NESTLÉ S.A.

2022 NINE-MONTH SALES CONFERENCE CALL TRANSCRIPT

19th October, 2022, 14.00 CEST

Speakers:

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

Slide: Title slide

Good afternoon, and good morning to everyone, and welcome to the Nestlé nine-months 2022 sales webcast. I'm Luca Borlini head of the Nestlé Investor Relations team. Today I'm joined by our Chief Executive Officer, Mark Schneider and our Chief Financial Officer, François Roger. Mark will begin as usual with our key messages and discuss the full year 2022 guidance; François will follow with a review of the nine-month '22 sales figures. We will then open the lines for your questions.

Slide: Disclaimer

Before we begin, please take note of our disclaimer. And 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'm pleased to report that our sales growth momentum continued to increase in the third quarter. As a result, we're now reaching organic sales growth of 8.5% for the nine-month period of 2022.

As in the previous quarters this year, growth was primarily driven by pricing. We maintained our responsible approach to pricing, but further pricing steps were clearly needed to react to significant levels of global inflation hitting us.

Real internal growth remained resilient for the nine-month period but dipped into negative territory for Q3 at minus 0.2%. Short term and in the face of extraordinary pressures, this is unavoidable and should not be a cause for concern. As we look at next year and beyond, we continue to work towards a healthy development of our volume and mix. François will show you later that our 3-year real internal growth average for this quarter, which is a good underlying growth metric at times of significant pandemic-related volatility, remains quite stable at around 3%.

Our volume growth, which remained positive in the first half, turned slightly negative. In addition to supply chain constraints and the super high base of comparison, volume development was reduced by active and conscious choices to cut the number of low rotation and underperforming SKUs. This strategy, which we call 'cut the tail to push the head', is one of our ways to counter cost pressures and supply chain limitations. It is one of several strategies that enabled us to limit the pressure on our underlying trading operating profit margin compared to the reduction we witnessed in our gross margin. Over time, this strategy is also expected to give us top line benefits through better on-shelf availability and visibility of our core SKUs.

Next, I would like to turn to portfolio management. It has generally been a muted year so far. Our focus clearly has been on operating management at this challenging time, but I am pleased to report steady progress in building some of our growth pillars. Just this morning, for example, we announced the acquisition of the Seattle's Best Coffee brand from Starbucks. We have 4 years of experience with this brand since it was part of our highly successful global coffee alliance with Starbucks. Full ownership of this brand will now allow an even more complete integration of this business in our highly efficient coffee supply chain.

In addition to the iconic premium brand of Starbucks, we have come to like this trusted brand a lot. It gives us a highly credible midrange mainstream offering that competes very effectively and protects the premium positioning of Starbucks.

We have also patiently and steadily built our Nestlé Health Science portfolio this year, not in leaps and bounds, but with very manageable incremental steps. While we will focus on Nestlé Health Science in our Investor Day at the end of November, I would like to stress two key items today.

First, do not overinterpret the current short-term organic sales growth compression. Mathematically, this had to happen after two years of extraordinary sales growth during the peak pandemic period. We had told you ahead of time that this was unavoidable. And compared to our plans, the slowdown is less than we expected. We also continued to gain market share in VMS, which bodes well for future growth. In an era of increased consumer health interest, all signs point to continued attractive category growth once the strong COVID quarters are lapped. Our acquisition models and valuations for the deals we made in this space during the pandemic fully reflect this temporary post-COVID growth compression.

Second, I would like to reconfirm that we have no intention of turning Nestlé Health Science into a pharma business. While a few of Nestlé Health Science's products are prescriptiononly, the vast majority falls firmly in the area of fast-moving consumer goods, which is our and your home turf.

Nutritional supplements and vitamins in particular are fast turning into major branding and premiumization opportunities. We saw this trend early and are leading it with globally recognized and trusted brand names.

Slide: Business as a force for good: Nescafé plan 2030

I will now turn to the Business as a force for good section on Page 5. Two weeks ago, we published our Nescafé plan 2030. Following similar efforts in our cocoa sourcing, you're now seeing us bring the power of regenerative sourcing to another significant category of ours, coffee. Building on long-standing work in the field of coffee farming, you see that regeneration is firmly taking hold in our leading global coffee brand, Nescafé. It is no longer something that is limited to premiumized and exclusive offerings. We're taking this approach mainstream to the benefit of all coffee lovers, farmers and farming communities, as well as the planet.

Slide: 2022 guidance updated

Before handing it over to François, I would like to cover the updated guidance. Following the strong third quarter, we're now in a position to raise the organic sales growth expectation to around 8%. While this is lower than our nine-month organic sales growth performance, I would like to assure you that this is not due to any particular concern. It simply reflects a healthy amount of caution at a time of significant economic and geopolitical uncertainty. All other aspects of our guidance remain unchanged and are fully confirmed.

With this, I would like to hand it over to François.

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

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Thank you, Mark, and good morning or good afternoon to you all.

Slide: Nine-month sales growth

Let me start with the highlights for the nine months. Organic growth reached 8.5% with pricing of 7.5%, reflecting significant cost inflation. RIG was resilient at 1%, following a high base of comparison in 2021, continued supply chain constraints and the effect of SKU optimization initiatives. We have seen limited demand elasticity so far.

Net acquisitions increased sales by 1.2%, largely related to the acquisition of the core brands of the Bountiful Company and Orgain, a leader in plant-based nutrition. Foreign exchange had a slightly negative impact on sales growth. Total reported sales for the first nine months were CHF 69.1 billion, a 9.2% increase versus last year.

Slide: Broad-based growth across developed and emerging markets

Turning to the distribution of growth between developed and emerging markets, organic growth in developed markets reached 7.4%, mostly driven by pricing with slightly positive RIG. Growth in emerging markets was 10.2% based on both pricing and RIG. Growth was supported by continued momentum for affordable offerings, particularly in AOA.

