CCH – 2018 Half-year financial results
Conference call script – 9 August 2018

CORPORATE PARTICIPANTS

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Michalis Imellos - Coca-Cola HBC AG – CFO

Basak Kotler - Coca-Cola HBC AG - IR Director

Operator

Thank you for standing by ladies and gentlemen, and welcome to Coca-Cola HBC's conference call for the 2018 half-year results. We have with us Mr. Zoran Bogdanovic, Chief Executive Officer, Mr. Michalis Imellos, Chief Financial Officer, and Ms Basak Kotler, Investor Relations Director. At this time all participants are in listen only mode. There will be a presentation followed by a question and answer session. If you wish to ask a question, please press star one on your telephone keypad at any time and wait until your name is announced. I must also advise that this conference is being recorded today Thursday, August 9, 2018. I now pass the floor to one of your speakers, Ms Basak Kotler. Please go ahead.

Basak Kotler - Coca-Cola HBC AG - IR Director

Good afternoon. Thank you for joining our call today to discuss Coca-Cola Hellenic Bottling Company's results for the first half of 2018.

Today, I am joined by our Chief Executive Officer, Zoran Bogdanovic and our Chief Financial Officer, Michalis Imellos.

Following the presentation by Zoran and Michalis, we will open the floor to questions. In order to facilitate a good Q&A session, we suggest that you ask your questions one at a time, waiting for us to answer one question before you ask another. The operator will keep your line open, until we have exhausted all your questions.

Before we get started, I would like to remind everyone that this conference call contains various forward looking statements. These should be considered in conjunction with the cautionary statements on the screen. This information can also be viewed in our press release issued today.

Now let me turn the call over to Zoran.

Zoran Bogdanovic - Coca-Cola HBC AG – CEO

Half-year highlights

Thank you Basak. Good afternoon everyone and thank you for joining our half-year results call.

I will start by giving an overview of the first six months. Michalis will then take you through our financial performance, before I discuss our operational performance and outlook for 2018.

We delivered a strong set of results in the first half, as the evolution of our portfolio gathers pace. Our new categories, flavours, reformulations and packages are gaining traction across our markets, with 34 million cases of volume in the first half, representing 3.2% of our volume. These new product launches and tailored commercial activation enabled us to capitalise on favourable weather conditions and the FIFA World Cup.

Revenue growth, up 6.4% on an FX-neutral basis, accelerated in the second quarter, driven by both volume and price/mix improvements.

Volumes grew in all three of our geographic segments, resulting in 4.6% growth overall. Within this, Sparkling beverages volume was also up 4.6%. I will give you some more colour on this in a few minutes. As anticipated, volume growth in Russia and Nigeria came through in the second quarter.

FX-neutral revenue per case growth moderated slightly as we cycled price increases taken in Emerging markets in 2017. Nevertheless, the combination of price increases, category and package mix delivered 1.8% improvement.

The investments to support the FIFA World Cup and our revenue growth initiatives resulted in a 30 basis point increase in total marketing expenses as a percentage of revenue. Notwithstanding this increased investment, we delivered a 60 basis point improvement in comparable EBIT margin in the period.

Comparable EPS was 60.3 Euro cents, up 4.7% on the prior-year period.

With that, I will turn the call over to Michalis.

Michalis Imellos - Coca-Cola HBC AG – CFO

Financial review

Thank you Zoran and hello everyone.

In line with our practice, as I take you through our financial results for the first half of the year, I will refer to comparable figures which exclude the impact of restructuring costs, the mark-to-market valuation impact of commodity hedges and specific non-recurring items.

Financial performance overview

Volume growth of 4.6% was broad based across the segments and accelerated in the second quarter, supported by new product launches, good weather and FIFA World Cup activations. Both Russia and Nigeria returned to growth in the second quarter and our medium-sized Emerging and Developing segment countries maintained their positive momentum.

Currency-neutral net sales revenue grew by 6.4% in the first half of the year. We are pleased to see reported net sales revenue increasing by 0.5%, despite the resumption of currency depreciation in our emerging markets.

FX-neutral revenue per case grew in all segments, up 1.8% overall, with positive contributions from price, package and category mix.

