CCH – 2017 third-quarter trading update
Conference call Q&A transcript – 9 November 2017

CORPORATE PARTICIPANTS

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Basak Kotler, Director Investor Relations

QUESTIONS FROM

Edward Mundy, Jefferies

Andrew Holland, Societe Generale

Komal Dhillon, JPMorgan

Sanjeet Aujla, Credit Suisse

Edward Mundy, Jefferies

Chris Pitcher, Redburn

Andrew Holland, Societe Generale

QUESTIONS AND ANSWERS

Telephone Operator

Ladies and gentlemen, as I said before, if you would like to ask a question please press *1 on your telephone keypad.

Thanks for waiting, so the first question comes in from the line of Edward Mundy, from Jefferies. Please Edward go ahead.

Edward Mundy, Jefferies

Morning Michalis, morning everyone. Three questions please, first of all are you able to quantify the impact of the good summer weather on your Q3 volumes?

Secondly, I think this is the first time you've used this language, the emergence of a more inflationary environment in the Established markets, I was wondering whether you were able to go into that in a little bit more detail and does this feel sustainable?

And then the third question is around your Developing markets, you know very strong revenue per case for the first nine months, does this feel sustainable into 2018?

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Okay, thank you Ed, good morning. So the summer weather was more prominent, the good summer weather was more prominent in Southern Europe. We also had some headwinds from summer weather more in Eastern Europe, particularly Poland and Russia. So on balance I wouldn't say that overall there is a very significant major positive impact as a result of weather and that's why we don't call it separately in the results.

Now when it comes to the inflationary - more inflationary environment in the Established markets we have seen that in a number of our countries the inflation is edging significantly better than the prior year in 2017. And despite the fact that we don't believe that this leads to a significant change in our strategy in terms of list price increases, we believe that it does help us as a general environment to manage better our promotional pressures in these markets. And this is where we see the effectiveness of our promos in Established and also in the Developing markets improving and that's how we saw quite a significant positive impact particularly in the Established markets as a result of that.

Now when it comes to the Developing with regards to the revenue per case, in the Developing the currency neutral revenue per case was up 2.1%, with quite a bit of a slowdown I would say versus the growth that we saw in the first half, which was 3.4%. And there, there are three main reasons why this trend happened.

First of all the higher contribution of Water in the mix, so category mix in quarter three was influenced by the increased Water and therefore negatively. Pack mix - we had some extra promo in multi-serves in some of our countries, particularly in Czech, so that also influenced the slowdown in quarter three. And also we see across the board an acceleration of modern trade, of the modern trade channel mix, particularly again in Czech. And these were areas that influenced the slowdown of the currency neutral revenue per case growth in the Developing.

Edward Mundy, Jefferies

Michalis my question was more that - I mean you also faced a much tougher comps I think for revenue per case in the Developing markets, so I'm certainly surprised - your 2.1% in Q3 certainly surprised on the upside there. Do you feel that this type of - you know 3% revenue per case growth for nine months is that sustainable for fiscal '18?

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

So yes we see that being sustainable and versus prior year we saw in the Developing markets pricing and overall category mix being better. Channel and pack mix was flattish. And overall we see that this is a trend that we can sustain.

Edward Mundy, Jefferies

Great thank you.

Telephone Operator

Okay thank you very much. So the next question comes from the line of Andrew Holland from Societe General. Please Andrew go ahead.

Andrew Holland, Societe Generale

[Gap in audio] you anticipated that Russia would get better, it looks like it is, do you think that's now a sustainable more positive trajectory, do you think we're seeing bottoming out and the Russian market - or just thinking of Russian sales will trend more positive?

And then thirdly on Nigeria on pricing ...

Basak Kotler, Director Investor Relations

Apologies, it's Basak here, your line was actually not active until about ten seconds ago. Would you mind repeating your first question?

Andrew Holland, Societe Generale

Yes I'd be delighted. Okay so the first question was on the Stevia Coke that you're highlighting in Greece, can you just say how that is being badged and marketed, is it a sort of a variation of classic Coke, or is it a variation of Coke Zero, or just how is that appearing to consumers?

And then secondly whether your Russia trajectory we can assume now is positive, you're seeming to say that it's bottoming out, is that now getting positive?

And then finally on pricing in Nigeria, you draw attention to very big price increases, 30% in the last 12 months, is there more of that to come, or are we going to see more sort of normalised pricing in Nigeria?

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Thanks Andy, so with your first question it's I would say a unique product of Coke with stevia and no calories, so we don't have something else like this - an innovation like this in our other markets. And Greece has some particular characteristics that have led us to develop this product with a strong light category that has been consistently improving, the contribution overall in Sparkling, with some local competition exactly in this segment. And we are very pleased with the launch of this product and the first results. Of course it's early days, it's around six months or so, but all the initial reception of the product in the market is very encouraging.