Slide: Strong momentum in retail and further recovery in out-of-home

Turning next to the breakdown of sales by channel. Organic growth for retail sales remained robust at 7.3% for the nine months. Growth accelerated in the third quarter. Within retail, e-commerce sales grew by 8.4% building on a 17.2% growth for the nine months of 2021. Organic growth in out-of-home channels reached 26.1% for the nine months, with sales exceeding 2019 levels. In the third quarter, growth was supported by strong RIG and pricing.

Slide: Resilient RIG

Given the volatility of RIG over the last few years in the context of the pandemic, a 3-year RIG average provides a clearer picture of underlying growth trends. As can be seen on the chart, the level of underlying RIG by quarter remains relatively stable. For the nine months, RIG remained resilient at 1%, following a high base of comparison in 2021 and continued supply chain constraints. As we mentioned during our call at the half year, we expected to see some demand elasticity going forward. We are seeing some, more specifically in Food and Dairy, but the level remains limited in the context of the pricing actions we have had to take. In the third quarter, we also began to see the effect of our SKU optimization initiatives.

Going forward, we will continue to closely monitor consumption patterns given the volatile macroeconomic environment and pressure on consumer purchasing power.

Slide: Zone North America

Let's now look at the results of our seven operating segments, beginning with Zone North America, where we saw 11.2% organic growth. RIG was 0.1%, impacted by a high base of comparison in 2021 and supply chain constraints, particularly for Purina PetCare. Growth was supported by pricing, sustained momentum in e-commerce, as well as a further recovery of out-of-home channels.

By product category, sales in Purina PetCare, Nestlé Professional and Starbucks out-of-home products grew at a strong double-digit rate. Infant formula recorded strong growth following supply chain constraints in the market. Baby Food posted robust growth based on innovation. The recently launched Plantastic range of plant-based offerings resonated strongly with consumers. Frozen Food reported low single-digit growth with positive contribution from Pizza and Frozen meals.

Slide: Zone Europe

Shifting to Zone Europe, organic growth was 7.1%, supported by pricing across most geographies and categories. In a challenging environment, RIG remained resilient at 1.5% despite a high base of comparison in 2021 and supply chain constraints. Growth was supported by pricing, further recovery of out-of-home channels and innovation.

By product category, the key growth drivers were Purina PetCare and Nestlé Professional. Sales in Water grew at a double-digit rate with positive contributions from most brands. Sales in Infant Nutrition also grew at a double-digit rate based on continued strong demand for human milk oligosaccharide products or what we call HMOs. Coffee posted low single-digit growth following a high base of comparison in 2021. Garden Gourmet plant-based products continued to see strong double-digit growth, boosted by new product launches.

Slide: Zone Asia, Oceania and Africa

Moving now to Zone AOA. The Zone reported high single-digit organic growth, with positive contributions from all geographies and categories. Growth was driven by pricing, SKU optimization and the further recovery of out-of-home channels. By geography, all regions posted positive growth with particular strength in Southeast Asia, South Asia and Africa.

By product category, Culinary was the largest growth contributor. Coffee reported high single-digit growth. The Zone launched Starbucks ready-to-drink products in selected markets, including Australia and Indonesia. Sales in Nestlé Professional grew at a strong double-digit rate across geographies and categories. Infant Nutrition, Milo and PetCare all posted high single-digit growth.

Slide: Zone Latin America

Next is Zone Latin America, which maintained double-digit organic growth with broad-based contributions across categories and geographies. Growth was supported by pricing, strong execution and further momentum of out-of-home channels. By geography, Brazil reported double-digit growth. Sales in Mexico and Chile grew at a high single-digit rate.

By product category, Confectionery was a key growth contributor, reflecting strong demand for KitKat and key local brands, particularly Garoto in Brazil and Carlos Quinto in Mexico. Purina PetCare, Coffee and Nestlé Professional all reported double-digit growth. Infant Nutrition saw high single-digit growth with market share gains and Dairy posted mid-single-digit growth led by fortified milks and home baking products.

Slide: Zone Greater China

Turning to Zone Greater China. Organic growth was 4.7% based on solid RIG and pricing. As a reminder, inflation remained relatively limited in the region. The zone continued to be impacted by COVID-19 related movement restrictions. Growth was supported by strong operational execution, e-commerce momentum and continued innovation.

By product category, Infant Nutrition reported double-digit growth with improving market share trends for NAN and Illuma. Coffee posted high single-digit growth, led by Nescafé soluble coffee and Starbucks products. In Confectionery, Hsu fu chi and Shark Wafer both reported high single-digit growth.

Slide: Nespresso

Next is Nespresso, which reported low single-digit organic growth following 11% growth in 2021, with consumption remaining above pre-pandemic levels. Growth was supported by continued momentum for the Vertuo system. Sales for out-of-home channels further recovered, with continued expansion of the Momento system, as well as improved sales development for the Office segment.

By geography, North America posted double-digit growth with continued market share gains. Europe reported a sales decrease following high single-digit growth in 2021. Other regions combined reported high single-digit growth.

Slide: Nestlé Health Science

Finally, let's turn to Nestlé Health Science. The business posted mid-single-digit growth, building on two consecutive years of double-digit growth. Pricing, innovation and geographic expansion supported growth. Consumer Care reported low single-digit growth. Healthy Aging products grew at a double-digit rate. Growth in vitamins, minerals and supplements was close to flat, following a high base of comparison, particularly for immunity-related products during the pandemic. Medical Nutrition reported double-digit growth with strong sales development for pediatric and allergy products.

By geography, sales in North America grew at a mid-single-digit rate. Europe saw positive growth, while all other regions combined posted double-digit growth.

Slide: Broad-based growth across categories

Let's now look at product categories. Growth was broad-based, supported by pricing across all categories. We are seeing consumer demand somewhat normalizing by channel for the nine months. Categories with greater at-home consumption, such as Dairy and Culinary, saw softer growth over a high base of comparison. By contrast, categories with greater exposure to out-of-home channels, on-the-go consumption and impulse buying, such as Confectionery and Water saw a strong recovery over a low base of comparison.

