

# CCH – 2018 first-quarter trading update

## Conference call Q&A transcript – 10 May 2018

### **CORPORATE PARTICIPANTS**

**Zoran Bogdanovic, Chief Executive Officer**

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### **QUESTIONS FROM**

**Sanjeet Aujla, Credit Suisse**

**Edward Mundy, Jefferies**

**Saranja Sivachelvam, Bank of America**

**Stamatis Draziotis, Eurobank Equities**

**Laurence Whyatt, Société Générale**

**Chris Pitcher, Redburn**

**Andrea Pistacchi, Deutsche Bank**

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### QUESTIONS & ANSWERS

#### **Telephone Operator**

Thank you. Ladies and gentlemen if you would like to ask a question please press \*1 on your telephone keypad and I'll be able to open up your line. So \*1 if you have a question.

The first question is from Sanjeet Aujla, from Credit Suisse in London. Please go ahead Sanjeet.

#### **Sanjeet Aujla, Credit Suisse**

Hi Zoran, my first question is regarding the competitive dynamics in Nigeria and Russia. You talked about intense price competition and I seem to remember in Nigeria you're running at a bit of a price premium to your competition. So can you just talk a little bit about how you're managing the competitive environment there, that's my first question?

#### **Zoran Bogdanovic, Chief Executive Officer**

Thank you Sanjeet. So let me just remind you, we indicated in the full year call that indeed Nigeria is going to be having a soft Q1 start and that has happened, because we knew that we would be cycling tough volume comparatives, as well as cycling a quarter where last year we've been with two price increases just before the last bigger price increase that we took on April 1st last year. So that has materialised and we knew that we will be trading at a price premium versus the key competitor and other competitors there.

So nothing surprising there. Basically the intensity of the competition is, as we anticipated, and based on that we have adjusted our plans, both for Q1, but even more importantly for the quarters that are ahead of us, with various pack, brand and price combinations.

In Russia we also see that competition has actually a bit more intensified in the quarter. Deciding to - what we see in the market, putting much more promo pressure. Our conscious choice was to respond to that to only a certain degree because we do prioritise the value creation game for us in our customers. And that has been the reason for the result. And that is what drove our choice.

We also saw, according to our plan, that as we were approaching the end of Q1, Russia came back to growth and this is what we also see - how it started in Q2.

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### **Sanjeet Aujla, Credit Suisse**

I understand thanks. My second question is just coming back to some of your revenue growth management initiatives, can you just give us a bit more colour as to maybe some examples as to some of the initiatives and how they are driving price/mix benefits across your business?

### **Zoran Bogdanovic, Chief Executive Officer**

Yeah sure. So indeed, as I mentioned in the last call, we have been intensively focusing as an organisation on raising these capabilities across all our business units. We are, this year, finishing our full rollout, and this will be valid in all markets, which means that we have first of all ensured that we have resources in all the business units who have the expertise, knowledge, we have in hand the tools which we are using which are helping us to read better the market dynamics, draw insights which we are then converting into sharp and focused actions.

Now in each market there is a specific dynamic on what we are focusing that depends on the market conduct, competitive play, so that's why I cannot say that all markets are having the same initiatives or strategies.

That means also that we, within this context, analyse very well and understand where are the opportunities for our strategic pricing, as well as various smart, or if you will, tactical pricing.

Secondly, how we focus on the evolution of our packages, where a bigger focus on smaller packages plays a continuously bigger role. That's why you will see examples where we are introducing smaller sized packages, so basically doing even bigger SKU proliferation within single serves. That's why you see in several markets where we are launching 250ml cans. Also, we are having multipacks of single serves, which are going into the organised trade, which clearly drives the value and creates the habit of the single-serve consumption in the 'at home' consumption.

RGM is helping us also that in a better and educated way we are improving our promotional effectiveness of what we are doing in the market, as well as what kind of combinations and multipacks we are executing in the market. And that helps us a lot.

Additionally, RGM also helps us to realise how we can better do stratification between the brands, which also is connected with our recognition of how do we premiumise and focus on premiumisation of certain categories, or even brands. An example is that we see Schweppes in many of our markets, actually I didn't mention it earlier, but I want to highlight that Schweppes in Europe is growing 18%. The only country where it is the exception is Nigeria, but that's also a conscious choice because we prioritise other brands, but Schweppes in Europe is growing 18% and that is also a result of our RGM focus and identified initiatives.

