

Slide: Our business as a force for good
Nestlé Health Science: Empowering healthier lives through nutrition

When it comes to our ambition regarding business as a force for good, I would like to talk about Nestlé Health Science this quarter. We are one of the leading global providers of medical nutrition, and a large part of these products go to cancer patients. Cancer is a horrible disease, but thanks to medical progress, cancer survival rates are increasing. The secret to successful cancer therapy is close coordination between all specialists that are involved in the treatment process. This is why the most innovative hospitals have created what they call cancer boards to ensure a high level of coordination while patients are in hospital care.

The same need applies though to outpatients who require close coordination between their medical and nutritional therapies. Anyone who has lived through a cancer episode in their own lives or with family or friends will tell you about the feeling of being left alone with a lot of uncoordinated expert advice. Patients are poorly equipped to deal with this need for coordination especially at such a difficult time of their lives.

This is where our COPES initiative, which we launched in the U.S. earlier this year, makes a difference. It provides patients with holistic advice and real-time access to address their medical and nutritional needs. Initiating and scaling a system like this shows that we are not content with just selling our products. We want to be sure that our patients' needs are effectively addressed. Patient first is our mantra, and this is one way to make it happen.

In summary, looking back on the first half on our various initiatives, I would like to reiterate what I said in our conference call last July. We are pleased but not satisfied. We are far from done, and there's more to come.

This concludes my prepared remarks. Let me turn it over to François now, and I look forward to answering your questions later.

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

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Thank you, Mark, and good morning and good afternoon to you all. Let me start with the highlights for the six months.

Slide: Strong half-year financial results

Total sales for the first half reached CHF 45.5 billion, an increase of 3.5% on a reported basis. Organic growth was 3.6% following an acceleration to 3.9% in the second quarter. The underlying trading operating profit margin reached 17.1% of sales. This is an increase of 100 basis points. Underlying EPS grew by 15.7% on a constant currency basis.

Slide: Half-year sales growth

Looking now in more detail at the moving components of our sales development. Organic growth was 3.6% in the first half. Real internal growth continued to be the main driver at 2.6%, remaining at the high end of the food and beverage industry. Pricing contributed 1%, reflecting the challenging environment in Western Europe and lower inflation in some emerging markets.

Going back to the organic growth. If we exclude the businesses that are currently under strategic review, namely Nestlé Skin Health and *Herta* charcuterie, organic growth in the first half was 3.4%. I would also point out that we had some favorable comparables linked to the trucker strikes in Brazil that negatively impacted our sales last year. We estimate that these benefited RIG and OG in the first half by around 10 basis points.

Net acquisitions added 1.1% of sales. The acquisition of the *Starbucks* license and *Atrium Innovations* more than offset divestments, mainly *Gerber Life* Insurance. Foreign exchange had a negative impact, reducing sales by 1.2%. On a reported basis, our sales increased by 3.5% to CHF 45.5 billion.

Slide: Further momentum in the Americas

This slide illustrates the development of our sales by geography. It includes both our Zones as well as our globally and regionally managed businesses. Organic growth and RIG were positive in all geographies. RIG accelerated notably in AMS and EMENA but slowed down in AOA mainly due to Pakistan and China. Pricing was positive in AMS and AOA but was slightly negative in EMENA due to the ongoing deflationary environment in Western Europe.

Slide: Growth acceleration in developed markets

Now looking at the growth dynamics between developed and emerging markets. Developed markets accelerated to 2.4% organic growth, their strongest first half in seven years. This was mainly driven by the United States, but there was a broad-based RIG acceleration in most developed markets in the second quarter. Pricing remained limited with positive pricing in the United States partially offset by negative pricing in Western Europe, Oceania and Japan.

Growth in emerging markets was 5.3%. The biggest driver was Latin America, particularly Brazil, which posted double-digit growth. As I mentioned before, Brazil had good underlying growth, but it did also benefit from easy comps following the trucker strikes last year as they had maintained mid-single-digit growth. Eastern Europe did well with high single-digit growth led by Russia, and China slowed to low single-digit growth.

Slide: Zone AMS

Let's now move to our five operating segments, starting with Zone AMS. Sales hit CHF 15.7 billion with a further increase in organic growth momentum to 3.9%. RIG was positive at 2% with largest contributions from the United States and Brazil. North America maintained good sales development throughout the first half. There was a significant acceleration to mid-single-digit growth in the second quarter, which made it the strongest quarter for North America in the last eight years.