Within Powdered and liquid beverages, Coffee saw high single-digit growth over a high base of comparison in 2021. All brands contributed positively to growth, with sales of Starbucks and Nescafé ready-to-drink products growing at a double-digit rate. Cocoa and malt beverages reported high single-digit growth, driven by strong demand for Milo and Nesquik ready-to-drink formats. PetCare reported strong double-digit growth with mid-single-digit RIG. Science-based, premium and veterinary products saw strong sales developments. Growth was also supported by continued e-commerce momentum on innovation.

Nutrition & Health Science posted 8.5% growth. Infant Nutrition reported 11.5% organic growth with a strong recovery across all geographies, particularly in China. Growth was supported by continued demand for HMO Infant formula products, with sales reaching almost CHF 1 billion and growth of around 15%. We have already discussed Nestlé Health Science.

Prepared dishes and Cooking Aids saw 2.6% growth driven by strong sales development for Ambient culinary, particularly Maggi in Zone AOA. Vegetarian and plant-based food products delivered double-digit growth led by Garden Gourmet, innovation continued to drive growth with a new chicken analog and the further rollout of Vuna, our plant-based tuna alternative across Europe. Growth in Frozen food was slightly positive.

Milk products and Ice cream reported 4.8% growth. The key contributors to growth were coffee creamers and home baking products, as well as Nino in Brazil and Yiyang in China. Growth in Confectionery reached 10.7%, reflecting strong momentum for KitKat seasonal products and key local brands. Sales in Water grew by 15.1% despite supply chain constraints. Growth was driven by international premium brands and the strong recovery of out-of-home channels.

Let me now hand over to Luca, who will manage the Q&A.

Q & A Session

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

Thank you, François. With that, we move to the Q&A session. (Operator Instructions) The first question is from Warren Ackerman at Barclays.

Questions on:	**RIG** **Gross margin**

Warren Ackerman, Barclays:

Warren here at Barclays. I've got two questions. First one is on RIG in the quarter. You mentioned a few factors. Can you quantify the impact on SKU rationalization? It seems like it was mainly an Asia issue. And then the RIG was also weaker in Nespresso and Health Sciences in particular. I know you said it was a tough comp on a 1-year view. But even on a 3-year stack view on Nespresso and Health Science, it does seem to be decelerating. I was just wondering, Mark, whether you can reiterate that there's no underlying slowdown in those two areas. Because on my math, to keep the RIG momentum that you've seen in the last couple of quarters, you would need the RIG to be back into plus 2% or certainly positive in Q4. Just wondered what your thoughts were on that.

And then secondly, just on the gross margin. You talked about gross margin compression quite significantly in the first half, but you have also been talking about gross margin stabilization in the second half. I was wondering whether you're able to talk about whether the pricing is now kind of matching the inflation, and we should be actually seeing the gross margin coming back in the second half looking into next year. That would be very helpful.

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

Warren, thanks. And maybe I'll take a first crack at your questions, but then also hand over to François for some additional detail.

Let me just start with the second one on gross margin and to confirm that we are still in the process of having to catch up. As you saw from the half year numbers, there was still a pretty sizable gap to the period before the onset of inflation. We're still in the process of catching up. There is a pretty significant full year effect that we're facing, and this will take us into '23, there's no question about that. We need to be resolved and need to remain disciplined when it comes to pricing action because not all of the things that have hit us have been recovered.

Regarding RIG, a few thoughts. So first, maybe I'll give you a bit more color on this SKU rationalization project. Let me also say this one will figure more prominently in our Barcelona Investor Day. Laurent Freixe, who is leading that for us internally, will present on it. It's something that we kicked off earlier this year when we saw that after the beginning of the Ukraine war, that clearly inflation was going to be a much more significant factor this year than before, and that supply chain constraints were also going to continue to a larger extent than anticipated. I think we started on a timely basis, which is why we're now standing to reap some pretty significant full year benefits. But Laurent will itemize that to a greater a degree of detail then when we present in Barcelona. But it's a good one because it gives us efficiencies, and yet at the same time, it also should lead to growth for the core SKUs, the ones that are high rotation and most successful. I think it's not only about cutting the tail. It's also about pushing the head. As you rightly pointed out, AOA is one of the Zones where we were particularly disciplined in implementing that. But let me confirm to you that this is a global project with a global reach, and everyone here inside the Group is participating because everyone sees the immediate benefits of that and also the benefits going forward.

Generally, when it comes to that ever so slight RIG decline in this third quarter, let me just address one common misconception, and that is people make too much of a push-pull relationship out of it with pricing. Pricing goes up; hence, the RIG has to come down. That is too simplistic. So, the point that François and I were trying to make to you is that it's a number of contributing factors. Clearly, the high comparables from previous year are a big feature of that. Then we have supply chain constraints, and those are also uneven. So, for example, AOA is one of the zones that was hit more by it. Then we have the pricing, which clearly there has been some trading down, and that's something we have to face. And then we have the voluntary actions here that come from SKU rationalization across all Zones, but in particular, for AOA. So, it's really, to our count, 4 major buckets that was feeding that limited and muted RIG development. But let me hand it to François for some more detail.

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

Just to reinforce what Mark is saying as well, if you look at it on the high base of comparison, we can clearly see when we look at the development of our sales and our growth by category, everything is normalizing post COVID. If you look at at-home consumption, everything that we have there is actually having negative RIG developments. And everything that is out-of-home is having significant growth levels today, which is clearly the evidence that the low level of RIG that we see now is clearly the consequence of the normalization of the post-COVID era.

And I just want to say one more word on Nespresso and NHS. We are not concerned by the development there. If you look at Nespresso in the first 9 months, we are sales-wise on a comparative base, 20% above where we were in 2019 in sales. So, this is the evidence that the business is not suffering over the medium term. It's just a consequence of once again, this soft landing post-COVID. And we are with volume levels, which are above pre-pandemic level. NHS, exactly the same thing. We have gone to over 2 years of strong double digit, even last year, it was almost 20% growth during the pandemic, which is the reason why you can see a negative RIG this year, but no specific concern there.

