NESTLÉ S.A.

2022 FULL YEAR RESULTS CONFERENCE CALL TRANSCRIPT

16th February 2023 14:00 CET

Speakers:

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

Slide: Title slide

Good afternoon, and good morning to everyone. A warm welcome to the Nestlé Full Year 2022 results webcast and thanks for joining. I'm Luca Borlini, Head of Nestlé Investor Relations. Today, I'm joined by our CEO, Mark Schneider and our CFO, François Roger. Mark will begin with an overview of 2022 and discuss the 2023 guidance. François will follow with a review of the full year 2022 sales and profit figures. We will then open up 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:

Slide: Title slide

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

It's good to update you today on where we are. As you can imagine, a lot has happened in this turbulent and demanding year. And all the more, I'm pleased to say that Nestlé has been able to prove its resilience and dependability at this very demanding time.

Slide: Key messages

Let’s move to some of our key messages here. The slides I'll walk through are similar to the ones from the press conference this morning. Where we've seen insights from this morning, we're also trying to offer some value added and some reaction on our part in order to advance the debate. So clearly, from our perspective, when it comes to the financial performance, we consider it very resilient in a volatile and turbulent time.

Organic sales growth of 8.3% was smack in the middle of our guided range of 8% to 8.5%. It was also noteworthy and positive that the real internal growth, so the sum of volume and mix, came up ever so slightly positive for the full year. The mix, which of course, is a very important indicator for us since it measures the rate of progress and innovation, outweighing the negative coming from volume development.

I know that there's a lot of concern among you about the volume and RIG development, specifically in the fourth quarter. I hope between François and me, we will be able to address some of that. We are obviously a lot less spooked about this than you are because I think there are perfectly explainable reasons that are not solely related to pricing that were leading to this development.

Underlying trading operating profit margin, it decreased as we guided you to expect throughout the year due to significant inflation, but I think we were able to limit the decrease to a better extent than anticipated, 17.1%, certainly above what outside estimates were. And I think what you're seeing is a significant focus on cost efficiencies, growth leverage to offset some of the effects of cost inflation.

So very pleased with that result, tremendous effort from the team. Again, pointing out the resilience of our financials at a very demanding time. Underlying earnings per share growth, 9.4%. So very close to the top end of that 6% to 10% constant currency underlying share growth rate that we led you to expect as part of our Barcelona Investor Day. As you saw from our guidance, this is also what we're confirming as a range again for this year. So here again, on the underlying earnings per share growth rate also a very consistent dependable performance.

We did not give up when it comes to building for the long term in this year. So clearly, when it comes to capex, in particular, but also innovation, sustainability, lots of good forward-looking spend that, of course, will deliver its benefits in the future years. Then also continued progress when it comes to portfolio rotation, where we are now at about 22% of our portfolio compared to the 2017 baseline.

You will see later that we made good progress on the Good For You, Good For The Planet agenda. Here is another item where, of course, at a time of inflation and affordability concerns, it would have been easy to cut corners. We chose not to do that because these are important strategic initiatives that, over time, the company will get measured on by consumers and the public at large, and, also you as investors and hence, disciplined, continued progress in that arena is important to us.

Then regarding the dividend, I think we're sharing some of the benefits of our value creation here with a dividend increase of 15 centimes to CHF 2.95. So, all throughout, I think, very consistent performance at a time that was marked by so much turbulence and volatility.

I also would like to thank team Nestlé for a tremendous job delivering this. Tremendous focus inside the company; operational discipline, making things happen as agreed and really keeping their eyes on the ball. Over and above that, I think whatever capacity is available towards the strategic development of the company, we're devoting it to that because we know that we're not just managing for today. We are also managing for tomorrow and for positioning the company well for the future.

Slide: 2022 achievements

With this, I would like to move on to the 2022 achievements in particular. And clearly, PetCare does stand out as the one category that delivered over and above. No question about it. To me, nonetheless, the second item Coffee is one that's worthy to point out. 8.1% is a very resilient number in a year that saw, on the one hand, spiking coffee prices, and on the other hand, also a normalization in this post-COVID world for so many markets around the world. Where clearly, the in-home consumption did, first of all, lap very strong quarters from the year '21, and also the in-home consumption gave way to at least some partial out-of-home consumption where, as you know, our market shares are less. So, in light of all of that, 8.1%, very strong performance. In particular, I continue to be very pleased with how the Starbucks Global Coffee Alliance is shaping up and continues to develop. We've been developing 1.5 billion of incremental sales in this line of business since 2018.

Emerging markets are clearly a base of stability. We're seeing in addition to the pricing-led growth, also very good RIG development in those markets. So, I think our strong presence in emerging markets is clearly paying off at this time. Then out-of-home channels showing a tremendous rebound. We're now above 2019 levels. Having said that, the rebound was a lot stronger in the first 9 months. Then we see some degree of normalization setting in, in the fourth quarter, which is simply a function of how the fourth quarter of '21 shaped up. Then also, we're seeing the negative impact in the fourth quarter out-of-home growth rate coming from China where, of course, the country was going through, clearly, some advanced COVID-related reductions. As a result of that, out-of-home consumption was quite muted.

We did make good progress. Moving on to the next section regarding underperforming businesses. China Infant Nutrition, a lot of progress done cleaning up the distribution system, simplifying it. SKU rationalization, a much clearer price-point positioning of our various brands and offerings and again, the results following on the heels of that. So that was very reassuring at a time when the birth rate in the Chinese market is still quite low.

Then one thing that I'll talk about later some more, that we discussed already in Barcelona and as part of our Q3 investor call, the streamlining of the SKU portfolio. That one was originally born as a consequence of some of the supply chain limitations we've seen. I think it has now grown into a full-blown strategic initiative that really gives us lots of bottom-line benefits, but also expected top-line benefits down the road. More on that later.

On portfolio management, two items worthy to point out. One is that new focus of Nestlé Health Science on Consumer Care and Medical Nutrition with Consumer Care breaking down into active nutrition and vitamins, minerals and supplements. As you know, we did not achieve our objectives with the Aimmune acquisition, and we are looking into alternatives for that. I think that new strategic positioning builds on what Nestlé Health Science is best at. Then there's lots of scaling up opportunity in those three bases going forward, and we'll focus on that.

So again, we regret that we did not meet our objectives here, but I also believe we found a good way out when it comes to future strategic position, ensuring the continued success story of Nestlé Health Science.

In Food and on Freshly, a similar situation, as you know, that business, while it clearly flew in the early days of COVID, that so, direct-to-consumer focus was too narrow. The products, however, were in pretty strong demand. So, combining with a firm, Kettle Cuisine, and now creating a fresh food business-to-business platform, in my opinion, is very much aligned with the needs of the times.

So, this would service foodservice operators that don't want to prepare fresh food on site, be it as a result of labor shortages or cost pressures. We believe that this is a niche that's very much in demand and that we can successfully exploit with this company going forward. So quite bullish on that.

I think what you're seeing here is two examples of us addressing situations that were not performing well early, but then also finding the proper strategic resolution going forward that ensures continued success for the company.

Slide: Good for You: continued progress on nutrition

I'll now focus on two of our strategic plans; Good for You, Good for the Planet. Let me start with Good for You and the nutrition side of things. As you know, this builds on literally 25 years of success with our Nutrition, Health and Wellness strategy. In that quarter of a century, I think we've done already a lot of progress regarding the reduction of sodium, sugar and saturated fats. It's clear that while the work goes on, there are limits. So, enjoyment-related categories will not be turned into health-related categories.

But nonetheless, across the full spectrum, a lot has been accomplished, and our research and development stays very much focused on that. Because there are limits to how much sodium, sugar and saturated fats eventually can come out, I think we also have to broaden our approach.

One is around transparency, transparency when it comes to labelling, but also when it comes to the entire portfolio. This is where we made some significant announcements from our end last fall. The first one is on global transparency. So we will rate, coming out with the report in the next few weeks, our entire global portfolio according to the Health Star Rating, which is the same one that's being used by the Access to Nutrition initiative. To our knowledge, among the major global food companies, we're the first ones to do this on the global scale to give you a good sense of where the entire portfolio stands.