Growth was relatively balanced between RIG and pricing. The largest contributor remained *Purina* PetCare, which had increased pricing and continued to see strong momentum in e-commerce and in premium brands. Beverages including *Starbucks*, *Coffee-mate* creamers and *Nescafé* had mid-single-digit growth.

Innovation and better execution supported growth in Frozen food. There was strong momentum in Ice cream and Pizza in the second quarter, which was achieved alongside the announced transition to a warehouse distribution model.

Latin America had mid-single-digit organic growth. Brazil had high single-digit growth supported by strong performances in Ambient dairy, Infant nutrition, Professional and *KitKat*. Mexico maintained mid-single-digit organic growth with strong contributions from *Nescafé* and Confectionery. *Purina* PetCare delivered double-digit growth in the region overall.

The Zone's underlying trading operating profit margin improved by 40 basis points to 19.2%. The improvement was supported by pricing, structural cost reductions and portfolio management. This more than offset cost increases from commodity inflation.

Slide: Zone EMENA

Next is Zone EMENA. Sales were CHF 9.2 billion. Organic growth was relatively consistent with previous quarters at 2.4%, with positive contributions from all sub regions. These results were driven by strong RIG of 3.7% as our pricing remained negative due to the continued deflationary environment in Western Europe.

By category, *Purina* PetCare and Infant nutrition were the main growth contributors. In PetCare, premium products and platforms such as *Felix*, *Purina ONE* and Tails.com were the key growth drivers. Coffee was slightly negative in the first half but rebounded to positive growth in the second quarter as strong RIG offset negative pricing. Confectionery improved with double-digit growth for *KitKat*. Vegetarian products did well, posting strong double-digit growth in Western Europe. The plant-based *Garden Gourmet Incredible Burger* was launched in nine markets in the second quarter.

The Zone's underlying trading operating profit margin increased by 10 basis points. This was based on structural cost reductions and favorable mix. Marketing and commercial investments increased to support innovation and brand building.

Slide: Zone AOA

Moving now to Zone AOA with sales of CHF 10.7 billion. Organic growth was solid at 3.3% with RIG of 2.3% and pricing of 0.8%. The slower growth in Zone AOA was in large part due to negative sales development in Pakistan with a challenging trading condition particularly in the Dairy category, which has been hit by milk price deflation.

China saw softer growth in some categories, but reported good growth in Culinary and Ice cream. This is consistent with softer food and beverage category growth, which reached the lowest level in a decade according to Nielsen and Kantar panels. Southeast Asia had strong growth with Vietnam and Indonesia posting double-digit growth. Most product categories contributed, especially ready-to-drink *Nescafé* and ready-to-drink *Milo*. South Asia excluding Pakistan had high single-digit growth with strong performances from *NAN*, *Maggi* and *KitKa*t. Japan and Oceania returned to positive growth on the back of improved RIG momentum in the second quarter. Sub-Saharan Africa maintained mid-single-digit growth.

In terms of category, *Purina* PetCare was again the standout performer, growing at a double-digit pace with Infant nutrition delivering broad-based mid-single-digit growth. In Coffee, there was strong demand for *Starbucks* products in the markets where we launched it, Japan, South Korea, Hong Kong and Taiwan.

The Zone's underlying trading operating profit margin improved by 40 basis points to 23.1%, supported by pricing, structural cost reduction and favorable mix. Marketing investments increased to support innovation and brand building.

Slide: Nestlé Waters

Moving on to our globally managed businesses and starting with Nestlé Waters. Total sales were CHF 4.0 billion. Organic growth was 1.4%, driven entirely by positive pricing of 4.7%. RIG declined by 3.3% as a result of price increases in the United States and slower growth in Europe.

In North America, organic growth was slightly positive due to the significant price increases we took last year to pass on cost inflation in packaging and distribution. However, this positive pricing had a negative impact on RIG.

Within North America, our premium brands had high single-digit growth on *ReadyRefresh*. Our direct-to-consumer business had mid-single-digit growth, benefiting from a new online platform and improved execution. But in the mainstream segment, *Nestlé Pure Life* had negative growth.

Europe had negative growth as unfavorable weather conditions contributed to a deceleration in the second quarter. Emerging markets improved to high single-digit organic growth with strong momentum in Asia, Turkey and Egypt. *Nestlé Pure Life* made a strong contribution to growth in emerging markets with the launch of sparkling and flavored offerings.