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

Next question is from John Ennis at Goldman Sachs.

Questions on:	**PetCare effect of future increase in capacity**

John Ennis, Goldman Sachs:

I have a question on PetCare, please, which I guess has been a standout performer for a while now. I guess, look, we've seen a number of capacity announcements over the last year or so from you, Hills, Freshpet, Mars, et cetera, the list goes on. So, when you think about this capacity coming on stream over the next 3 years, I guess, what does it mean for the industry? Does it create promotional pressure? Is it going to create an increase in SKU fragmentation again, or does it simply get absorbed by the anticipated volume growth you are forecasting for the industry? I'm just very keen to hear your thoughts on what all this new capacity is going to mean for industry growth outlook.

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

Thanks, John, and obviously, when we greenlighted those investments over the past few years, this whole notion of future supply and avoiding a glut and oversupply and idle capacity was, of course, high in our minds because those are pretty significant CapEx investments -- and with some of the construction inflation we're seeing now, they have become even more pricey. But I think this is where the very strong underlying growth dynamics of PetCare come in as a saving grace. And this is independent of the onetime step-up that we've seen as a result of COVID. There are some pretty long-term growth drivers here, building on emerging markets and the calorific conversion that we're seeing there when people turn to dedicated pet food as opposed to feeding the pet with household food waste. And in developed markets, we're seeing ever more premiumization and interest in higher value offerings. And those two growth drivers continue to apply. They were already in place before COVID. They continue to apply now.

So clearly, when we did some sensitivity analysis, it was very clear that even if some other people also have significant capacity investments and even if maybe we design things a tad too large and if there's a temporary demand downturn, eventually you will grow into it. There's no question. And hence, any pressure here, if anything at all, will only be short term. In our case, I think we were running pretty close to capacity limits already. And if anything, we probably waited a little bit too long because no one saw COVID coming. Then, of course, we accelerated those investments. But I'm not concerned going forward here that it would lead to significant oversupply and price pressure simply because the category dynamics are so great.

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

Next question is from Guillaume Delmas at UBS.

Questions on:	**Managing tension between affordability and re-building margins RIG in Western Europe**

Guillaume Delmas, UBS:

Two questions for me, please. The first one, Mark, is on Nestlé responsible pricing approach, so ensuring your products remain affordable. My question here would be, how do you reconcile this commitment and the comments you made in late July about not having a longer-term margin reset, which seems to indicate a strong focus internally on rapidly restoring your level of profitability? So how to reconcile this at least apparent tension between affordability and rebuilding margins. Should we read into this that you may be looking at stepping up your productivity and efficiency efforts going forward?

Then my second question is going back on RIG, but this time zooming in on Western Europe. Because if I look at your performance in mature markets, RIG seems to have slightly deteriorated in Q3 despite North America improving quite significantly in the third quarter on the RIG front. So, wondering what you've seen in the quarter in Western Europe in terms of maybe trading down potential delisting or maybe this impact on SKU optimization? So, any color on this would be helpful.

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

Look, on the first one, when we talk about responsible pricing in an inflationary setting, I think most of it has to do with timing. And I think you've seen this play out over the last 1.5 years where we were not fully holding up our gross margin, day 1, and that was unavoidable. And that means we're not passing on all the inflation right away. That we were also very clear that eventually, we will have to catch up because what we don't want to do is permanently weaken the company and make it live on a lower gross margin level or profit margin level when it comes to the operating profit margin. To me, it's about timing. And I think especially in more high inflation emerging markets, people are used to that. Over time, the salaries and the incomes are inflating too. So, it's more about the fact that you keep things affordable when prices are rising, so that the salary levels and disposable income can catch up and affordability is assured. So, it's time as opposed to absolute amounts that I think make this approach special. And I think in Food and Beverage, it is almost a social responsibility, and I think we've been living it in this period. For Western Europe, let me hand it to François for some more detail.

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

Guillaume, in Western Europe, actually, our RIG has been fairly resilient around 1.5%. You have seen that we have done less relative to the U.S. Actually, we are a little bit north of 5% in pricing, while we are north of 10% in the U.S. So it's going to take a little bit more time in Western Europe to implement pricing. This is also part of responsible pricing as well to spread it over time so that consumer can absorb it. And in the U.S.,usually you can do things a little bit faster as well.

So we have not seen really clear evidence of down-trading in Europe. We had actually limited impact as well of delisting, given that we have had a very staged approach in terms of pricing in Europe, which we did not go for big amounts in one go, but spread it over time. I think it has proven to be fairly efficient. Trading down, we expect, though, in Europe, we are concerned by the outlook in Western Europe, especially so that the energy crisis that is coming is essentially a European one that will hit consumer purchasing power. So we are a little bit more concerned for Q4, Q1, Q2 next year, to be seen. But so far, so good, but something we are monitoring very closely.

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

Next question is from Céline Pannuti at JPMorgan.

Questions on:	**Volume and mix in 2023** **Cost inflation**

Céline Pannuti, JPMorgan:

My first question is in fact a rebound on the volume and mix commentary. Mark, you said in your remarks that you expect next year a healthy development of volume and mix. I would interpret that's clearly above 0% for the RIG in '23. So, I just want to know what kind of down-trading impact are you factoring when you are seeing that.

My second question, you also mentioned that pricing will accelerate next year. Can we have a bit of a view of what kind of cost inflation you bake in when you say that? And with regard to discussion with retailers, is it getting harder you think, to pass on those price increases?

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

Céline, I'm happy to comment. On the volume mix, I just want to be clear, this did not constitute guidance. And the choice of words was 'we're working on this' because we are very much focused on healthy RIG development and RIG, as you know, is the sum of volume and mix. So, I wanted to reassure everyone that we're not turning into an organization where it's all about short-term price taking at the expense of RIG. And so, we're working on this, but specifically, what we expect then for the next year, in a volatile environment like this, I think there's good reason to wait then for February and to give you then our expectations.