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And maybe just one last point to say Sanjeet. I mentioned that in Q1 the volume of Sparkling drinks has been 2.8% up. At the same time, Sparkling revenue grew 5%. So that clearly also tells you how revenue grows faster than volume, which is our key objective.

That is not valid only for Sparkling, but equally it is also valid in Water, where we are playing both - and I would say a good balanced game between volume and price/mix. So volume of Water in Q1 grew 0.9%, but at the same time revenue of the Water grew 2.4%.

So I'm very passionate about it, so I could talk for ages about this, but I hope this gave you a solid flavour of what are those things that we are working on and that even going forward we will be focusing on. Thank you.

### **Sanjeet Aujla, Credit Suisse**

That's great, thanks Zoran.

### **Telephone Operator**

The next question is from Edward Mundy, from Jefferies in London. Please go ahead Edward.

### **Edward Mundy, Jefferies**

[Audio jumping] Morning everyone, first question is you mentioned that Russia has gone back into growth in the first quarter - can you indicate to us whether the price environment is more normalised into Q2?

### **Basak Kotler, Director Investor Relations**

Apologies Ed, that is a very bad line, could you at least repeat your question.

### **Edward Mundy, Jefferies**

Sure, let me try again. So you indicated Russia has gone back into growth at the end of the first quarter, has the pricing environment improved or normalised into the second quarter?

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### **Zoran Bogdanovic, Chief Executive Officer**

Thanks Ed. Well, we actually do see that it continues to be quite price sensitive - sorry price intense, so we don't see that it is easing off. But what is important to say in Russia is that our planned RGM initiatives and changes that we are doing in the market have been launched at the end of Q1, so effectively they are kicking in from Q2 and that's why we know that a number of these moves that we are doing are also taking into account this intensive competition that is at the moment visible in Russia.

### **Edward Mundy, Jefferies**

Thank you. And my second question is on currency, presumably given that you don't mention currency within the Q1 trading statement there's no change to the outlook given back with fiscal 2017 results of the €30m adverse impact to EBIT?

### **Michalis Imellos, Chief Financial Officer**

Hi Ed, this is Michalis, so we do have some changes with regard to our expectations for FX and that's primarily because we have seen recently the ruble weakening quite significantly against the dollar. So let me just give you some colour about quarter one first and then a little bit on the full year.

So in quarter one, we had a situation where the euro, versus prior year, strengthened quite significantly against the dollar, that was approximately 13%. And this resulted in the dollar based currencies like the ruble to weaken significantly versus the euro. So for example the ruble weakened against the euro by about 12% year over year in quarter one, despite the fact that it strengthened against the dollar in the same period by about 2%.

So that means that in quarter one we saw transactional FX being positive year over year, but translational being strongly negative as a result of the euro strengthening and all the cross rates being quite strong. So overall in quarter one we saw FX being negative year over year by about €5m in the first quarter.

Now, what's happening in the full year compared to the guidance that we gave back in February for a €30m hit, based on the levels of hedges that we had at that point in time and the spot rates at that point in time. As I said the ruble has weakened recently against the dollar, it's about 8% depreciation. And we saw also some other currencies, like for example the Swiss franc and the Polish zloty also moving to a weaker position, around 3% to the euro.

So that means that both the translational and transactional FX will deteriorate on a full year basis, compared to the February guidance, based on the spot rates that we see now. And that means that we expect, based on the hedges we have and the current spot rate, the FX hit on

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the full year to be around €45m, so from the €30m to €45m and the ratio of transactional to translational will stay at more or less 1:2, transactional to translational.

Now, of this €15m deterioration versus the February guidance I would say two thirds is attributable to the ruble, to Russia and the rest is all the other currencies to a smaller extent.

We are quite well hedged, having said all that, we are more than 80% hedged on the ruble to dollar and around 50% on the ruble to euro, which plays a role both on transactional and - plays a role on transactional. Obviously we are not hedged on translation and that's where the exposure is.

And I would conclude by saying that this extra €15m has always been part of our plans when we were starting the year. So with the acceleration of the year to go top line that you heard from Zoran we are confident that we can fully absorb this extra €15m impact, should it materialise and should the current rates continue throughout the year.

### **Edward Mundy, Jefferies**

Very clear, thanks very much. And just my final question, Zoran you mentioned quite a lot of innovation coming through on some of the core Sparkling brands, are you able to indicate as to whether those are coming in at a higher price point and also the level of cannibalisation to the core brands?