On a global basis, the international premium brands maintained high single-digit growth driven by innovation such as *S. Pellegrino Essenza* and *Perrier & Juice*.

The underlying trading operating profit margin increased by 180 basis points to 11.8%. The improvement was based on increased pricing and structural cost reduction. This more than offset the further increase in PET packaging costs as well as higher marketing investments.

Slide: Other Businesses

The last of our operating segments is the Other Businesses, which includes *Nespresso*, Nestlé Health Science and Nestlé Skin Health. As you know, we are currently exploring strategic options for the Skin Health business but its sales remain consolidated and included in our organic growth until the process is finalized later this year. Total sales for the Other Businesses were CHF 5.8 billion. OG accelerated to 7.4% driven by strong RIG of 6.7%. Pricing was positive at 0.7%.

Nespresso maintained mid-single-digit organic growth with strong double-digit momentum in North America and Asia. Europe was resilient with positive growth in a competitive environment, and these good results were supported by continued strong demand for the *Vertuo* system as well as for *Nespresso*'s limited editions.

Nestlé Health Science sustained mid-single-digit growth based on strong sales development in medical nutrition and geographic expansion in emerging markets. Innovation provided additional growth momentum with strong demand for the recently launched doctor-formulated CBD products, which are the THC-free and non-GMO certified. Nestlé Skin Health had double-digit growth, confirming its strong recovery since its reorganization.

The underlying trading operating profit margin of Other Businesses increased by 320 basis points to 19.6%. This was the result of broad-based improvement in all businesses, particularly Nestlé Skin Health.

Just as a reminder, Nestlé Skin Health has been classified as an asset held for sale since January. This means that we have stopped depreciation of this business, which increased the underlying trading operating profit margin. As I mentioned earlier, this has been around a 20 basis points benefit to the group margin.

Slide: Positive organic growth across the portfolio

Looking now at growth by product categories. All categories developed positive organic growth, which illustrates the strength of our portfolio. Powdered and liquid beverages saw slower growth of 2.7%. This was largely due to negative pricing in Coffee as a consequence of sustained deflation of green coffee prices. However, we did regain momentum in Coffee in the second quarter with mid-single-digit growth. The *Starbucks* brands contributed positively, and ready-to-drink coffee grew high single digit.

Nutrition and Health Science had strong growth, driven by RIG in all three subcategories. Infant nutrition maintained its solid momentum with 4% organic growth. Milk products and Ice cream grew by 3%. Within this, Ambient dairy improved driven by both pricing in Brazil and Ice cream in the U.S., which had a good performance driven by innovation. Coffee creamers maintained mid-single-digit growth.

PetCare continued to see strong growth globally based on e-commerce, super premium and natural offerings. *Purina Pro Plan*, *Purina ONE* and *Tidy Cats* were key growth platforms.

In Prepared dishes and cooking aids growth improved driven by RIG. There was positive growth in U.S. Frozen food with *Hot Pockets* and *Stouffer's*, and *Maggi* maintained strong growth in emerging markets.

Confectionery growth was solid, based on strong RIG with some negative pricing in Zone EMENA. Waters, we already discussed.

Slide: Underlying TOP margin by products

Moving now to the evolution of operating profit by product category. Our largest categories, Powdered and liquid beverages, which is mainly Coffee, Nutrition and Health Science as well as PetCare, continued to deliver the highest levels of margins in our portfolio. The profitability of Powdered and liquid beverages were slightly down due to product mix. We increased our marketing and commercial investments mainly in Coffee, which includes support behind the recent *Starbucks* launches.

The margins of Nutrition and Health Science increased significantly. As I mentioned earlier, this was largely due to the recording of Nestlé Skin Health as an asset held for sale, which means that we are no longer incurring depreciation and amortization for this business. PetCare margins decreased mainly due to higher input cost related to grains and packaging.

Milk products and Ice cream margins increased, helped by pricing and operating leverage. Confectionery margins came down slightly due to higher input costs and increased marketing and commercial investments. Water continued to restore its profitability. This was based on positive product mix and structural cost reductions.

Slide: Gross margin improvement

Looking now at our gross margin. We saw solid increase of 60 basis points versus the prior year, finishing the half at 49.9%. We had increased commodity and packaging cost in the first half, but these were more than offset by price increases, positive business mix and structural cost savings in manufacturing. For the second half, our comparables become less favorable and our input cost will increase more than in the first half, so the margin development will not be as strong.