Likewise, on the pricing, I didn't mean to indicate that our pricing will yet accelerate from here. What I was trying to indicate is that pricing will need to continue when it comes to the remainder of this year and next year as we're still in catch-up mode towards repairing and restoring our gross margin. But I didn't want to guide anyone specifically whether the pricing pace would stay the same, accelerate or slow down. So, I hope that's helpful.

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

Next question is from Patrick Schwendimann at Zurcher Kantonalbank.

Question on:	**RIG expectation for the next quarters** **Margin development in H2**

Patrik Schwendimann, Zürcher Kantonalbank:

Patrik from Zurich Kantonalbank. Again, on the RIG question, would it be a fair assumption to expect a slight negative RIG for the next couple of quarters because of these high comps and because of this SKU effect? That's my first question.

And second question, in terms of the margin development, Mark, you have mentioned before that you want to have a full margin recovery over time, with today's knowledge, do we believe there's already a first step in the right direction possible in H2 and in '23?

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

Patrik, I would love to be helpful. But as you know, with our Q3 update, all we're doing is give you the latest on our sales numbers. You've seen us confirm our other aspects of the guidance, including the underlying trading operating profit margin, but I wouldn't want to speculate on where we stand now specifically when it comes to improving on that. And for the first question on RIG, maybe I'll hand it over to François.

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

Patrik, on the RIG, we don't provide any guidance on the RIG by quarter. The only thing is that you know that already, but in Q4, the comps are not necessarily easier than they were in Q3 because we had a RIG of 4% last year. It was 4.4% in Q3 last year. So, it's pretty equivalent. This is almost 2x what we had experienced pre-COVID level. So, which means that the pressure on RIG coming from the comps remains at least for one quarter, the coming one. So, we are really working to preserve RIG, as Mark indicated earlier, to preserve it into positive territories. And we are working on the two components as well. Mix is still in positive territories, which is a good indication of our capacity to innovate, our capacity to premiumize as well. This is largely where we are creating value, so very happy with that.

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

Next question is from Bruno Monteyne at Bernstein.

Questions on:	**Normalization of demand** **Areas most at risk of downtrading**

Bruno Monteyne, Sanford C. Bernstein:

Just coming back on the first impact you talked about, which is the normalization of the very high demand in several areas during COVID. How many more quarters should we expect of that normalization? Is the quarter four the last quarter the normalization, or do you think that can last well into next year?

My second question is you did mention that it's largely this normalization, but you did also mention some price elasticity and downtrading. If you had to look for downtrading to private label or price elasticities going badly, which areas do you see it in? And can you quantify how big it is in those potentially problematic areas?

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

So, the normalization of COVID, I think probably one more quarter, Q4. After that, I think it starts to normalize because it will correspond to the 3-year when COVID started, so I think that we should be back to a normal situation.

As far as elasticity is concerned, so as we have said, we have not seen much yet. It is, I would say, less a function of geography so far. And if you look at the example of emerging markets, they have proven to be very resilient in spite of the fact that affordability matters more, but that shows the power of our brands as well. So, we did not see much elasticity in emerging markets. We are, as I said, from a geography point of view, more concerned about Europe in the next couple of quarters because of the energy crisis.

If we look at it by category, wherever we saw a little bit early signs of elasticity is probably in Dairy and Food. That's probably where we are less premiumized as well. If you take categories where we are more premiumized like Coffee, like PetCare, obviously, like Water with our premium waters, we saw less elasticity as a consequence.

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

Maybe, Bruno, if I can build on a few thoughts here, I think one of the benefits of having a number of brands at different price points is that even when people do trade down, it doesn't mean automatically we're losing those consumers. There's a good chance to catch them at a different price point. And then another thought on private label, this is a time when you have several trends now, overlaying each other. So, one is the post-COVID normalization and the other one is supply chain inflation. As you know, private label did suffer during COVID times. And so, there was going to be some recovery to be expected anyways. So not all of the recovery has to do with inflation. Some of it is simply the normalization of their supply chains. And as you can imagine, when you have several of these trends overlaying each other, it's sometimes pretty hard to read out exactly which part is due to which. But do keep in mind that some of it is the normal post-COVID recovery of private label.

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

Next question is from James Edwardes Jones at RBC.

Questions on: Price gap between Nestlé brands and private label
VMS slowdown

James Edwardes Jones, RBC :

Carrying on the private label point, are you able to say anything about the price gap between your brand and private label. Has it narrowed and to what extent has it narrowed?

And also on VMS, you attributed to third quarter slowdown obviously to tough comps. Given the relatively discretionary nature of the category, how confident are you that it's not anything more than that?

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

So, James, I think on VMS, feeling really good that this is very similar story to what we've seen in Nespresso, that we've seen outsized growth here for two years when people were really trying, in particular, to strengthen their immune systems. There's plenty of other health objectives that people are pursuing, the interest when it comes to Google searches and all sorts of consumer questions on optimizing your health outcomes. That one has not gone away. There's a willingness to pay for that. And so, in my opinion, this is truly a lapping issue. And as I mentioned, we properly reflected this when we did deals during the pandemic since we knew that at some point this period of outsized growth was coming to an end. We reflected this in our business models. And we're very happy overall with the branding opportunity that VMS affords.

So as François indicated, Q4 is still a quarter, where, of course, we're seeing RIG-related high comps. But over time, I think with '23 and beyond, you will see the more normalized growth of a category like this shine through. And then with regards to the first question, let me hand it to François.

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

James, on the private label one, so inflationary pressure impacts all players in the industry, including private labels. And actually, the pressure is typically more pronounced for private labels since input cost typically represent a higher proportion of their sales. So as a consequence, what we have seen since the beginning of the year is private labels had to implement significantly higher percentage of increase than branded products. It was typically around 2x more than what we did. So as a consequence, we don't think that the price gap between private labels and branded products has neither narrowed nor extended. It's probably the same as before.