Then for fourteen major markets around the world, we will use the prevalent national rating system to also provide a rating of those national portfolios. So that's, in our opinion, a key progress on the transparency front. As you know, we complemented that with a step-up in our responsible marketing initiatives and enlarged the age bracket of our marketing to children policy and go now, starting from July, from 0 to 16. We will not stop there. I think we have exciting new initiatives underway for this year.

Again, regarding targeting, we would like to work and publish with you a target number for the healthier parts of the product portfolio. So, the ones that are rated 3.5 under the health star rating system or above and give you an expected sales figure for several years down the road for that bucket.

Then the other thing we're working on, since we do believe in the future promise and potential of plant-based food, to give you a sense of where we can take that business, the plant-based food and beverage over time. So, both of these are projects that are in the works and that are forthcoming later this year.

We will also clearly continue to work on other transparency commitments and responsible marketing commitments. So, this work was not let up. All of that comes on top of ongoing work that we do, as you know, when it comes to affordable nutrition, especially in emerging markets, and also our highly successful drive on micronutrient fortification.

So, lots of work going on in this area. It is the core of what we're selling. Nutrition is, at the end of the day, when tasty and balanced diets are the core of what we're selling. So, upgrading our ambition levels here over time, I think, is important.

Slide: Good for the Planet: progress on greenhouse gas reduction

Next, under the Good for the Planet header. Obviously, lots of eco-initiatives, lots of initiatives underway that are designed to improve our sustainability footprint. But greenhouse gas emissions is clearly one that is a percent of our activities. Here also, I think after a very successful 2022, we have progress to report. I told you last year that peak carbon was behind us already. We crossed that sometime in 2019, 2020. But now we are also below the 2018 starting levels. So, when you think about our net zero road map, the one that went from 2018 and then extends to 2050, where we intend to be net zero. We're now below the baseline emission levels there from 2018. To our knowledge, one of the very few companies that has reached that milestone.

We're also on track for the 20% carbon emission reduction by 2025 versus the 2018 level. And we expect to make significant progress this year and in the next two following years. As you can imagine, in some of these initiatives, especially when it comes to planting trees, for example, in your agriculture supply chain, some of them have lead times because any carbon reduction related to that does not get counted for the first two years and only then slightly ramps up. So that's why we knew the whole progress was going to be somewhat back-end loaded. But against that backdrop, I think where we are already, we have good reasons to be happy, and we feel good about the 2025 target at this moment in time.

Slide: Key focus areas for 2023

Moving on to some key focus areas for 2023. Let me start at the center of the slide with the operational side. One thing I said at the press conference this morning in turbulent moments like these, good operations and good operational management eat strategy for breakfast. So clearly, protecting volume growth is something that's very important to us. I think our TASTY project, that we described to you and that we're expanding now, is geared towards helping that over time. We will continue to focus on driving cost efficiencies, which are very important to us. And, of course, we're also, after taking it somewhat easier on marketing investments in 2022, we will ramp up that again in 2023.

François will explain later to you that, of course, the marketing spend also needs to be seen in conjunction with the trade spend. And so, the picture may not be as bleak as you think. But nonetheless, we believe that in 2023, there is room for further marketing investments. As a branded goods company, these are very important to us.

On the strategic front, we will accelerate portfolio optimization. That is an area that's important to us. In a sense, we will have a complete scalable set of efforts from SKU optimization to the entire portfolio. I'll explain that on one of the following slides. Then continued focus on fast relevant, impactful innovation is going to be important to drive mix. Then we will continue to lead on our climate sustainability and nutrition agendas.

Financially speaking, restoring the gross margin is key, clearly, after this tremendous surge in inflation. Also, renewed focus, stronger focus on cash flow generation. We made some deliberate choices to run up inventory levels to ensure at all times that our supply chain holds up. But I think with some of the COVID fears and supply chain constraints around the world easing, now is the time to work that down again, reduce the net working capital and focus on cash flow generation.

Slide: Accelerating portfolio optimization

That brings me to the portfolio optimization slide, and this is one I'd like to spend a minute on because from what used to be a very tactical operational tool to react to supply chain shortages, this has now morphed into a major strategic and company-wide initiative that, in my opinion, has significant promise. So originally, when you had shortages, clearly, it was a choice of focusing on the articles that were most in demand with our consumers and the retail partners. This led us then to what we call, cutting the tail in order to push the head. But once we started doing that, we saw that there was tremendous promise in it, and we scaled it up and accelerated it quite a bit.

Clearly, we noticed that we haven't done that sort of exercise for a long period of time, the overall SKU portfolio had proliferated and there was tremendous promise when it comes to cost efficiencies near term and even increasing the organic growth longer term, by focusing on the items that are most in demand. So, this is what I described this morning in the press conference as a win-win-win situation where clearly, consumers are going for the most popular articles, retailers like high rotation items. And for us, having a more limited SKU line-up also means less complexity, more operational efficiency and then, of course, an even better on-shelf availability for the items that are in demand.

So, this was the starting point. From there, we took it somewhat broader and bolder and even now we start to look at entire brands and segments and geographies as itemized here. In cases where we cannot sell a business, we're not afraid of walking away from it as long as we do it right. A good example here is the Frozen food Canada business that you see the bottom left-hand corner [of the slide], that was an announcement from a few weeks ago. This is a book of business of about CHF 150 million. It's a business that was not really sellable and not really a winning proposition because we don't have our own local manufacturing in Canada. These products were made in the U.S. and then imported. Clearly, by the time you're talking transportation and you're talking currency, it was hard to turn this one into a winner. But we believe that walking away from it and winding it down over a period of two years, while being a drag on RIG and organic growth for the short term, clearly will have significant benefits for the business going forward, and that is essentially what we're interested in.

While this example may stand out size-wise, you will see lots of smaller ones where I believe making the tough choice short term, even though it does impact RIG and it does impact OG for the moment, clearly, will have benefits then down the line because you will free up capacities, you will free up supply chain, you will free up resources to focus on the proven winners and to make the most of those. That was one of the key factors, one of three, behind some of the stronger-than-expected volume reduction in Q4, because we were scaling this thing up as fast as possible.

The Frozen food Canada announcement is not among them, this was a '23 announcement, and as I said, we'll be winding this down in '23 and '24. But on a smaller, more regional scale, we've done lots of decisions already in the fall of '22 now that were impacting the RIG and the OG for the fourth quarter. But again, with a good business logic and expected benefits down the line. Then, of course, we're reallocating those resources towards high growth, high margin, high rotation products, and that is what everyone wants.

Slide: 2023 guidance

With this, I would like to turn to the 2023 guidance. I would like to confirm that we expect organic sales growth range between 6% and 8%. So, this will continue to be pricing led. We're not in a position, and I think this is in line with prior practice, to give a breakdown here between the pricing part and the RIG part. I'm asking for your understanding on that. But it will be pricing-led. Nonetheless, we're also seeing good development, especially towards the end of the year, and we're working hard when it comes to stabilising RIG.

The underlying trading operating profit margin is expected to be between 17% and 17.5%. So this is very much in line with the kind of path that we have laid out for you as part of our Barcelona Investor Conference and we expect to make meaningful progress towards that 2025 goal. That then also translates into a bracket for the underlying earnings per share growth in constant currency between 6% and 10%, so similar to the bracket that you have seen for this year.

This concludes my part of the presentation. With that, I would like to hand it to François. And then later on, we'll be happy to answer your questions.

François Xavier Roger, Nestlé S.A., Chief Financial Officer:

Slide: Title Slide

Thank you, Mark. Good morning to you all.

Slide: Resilient financial performance

Let me start with some of the key highlights for 2022. In a year shaped by volatile macroeconomic and geopolitical events, we delivered record financial results.