Slide: Underlying TOP margin +100 bps

So looking at our underlying trading operating margin. It increased by 100 basis points to 17.1% from 16.1%. The gross margin increase of 60 basis points that I just walked you through was the largest contributor. We also saw lower distribution costs driven by moderation in freight costs, which helped by 20 basis points. And we were also successful in keeping our G&A costs under control. This contributed more than 20 basis points to the margin increase. At the same time, we have been able to increase our marketing investment to support our brands.

Slide: Underlying EPS +15.7%*

Moving on to net profit and underlying EPS. Trading operating profit margin increased by 90 basis points to 15.5%. The group tax rate increased by 110 basis points to 27.5%, but the underlying tax rate declined by 280 basis points to 21.4%. The decrease resulted mainly from the development of our geographic and business mix. Net profit decreased by 240 basis points to 10.9%. This decrease reflects the fact that in the first half of 2018, net profit benefited from the disposal of the U.S. Confectionery business.

Underlying earnings per share increased by 15.7% in constant currency and by 14.6% on a reported basis to CHF 2.13. The increase was mainly the result of improved operating performance and lower taxes.

Nestlé's share buyback program contributed 1.9% to the underlying earnings per share increase, net of finance costs.

Slide: Continued focus on working capital

Moving on to working capital. The 50 basis points decline showed that over the last 12 months, we continue to make improvements on our working capital as a percentage of sales on a 5-quarter average basis. Following several years of significant progress in working capital reductions, we continue to see opportunities for further improvements but at a more moderate pace going forward.

Slide: Free cash flow

We had a strong free cash flow, reaching CHF 4.1 billion in the first half. The increase was mainly driven by the higher operating profit and also by improved working capital. Please be aware that due some seasonal dynamics and higher commodity costs in the second half, the improvement in working capital and free cash flow at year-end will be more moderate than it has been in the first half. We continue to work on all the levers of cash generation: growth, margin improvement as well as working capital improvement.

Slide: 2019 guidance confirmed

We confirm our full year guidance. We now expect organic sales growth of around 3.5% for 2019. That takes into account a number of factors: first, we will begin to face tougher comparables in the second half or more specifically in Q4. Second, the businesses under strategic review have added around 20 basis points to the growth in the first half but this will not be fully the case in the second half as we expect to dispose mainly of Nestlé Skin Health. Third, there had been some benefits from easy comparables in Brazil in Q2 owing to the trucker strike, which will not repeat, in the second half. If we exclude one-off items such as Brazil, H2 will be pretty similar to H1 at around 3.5%.

For our full year underlying trading operating margin, we expect to land at or above 17.5% in 2019. This means that we will reach the lower end of our 2020 guidance one year ahead of the original plan. Our margin development has been strong in the first half, and we expect a more modest development in the second half as we face tougher pricing comparables and higher input costs.

Let me now hand over to Luca for the Q&A session.

Q & A Session

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Thank you François. With that move over to the Q & A session. We open the lines for questions from financial analysts. (Operator Instructions) The first question comes from Céline Pannuti from JPMorgan.

Questions on:	**Outlook for year** **Starbucks and Plant-based opportunities**

Céline Pannuti, JP Morgan:

My first question is to rebound on the outlook, and thank you for fleshing out the disposal impact for Q4 comp. Just wanted to know whether -- as you look at your markets, and we see that the U.S. is one of the best performance in years, China has been slowing down, has there been any issues that would worry you as you go into H2 and which weighed on your decision to guide to 3.5% for the second half of the year?

The second question I had was to come back on the two areas you flagged where you see exciting opportunities, *Starbucks* and Plant-based. So on *Starbucks*; is it possible to understand how much this contributed to the Coffee acceleration in Q2? And what is the opportunity? I think you said big, really big. So can you help us to understand -- to size that?

Likewise for Plant-based, can we know how much that contributed in the first half? And what do you think the opportunity is from a total industry perspective?

Mark Schneider, Nestlé S.A. Chief Executive Officer:

Céline, thanks. This is Mark. So I guess on the outlook, there's not a specific issue here on the U.S. market that we're aware of that makes us more cautious for the second half. I think François outlined the mechanics pretty well that give us a bit more caution. Overall, it is important for me that you can always rely on the kind of expectations and outlooks that we're giving, and hence, that meet or exceed culture is a very important one to me.