Now going to Russia, obviously we are very pleased with the stabilisation of the volume in quarter three, on the back of also the benefit from listing Sparkling in a big discounter which we mentioned in our previous call, Red and White. A very good in-store activation overall. And despite I would say a generally cooler summer, especially in July.

So all the macro, first of all, indications are very positive, GDP is gradually improving, it has turned now positive, we see rising real disposable income, oil price stabilising in good levels, inflation also is stabilising at relatively low levels, the rouble is quite in a good place and stable; so all the macros are pointing in the right direction. This has not quite reflected yet with regard to the NARTD market, where we still expect a decline in 2017 and a similar decline also with regard to Sparkling. The trends with the modern trade continuing to grow and fragmented [means fragmented trade channel] continuing to face challenges is there.

And what we have seen against this overall backdrop is Sparkling growing mid single digit with good broad based growth in both Coke regular and of course strong growth in Coke Zero. Innovations coming from the flavours in Sprite, in Schweppes. Juice which is a very important category in Russia we have seen the premium and mainstream offerings growing very well. We had some challenges in the value segment due to some local competitive pressure. So we saw Juice declining by very low single digit.

So overall we see across the board good developments and as we have said also in the beginning of the year we are working to see volumes in Russia stabilise by the end of the year. And this is where I believe the success will be for this year and certainly build from this strong base for 2018.

And finally your third question was about Nigeria pricing. You are very well aware that the three price increases that we took since early quarter four last year were a lot in response to the major devaluation of the currency and it was more of a price reset. Going forward, what we see is first of all inflation continuing to be at high levels of mid teens.

We see some good stabilisation in terms of the naira exchange rate; however the affordability concerns are there of course. And we see also quite intense competition. The competition has not followed our third price increase, so there is - there are some mix if you like factors that we have to take into account. But certainly pricing is not going to be as dramatic as we have seen in 2016 and '17.

Andrew Holland, Societe Generale

Okay, that's helpful although I'd love some quantification of less dramatic, can we say single figures inflation - price increases?

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

We are at the point that we are drawing our plans right now, finalising our plans. As I said a lot will depend on some of those factors and how they pan out, especially with regard to competition. But we have this year an effective price increase let's say taking into account also what happened last year of around 25%. That is what I call dramatic, so for next year certainly I should not expect that we can be above inflation in any way.

Andrew Holland, Societe Generale

Okay that's helpful, thank you.

Telephone Operator

Okay thank you, the next question comes from the line of Komal Dhillon from JPMorgan. Please Komal, go ahead.

Komal Dhillon, JPMorgan

Hi good morning, just a follow up as well on Nigeria from another angle I guess on the volume front. So you've got another difficult comp in Q4 and you've previously said you expect maybe to be flat in Nigeria in terms of volumes this year, is that still valid?

And then on the exchange rate front as well, it seems like there's been no change for Hellenic in terms of operational exchange rate, is that correct?

And then in terms of volumes I know you've said all this - you know there's a lot of uncertainty around what competition does. But how should we be thinking about volumes in 2018 in Nigeria?

And then one last thing please on input costs. So we are hearing about a more inflationary commodity cost environment from other bottlers, even concentrate price increases from Coke. Are you seeing the same and what should we be thinking about for '17 and '18? Thank you.

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Thanks Komal. So yes we would see success to close the year with flattish volumes in Nigeria. There is as you've said tougher comps in quarter four. Technically we are not yet out of the low season in October, so November and by far more December are the critical months to see whether we will be able to hit this flattish performance in terms of volume year over year. This is what we are working on.

When it comes to the - I think your second question was about the FX rate in Nigeria, is that right?

Komal Dhillon, JPMorgan

Yes, I mean obviously there's a dual rate but it sounds like you are still operating at the same FX rate, is that correct?

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Yes we - look we have seen a significant devaluation obviously as we were coming towards the end of 2016 and in the early '17. However now the naira against the dollar has stabilised at around 360 naira to the dollar, this is a very good level and most importantly we are able to find significant liquidity in the local market at this rate. And in combination with the fact that the oil price it seems to stabilise at good levels for the Nigerian budget. And as I said the fact that we do see the market, the currency market returning to some normality with a lot of available liquidity this gives us a good feeling for this year, for closing the year, but also for going into 2018.

Now in terms of volumes for '18 in Nigeria clearly Nigeria is an engine of growth for volumes for our Group and certainly as I said we are in the process of finalising plans, but certainly we are looking for volume growth in Nigeria in 2018. We will come back with more details in the February call.

And finally when it comes to the input costs, so we started the year with an expectation for 2017 to be as we said in the high single digits. We came in August with an updated guidance and improvement to mid single digit. What we are seeing now for the full year is that we might have some extra good news, small good news, and we are seeing probably at the low end of the mid single digit, the growth of the input cost per case currency neutral for '17.