Gross profit margin declined by 10 basis points, as the improvement in price/mix did not fully offset the impact from adverse currency movements and the reporting of excise taxes in revenue.

Operating expenses as a percentage of revenue improved by 60 basis points driven by top-line operating leverage, notwithstanding a 30 basis point increase in investments in marketing. We did however, benefit from the cycling of prior year's bad debt provision in Croatia and partial recovery thereof in the first half of this year, which amounted to 40 basis points in total.

Financial performance overview

Comparable operating profit increased in the first half by 6.7% compared to the prior-year period, and comparable operating profit margin expanded by 60 basis points to 9.6%. Better price/mix, volume and operating leverage, as well as lower input costs drove this positive result.

As I have already mentioned, depreciation of our Emerging segment's currencies resumed in the first half, resulting in a 23 million Euro currency headwind. Major drivers were the Nigerian Naira and the Russian Rouble, followed by the weaker Swiss Franc.

Financing cost increased by 1.6 million Euros in the period, mainly as a result of lower interest returns on cash deposits.

Comparable EPS reached 60 Euro cents, 4.7% higher than the prior-year period.

Working capital balance has improved significantly in the first half compared to the prior-year period. We are on track to reach, once again, our target of triple-digit negative balance for the full year.

We generated strong free cash flow of 126.8 million Euros in the first half, an improvement of 31.7 million Euros year on year. Higher operating profit and lower tax payments were partially offset by higher capital expenditure and lower cash generated by working capital movements.

Acceleration of revenue growth in Q2, driven by volume

Turning to the revenue performance, volume was the main driver of the 6.4% currency-neutral revenue growth in the first half of the year. The second quarter was the biggest contributor, as the acceleration of our commercial initiatives and the new product launches capitalised on the favourable backdrop presented by good spring and June weather and the FIFA world cup, supporting volumes.

In the first half, currency neutral revenue per case growth moderated to 1.8%, driven by a slowdown in the Emerging segment.

In our Established markets, currency neutral revenue per case increased by 1.1%, driven by favourable price mix, as the result of the sugar tax implementation in Ireland, and small price increases selectively taken in other markets, as well as positive category and package mix.

In Developing markets, currency neutral revenue per case grew by 0.9%, influenced by higher promotional activity during Easter combined with high Water volume. Favourable impacts from price, category and package mix, were partially offset by negative channel mix.

The Emerging markets saw a slowdown in the currency neutral revenue per case growth, mainly due to the cycling of the price increases taken in Nigeria in 2017. The growth of 3.8% was the result of favourable price, package and category mix, partially offset by adverse channel mix.

Input costs positively influenced by declining sugar prices

Turning to input cost:

Currency neutral input cost per case was down by 0.9% in the first half of the year. This is slightly more benign than the guidance we gave in February.

The main driver for the input cost improvement was sugar, for which our coverage was very high at rates that represent a low-teens percentage decline compared to the prior year. The very good crop and the abolition of the EU quota regime have led to an oversupplied market, pushing the spot rates to very low levels.

PET prices did increase in the first half of the year, in line with higher oil prices. However, with careful management and certain well-timed pre-buys, we secured better pricing than market spot rates.

Aluminium saw rate increases in the first half of the year, but with good management of contracts and favourable hedges, we have minimised the impact.

Operating leverage delivering, notwithstanding higher marketing investment

Turning to our OpEx performance

We have worked hard over the years to right-size our operating cost base, and we continue to use our infrastructure effectively while we grow the topline. In the first half of the year, this resulted in comparable operating expenses reducing to 28.0% of revenue - a 60 basis-point reduction compared to the prior year.

Let me walk you through the key drivers.

Sales expenses as % of revenue improved by 70 basis points, driven by the cycling of prior year's bad debt provision in Croatia and partial recovery thereof in the first half of this year.

Administration and other costs as % of revenue improved by 40 basis points, mainly reflecting the good operating leverage effect.

Direct marketing and marketing expenses as % of revenue increased by 30 basis points, to support the new product and flavour launches, the FIFA related commercial activities and other revenue growth management initiatives.

Warehouse and distribution expenses as % of revenue grew by 20 basis points, driven by higher costs related to fuel, tariffs and higher volumes sold.