Specifically here on the second question, as you know, we're trying to be very helpful. But on *Starbucks*, I have to leave it with this anecdotal assessment because with the low number of markets where we are right now, this will get down into competitive information fairly quickly, and at this point, we're totally committed to maximizing this opportunity. I think in markets where we are present, so take Japan and Korea and Asia, take North America, the U.S. market or take The Netherlands or Italy in Europe, I think market data will show very clearly that this is a successful ramp-up, but it's hard for me to give you any specific summary numbers at this point.

The same on Plant-based. Again, we haven't put a numbers collar around it. As you know, there's a lot of excitement out there, and I think the direction we're going is not only supported by consumer tastes which are changing but also by number of nutritional studies like, for example, the Lancet-EAT report.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Thanks, Céline. The next question comes from Warren Ackerman from Barclays.

Questions on:	**Zone AOA performance, specifically China and Pakistan** **Coffee**

Warren Ackerman, Barclays:

It's Warren here from Barclays. Also two questions. The first one is could you perhaps, Mark, dig into Zone AOA in a bit more detail? 3.3% organic growth in light of the great performance elsewhere is a bit light. I hear you on China and Pakistan. Just wondering whether you can flesh out what's going on in China. Are you seeing any impact from kind of swine flu on disposable income in China? Why is the market so soft? Likewise, Pakistan, how negative is negative? And should we expect a similar growth rate in the back half, in the second half?

Then secondly, on Coffee, pleasing to hear the underlying improvement in the second quarter. I just wondered whether you can sort of flesh out what you're seeing on your biggest brand of *Nescafé* in terms of underlying development, market share. Where are you seeing that RIG improvement? And do you think the pricing negativity continues into the back half or not?

Mark Schneider, Nestlé S.A. Chief Executive Officer:

Thanks, Warren. So on AOA, when it comes to Pakistan, as you know, it's a little difficult for us to comment on this in detail because Pakistan is also a publicly listed entity. For Q1, you saw a negative growth rate of minus 10%, and there's a very tough economic slowdown and also tough regulatory environment. But within that framework, we're working very, very hard to improve the situation, and so I'm cautiously optimistic here when it comes to the midterm for Pakistan.

China, as you know, the consumer goods area has been very muted in the first half. I think that's a picture that's not just reflected here by our performance but also some other companies'. We see that in particular in the mainstream areas. That includes, for example, *Hsu Fu Chi* and *Yinlu*. We've seen also some pressure in Confectionery, so *Hsu Fu Chi* again was the problem here. So we're working very hard to improve. And as always, long term, we're quite bullish on this key market.

On Coffee, as you know, the fact is that green coffee prices are still very low, and hence, for the more premium brands, it's easier to overcome that situation. On our more mainstream offerings like *Nescafé*, this creates a bit more pressure. But we also see a number of interesting premiumization opportunities in the *Nescafé* space.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Thanks, Warren. Next question is coming from Jean-Philippe Bertschy from Vontobel.

Questions on:	**Hsu Fu Chi** **Further improvement in Waters**

Jean-Philippe Bertschy, Vontobel:

I have two questions. The first one is with regard to *Hsu Fu Chi*. I think you have a fantastic opportunity with *Starbucks* and as well with the Plant-based products. I think the initiative with the cancer digital platform is as well very attractive. How do these assets in China fit your strategy and of course, if it's not distracting for your capital allocation?

The second one is on Waters. We see some improvements. How far can you improve this division especially in the U.S., in the mainstream products?

Mark Schneider, Nestlé S.A. Chief Executive Officer:

Okay. Thanks, Jean-Philippe. So on *Hsu Fu Chi*, clearly, the troubles here go back also to the Chinese New Year season, beginning of the year that, I think, broad based in the industry has been a bit of a disappointment. This is, of course, where Confectionery and some of the *Hsu Fu Chi* articles in particular are hit. I think we're working very hard when it comes to offering new product varieties, and so overall, I think there's a lot of work underway to improve the situation.

On Waters, you're quite right, the future is in premium offerings, sparkling, flavored, functional waters, that kind of work. There's a lot of intensity inside the organization, but this also takes a bit of time to get traction. Remember Waters is a pretty massive operation here at around CHF 9 billion.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Thank you, Jean-Philippe. Next question is from Alan Erskine from Crédit Suisse.

Questions on:	**Infant nutrition business** **Atrium**

Alan Erskine, Crédit Suisse:

Two questions. One, could you give us an update on the Infant nutrition business. Just how that performed in the quarter. Secondly, could you give us an update on *Atrium*? Is it still growing double-digit?