As you can see from the chart, our reported sales growth was strong at 8.4%, adding CHF 7.3 billion of sales. In Swiss Francs, our underlying trading operating profit increased by 6.5% or CHF 1 billion.

Underlying earnings per share growth was robust, increasing by 9.4% in constant currency to CHF 4.84. We increased our returns to shareholders to CHF 18.2 billion, the highest-ever level on an annual basis.

Slide: Full-year sales growth

Organic growth was 8.3%. Pricing increased to 8.2%, reflecting significant cost inflation. RIG was positive at 0.1%, following a high base of comparison in 2021, supply constraints and portfolio optimization actions.

Net acquisitions increased sales by 1.1%, largely related to the acquisition of the core brands of The Bountiful Company as well as Orgain.

Foreign exchange decreased sales by 0.9%, turning negative in the second half.

Total reported sales reached CHF 94.4 billion, an 8.4% increase versus last year.

Slide: Strong growth across developed and emerging markets

Turning to the distribution of growth between developed and emerging markets.

Organic growth in developed markets was 7.1%, based on increased pricing. RIG was negative following a high base of comparison in 2021.

Growth in emerging markets increased to 10.0%, with strong pricing and positive RIG. Growth was driven by Latin America, Africa and South Asia, with continued momentum for affordable offerings.

Slide: Resilient mix, volume and market share in 2022

This chart shows the evolution of our growth factors over the last five years. Overall, the group's RIG in 2022 was positive at 0.1%. In the context of significant volatility, we felt there was merit in breaking out RIG into its two components, namely mix and volume.

To enhance the quality of this analysis, we excluded Water and Health Science which results in a slightly negative RIG for 2022 of minus 0.1% on this chart. As you can see, mix has historically been a key driver of organic growth, supported by premiumization and innovation. Mix remained resilient in 2022 at 1.6%, indicating that we have seen only limited down trading by consumers to date. In 2022, pricing became the largest contributor to growth.

Looking at volume, we saw an exceptional step up in 2021, with growth almost three times higher than historical levels, in the context of elevated pandemic-related demand. This exceptionally high base of comparison and supply constraints negatively impacted our 2022 volume growth. Overall, the average volume growth for the last two years at 1% was only slightly lower than pre-pandemic levels, reflecting limited pricing elasticity to date.

The recent volume evolution is more reflective of overall market conditions. Indeed, we continue to see more than half of business cells gaining or holding market share, in spite of some supply constraints and deliberate decisions to optimize our SKU portfolio. When looking more specifically at our Billionaire Brands, which account for more than 70% of our sales and saw organic growth of 10%, we are gaining or holding share in close to 60% of business cells.

Slide: Q4-2022 RIG impacted by additional transitory factors

Looking at Q4 RIG more specifically. Beyond the high base of comparison at 4% in the fourth quarter 2021 and supply constraints, Q4 was also impacted by three additional transitory factors, which had a negative impact on RIG of around 160 basis points.

The two largest factors were the normalization of out-of-home growth and the acceleration of SKU and portfolio optimization actions.

The normalization of out-of-home growth reflects the unwinding of pandemic-related volatility. Growth decelerated from 18.3% at the nine months to 6.1% in the fourth quarter, toward a level more in line with what we saw pre-pandemic.

Second, we accelerated our SKU and portfolio optimization program, which is part of Project TASTY and has delivered almost CHF 1 billion of savings in 2022. The portfolio optimization component of this program has delivered strongly to date, giving us the confidence to broaden its scope beyond SKUs to include brands, segments and geographies. In Q4-2022, the acceleration of this program led to a more negative impact on RIG than previously communicated. Going forward, we confirm that the RIG impact is expected to be negative for H1-2023 and turn 20 basis points positive for the full year as we start to reap the benefits of growing the head. The expansion of the program will support growth and margin in 2024. The recently announced discontinuation of our Frozen food business in Canada, with annual sales of around CHF 150 million, is a good example of the new broader scope of our portfolio optimization program.

Third, Water saw a RIG decrease in the fourth quarter as a result of temporary capacity constraints. This capacity reduction follows our recent decision to upgrade our Perrier production facility. The decision will impact our Water RIG for a few more months.

Overall, while we are actively working to protect RIG in 2023, we expect RIG to be negative for the first half, as the three factors mentioned here will continue to impact our business.

Slide: Zone North America

Let's now shift focus to the results of our seven operating segments, beginning with Zone North America, where we saw 10.3% organic growth, driven by pricing of 11.6%. RIG was resilient at -1.3% in the context of a high base of comparison in 2021, supply constraints and pricing.

In the fourth quarter, RIG was -4.9%, largely impacted by portfolio optimization actions, a moderation of growth in out-of-home channels and temporary capacity constraints for *Perrier*.

The Zone saw broad-based growth contributions across strategic brands and categories, driven by pricing, strong operational execution and continued momentum in e-commerce. The Zone also saw market share gains, led by Pet food, Portioned coffee and Baby food.

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 double-digit growth, reflecting supply constraints in the market. As a reminder, we sold the Gerber Good Start brand in the fourth quarter to focus on our core baby food business, which includes purees, snacks and cereals. Premium Water posted mid single-digit growth, with a sales decrease in the fourth quarter mainly due to temporary capacity constraints.

The Zone's underlying trading operating profit margin increased by 70 basis points, with a notable improvement in the second half of the year. Pricing, growth leverage and portfolio management more than offset significant cost inflation.

Slide: Zone Europe

Next is Zone Europe. Organic growth was 7.2%, driven by pricing. RIG was positive at 0.9%, despite a high base of comparison in 2021 and supply constraints.

In a challenging and disrupted environment, Zone Europe demonstrated resilience, particularly in Ukraine, where Nestlé announced a CHF 40 million investment for a new production facility.

The Zone also continued to see market share gains in Confectionery, Pet food and Infant Nutrition.

By product category, the key growth drivers were Purina PetCare and Nestlé Professional. Within PetCare, Lily's Kitchen and Tails.com both grew by more than 20%. Sales in Water saw double-digit growth, with a sales decrease in the fourth quarter mainly due to temporary capacity constraints for Perrier. Coffee posted mid single-digit growth, led by Nescafé soluble coffee and continued strong sales developments for Starbucks by Nespresso. Infant nutrition reported double-digit growth, with strong momentum for premium infant formulas, including human milk oligosaccharides products. Garden Gourmet plant-based products continued to see double-digit growth, fueled by new product launches.

The Zone's underlying trading operating profit margin decreased by 190 basis points, as significant cost inflation and the impact of war-related supply constraints was not fully offset by pricing, growth leverage and cost efficiencies.

Slide: Zone Asia, Oceania and Africa

Moving to Zone AOA. The Zone reported high single-digit organic growth, with contributions from most geographies and categories.

Growth was driven by pricing, a continued recovery of out-of-home channels and innovation. The Zone saw market share gains in Coffee, Culinary and Infant Nutrition.

By geography, all regions posted positive growth with particular strength in South Asia, Middle East and Africa as well as Oceania.

By product category, Culinary was the largest growth contributor, led by Maggi. Sales in Nestlé Professional grew at a double-digit rate across geographies and categories, driven by increased distribution. Coffee, Cocoa and malt beverages as well as Purina PetCare all posted high single-digit growth, supported by new product launches. Growth in Infant nutrition reached a high single-digit rate, with broad-based contributions from most geographies. Ambient dairy saw a slight sales decrease, largely driven by portfolio optimization.

The Zone's underlying trading operating profit margin decreased by 110 basis points. Significant cost inflation more than offset pricing, growth leverage and disciplined cost control.

Slide: Zone Latin America

Next is Zone Latin America, which reported sustained double-digit organic growth, led by pricing of 11.6%. RIG was resilient at 1.5%, building on a high base of comparison in 2021.

The Zone's growth was broad-based and supported by strong operational execution and continued momentum of out-of-home channels. The Zone saw market share gains in Infant nutrition, Pet food and Culinary.