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

And James, maybe one additional thought. So clearly, I mean it's hard to make these statements across all categories and geographies, but I'm also very much in support of what François said. The one other one to watch that I think is playing in our favor is the out-of-home and in particular eating out in restaurants or having a coffee at a bar or whatever. So clearly, that's where you're also seeing significant inflation and you're also seeing sometimes additional cost issues because of labor cost and sometimes also truly service quality issues because of labor scarcity. And so, I think as families have a harder time here making ends meet, one thing that can be expected is that they reduce the number of out-of-home occasions. And that actually is a bit of a tailwind and will be a bit of a tailwind towards in-home consumption, which, of course, favors us with the stronger market shares in home consumption.

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

Next question is from Jeremy Fialko at HSBC.

Questions on:	**Tailwinds for RIG in 2023** **Market share for Nespresso and Starbucks vs compatibles**

Jeremy Fialko, HSBC:

A couple of questions from my side. When you look at the RIG, I think there's been a lot of discussion around kind of elasticity, comps, SKU rationalization, et cetera. et cetera. But when you look into subsequent quarters 2023, can you talk about any particular tailwinds that there might be on the RIG side? So, for example, the supply chain sorting out, the capacity coming online, any areas where you've got easy comps. Perhaps you could elaborate on those areas, if any.

And then secondly, on Nespresso, you've obviously been quite confident in terms of the underlying demand. Perhaps you could just then, when you look at the market share, so Nespresso, Starbucks then the generics, there's been no real change in terms of the market shares of the different players producing Nespresso compatible capsules and that you are kind of holding or gaining share within that?

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

Jeremy, I'll hand it to François for the second question. On the first one, just let me leave you with a high level of thought, and that is the only one thing in this turbulent time that you can say a relatively good degree of certainty for '23 is that this pressure from these extraordinarily high comps on RIG that, that one is going to be less in '23 than it was in '22. That's assuming that the COVID pandemic continues to ease now and doesn't get a lot worse. But that's the only thing you can say. On everything else, I think the visibility at this volatile time is so low that at this point, I wouldn't want to speculate on it.

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

So, on Nespresso also, I reiterate the fact that we are confident about where we are with Nespresso today, with organic sales growth that are around 20% higher than they were three years ago. This is only for Nespresso on a comparable basis and consumption is above pre-pandemic level. That does not take into account the additional sales we have through Starbucks and other Nespresso compatible capsules. And just for your information, as you know, we have actually gained with Starbucks and other Nespresso compatible capsules, about 20% of the compatible market in three years worldwide, which is quite significant. And we need to look at the market share in a comprehensive way. And I think market share had been relatively stable or even we have gained a bit as a consequence of this compatible market. So, no concern on that front.

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

Next question is from James Targett at Berenberg.

Questions on:	**Performance of Premium, mainstream and value segments** **Market share**

James Targett, Berenberg:

Two questions from me. Just firstly, could you give us some color on the relative performance in Q3 between your premium and mainstream and value segments, if there's any big change in trends there?

And then secondly, just on competitiveness. Are you seeing an impact in market shares following the recent pricing increases? And what kind of share losses would you tolerate before you look to adjust price levels?

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

James, let me start out on the second one and then hand it to François for the first one. I think a good example where you see a reaction was our Prepared meals in the U.S., where we clearly took some of the pricing early, and we saw some of our competitors do it later. And so yes, short term, there was a RIG and volume reaction. But as you see from that description, it's not about how much are we willing to accept here in a volume slowdown, because over time this inflation is so significant that it boils down to timing decisions. I mean it's not like people can afford to completely forgo the pricing, and then just smile all the way to the bank based on the share that they're gaining. It's too big. And that's why I think pricing early has turned out to be the right strategy, and we fully stand by it. And over time then we can expect to regain some of the shares that short term may get lost.

One more reason for not overinterpreting short-term market share data here because with this pricing action going on and pretty significant pricing action, you have pretty significant ups and downs. But that's why the timing one is so specific. And that specific example is also a good explanation why you saw some slowdown here on Prepared meals as you look at this year.

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

James, a few words on premium products. So premium products, as you know, account for about 1/3 of our sales. That's significant development versus where we were in 2012, we were only at 11%. If we look at since the beginning of the year, premium products grew slightly, very slightly below the group average. But it's essentially coming from a high base of comparison with two consecutive years of double-digit growth. So, we had very attractive growth in premium products driven by Purina PetCare, Water as well, Infant Nutrition. But as we explained earlier, Nespresso and Nestlé Health Science were particularly impacted by the high base of comparison in the context of the pandemic with a high level of at-home consumption and the search for health immunity benefits.

What is important as well, as far as premium products are concerned, is to say that we have not seen any demand elasticity linked to pricing for this category which can be easily understood. Because the level of price increase that we had to implement for premium products is more limited. And on the top of it, premium consumers typically have less financial constraints. So, no concern on that one.

Maybe just a few words on affordability at the other extreme of the consumer pyramid. They are becoming obviously more relevant to consumers at the time of inflation and economic pressure. And this is the reason why we have increased our level of offerings for affordable products, and which is entirely focused on emerging markets, and they have been very resilient. And if we look at the 9 months, they have actually grown double digit, 10.8%, led primarily by AOA. And the growth in affordable offerings was broad-based across most categories, but with particularly strong growth in Cooking aids and Beverages.

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

Next question is from Pinar Ergun, Morgan Stanley.

Questions on:	**Supply chain** **PetCare acquisitions**

Pinar Ergun, Morgan Stanley:

Two questions from me. The first one is on the supply chain. Can you please discuss the latest dynamics here and whether constraints have been easing in any parts of the world? How have your inventory management practices changed, if at all, since H1?