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

On Infant nutrition, I mentioned it during my comments. So the business is doing well. We grew actually 4% in the first half, which is interesting and attractive. The growth has been fairly well spread over the different Zones and regions. We are doing better actually whenever we premiumize, so we continue to do very well with HMOs, human milk oligosaccharides, which is interesting. There was a bit of a slowdown maybe in China. We talked about it. But still, I mean, we continue to grow nicely.

As far as *Atrium* is concerned, we are very happy with that acquisition. We had some comparables which were a little bit difficult at the beginning of the year but the business continues to do very well. So we are expanding with quite a lot of new offerings and new products. We have as well diversified a little bit in food, drug and mass, which had started already last year. So we are extremely happy with the acquisition and very much in line with the original plan when we did this acquisition.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Thanks, Alan. Next question is from Jon Cox from Kepler.

Questions on:	**Pricing** **Tax Rate**

Jon Cox, Kepler Cheuvreux:

Thanks very much, Jon Cox, Kepler Cheuvreux. Two questions. Actually, the first question is really on the pricing. Q2 pricing seems to be worse than Q1 when actually we've seen sort of a sequential improvement in pricing really since Q1 last year. Just wondering, are things going backwards again on pricing? Or would you still assume that pricing will improve going forward?

Then just a second question on the effective tax rate for the year. You mentioned the underlying tax rate stands at 21.5%. I'm guessing you don't want us to start penciling in that figure for the next few years, but wonder if you could give us a bit guidance on the tax situation because, obviously, it makes a huge difference to EPS if we start to pump in a lot lower numbers.

Mark Schneider, Nestlé S.A. Chief Executive Officer:

Thanks, Jon. Let me take the first one and then hand it to François for the second one. So look, on pricing, we stay as focused as ever because I think this is a key lever that we need to watch very carefully. As you know, we have a lot of initiatives underway when it comes to improving revenue management. But it's also important to note that we started now in Q2 to lap some of the significant pricing that was taken last year, most notably in Waters. Hence, you always get into this year-over-year situations where sometimes things look a bit more muted. But when it comes to the underlying substance, where it's important for us, for our high-quality good products, that we get paid properly, this is something that we remain very much focused on.

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

So on the underlying tax rate, so we are slightly north of 21%. So the decline that we have seen is largely the consequence of the development of our geographic and business mix, which is something that we expected anyway. It is underlying tax rate, which indicates by itself that this is likely to be sustainable.

That being said, let's make a caveat there. It is obviously sustainable at constant scope and business mix. If we have the same scope and same business mix tomorrow, we should be around that level. As an example, the disposal -- the coming disposal of Nestlé Skin Health will probably increase marginally our underlying tax rate because they are enjoying a lower tax rate. So once again, sustainable bar any change in scope and mix.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Next question is from Alain Oberhuber from MainFirst.

Questions on:	**Ice Cream in the US** **Restructuring costs**

Alain Oberhuber, MainFirst:

Also from my side, two questions. First is regarding the U.S. Could you elaborate a little bit on the U.S. Ice cream business and several subcategories you have in U.S. Ice cream arena?

And on restructuring costs, where do we stand and what could we expect for the full year?

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

So U.S. Ice cream business is doing well. We are growing mid-single-digit - strong mid-single-digit in Q2, really driven by *Häagen-Dazs* and *Outshine*. *Dreyer's* is a little bit soft. Much of the growth is actually coming from innovation, which is really helping. We are very pleased by the fact that we are gaining market share, which is very good. And it's not only about growth, but we saw an improvement as well in terms of profit. One usually is driven by the other one, so we were very pleased by that.

In terms of restructuring costs, we indicated during our Capital Market Day in Arlington that we expect to be around CHF 700 million for the full year, and that is including the announcement that we did regarding the move away from DSD in the U.S. We confirm that figure for the time being, so we'll be around CHF 700 million for the full year 2019.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Next question comes from Pierre Tegnér from ODDO.

Question on:	**Pricing**

Pierre Tegnér, Oddo:

Thank you for taking my question. I have just one question coming back on the pricing discussion. As you know, it's quite important because it's an important point in terms of pricing power. But could you help us in giving us the balance between the mix and the volume we see in the RIG? Because it's quite difficult to see how much is improving your pricing power through the mix and through the innovations and the ramp-up of the quality of your products. So can we have an idea of the mix we see in the organic growth and the RIG?