By geography, Brazil reported strong double-digit growth. Sales in Mexico, Chile, Colombia and the Plata region continued to grow at a double-digit rate.

By product category, Confectionery was the largest growth contributor based on strong demand for KitKat and key local brands. Purina PetCare, Coffee and Nestlé Professional all reported strong double-digit growth. Dairy posted high single-digit growth, led by fortified milks and home-baking products.

The Zone's underlying trading operating profit margin decreased by 70 basis points as cost inflation and one-off items in the second half outweighed pricing, growth leverage and disciplined cost control.

Slide: Zone Greater China

Turning to Zone Greater China. We are pleased to see significant progress on the turnaround of our business in China, following the new organizational structure and leadership.

Organic growth was 3.5%, with pricing of 2.5%. RIG was 1.0%, impacted by COVID-19-related movement restrictions. Growth was supported by strong operational execution in a challenging environment, robust demand in e-commerce channels and continued innovation.

By product category, Infant Nutrition saw high single-digit growth, with improved market share trends for NAN and Illuma. Coffee posted high single-digit growth, led by Nescafé soluble and Ready-to-drink coffee as well as Starbucks products. In Confectionery, Hsu Fu Chi reported high single-digit growth, helped by innovation, including the successful launch of savory snacks. Sales in Purina PetCare grew at a double-digit rate, with strong growth in specialty channels and e-commerce. Following movement restrictions, Nestlé Professional saw a mid single-digit sales decrease with market share gains supported by new customer enrollments and product launches.

The Zone's underlying trading operating profit margin increased by 260 basis points. Favorable mix and disciplined cost control more than offset relatively low cost inflation.

Slide: Nestlé Health Science

Next is Nestlé Health Science. The business posted mid-single-digit growth over a high base, with two consecutive years of strong double-digit growth during the pandemic. Our three-year

RIG average was 8.9%. Innovation, geographic expansion and market share gains supported growth.

Consumer care reported positive growth. Active nutrition saw double-digit sales led by healthy-aging products as well as the continued expansion of Vital Proteins and Orgain. Growth was helped by increased distribution, new product launches and geographic expansion. Vitamins, minerals and supplements saw a sales decrease impacted by a high base of comparison, particularly for immunity-related products during the pandemic.

Medical Nutrition recorded double-digit growth, with strong sales developments for pediatric and allergy products. Acute medical care products also posted strong growth based on new product launches.

By geography, sales in North America grew at a low single-digit rate. Europe reported positive growth, while other regions combined posted high single-digit growth.

The underlying trading operating profit margin of Nestlé Health Science was unchanged versus the prior year as cost synergies from newly acquired businesses, pricing and growth leverage were offset by cost inflation and growth investments.

Slide: Nespresso

Finally, Nespresso, which reported mid single-digit organic growth, driven by pricing. RIG was -1.7%, following exceptional growth of 8.2% in 2021 during the pandemic. Comparable organic sales for Nespresso are around 20% higher than they were three years ago, and the three-year average RIG was 4%.

Growth was led by broad-based momentum for the Vertuo system. Growth was also supported by a strong recovery of out-of-home channels, with continued expansion of the Momento system and 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, with growth turning positive in the fourth quarter. Other regions combined recorded high single-digit growth.

The underlying trading operating profit margin of *Nespresso* decreased by 150 basis points, impacted by cost inflation and investments in the roll-out of the *Vertuo* system, which were not fully compensated by pricing.

Slide: Broad-based growth across categories

Let's now look at product categories. Organic growth was broad-based, supported by pricing across all categories. The contrasted category dynamics in 2022 largely reflect the residual effects of COVID as consumer demand somewhat normalized by channel. Categories with greater at-home consumption, such as Dairy and Culinary, saw negative RIG over a high base of comparison. By contrast, categories and businesses with greater exposure to out-of-home channels, on-the-go consumption and impulse buying, such as Confectionery, saw a continued strong recovery.

Within Powdered and liquid beverages, Coffee saw high single-digit growth, building on a high base of comparison in 2021. Growth was broad-based across brands, segments and geographies and led by a strong recovery for out-of-home channels, which grew at a strong double-digit rate. Sales of Starbucks and Nescafé ready-to-drink products grew at a double-digit rate. Overall, sales of Starbucks products grew by 12.9% to reach CHF 3.6 billion, generating an additional CHF 1.5 billion of incremental sales since 2018. Cocoa and malt beverages reported high single-digit growth, driven by strong demand for Milo and Nesquik ready-to-drink formats.

PetCare posted its third consecutive year of double-digit growth despite supply constraints, with mid single-digit RIG. Science-based, premium and veterinary products saw strong sales developments. Growth was also supported by pricing, continued e-commerce momentum and innovation.

Nutrition and Health Science posted 7.4% growth. Infant nutrition reported 10.1% organic growth, with a strong recovery and market share gains across most geographies, particularly China. Infant formula growth was supported by continued robust demand for human milk oligosaccharides products, which grew at a double-digit rate, with sales reaching CHF 1.3 billion in the fourth year of marketing. We have already discussed Nestlé Health Science.

Prepared dishes and cooking aids saw 3.1% growth, driven by strong sales development for ambient culinary, particularly Maggi in Zone AOA. Sales in vegetarian, plant-based food grew at a mid single-digit rate. Garden Gourmet in Europe continued to see double-digit growth, while sales for Sweet Earth in North America were impacted by SKU optimization. Growth in Frozen food was slightly positive over a high base.

Milk products and Ice cream recorded 5.4% growth. The key contributors to growth were coffee creamers, affordable fortified milks and home-baking products.

Growth in Confectionery reached 9.4%, reflecting strong demand for KitKat, seasonal products and key local brands. In 2022, KitKat posted double-digit growth with over 5 billion bars sold in 87 countries.

Sales in Water grew by 11.0%, despite temporary capacity constraints.

Slide: Underlying trading operation profit margin by category

Moving now to profit margin by product category. Most categories saw a margin decline as pricing, growth leverage and efficiencies did not fully offset input cost inflation.

There are a number of exceptions though. In Infant Nutrition, pricing, growth leverage and favorable product mix drove a 160 basis point margin increase.

Confectionery also saw a margin improvement as pricing and growth leverage more than offset cost inflation.

It is worth calling out that PetCare also saw a significant margin improvement in the second half.

Water also saw its margin temporarily affected by capacity constraints in the fourth quarter and inflationary pressures particularly linked to energy.

Slide: Inflation more than offset pricing, growth leverage and efficiencies

Next is underlying trading operating profit, which increased by 6.5% or CHF 1 billion. As a percentage of sales, it decreased by 30 basis points to 17.1%.

In 2022, gross profit increased by 2.5% to CHF 42.7 billion. Our gross profit margin decreased by 260 basis points to 45.2%, as significant input cost inflation more than offset pricing, efficiencies and growth leverage. In the second half, we saw a further gross margin decrease, as inflation was materially higher than we anticipated in the summer, primarily due to energy as well as labor costs.

For the first half of 2023, we expect our gross profit margin to decrease versus the corresponding period in 2022. Going forward, restoring our gross margin remains a top priority.

Distribution costs as a percentage of sales decreased by 20 basis points, mainly as a result of the disposal of the Nestlé Waters brands in North America.

Marketing, administration and R&D expenses as a percentage of sales decreased by 210 basis points, supported by sales growth leverage and disciplined cost control. Consumer-facing marketing spend decreased temporarily, following a lower level of marketing activities in the context of supply constraints. Marketing spend increased in the second half of the year. Going forward, we expect to increase our level of marketing investments, both in absolute amount and as a percentage of sales. Bear in mind that we should not only look at marketing, but also at trade spend. We always look at marketing and trade spend jointly because we arbitrate very often between these two lines of the P&L. In 2022, our total marketing and trade investment increased in Swiss francs versus the prior year.

Overall, sustainability investments, mainly recorded in cost of goods sold, were around CHF 700 million.