### **Zoran Bogdanovic, Chief Executive Officer**

Thank you. So first of all let me just say and build on what I said in the last call, is that this year really indeed we see and we will see a much higher level of innovation than we've seen in the past or actually ever. And this year we see that coming through either as the new brands, or packages, or reformulations, and the majority of that, even though it started in Q1, but effectively it starts from Q2 onwards.

So it really depends on various packages and sizes, but we do always have in mind that we are looking after a product and brands that will drive the value for us and the customers. So for example we are extremely happy that we are starting in Q2 with a full new category of plant based beverages, which is clearly enhancing us, or bringing us on the journey towards the total beverage company that we are evolving to. That has higher NSR per case.

We are also starting with Smartwater as a way to also bring more value into the category that doesn't have, versus other categories, a bigger value. So Smartwater also commands that higher value per litre that is very good for us as well as customers and of course consumers because it offers a distinctive product benefit.

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Also in the Sparkling category as well we have various flavour extensions which are mostly related to Coca-Cola Zero extensions because we see that that is working extremely well, it further fuels our strong growth of the light and zero segment. And in some of the markets those extensions are coming at a premium to the regular variant.

Also, we have launched already at the end of Q1, a new brand into the Adult Sparkling, which is Royal Bliss, which has been launched in Italy, Austria, Switzerland, Hungary, that comes at even a significant premium to the Coca-Cola brand. And also we had a number of extensions on Schweppes which I mentioned a little bit earlier, which almost in all markets where we operate already has a premium to Coca-Cola. And such extensions which offer very unique flavour combinations are giving us a good leverage to come at even a higher price premium. That has been also combined with innovation in the packaging that we have done, which further enhances the premiumisation justification of what we do in the market.

I hope that answers and gives you a sufficient light into what we are doing there.

**Edward Mundy, Jefferies**

Thanks very much.

**Telephone Operator**

The next question is Saranja from Bank of America London. Please go ahead Saranja.

**Saranja Sivachelvam, Bank of America**

Good morning, thanks for taking the question. The first one is about Russia and Nigeria, so given what you've elaborated on in FX and trends, what's driving the forecast for recovery in these markets going forward?

**Zoran Bogdanovic, Chief Executive Officer**

Thank you Saranja, you don't mean on FX, but overall?

**Saranja Sivachelvam, Bank of America**

Exactly, thanks.

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### **Zoran Bogdanovic, Chief Executive Officer**

So first of all we do see that in both of the markets, like in Russia we do see that slowly but steadily the market is improving, also the level of inflation that at the moment we see and that is there also is encouraging. Also Nigeria is in this stable economic trending, which is very good. So that's the starting point.

Now let me just say in Nigeria we have started with a high speed line in March which is critical for our product availability in a critical package of PET, and that helps us going forward to close some of the availability gaps that we had so far.

Also we did have in Q1 certain issues with our juice line which has disrupted our availability in Juice and it was not continuous which has been fully fixed. So we are operating now full speed also in this category.

Plus that we have very strong plans in the remainder of the year from activation of the FIFA and Nigeria being in the World Cup. That plays a very important role for Nigerians and the way we are activating that with the Coca Cola Company we believe is strong and gives us the confidence that this will guide transactions and revenue for us and our customers.

In Russia first of all we have completed in April a full listing of the Fuze Tea with all the key accounts. As I mentioned in the earlier question effectively from Q2 we are starting with our new OBPPC strategy which is introducing some of the single serve packs in the market. We also have a small downsize of one litre to 0.9 litre to strike a better balance of keeping the price point and better price per litre value.

We have to bear in mind also that in Russia we will be cycling the very poor summer of last year. Also I mentioned that already in March and April trading is encouraging and in line with our expectations.

And last but certainly not least is that Russia hosting the FIFA World Cup. We are just now entering in the heat of the activation and campaign with this great property that we will be activating so we have a number of reasons that do give us confidence that both in Nigeria and Russia we will be bouncing back from Q1 and we will see growth in the coming quarters.

### **Saranja Sivachelvam, Bank of America**

Thank you. And just one other question please. Appreciate that the Irish sugar tax has only been in place for a short time but what are your initial thoughts around it, and I saw in a press release that there was some trade loading ahead of the price hike? Thanks.