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

So we don't provide the breakdown between volume and mix in RIG. So RIG is a good indicator of our capacity to drive volume and a good indicator as well of our capacity to premiumize because of the mix. So both components are moving in the right direction, but we don't share the detail.

Mark Schneider, Nestlé S.A. Chief Executive Officer:

So Pierre, sorry we can't be more helpful, but I think you should draw comfort from the fact that we have an industry-leading RIG figure, so there must be something positive going on there.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Next question is from John Ennis, Goldman Sachs.

Question on:	Coffee and main contributors to improvement

John Ennis, Goldman Sachs:

Just one for me, please. Coming back to Coffee. I wonder if you could highlight the main countries which have really contributed to the improvement in Coffee that we saw in the second quarter. Maybe you could also reference Japan specifically within that remark given this was a country highlighted in 1Q as being somewhat challenging.

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

So in Coffee, we are very pleased indeed to be back into the mid-single-digit space in Q2, which is essentially driven by RIG. We were quite happy to see some recovery in Japan as well, and we flagged the fact that it was a little bit soft in Q1, which was largely due to price increases that we took last year. We were even more pleased by the fact that we returned to positive growth in EMENA. In EMENA, as you know, we had some price pressure. But the price pressure remains, which is largely linked to the coffee bean price levels. But that being said, we have been able to go back into positive growth essentially through an increase of our volume and RIG. So it's very good.

If I look at it by subcategory, the main drivers of the growth have been ready-to-drink, portioned coffee, starting with *Nespresso* and *Starbucks* and as well as *Nescafé* in emerging markets. So it's not only Japan and EMENA, but *Nescafé* in emerging markets saw an interesting development in the second quarter. Overall, our market shares have been improving as well, so I would say that -- very pleased overall by the developments both in terms of geography and categories.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Next question is from David Hayes, Société Générale.

Question on:	Biggest surprise and biggest challenge of the last three years

David Hayes, Société Générale:

So just one question for me and really for Mark. Mark, you've been in the business now for, I guess, around three years, so just a very broad question. When you look back three years, when you look at where you are now with the business, what's your biggest surprise that you found coming into this new industry from where you were before? Also, what's been the biggest challenge to achieve out of everything that has evolved so far?

Mark Schneider, Nestlé S.A. Chief Executive Officer:

Thanks, David. Look, I think the biggest surprise to everyone, whether you're new to the industry or whether you're an old hand, is simply -- for the last three years is the amount of change that has occurred in this industry and in particular the amount of innovation that has been brought to the market by small and mid-sized focused companies. The challenge was very clear. We had to rise to this level and basically meet that rate of innovation; hence, the changes we've done to our research and development organization. And also when it comes to launching products faster and learning on the fly and working with versions 2.0, 3.0 to learn as we go as opposed to answering all the questions first, and then launching maybe too late. That sort of approach, I think, spreading back in the organization, this is where we responded well, and where, I think, we are much nimbler now and doing well. This is where the industry is going, and continues to go, and hence, you'll see more efforts in that regard.

A good example, case in point, I think, very easily trackable from the outside was the fast launch of *Starbucks* products. As you know, we only closed this transaction in late August last year. We already unveiled the product line with 24 SKUs in mid-February. By mid-March, we are on the store shelves. Now you just saw the launch of the creamers. I'm already telling you that there's a second wave of markets coming from October and there's a new wave of SKUs coming from January. So it's a constant flow of new products coming to the markets, and this will be no different in approach from what any start-up would do. I think this is where we had to up our game, and we did successfully.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Next question is from Andreas von Arx from Baader.

Question on:	**Nestlé Waters**

Andreas von Arx, Baader:

Just one question on the Water division. If you please could provide some detail on where you have spent the CHF 90 million restructuring costs. Let's say on which countries, brands, segments or facilities. I just note that this is around 30% of your total restructuring costs for a division that only does less than 10% of sales and CHF 90 million equals more than 200 basis points and also puts a bit different light on the 200 basis point margin improvement that you have made in that division. I mean, for you, I think it's core division. However, I think, from the outside, one can get the impression that you're unwinding here unwanted businesses via restructuring costs.

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

Andreas, let me take that one. So the restructuring costs that we allocated to the Water division essentially have been spent in the U.S. and in France. We actually closed one factory in the U.S., in Phoenix. We did some restructuring in France as well, mainly in Vittel, but for sub-brands of Vittel, which are Contrex and Hépar, so it's highly focused on the U.S. and France.