Slide: Net profit impacted by exceptional items

Moving on to P&L items from underlying trading operating profit down to net profit.

Restructuring expenses and net other trading items decreased by 30 basis points, slightly below the prior year across most items.

As a result, the trading operating profit margin was unchanged versus the prior year on a reported basis at 14.0%.

Taxes as a percentage of sales increased by 30 basis points on a reported basis. The underlying tax rate was relatively stable at 20.9%.

Lower income from associates and joint ventures largely reflects the disposal of some L'Oréal shares in 2021.

Slide: Strong increase in underlying earnings per share

Moving to underlying earnings per share, which increased by 9.4% in constant currency and by 8.4% on a reported basis to CHF 4.80. The largest contributor to the improvement was our strong organic growth. Nestlé's share buyback program also contributed 1.8% net of finance cost.

The line Others, mainly related to income from joint ventures and associates, contributed 2.2% to growth, driven by increased contributions from L'Oréal and Froneri. The negative impact of foreign exchange reflects the currency depreciation of the Euro-denominated L'Oréal income.

Slide: Sustaining strong operating cash flow generation

Our cash generated from operations before changes in working capital remained solid and dependable at around 20% over the last six years.

Free cash flow decreased from CHF 8.7 billion to CHF 6.6 billion, reflecting our decision to temporarily increase inventory levels in the context of supply constraints, the energy crisis in Europe, as well as elevated capital expenditure.

As working capital and capex normalize, we should see an increase in free cash flow, trending back toward 12% of sales by 2025, in line with our mid-term financial targets.

Slide: Return on invested capital

The Group's return on invested capital before goodwill and intangibles decreased to 39.4%, reflecting a temporary increase in inventories and a higher level of capex.

The Group's Return on invested capital after goodwill and intangibles was 12.2%, unchanged versus the prior year. Without the impact of impairments, return on invested capital increased by 10 basis points to 14.3% in 2022.

The Group's ROIC has been relatively stable over the last three years at between 14% and 15%. This is a level two times higher than our WACC and comes even as we have made significant acquisitions.

Slide: Net debt

Net debt increased by CHF 15.3 billion to reach CHF 48.2 billion as at December 31, 2022. The increase largely reflected the dividend payment of CHF 7.6 billion and share buybacks of CHF 10.5 billion.

Our free cash flow in 2022 was exceptionally low due to our decision to temporarily increase inventories in the context of supply constraints and the energy crisis in Europe. This impact will reverse in 2023 and 2024, with a significant cash flow benefit.

During 2022, we returned a record CHF 18.2 billion of cash to our shareholders in dividends and share buybacks.

We are committed to maintaining our practice of increasing the dividend every year in Swiss francs. At the next Annual General Meeting, the Board of Directors will propose a dividend of CHF 2.95 per share. If approved, this will be the 28th consecutive annual dividend increase. The company has maintained or increased its dividend in Swiss francs over the last 63 years.

Net debt to EBITDA ratio at 2.45 times needs to be seen in the context of a temporary increase in inventories.

Q & A Session

This concludes my remarks. I now hand over to Luca to open the Q&A session.

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

Thank you, François. With that, we move to the Q&A session. We open the lines for questions from financial analysts. (Operator Instructions)

The first question comes from Jon Cox, Kepler Cheuvreux

Questions on:	**FY-23 organic growth guidance Contributors to weakness in Q4**

Jon Cox, Kepler Cheuvreux:

Two questions. One, just to make crystal clear on the guidance, this includes the impact of the SKU phase out? I think some in the market maybe think that it does not include that SKU phase out. So that 6% to 8% is a hard 6% to 8%.

The second question, just on the slides you showed 15 and 16 in terms of the weakness in Q4. You mentioned mix is about 1.5%. So then can we assume the volume decline was about 4% in Q4? And then just bearing in mind the split that you gave for the 2.6% decline, can we roughly assume 1.5 points is the SKU rationalization maybe 1.5 points is the out-of-home change? And then maybe 1 point is the supply chain constraints.

Mark Schneider, Nestlé S.A., Chief Executive Officer:
Jon, I'll hand it to François for the second question. But on the first one, just to confirm, yes, this is a hard guidance of 6% to 8%. We're not playing around with guidance terms, as you know, and this includes the impact of SKU rationalization. So, you see we're feeling very confident about a very decent sales development in light of these longer-term undertakings.

François Xavier Roger, Nestlé S.A., Chief Financial Officer:
On my slide 15 or 16, on this, the RIG negative impact in Q4 at 2.6%. The three main factors that I mentioned contributed about 160 basis points. There is one -- the last one, the Water one, which has a smaller contribution. And the bulk of this 160 basis points decline, impacting Q4 that will continue for H1, is coming from this SKU optimization as well as the out-of-home growth slowdown.

Don't forget as well, so we don't want generally to go too much into that, but in Q4, we had one less invoicing day as well. So don't go too far in interpreting the negative decline of volume in Q4.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from Guillaume Delmas at UBS.

Questions on:	**Mid-term margin outlook** **Inflation**

Guillaume Delmas, UBS:
Two questions for me, please. The first one is on your medium-term margin outlook. Because you reiterated today, your ambition to restore your gross margin to the 2020 levels. So that would effectively mean a 400 basis points gross margin uplift over the next few years. Based on your medium-term margin outlook of 17.5 to 18.5, I mean this implies some significant step-up in SG&A to the tune of 250 to 350 basis points. So, my question is, what returns do you anticipate on these incremental investments because with such a heightened level of

investment and a stronger, leaner portfolio, would it be fair to assume that your organic sales growth could go from 4% to 6% to more like 5% to 7%?

Then my second question is on inflation. I appreciate it is probably still early days. But at this stage, what level of cost inflation would you expect for 2023? How do you think it will compare to the levels of inflation you faced last year? And is there a scenario maybe whereby you could actually face some deflation by the time we get to the back half of the year?

Mark Schneider, Nestlé S.A., Chief Executive Officer:
Let me try and take a first crack at both of these and then also hand it to François for some additional detail. On the second one, again, we're trying to be helpful, but I don't think at this point, it is good here to speculate on exactly where input cost inflation is going to go. As you saw frequently in the past, anyone who speculated on this in the last two or three years have frequently ended up wrong. It then also sends the wrong signals when it comes to retailer negotiations. It's not in the best interest of shareholders to speculate on that, and hence, we're refraining from it. So, I'm asking for your understanding.

When it comes to the medium-term outlook in 2025. Do keep in mind that -- what the guidance and expectation is on, is on the underlying trading operating profit margin. So, the 17.5% to 18.5% that we're getting there. What's very hard to estimate in this volatile environment and three years ahead of time is exactly what the breakdown is between operational improvements, overheads and then ultimately, of course, the gross margin. What we're trying to explain is that, of course, the gross margin needs to repair somewhat to get back there because clearly, it came down quite a bit, in the face of inflation. Typically, as inflation eases, some of that should repair as a result of the price increases we've done and input cost over time coming down again. But don't assume that this is an exact like-for-like. 2025 is not going to be a copy of 2020. What we feel confident about is that we have a set of initiatives that will lead us to an underlying trading operating profit improvement to come back to that old range of 17.5% to 18.5%. How exactly then the other ingredients that add up to the underlying trading operating profit margin, how they will shape up, we need some flexibility there.

François Xavier Roger, Nestlé S.A., Chief Financial Officer:
Guillaume, just to complement what Mark said, I can just give you some color on two more specific items. Obviously, the structural cost benefit or I would say, the growth leverage benefit that we have. You know that historically, we have generated between 50 to 70 basis points of benefit to the bottom line. We expected that to continue as well. And in addition to that, this program that we are starting now with SKU and portfolio optimization, they will impact very

positively on margin. As by the way, it has been the case in the past as well, but we expect these two items to continue to contribute positively to our margin development in the next couple of years.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from Céline Pannuti at JP Morgan.