Now looking ahead into 2018 first of all just to say that we are very well covered, very well hedged in the majority of our commodities. Certainly on EU sugar, but also on world sugar we are 100% covered in Russia and around three quarters in Nigeria.

When it comes to aluminium we are also we believe in a good place because we are around 45% hedged for 2018 and at prices that are significantly better than the forward rate that we see for aluminium for next year. And overall we are at the point where we are finalising the plans because the mix also plays a significant role there. But we don't see that input costs will be a major issue going into 2018.

Komal Dhillon, JPMorgan

That's very clear thank you. Just quickly anything on concentrate prices?

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

No there is nothing, no further update on - nothing that has changed.

Komal Dhillon, JPMorgan

Okay thank you very much.

Telephone Operator

Okay thank you very much. So we currently have no questions coming through so another reminder, ladies and gentlemen if you would like to ask a question please press *1 on your telephone keypad. Thank you.

Our next question comes from the line of Sanjeet Aujla from Credit Suisse. Please Sanjeet go ahead.

Sanjeet Aujla, Credit Suisse

Hi there, I'd just like to pick up on the price mix developments particularly in Established. That's the strongest price mix we've seen there in three years. Can you just elaborate a bit more as to how you - to what extent you think those trends are now sustainable with the pickup inflation we've seen there?

And also in Emerging the deceleration in price mix which was perhaps a bit more pronounced than what I was expecting. Can you just elaborate a little bit on that and to what extent you think the 4% is the run rate for the next few quarters or can you accelerate that as you perhaps take a bit more pricing? Thanks.

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Thanks Sanjeet. So starting with Established revenue per case in quarter three we were up 1.1% and that was significant acceleration versus the first half which was 0.2%. Here I would say that there are more or less three factors at play.

First of all we do have the effect of the modest price increases that we took at the beginning of the year coming in full scale into quarter three compared to prior year. Secondly we have much better promo effectiveness overall as inflation improves so we talked about the positive developments of inflation in Established markets earlier, this is really helping to ease the pressure off promotions in Established markets. And in addition we have some significant improvement, structural improvement, in terms of our processes, our tools, our focus behind return on promotions, so the profit or the incremental profit generated from promos, the return on the investment and overall how we select the appropriate promos for the appropriate parts of the portfolio and channel and that is gradually bearing fruit in the results. And I would say also that the good summer weather which particularly benefited Established with Southern Europe helps compared to the first half because there is a stronger pull on the single serve packs which obviously attract much less promo compared to the mix that we saw in the first half.

So this is really what is at play that helped us to accelerate the growth. And looking ahead in quarter four I would say that we are working to continue with this positive momentum especially as Water will reduce obviously its contribution in the mix.

Now moving to Emerging revenue per case, that was up 4.2% in the quarter and that was a significant slowdown compared to the first half growth which was 8.6%, and that was of course expected and we had flagged this in our earlier calls. Now here there are a few, again a few factors at play. First of all Russia with more promo pressure, especially also because of the poorer weather and the acceleration of the modern trade. And also take into account the fact that we had an acceleration in the negative pack mix hit in Russia because of the listing in this major discounter Red & White, so on one hand this generates significant incremental volume but on the other side it affects the pack mix and therefore the revenue per case.

In Nigeria we have as I mentioned earlier additional competitive pressure being in the low season and that also affected the revenue per case. And of course the absence of any additional pricing in Nigeria. The channel mix in also some of our Emerging markets was more challenging as the weather in the summer was not as good. And of course we are cycling the price increases that we took in Russia in late quarter two last year.

So these were the reasons, and all pretty much expected, why the revenue per case slowed down in quarter three. And going ahead in quarter four I would say that clearly we are working to maintain this momentum although I would say that it would be a success to exceed quarter three, the quarter three growth rate in quarter four, given also the fact that we are cycling Nigeria's first price increases that took place in quarter four last year, and of course the ongoing promo pressure in Russia also in light of the low inflation in the country.

Sanjeet Aujla, Credit Suisse

Okay thank you.

Telephone Operator

Thank you very much Sir. The next question comes from the line of Edward Mundy from Jefferies. Please Edward go ahead.

Edward Mundy, Jefferies

Hi thanks for taking my follow up. Two more please. Do you see any potential regulatory hotspots in terms of sugar taxes in any of your territories?

And then the second question is around Tea. You know clearly no surprise that Tea remains weak in Q3, sort of broadly in line with what happened in the first half. Can you just remind us where you are with regards to replacing Nestea in 2018 with some of the Coke brands such as Fuze and Honest Tea?

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Okay thanks Ed. So with regard to sugar tax first of all we know about Ireland and the UK where the sugar tax is due to take place or to come into effect in April next year. With regard to Russia which was another place where there has been some discussions in the past, the 2018 budget does not include an excise tax on soft drinks. However so for '18 it seems that we will not have an impact. Potentially a discussion might reopen sometime late in '18 for inclusion in the '19 budget.