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### **Zoran Bogdanovic, Chief Executive Officer**

Well as you said it's fresh as in the Republic of Ireland it only started as of May 1st. And I would just say that there is nothing so far that indicates any worry or concern or anything like that. I have to give credit to the local team which well in advance has prepared very thoroughly for this change and that has caused a number of moves that were done in the market, obviously in the pack and price which means that we have introduced now two smaller packages for regular Coke which is 250ml can, 375ml PET. So to keep the critical price of Coca-Cola intact. Also in the larger packages we have reduced 1.75 to 1.5 on Regular Coke. So we have done critical adjustments. There has been excellent collaboration and buy in of customers who have also recognised that these adjustments are well suited to amortise and to deal with the tax.

As a reminder as well we already now 60% of our portfolio is below the threshold of the levy so will not be impacted. So we are already on a strong base coupled with these pack price changes that have been done, excellent collaboration with customers, communication. So we believe that we are as good as one can be in dealing and accepting the new reality in both of the Irelands.

### **Saranja Sivachelvam, Bank of America**

Thank you very much.

### **Telephone Operator**

The next question is from Stamatis Draziotis from Eurobank Equities in Athens. Please go ahead Stamatis.

### **Stamatis Draziotis, Eurobank Equities**

Thank you very much. Just a quick question from my side. Could you just quantify what the Easter impact was in the Established and the Developing segments please?

### **Zoran Bogdanovic, Chief Executive Officer**

Thank you Stam. I think mentioned earlier the effect of Easter in Established; we estimated it is around 50 basis points whereas in Developing we said it's 3%. The reason that also in Established as Easter came this year earlier than effectively being end of Q1 or being on April 1st in some of the markets like Italy, Austria where weather and winter lasted longer than we

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really wanted, that really minimised the impact of the Easter and we really didn't see the usual effect of what Easter should bring for our type of business.

### **Stamatis Draziotis, Eurobank Equities**

That's very helpful, thank you. And just a very quick follow up on the question on the cost side. You talked about the adverse effects impact and the update you had on that given the recent move of the rouble. Just wondering about the input cost inflation on FX neutral basis. Does this still remain based on your estimate in the low single digits?

### **Michalis Imellos, Chief Financial Officer**

Hi Stam. No change on the input cost front, everything is moving exactly in line with expectations. And that's no surprise because as we were saying also in February we are extremely well hedged for 2018. We are already fully covered in EU sugar; we are fully covered in Russia sugar-wise, more than 80% in Nigeria. Aluminium we are 75% covered already.

So the only commodity that we are potentially more open is resin. We are right now around 35% to 40% on a full year basis covered. So what we see is a price in the resin that is very close to where we were expecting. We see very, very small good news on world sugar because the spot rate has moved recently at very low levels. So all in all reiterating the guidance we gave in February for low single digit increase in input cost per case currency neutral on a full year basis.

### **Stamatis Draziotis, Eurobank Equities**

That's great, thank you so much.

### **Telephone Operator**

And we have a question from Laurence Whyatt from Société Générale in London. Please go ahead Laurence.

### **Laurence Whyatt, Société Générale**

Hi good morning. Thanks very much for the questions. My first one is a follow up from the previous question on the Irish sugar tax. Those volume reductions that you mentioned seem

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to be pretty large, about 25% volume reduction on those two pack sizes that you mentioned. Are you therefore taking price on those if you're putting those through at the same price as the original pack sizes and therefore getting a slight benefit from the sugar tax?

**Zoran Bogdanovic, Chief Executive Officer**

Hi Laurence. Sorry can you just clarify on which volume reduction you mean? You mean on the pack sizes?

**Laurence Whyatt, Société Générale**

Yeah exactly. So it sounded like you've taken your PET down from 500 to 375, that's about a 25% reduction, and then the 330 can down to 250ml which is just shy of a 25% volume reduction.

**Zoran Bogdanovic, Chief Executive Officer**

It's excellent that you asked this question because I just need to clarify. I have mentioned the additional packages that we are introducing in the market which are coming on top of the half litre which stays in the market.

**Laurence Whyatt, Société Générale**

Okay that's very clear then, thank you very much for clarifying that.

The second question, again on sugar taxes, we've obviously had a lot of press in the UK market around the sugar tax and no doubt Ireland has had something similar. I'm sure you're constantly in dialogue with the numerous countries that you deal with in terms of the health lobbies and the governments that are interested in the health of their citizens. Since the introduction of these taxes, particularly in 2018, have any of those discussions intensified with either government health officials or health lobbies in any of your countries?

**Zoran Bogdanovic, Chief Executive Officer**

Well first of all those kind of considerations in the countries in our territories are really not widespread. And secondly we have not seen that anything has intensified because of the

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situation in Ireland and in GB because of this tax. So nothing that we would really say that has been triggered further or anything like that.