Questions on:	**Portfolio rationalization** **Trade spend and A&P**

Céline Pannuti, JP Morgan:
My question is coming back on the portfolio rationalization. François, you mentioned that it would be a magnitude of 160 basis points in Q4 and then we should expect this to continue to into the first half. But I also feel that some regions like LatAm, Europe didn't seem to have seen yet an impact. And you've seemed as well to broaden it by geography and business. So I just want to understand how much more step-up we should expect in '23? And you also said that, for instance, business in Frozen food in Canada will take two years to wind down. So how long will that last for? That's my first question.

My second question is on trade spending and A&P. I'm a bit surprised that your trade spend went up in '22, given that many people were talking about trade spend optimization in order to pass through pricing. So can you explain a bit this. And if you wind down trade spend in '23, how can you quantify the potential impact this could have on your volume?

François Xavier Roger, Nestlé S.A., Chief Financial Officer:
On the portfolio optimization, the 160 basis points I mentioned is for the sum of the three items, not only for portfolio optimization. Just to give you some more color as well, we do confirm that this program will have a positive impact on RIG and OG for the full year 2023, but it will have a negative impact in the first part of the year. As you know, there are two parts to it. There is the cutting the tail, the classical one, which we are somewhat suffering from a little bit currently and in the last quarter of 2022, for example. But as we progress over time, we expect to really get the benefit of pushing the head, which is the reason why net for the full year, we expect to have a positive impact there.
On the trade spend, so what is important is to look, as I mentioned in our Barcelona conference, not only to look at marketing spend, which did decrease last year for us in the context of supply chain disruption as well. Take the example of PetCare, for example, since

we did not have enough products to sell. There was no point in a certain number of instances to invest in advertising and publicity.

But if we look at the total amount, which I mentioned as CHF 28 billion last year during the Barcelona conference, this amount, in its entirety for the two components, did increase in absolute value last year. Within that, we feel that it's relevant in a certain number of cases to arbitrate between these two amounts. And it is true that trade spend has increased in absolute value last year. We thought that it was appropriate in a certain number of cases, to make sure that our products remain affordable at a time when we went for significant price increases. It seems to have paid off because when we look at our market share, it has been resilient. And if you look at more specifically at our market share for Billionaire Brands, in almost 60% of the cases, it did increase or stabilize. So, we think that it has worked fairly well in the course of 2022.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from Patrik Schwendimann at Zürcher Kantonalbank.

Question on:	**Main growth drivers** **Acceleration of portfolio optimization**

Patrik Schwendimann, Zürcher Kantonalbank:
You have mentioned Mark that you are confident to reach the 6% to 8% organic growth guidance for the current year. In terms of product categories, what will be the main growth drivers behind this one?

And second question, you also have mentioned that you would like to accelerate portfolio optimization. You just have mentioned, the Frozen food business in Canada. Are there also large divestments possible in the current year?

Mark Schneider, Nestlé S.A., Chief Executive Officer:
Thanks, Patrik. So I have no particular announcement at this point when it comes to categories. I expect it to be reasonably broad-based, which I think is one of the Nestlé's strengths. So clearly, some of the high-performing categories when it comes to organic growth, so think PetCare, I think will continue to do well. But other than that, I don't have a lot more detail at this point that I would like to share.

On the portfolio, let me spend a minute on that because clearly, what we are showing with this? And at the risk of beating the Canada example to death, I mean we're showing you that we're willing to walk away from a book of business, take the hit on RIG, take the hit on the underlying volume and organic growth and basically simplify the company, focus the growth spend and actually use those resources to advance the winners. It doesn't mean we're eager to walk away. And so, if we can sell something, we will sell it. But we are ready to walk away. And I think this builds on a period when you think back to the time before COVID, there was a period of four to five years when, us included, everyone in the industry was really striving for organic growth. I think at that time, in hindsight, it's clear to me that we were probably taking it a little easy on this permanent process of SKU rationalization, that should be going on in company like us that has such a large number. We were probably at the time, a bit more reluctant to take these hits on volume, RIG and organic growth. As a result of that, the product programs swelled up a little bit, especially since we were cranking up innovation a lot and had a nice new stream of innovative products coming to market. As I explained in the prepared remarks, what got our attention initially was the supply chain constraints. There we had to make choices like how do you use limited resources to make either one product or another. But then once we saw the tremendous benefits from that, we saw that there is a significant opportunity here to do more and really play to win, as opposed to just play to have another SKU on the shelf. And focus on profitable growth, that's essentially what we're after. So that will include some further SKU items but that will also include some divestitures over time so that we are even more focused. We will continue as a multi-category diversified Food and Beverage company, no question. But we believe that the company overall within that broader scope will benefit from even more focus than before. That's essentially what we're after. This is where the supply chain constraints, just opened our eyes in terms of that additional upside that we've left on the table.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from Warren Ackerman at Barclays.

Questions on:	**SKU Rationalization** **Supply chain constraints – timing of easing**

Warren Ackerman, Barclays:
Two from me as well. The first one is just a follow-up on the SKU rationalization point. I know we've had a few questions on it, but that 150 bps in the Q4 quarter, how much of that was just the SKUs? And related to that, the 20 bps that you reiterated from the CMD for '23 is great to know that. And it's great to hear it's still happening. But in terms of the phasing of that, it sounds like it will still be negative. I'm trying to understand why does it swing suddenly back positive? How can you be sure of the number 20 bps for the full year when you've got so many things

moving around. Just interested in the mechanics of how you can be so precise on the 20 bps, that would be helpful, that additional color.

Then the second one is just on the supply chain constraints. It's been a feature now for quite a few quarters. A lot of your competitors are now saying things are easing significantly, but it sounds like for Nestlé, that isn't the case. So, I'm specifically interested in Pet food. You have a lot of new capacity coming online from Pet food. Can you maybe explain the phasing of the capacity increases? In short, when do you expect the supply chain constraints in Pet -- and it's also Coffee-Mate, but mainly in Pet, stopping being an issue? And is there a worry about eventual overcapacity in Pet food because all the premium players are adding capacity at the same time?

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

Let me start on the second one and then hand it to François for the first one. And so, you're absolutely right. If we are citing supply chain constraints, maybe a tad more often than some of our peers, I think it is due to the fact that we have such a large and successful Pet food business. And we are a little bit the victims of our own success here because, as François pointed out, this is now the third consecutive year of double-digit growth. We were even close to capacity limits before COVID and had started to greenlight some of the capacity enhancement programs, then came COVID and that huge surge in pet adoption and demand, and this is something that no-one had on the radar screen. As you can imagine, especially when it comes to greenfield sites, these things do take some time for planning and permitting and then putting the capacity into the ground and getting them up and running. So, we expect that to come on stream, depending on what geography you look, at in '23 and '24. But clearly, yes, it did take some time. I think Pet food, and Pet food North America in particular, were pretty much hit by this, and we expect that now to ease over the next 1 to 2 years. I'm not so concerned about the eventual overcapacity because we've done, as you can imagine, on major capex items here, we've done lots of projections about how things could turn out. And even if there is a little bit of overcapacity temporarily, it was very clear that with the underlying growth, which is so much intact, you will very quickly grow into it. So, I think going back several years, we're probably getting a little bit too close to our capacity limit. COVID struck and put us into this situation. As regrettable as it is that we can’t supply, it's also a nice problem to have because clearly those projects, into existing demand, are very, very certain projects. And it's all about now getting them implemented and getting them up and running.

François Xavier Roger, Nestlé S.A., Chief Financial Officer:

So, in the Q4 RIG impact coming from these three transitory factors, once again, the smaller one was the Water capacity constraint that we had at the *Perrier* plant. The main items are the two other ones. The slowdown of the out-of-home growth moving from 18% in the 9 months to around 6% in the fourth quarter. That is something that we expected for some time. And the second largest factor, they are relatively equivalent the two of them, is this portfolio SKU optimization. This is not an exact science, but I mean we have a good level of confidence on the fact that this will continue having a negative impact in H1. In addition to that, let's not forget that in H1, we will have the impact of this Canadian Frozen decision as well. But when we start entering into H2, we will get the benefit of what we call pushing the head. I mean we have been involved in that program for more than a year now. So, we start seeing the benefits of it. We have gained confidence about it. We start seeing increased service levels, for example, on many of these SKUs, as an example. So, we are very confident that the net impact will be positive in the second half of 2023.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from Tom Sykes at Deutsche Bank.