And the second one is on Pet food. There's been an increasing level of speculative corporate action around U.S. PetCare assets in the media. How do you think about potential consolidation in this industry? And would you consider expanding your reach further in PetCare through new acquisitions? Or are you focusing primarily on organic growth?

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

Thanks, Pinar. So, on supply chain, let me share this one with François. One element where we've seen a bit of easing is around global container shipping rates and availability. So, as you know, that was a major issue in 2021. I think that one has relaxed quite a bit. And it's not quite back down to where it was before. The price rises started about 1½ to 2 years ago, but certainly a lot better than we saw last year. At the moment, some of the key supply chain issues are the ones where we had run into our own capacity constraints. So, think about PetCare in the U.S. or think about PetCare in Australia that also was kind of dampening our volume and RIG growth in AOA for the third quarter. And then, of course, obviously, we will need to watch the geopolitical situation for any surprises that may be happening. But I think compared to last year and some of the shipping mayhem, we certainly have seen the situation relax somewhat.

You then have some very interesting one-offs. So, for example, when it comes to Waters, all of a sudden, the shortness on CO_2, which comes – when it relates to carbonated offerings, is of course a critical ingredient. That has to do with industrial gas suppliers no longer focusing on this because of high energy costs. In this unsettled world, you always have some short-term surprises to deal with.

Related to Pet food, obviously Pet food is one of our core areas. We are essentially playing in all of the key segments, but if there are ways to meaningfully improve our offering and our footprint in it, we would be open to it. I think as always, we have a duty to study anything that specifically comes to market. I wouldn't want to speculate on any of the speculation that's running around and rumors, but generally, when something happens, we feel a duty to look at opportunities. But obviously, for large categories like this, we also have to check very carefully for any relevant antitrust limits.

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

Pinar, François speaking. Just a few words on the inventory management. We have decided at the beginning of COVID to increase our inventory level in the context of significant shortages of raw material, packaging material. I think it was absolutely the right decision. We saw it that we had actually far less issues to supply the market than most of our competitors. We talked about it, it helped us to gain market share as well over the last two years. So clearly, the right thing to do as things are normalizing a bit, like Mark was saying. On the transportation side. I think it will normalize on our capacity constraints, internal ones over time. We have already started to work over the last couple of months to review our inventory level and come back to where we were two years ago. Just for your information, you could see it anyway. At the end of June, we had CHF 5.5 billion higher inventory level than 2 ½ years ago. Half of it is coming from the increase in the inflation in raw material and packaging material, but half of it was linked to the fact that we wanted to secure our supply, once again the right thing to do. So, it's going to take a little bit of time, but going to take probably a few quarters to come back to a normal situation depending on how things evolve in the market as well. But clearly something we are focusing upon today.

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

Next question is from David Hayes at Société Générale.

Question on:	**Supply chain dynamics**

David Hayes, Société Générale:

Just one for me, just following up on the supply chain dynamics, are the supply chain constraints improving as you expect them to? And the reason I guess I'm asking is I think you talked in the first half about lower marketing and brand spend because there's no point spending into gaining more demand if you can't satisfy it. But just thinking about that commitment you made for higher brand spend in the second half. Is that still the same? Is the supply chain constraint improvement such that you're spending as you planned to do when you talked about it back in July?

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

Thanks, David. And generally, as François indicated in the summer in our Q2 conference call, clearly we are targeting higher consumer-facing marketing spend in the second half compared to the first half. And so, we indicated our willingness to reaccelerate. As we mentioned here in this call, you still have select pockets where we are supply chain constrained particularly in the Pet food area. But let me give you another one, think about Hot Pockets where I think you may have seen some of the news about the factory fire we had earlier this year. Clearly, where those continue to apply, I think, a more muted approach on marketing spend makes sense. And obviously, on everything else, we're trying with supply chains easing to also hit the accelerator again and be sure that we're staying very relevant and high in everyone's awareness with our brands.

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

Next question is from Tom Sykes at Deutsche Bank.

Questions on:	**Promotional activity levels** **European margin**

Thomas Sykes, Deutsche Bank:

Just firstly, on list prices and how sticky you see your list prices when commodities come down. What discussions are you having with retailers about the level of promotional activity that you would have to have the other side, as the raw material pressures do ease? And just to be clear, in terms of the RIG calculation or promotional activity that just goes into net price, that doesn't have an impact on the RIG question.

And then you've mentioned several times the weakness that you're expecting or the potential difficulties in Europe. And obviously, the timing of price increases and being able to catch up, Europe's got potentially weaker labor productivity. Is it fair to say that we should expect the European margin to be a bit weaker year-on-year in H2 versus H1 at all, please?

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

So, Tom, on the first question, let me just say, it's important that we do not overinterpret some temporary easing on some of the commodity input costs that we are seeing, that we saw this summer. Because even with some of the temporary easing, when you look at the full year development compared to the same period last year, then there's still quite a gap that needs to be filled. So, this is a difference between a commodity trader and us where, yes, for a trader, if something eases from one week to another, that's relevant. For us, clearly, things are not yet coming down to the levels that we have seen before the start of the inflation. And even if there is an easing, we don't feel the benefit the next week because typically, a certain amount of your inputs are hedged and hence for a number of months you're still sitting on those forward contracts and the higher input costs that they imply.

So that's why when you look at the full year effect and some of the ongoing hedging, clearly, there's momentum on the input cost increases and hence, on pricing for the rest of this year and going into '23. There's no question about that. And hence, any question here on how lower input costs would translate then into pricing going forward, that's still quite a while away. We're still talking about increases here, and that math applies pretty much to every other manufacturer as well. And then maybe for the second question, I'll refer to François.

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

Just to complement what Mark is saying as well, we are not down in terms of input cost inflation because there is one item that will come to a larger extent at the beginning of next year, which is salary and wages, because typically, it comes at the beginning of the year. So, you may have some commodities going down. But energy prices are another item that goes up as well.