### **Laurence Whyatt, Société Générale**

Okay thank you very much. And then finally just a clarification really. You mentioned that your Developing business got an additional 3% growth you think from the timing of Easter. Could you give similar numbers for your other two divisions and therefore an overall effect of the timing of Easter on your Q1 numbers?

### **Zoran Bogdanovic, Chief Executive Officer**

Indeed so 3% in Developing. I mentioned earlier 50 basis points in the Established. And the Emerging we don't see - basically we didn't see the impact, we didn't see it.

### **Laurence Whyatt, Société Générale**

Excellent, that's all very clear. Thank you very much.

### **Telephone Operator**

The next question is from Chris Pitcher from Redburn in London. Please go ahead Chris.

### **Chris Pitcher, Redburn**

Good morning. A couple of questions or one question really on competition. Can you give us a bit more colour on where the competition is coming from specifically in Nigeria and Russia? Is it Pepsi, is it the local B brands or is increasingly from the brewers as they push into soft drinks with low and no alcohol beer? Thanks very much.

### **Zoran Bogdanovic, Chief Executive Officer**

Thank you Chris. So in both of the markets you mentioned yes Pepsi is the key competitor. So they are the key competitor and they have been - obviously with probably their own objectives they've been intensifying the price sensitivity and intensity in the market.

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Now in Nigeria also apart from the Pepsi you have a number of smaller players but this is something that we have seen always in Nigeria that a number of the players come and go. So you know we do pay attention not only to always the key competitor but we always look at the broader market. And when we design our plans for the next years and how we cause correct what we do in a current year takes into account the key competitor but also the other ones. So we take all those into account.

### **Chris Pitcher, Redburn**

Could you be a bit more specific on what the brewers are doing and maybe extend it to Italy as well where the brewers are going after the no alcohol occasion?

### **Zoran Bogdanovic, Chief Executive Officer**

Yeah. Look nothing - I mean you know that in Nigeria brewers are in malt which is kind of a specific category for that country. So nothing new or unusual there. But also across the rest of the countries we haven't seen anything that is visibly accelerating versus what we have seen in the past years that here and there with small percent of their portfolio they are doing stints into non-alcohol beer or some Radlers or these types of things. But nothing that I would say we would report as a big or significant increase.

But let me just also add that to build on what I said earlier, when we see what happens in the market we equally always keep on the radar screen what all these guys also in the beer sector are doing because we all start with the consumer and what are the occasions. So we take that very well into account when we also design what we will do.

### **Chris Pitcher, Redburn**

Thank you. And maybe just one quick clarification, apologies if I missed it. Did you give an absolute impact of the pre buying in Ireland on the volume number?

### **Zoran Bogdanovic, Chief Executive Officer**

No you didn't miss it because I didn't mention it. And there was really nothing significant and we didn't hear any - we didn't see any serious pre-stocking, maybe it was around 1% but really nothing major.

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**Chris Pitcher, Redburn**

Thank you very much.

**Telephone Operator**

And we have a question from Andrea Pistacchi from Deutsche Bank London. Please go ahead Andrea.

**Andrea Pistacchi, Deutsche Bank**

Yes good morning. My question is on constant currency net revenue per case please. I think at the full year results your suggestion for the full year it was that in Established markets that you could improve a bit what you did in 2017, and for Developing markets you also said slightly better net revenue per case this year.

Q1 was a bit slower on both. I appreciate there's less channel mix but has it changed in any way your expectations for the full year?

**Zoran Bogdanovic, Chief Executive Officer**

Thank you Andrea. So well short answer is no. In the Established indeed with this plus 0.8% but we do see that we will have another year of the NSR per case growth. So we confirm that outlook.

And in the Developing we do see that we would be around 2017 possibly a bit slightly higher but we do confirm also that piece.

**Andrea Pistacchi, Deutsche Bank**

Okay thank you.

**Telephone Operator**

Ladies and gentlemen as a reminder if you have a question please press \*1 on your telephone keypad. Thank you.

We have no further questions so I'll hand back to your host to conclude. Thank you.

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### **Zoran Bogdanovic, Chief Executive Officer**

Thank you operator. I want to thank you for joining us today and for all your questions that facilitated a good discussion around our first 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 are pleased with the results that these initiatives have delivered in the last three years. We look forward to sharing more progress with you in the coming period. Thank you and have a great day.

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