Mark Schneider, Nestlé S.A. Chief Executive Officer:

Yes. Andreas, let me build on this. I mean it shouldn't be surprising. When you go back several conference calls here for the past quarters, several of your colleagues asking us what are we going to do to respond to the situation. So we are very focused, and that results in restructuring activity. That's a good thing. That's a sign of improvements to come. So frankly, I see it as something that's encouraging. We're not just taking the status quo and sit on it.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Thanks, Andreas. The next question is from Jeremy Fialko from HSBC.

Questions on:	**Market Share** **Main contributor to acceleration in US**

Jeremy Fialko, HSBC:

Jeremy Fialko, HSBC here. So a couple of questions for me. The first one is could you talk about what you think the end market growth rate is at the moment and to what extent you're outperforming your end markets and approximately what percentage of, let say, your country category sales you think you're gaining market share in?

Then the second question is just coming back to the U.S. And perhaps if you could talk a little bit about what has been the main contributor to this really nice acceleration that you've seen in the quarter. Again, is it a market linked thing or is it much more down to your own initiatives and your own sort of inflections in market share?

Mark Schneider, Nestlé S.A. Chief Executive Officer:

Let me start with the second one, Jeremy, and then hand it to François for the first one. I think for the U.S., really getting it right in some of the big and important categories, that has been decisive. So take PetCare, for example, which is operating at a very high level now, Coffee creamers, the Coffee business. So getting the big chunky categories right and making sure that we have good, solid, tangible underlying improvement there, I think that proved to be the winning formula.

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

Jeremy, in terms of market share, you know that the way we can measure it is to look at the number of cells, as we call it, which is when we cross market and categories where we increase our market share or lose market share. So if we look at it, we have about 58% of the cells where we are gaining or stabilizing our market share and 42% which is down. If I look at the breakdown between up and stable, it's about in 49% of the cases, we increased our market share. In 9% of the cases, we stabilized them; and 42%, down, which is actually better than where we were a year ago. We used to be traditionally around 45% up, now we are much closer to 50% up. And the number of cells where we have stable has been fairly constant around 10%. So we are doing better than over the last couple of years.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Next question is from Patrik Schwendimann from Zürcher Kantonalbank.

Questions on:	**Underlying margin** **RIG in Western Europe**

Patrik Schwendimann, Zürcher Kantonalbank:

I have a question regarding the underlying margin. What will be the basis for H1 of the underlying margin excluding Nestlé Skin Health? So that's my first question.

Second, regarding the Western Europe RIG, which was very strong with 3.7%. Congratulations for this one. How much of this is due to more exposures to hard discounters?

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

Let me take the underlying margin side. So as we said, our underlying margin has increased 100 basis points. If we exclude Nestlé Skin Health, it would be about 80, so the contribution is about 20 basis points. And if we look at the margin itself, once we have classified Nestlé Skin Health as an asset held for sale, their margin is pretty much in line with the average margin of Nestlé, so there is no dilution or accretion impact there.

Patrik Schwendimann, Zürcher Kantonalbank:

So basically, the baseline will be roughly 17%, next year when you look back

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

Sorry, I could not hear your question.

Patrik Schwendimann, Zürcher Kantonalbank:

I mean, next year, when we look back at H1 '19, then you will say, well, underlying last year, 2019, excluding Nestlé Skin Health was 17% then also roughly?

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

No, because we will not restate -- we are not going to restate 2019, so we will leave it as it is today.

Patrik Schwendimann, Zürcher Kantonalbank:

Sure. I know, but just to have an idea.

François-Xavier Roger, Nestlé SA, Chief Financial Officer:

Yes. So this is the figure that I gave you earlier, which is no dilution, no accretion; and on the one hand, but the contribution to the margin improvement, which is about 20 basis points.

Mark Schneider, Nestlé S.A. Chief Executive Officer:

Patrik, on your second question, look, the EMENA RIG growth was very good. We're encouraged by that, seeing good trends. It was broad-based, so there's not a significant individual item that I would want to flag.

End of Q&A session.

Luca Borlini, Nestlé S.A, Head of Investor Relations:

Thank you. We don't have any more questions, so we come to the end of our session today.

Mark Schneider, Nestlé S.A. Chief Executive Officer:

Thank you for joining us. We'll talk to you next quarter. Looking forward to it.

End of Transcript