On Europe, you said it. We have done less pricing year-to-date. And by the way, for your information as well, traditionally, we could do only one batch of price increase a year in Europe and this year, we are doing more than that. So, we have increased prices a little bit further during the year. But we spread it over the year and traditionally, we do again some at the beginning of next year. So, I don't want to comment on the margin of Europe specifically because we don't guide at that level, but as we indicated earlier, we are spreading pricing in Europe over a longer period of time.

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

Next question is from Jon Cox at Kepler.

Questions on:	**SKU volume impact** **Gas disruption in Europe**

Jon Cox, Kepler Cheuvreux:

A couple of questions for you. Just on the SKU volume impact, you mentioned we'll hear more about it when we get to Barcelona. Wondering if you can just give us a rough idea of what that may be in terms of 1 point or 0.5 point, or just something. And as part of that, is there any reason why you can't reiterate the Nestlé model for next year in terms of that mid-single-digit organic sales growth, incremental margin gains? Any reason why you wouldn't be able to mention that?

And just last one on the gas situation in Europe, I know you've been asked 100 times about it, but just wondering what your preparedness is for any gas disruption we may have in Europe over the winter.

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

Yes, thanks, Jon. And to start with the second one. Obviously, a lot of work has gone into each and every one of our 110 European manufacturing facilities to be sure that we look into alternative energy sources, just in case there is an interruption in that. Also, we're using every opportunity to lower the total energy input needed for these factories because, frankly, it also comes down to simply saving energy, which is good business and also an act of solidarity at this time of energy insecurity. So, all spring, summer and fall, we worked really hard on this. And I think we're sitting now on some very good preparedness plans and reduction plans for each of these facilities, and that's an ongoing effort. Whether that's going to be enough or not, clearly, there's lots of unknowns here on how difficult this winter is going to be. And I think this is the kind of uncertainty that we are facing in our personal lives now as we look at the winter here and how it will unfold. So, this is why it's hard to provide a specific forecast.

And maybe I'll hand it to François for the other question.

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

Jon, on the SKU and volume impact, so these activities that we are doing at SKU level, they have a positive impact on margin. This is actually the objective. And they have a marginal negative impact on OG, organic growth on volume and RIG. I cannot quantify it at this stage because this is part of what we will share in Barcelona, but we started this program at the beginning of Q2, so it did not have a real impact in Q2. Started to have some impact in Q3, as we said, more specifically for AOA, which is the main reason why we moved into negative territory for AOA specifically in Q3. But once again, we will share more information during our Barcelona conference.

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

We have 2 remaining questions, one from Andreas von Arx and the other one from Warren at Barclays. Andreas, please go first, and then Warren will follow.

Question on:	Resilience of PetCare Category

Andreas von Arx, Baader-Helvea:

So, on PetCare, in the recession of 2009, this has been a very resilient category. However, it is a different category today. It's much more premium, much larger, different distribution channels and a different competitive environment. Do you see any reasons why in an upcoming recession, the consumers might react different than in 2009, or do you still believe this is one of the most recession-proof category?

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

Thanks, Andreas. And the short and reassuring answer is that it certainly is one of our more resilient categories. I think many crises have proven that in the past. And the world financial crisis is not the only comparison point because as we look around the world, we've also seen in select markets temporary and more limited crisis. And generally, Pet food has continued to hold up really well there.

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

Warren, go ahead. You are the last question.

Questions on:	Buitoni update and Toll House recall China Infant formula

Warren Ackerman, Barclays:

A couple of follow-ups. The first one is just, Mark, I know you get a question about Buitoni a lot. But is there any update on this? Because clearly, it's a very high topic for investors. Are we still waiting for the French investigation for you to make a formal statement? I know it's very sensitive, but it would be great if we could any more color that you have. And I also note that Toll House had a recall in the U.S. on plastic. I'm just wondering whether -- given the situation in France and now that, where we are on all of this.

And then secondly, on China Infant formula. We didn't get a chance to talk much about that, but double-digit growth, very impressive in the quarter. Can you maybe elaborate a little bit about what's going on with Illuma and Nan? Market share is improving, is that just share gains, or are you seeing any signs that the market is improving?

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

So clearly, on Buitoni, this continues to be a very high priority item. I would like to do the same as I did in previous conference calls, and that is express my full sympathy and support to all the individuals and families that were affected by this. We take this very seriously and are in the process of working up all the internal details, fully cooperating, of course, with the authorities and making sure it's something that this doesn't happen again.
Over the summer, you will have also seen the news flow on the public apology that we issued, also a victim support fund. So, without taking away from any of the potential legal claims against us, we wanted to be sure that even in the short-term any cash needs are fully covered. So, on the inside and the outside, I think we are giving this a lot of visibility and priority. And as I mentioned in previous calls, you should not take from this very regrettable incident the conclusion that quality is something that we don't fully focus on. In fact, it's one of our highest priority internal items, and we'll continue to stay very focused on it. In that light, you should also see that latest voluntary recall in the U.S. where, to my knowledge, fortunately, no one got injured. This was a very early voluntary recall as soon as we heard some of the consumer complaints, but very different subject matter compared to what we're dealing with in France.

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

Warren, on Infant Nutrition in China. So, we are starting to get the results of what we have done over the last two years. To restructure that business. We launched new products. We went into Tier 3, Tier 4 cities. We restructured our distributor network, we changed the management as well. We always said that it would take some time and so very happy to see that we are coming back and starting to gain market share. More specifically, by the way, on stages 1 and 2, which is very positive for the future because it should probably translate into market share gains as well for Level 3. We are not fully done yet. It's still something which is in progress. But very encouraged by that. As you know, the market is a little bit under pressure because of volume decline with less births. But in that context, to gain market share, it's actually very encouraging, very positive.

End of Q&A session

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

With no further questions, we come to an end of our session today. So, we thank you again for the interest in Nestlé. As usual, if you have further questions, don't hesitate to be in contact with our IR team.

Wish you all the best. Stay safe and healthy.

End of Transcript