Question on:	**Pricing in 2023** **Nespresso - outlook for growth and ROIC**

Tom Sykes, Deutsche Bank:
Firstly, just in terms of the pricing impact on the 6% to 8%, I mean you don't want to split it out, but how many rounds of pricing do you think are in your expecting to conclude over the course of this year sort of compared to '22? Do you at all feel like you've lagged the list price increases of your peers? So, there's sort of conceptually some catch up in pricing, maybe as some of your peers are not increasing their prices by as much now.

And then is it possible to explore Nespresso? Just it looks like the fixed asset base in Nespresso went up quite considerably. And I guess that's probably to do with the Vertuo rollout. But the ROIC seems to have diminished quite considerably. One presumes therefore, in Nespresso. So what is the outlook near term for growth in Nespresso and where do you think you can get the ROIC back to, please?

Mark Schneider, Nestlé S.A., Chief Executive Officer:
Let me hit the first one and then hand it to François for the second one. So again, I don't think it's helpful to our shareholders to now speculate on how many rounds of pricing there will be. As you can imagine, this is highly specific by market and category. It's also clear that at this

point, we're not talking broad-based price increases, but very targeted by category, by situation and well justified by the data. Otherwise, retail partners and consumers will simply not accept price increases. It's also important to step away from the notion that all pricing needs to happen *de novo* from now because much of the pricing that will apply to the year '23 is pricing that may have been effectuated in the second half of '22 and then there's a full year benefit of 23 as well. Then there are price increases that were rolled out and agreed at the very end of '22 or now at the beginning of '23, but are taking effect now as we speak, over the next few weeks. Then depending on where inflation takes us, some additional action might be needed. That's why, again, don't imagine that everything has to be newly priced from the ground up now. Some of it is carryover from '22. And it's highly situation and category and geography specific. But clearly, as you see from the combined consolidated numbers, it's very clear and I think you see the same picture borne out with our peers, that inflation has left its mark on gross margins and profit margins. And clearly, some repairing still need to be done.

François Xavier Roger, Nestlé S.A., Chief Financial Officer:
I think your second question was on *Nespresso*. So there -- I mean, we are clearly putting ourselves in an investment position, developing *Vertuo*, which is still a protected system to start with. And so, we have a unique position there. It's a system that is growing nicely and really meeting the demand of consumers as far as the long coffee cups is concerned, given that it does short coffee cups as well. *Nespresso* is actually doing well overall, even if -- you look at the numbers for 2022, they may look a little bit depressed, but let's not forget that we are growing over an exceptionally high base in 2021. If you look at the growth in RIG on average over the last three years, it was at 4%, which provides a good indication of the good performance of *Nespresso*. And once again, on a comparable basis, sales in 2022 were 20% higher than a few years ago. So, I think this is the right thing to do as far as investing for growth in *Vertuo*. But let's not forget that the base of comparison was fairly high in the context of the pandemic in 2021.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from John Ennis at Goldman Sachs.

Questions on:	**Greater China margin** **Good for you Nutrition program**

John Ennis, Goldman Sachs:
My first is on the Greater China margin. Can you just give a few more details behind the 260 basis point expansion there? How much was mix versus SG&A savings? And is any of that

margin expansion temporary, i.e., will you reverse it in 2023, if you need to step up investments there? That's the first question.

And then my second question is, I suppose, a bit bigger picture. But as you look at your Good-for-You nutrition program, I guess, it seems sensible to try and grow that ratio. But how do you ensure that you don't become fixated on a percentage healthy food sales target here at the expense of some of the less healthy, more indulgent pockets of your portfolio, such as Confectionery, because I guess from the outside looking in that always seems to be the risk with those types of initiatives.

François Xavier Roger, Nestlé S.A., Chief Financial Officer:
John, let me take the first question on China. So, the increase of the margin in 2022 in China is essentially coming from the mix, given that we had a significant turnaround of our Infant Nutrition business that did help tremendously. You're aware as well of the fact that in China, we are suffering less from inflation. There was actually limited inflation in China. The improvement of our margin is actually satisfactory because it has to be seen in the context of lockdowns, which did impact our growth in our business overall, especially so that we are more exposed to out-of-home in China than in any other geographies.

Mark Schneider, Nestlé S.A., Chief Executive Officer:
John, very important question regarding the Good for You strategy. Let me be precise. We're not interested in a target on how the healthier parts of the portfolio would outperform the other parts of the portfolio. This will very likely take a shape of an absolute size kind of target because it is true that these parts of the business have been growing faster historically, and they are also slated to grow faster going forward. But you're absolutely right, no matter whether you're working in a part of the portfolio that is above a health star rating of 3.5 or below we're committed to both. We want to succeed in both. We believe in a healthy and balanced and tasty diet. And clearly, for the healthier part of the portfolio, the name of the game is expansion. Then for the other parts of the portfolio, it is about responsible marketing practices, responsible consumption, but within those limits also to go for success, and to go for market share and to go for growth, no question.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from Bruno Monteyne at Bernstein.

Questions on:	**Downtrading** **China Infant nutrition – new regulations**

Bruno Monteyne, Bernstein:

Mark, a few quarters ago, when we talked about private label gaining some share in the U.S. in ready meals and in pet food, you said it was largely capacity related. But if I heard you this morning on some of the interviews, I think you did signal that there were some signs of trading down. So, I'm just trying to see where is that trading down? Where is it starting to shift, where do you see some signs of that and how you expect it to develop?

And second of all, if we think about China Infant Nutrition, there's the new regulations that have started in February. Anything you can say about Nestlé's progress in going through that. I think you had the HMO introduction in China that hasn't been approved yet. Any update there of how you see that developing this year and future years?

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

Clearly, on whatever signs of trading down, we've seen, they have been limited and also remember we do have, in quite a few categories, brands at different price points. So, it's not necessarily that consumer is completely lost to us. When you look specifically at the North American market, one example, I believe, on a temporary basis, where there's been some trading down or some shifting to companies with less price increases was in Frozen food. But here again, looking at the underlying economics, we do believe that over time, this will normalize, and we believe that we will regain some of that share. I have no regrets about the pricing action that we have taken.

Very similar, we've seen some of that in Water offerings where maybe people have been trading a bit away, here in the European context, from premium water offerings to more mainstream water offerings or even private label. So, these are some examples. Again, in quite a few of those, it's a question we've been moving early with pricing, which I think is the right thing to do. Sooner or later, gravity will catch up with some of our competitors. And hence, at that point, that situation will correct itself because they will also then have to take pricing action or live with permanent reductions in their profitability. This is why, I believe, what we've done, and that is to go in early, is still the right way to go because it doesn't weaken your underlying profit picture and your ability to invest for the long term. Then over time, you will see that the situation will normalize. So, I'm not concerned. I think some of the snapback of private label, in particular, is very understandable, given that private label suffered a lot in 2020 and early '21, with supply chain constraints and under COVID. The big brands were the ones at the time that were gaining. Now you're seeing somewhat of a normalization of that situation.

François Xavier Roger, Nestlé S.A., Chief Financial Officer:
On the China Infant Nutrition market, I can just comment on HMO. So, filing has been made for us and for many of our competitors as well. So, there are different steps in the approval, so we are waiting for the approval. Obviously, we are very interested in getting those HMO approved in China and possibly for competition, given that when you look at the success that we have reached for HMO outside of China, CHF 1.3 billion of sales in year four. That's certainly one of the best successes that we have experienced over the last couple of decades. So, something that we are very much interested in China, but we don't necessarily have visibility on the timing of an approval process.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from Jeremy Fialko at HSBC.