Other than that and the fact that we do have in Hungary, Croatia and some other smaller countries some kind of sugar tax we don't see that there is somewhere another significant threat at this point as far as we know.

Now with regard to Nestea we are going in 2018 with Fuze in all our countries and we will have a dual approach of Fuze and Nestea in three countries, in Bulgaria, Romania and Hungary. Now we see that Fuze Tea will bring significant advantages to how we develop the category and how we implement this innovation. It will first of all enhance our position in the higher value part of this category because this is a category with significant expected growth up to 2020, faster than many of our categories. And we believe that we can bring some exciting new flavour innovations under the Fuze Tea brand. And this is going to bring quite some more excitement in the category. So the commitment is there. Of course the first year will be a challenge however we have very strong plans in all our markets to recover very quickly the expected challenge that we will see from the switch from Nestea to Fuze Tea.

Edward Mundy, Jefferies

Great thank you.

Telephone Operator

Thank you very much. The next question comes from the line of Andrew Holland from Societe Generale. Please Andrew go ahead.

Andrew Holland, Societe Generale

Thanks, hopefully you can hear first time round this time. And my question is just relating to Italy and the comments you've made there. And obviously that was helped by the warm weather and that boosted Water. I'm just trying to get a feel for the sort of underlying situation in Italy if the weather is normal and what that means for your product mix and for your sort of volume performance?

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Okay Andy, difficult to answer this very specifically. We had volume up very low single digit in quarter three. Summer did help certainly, both in terms of Sparkling but even more in terms of Water. Water was up mid single digit and was cycling easy comps I would say from last year, double digit decline. Here we are very pleased that we are able now to grow having de-listed the two lower value brands and now having fully cycled that. And our other two main brands are performing very well, especially in single serve.

Now Sparkling declined by very low single digit but we saw very strong growth from lights. Coke Zero was up high teens and Coke Zero Lemon which is a relatively new launch was very strong. Energy is doing well. And what gives us more optimism is the fact that we see a gradual stabilisation and improvement in the economy with a relatively weak expansion but expansion, good GDP forecast. And in this environment we expect to be able to deliver stable volumes and look to next year with stronger plans and more innovation in order to see growth also in Italy.

Andrew Holland, Societe Generale

Okay thank you that's very helpful.

Telephone Operator

Okay thank you. So the next question comes from the line of Chris Pitcher from Redburn. Please Chris goes ahead.

Chris Pitcher, Redburn

Thank you very much. Could I follow up again on your commentary around Russia pricing because given what we saw in terms of regional revenue per case movement, given your commentary on Russia talking about what looks to be positive category mix with Sparkling growing, value juices declining, Water not growing it would indicate to me that Russia has gone quite deflationary for you. Can you confirm that that is the case because it does seem with the modern trade continuing to grow that this could persist for some time yet? Could you give us a bit more colour on that? Thanks.

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Deflationary is definitely not the word that I would use. We see inflation stabilising at around 4%. That of course will be upper threshold in terms of the list price increases that we can take on a broad base. However there are a lot of elements within the revenue per case that will work to our favour. Channel is not one, agree with you. Modern trade will continue to grow. However when it comes to category mix and pack mix with all our plans around innovations about pack innovation, focus on single serve and the right type of activation and promotion of our multi serve packs in the channels we definitely see that we have room to continue to grow revenue per case in Russia.

Chris Pitcher, Redburn

Can you confirm that your revenue per case in Russia grew then in the third quarter?

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Yes in the third quarter our revenue per case - in quarter three was down in Russia, however we are seeing that as we go into quarter four we are expecting that taking out the impact that I mentioned earlier specifically for quarter three we are going to continue to improve.

Chris Pitcher, Redburn

Okay thank you very much.

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

Please also as I mentioned earlier consider that we had the significant listing in Red & White which is a major discounter and that as we cycle the lack of this major customer in the prior year has an impact overall in the mix.

Chris Pitcher, Redburn

Thank you Michalis.

Telephone Operator

Okay thank you very much. So ladies and gentlemen one final reminder. If you would like to ask your question please press *1 on your telephone keypad now. Thank you very much.

Okay there are no further questions so I will hand you back to your host Michalis Imellos to conclude today's conference. Thank you.

Michalis Imellos, Acting Chief Executive Officer & Group Chief Financial Officer

I want to thank you for joining us today and for all your questions that facilitated a good discussion around our third quarter performance. We have a clear roadmap for top line growth and margin expansion as well as the strategic initiatives that will get us there. We have been implementing these initiatives consistently and we are very pleased with the results that they are delivering. We look forward to sharing more progress with you in the coming periods. Thank you and goodbye.

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