Questions on:	**Pricing elasticity in 2023** **Expected CapEx expenditure**

Jeremy Fialko, HSBC:
So, a couple from me. First of all, I'm thinking about elasticities, I guess if we strip out the kind of 160 basis points, it means I guess, about 100 basis points of negative RIG was due to the more straightforward pricing elasticity. Do you think that's a sort of sensible number to be taking forward into the early part of 2023? Are you see any increases in elasticities as further price rises are implemented? So that's the first question.

The second one is on your CapEx plans now. At the Investor Day you said that your CapEx is going to be around 5% of sales over this '23 to '25 period. But now today, you say we've found all these new areas of rationalizing our portfolio, that can free up our capacity. Therefore, do you think it means that actually you might end up being able to spend a bit less on CapEx than you outlined a few months ago.

François-Xavier Roger, Nestlé S.A., Chief Financial Officer:
I would be a little bit careful with the elasticity, what you say because it goes beyond the 160 basis points. Let's not forget the two significant factors as well that have influenced our volume growth during the course of 2022. It has to do with the high base of comparison, and it was still high in Q4. Our RIG in Q4 2021 was at 4%, so it was a high base. Let's not forget as well about the supply constraints, even if some of them are softening a little bit as we progress over time, but these two factors did influence as well our volume. So, I would not conclude that

everything is coming from elasticity. Once again, elasticity, we have seen some, but to moderate level.

CapEx. We confirm that we expect to be around 5% for 2025. This is part of the guidance we have provided. I'm not totally sure that the portfolio activities that we are doing of optimization will impact the CapEx because the CapEx is on new needs especially for PetCare, for example. The new needs that we have are not with necessarily with the same products. So, we are investing essentially for Coffee-Mate, which continues to grow nicely, we invest in PetCare, where we see continued demand. So, it has a limited impact versus our base, what we prune in our portfolio is much more on some of the categories we mentioned, Dairy in the Middle East in the past or Dairy in Brazil or some of these products. So, it does not necessarily impact our CapEx going forward.

Mark Schneider, Nestlé S.A., Chief Executive Officer:
Let me build on that and just confirm. The whole model of this is that the RIG after taking the initial hit will repair. So, you're serving the same volume need, but you are serving it with fewer more focused, more successful brands and SKUs. And so that's why there's no immediate connection to capex.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from Jeff Stent at Exane.

Question on:	**US Frozen food vs Canadian**

Jeff Stent, Exane:
Just one question on U.S. Frozen foods. I appreciate you've obviously got manufacturing assets there, but contrasting versus Canada, why is the U.S. Frozen market, why the outlook there is so much better than perhaps is in Canada? If you could just contrast the sort of two businesses, that would be great.

Mark Schneider, Nestlé S.A., Chief Executive Officer:
Yes. Look, the simple answer is our U.S. business is fully geared and targeted towards the needs of the U.S. market. So, from the manufacturing sites and supply chain, all of this is optimized for the U.S. The Canadian business was one that was done on the side from the U.S., but it suffers from transportation and exchange rate disadvantages. That's why we're saying it was hard for us to compete in that effectively over time and make it into a long-term winning business. At the same time, from our perspective, the volumes weren't such, as I

mentioned the book of business is about CHF 150 million for us, so the volumes weren't such that it would justify a full-fledged investment and build-out of a brand and our own logistics and all of that. So, we believe it's the right thing to do and focusing instead, and winning, in the U.S. Frozen market is for us the better way to go.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
Next question is from David Hayes at Socièté Gènèrale.

Questions on:	**North American RIG reduction** **Capex, net interest costs, tax rate & FX impact on EPS**

David Hayes, Socièté Gènèrale:
Two for me. One on North America and then a housekeeping mop-up, I guess. So just on North America, the RIG, I think, was down 5% in the fourth quarter. You mentioned a little bit of that, I think, it was Perrier in the comments, but Pet obviously a key element there and that was still doing very well. Project TASTY, as I understood it, was a little bit more orientated towards Asia. So, the question is, is there any specific one-off, any specific category in North America that we should be thinking about in that fourth quarter RIG reduction?

And then the housekeeping mop up is just to see whether we can get anything in terms of outlook on capex percentage of sales, a bit following up on Jeremy's question, net interest costs, which obviously, inevitably were up second half, but any guidance on that? And then the tax rate and the FX impact on EPS as rates stand today? Any clarity on those moving parts in terms of the guidance will be fantastic.

François-Xavier Roger, Nestlé S.A., Chief Financial Officer:
David, let me take some of these questions. In terms of net interest rates, you could see that it was a moderate increase in the context of today, with interest having increased quite a lot. So, we moved from an average net cost of debt of 2% in 2021 to 2.2% in 2022. So, it was a moderate one. Obviously, if interest rates stay where they are, it will increase as we have to renew some of the debt. Don't forget that these rates are even before tax.

The foreign exchange impact, we had actually a moderate negative foreign exchange impact last year, - 0.9%. It was even positive in H1, negative in H2. As of today, it's negative, but this is something that is very difficult to forecast anyway because we don't have necessarily the visibility. But we know as of today, exchange rate were staying for the balance of the year, the foreign exchange impact for our total business, both to convert our sales, but on UEPS would be a more negative impact.

Outlook of capex, we don't provide the guidance year-by-year, but as I just said before, we expect still to have a relatively high level of capex in 2023, that might be the peak, and then we will start seeing the capex going down to around 5% by 2025.

And just to give you one example for the North American question on SKU optimization, there is one example that I can share with you, which is on Sweet Earth for plant-based food. We did restructure our portfolio of offering in the U.S. So it's not only a program that is valid for Asia, but it did have some implications in North America, and you can expect that it will have a stronger impact in North America, as you could see through the Canadian example.

Luca Borlini, Nestlé S.A, Head of Investor Relations:
So we have a final question from James Edward Jones at RBC before giving the word to Mark for his final comments.

Question on:	**Pricing philosophy**

James Edwardes-Jones, RBC:
I'm slightly confused on your attitude, your philosophy of pricing because in the past, you've spoken a lot about responsible pricing. But I thought I understood from one of your comments a few moments ago that you actually -- you feel you've led the way on pricing and others now need to catch up. Could you just clarify that a bit?

Mark Schneider, Nestlé S.A., Chief Executive Officer:
James, I think I can help out on that. It depends always on what particular category and geography you're referring to. For the vast part of our business that relates to developing markets where, clearly, whatever you offer also needs to be seen in the context of daily income and cash income. This whole notion of responsible pricing is one that continues to apply. There's many other markets, especially advanced markets and more premium products where I feel there it's about, at times, being proactive when needed. I think our management in the U.S., in particular, was quite proactive in their actions. There also, I think, what the U.S. market benefited from is that the inflationary surge started a little earlier because it didn't get started with the crisis that was caused by the invasion of Ukraine. It got started more in the second half of '21 on the back of some of the supply chain constraints and also the early inflation on labor that everyone had seen. So, the pricing there started a lot earlier. And I think the U.S.

management team was quite proactive in doing it. As you see now where things turned out for '22, I think they made the right call.

With that, I hope that answers the question.

End of Q&A session

Mark Schneider, Nestlé S.A., Chief Executive Officer:
I hope that the call was useful to you in addressing some of the concerns. We do understand especially in this context where everyone sees immediately pricing and inflation in relation to the volume development. If you only look at it through that lens, I do understand that there is amongst some of you concern over the Q4 volume and RIG development. I hope that some of the reasons that François I laid out to you addressed those. As I mentioned, you find us a lot more relaxed about the situation. I can also tell you that while this call is strictly about '22 and not about '23. When I look at how the year started, clearly, we're not seeing in Q4 the beginning of a trend that's worsening, but rather we're seeing a strong start to the year, and that implies specifically to volumes and RIG as well.

So again, I hope that the call was helpful in addressing some of these concerns, and we look forward to talking to you again as part of the Q1 conference call.

Thank you.

End of Transcript