As a result, we are pleased with the ongoing strong underlying performance of our operating expenses as a percentage of revenue, especially in view of the growing investments in the market that support the evolution and growth of our business.

Profit and margin growth

Turning to the operating performance, we are reporting comparable operating profit of 310.5 million Euros in the first half of the year, 19.4 million higher than in the prior-year period.

This is the result of the operating leverage on strong top line growth, with improvements in both volume and price/mix, partly offset by adverse currency movements, mainly in the Emerging markets.

Let me provide you with some more colour on the key drivers on a segmental basis:

The Established markets segment benefitted from volume growth, favourable price and product mix and lower operating expenses. These were only partially offset by the adverse foreign exchange impact, mainly from the Swiss Franc.

In Developing markets, higher volume sold, favourable price and mix, along with lower operating expenses driven by the cycling of prior year's bad debt provision in Croatia and partial recovery thereof in the first half of this year, led to an operating profit expansion of 23 million Euros.

In Emerging markets, volume growth and improvements in price and mix, partially offset the higher cost of goods sold, higher operating expenses and adverse currency movements.

Restructuring plans

As far as restructuring is concerned:

In the first half, we incurred restructuring charges of 4 million Euros, mostly focused on Established and Emerging markets.

For the full year, we expect restructuring costs to reach 25 million Euros, with estimated annualised benefits of 12 million Euros from 2019 onwards.

The savings in 2018 from initiatives taken in 2017 and those that will be taken in 2018 are expected to reach 11 million Euros.

Growing free cash flow driven by higher operational profitability

Turning now to free cash flow, we generated 126.8 million Euros in the half year, 31.7 million more than in the prior-year period.

Cash flow generation was supported by higher operational profitability and lower tax payments, while net capital expenditure increased by 14.6 million Euros.

We are investing in the business to support growth. Key areas of the capital expenditure increase in the period were new coolers placements across the majority of our markets, as well as new production equipment, mainly in Nigeria, where we invested in additional capacity to fulfil the growing demand for PET packages.

EBIT margin development

Before I conclude, let me walk you through the key components of our margin development.

The 60 basis point expansion in the EBIT margin can be explained as follows:

- 80 basis points of margin expansion from volume leverage – based on the 4.6% volume growth in the year, and accounting for some of the volume growth that doesn't contribute to operating leverage. The best examples are Premium Spirits and non-ready-to-drink Coffee, which are bought and sold as finished goods.
- 100 basis points expansion from revenue leverage – based on the 1.8% growth in currency neutral revenue per case, and netting off the impact of Premium Spirits

and Coffee as above, as well as sugar tax in Ireland, which is added to revenue only to be fully deducted from cost of sales.
- 10 basis points expansion from our cost productivity initiatives
- 70 basis points contraction from the combined impact of currency and input costs
- 20 basis points contraction from increased investment in innovation, which is driving our revenue.
- We also have a 40 basis point headwind from one-off costs. These include increased environmental fees, sugar tax, our investment into the redesign of our revenue growth management framework, partly offset by the positive impact of the Croatian bad debt we have talked about.

With that, let me now pass the floor to Zoran, who will take you through the operational performance for the year.

Zoran Bogdanovic - Coca-Cola HBC AG – CEO

Operational review and strategy

Thank you Michali.

Volume by segment

Overall, first half volume increased as stated by 4.6%, with all three segments contributing positively to volume expansion. We saw the anticipated acceleration in volumes in the Emerging segment, as both Russia and Nigeria returned to volume growth in the second quarter. The 5.1% increase in the half is the fastest growth we have seen in this segment in three years.

Looking at the segments

In Established markets, volume grew by 0.9% with a return to volume growth from Sparkling. Energy and Water also contributed positively, while Juice and RTD Tea declined.

Developing markets grew volumes by 8.9%, with all markets showing positive volume growth. Outside of RTD Tea, all categories grew volumes.

In the Emerging markets, where volume grew by 5.1%, Russian volumes were positive in the first half, while Nigeria's were down marginally. Both countries delivered strong volume growth in the second quarter. In addition, we continued to see very good growth from other countries in the segment, particularly Romania, Ukraine, Serbia and Bulgaria.

Volume growth by category

Looking at our performance by category:

Sparkling volumes increased by 4.6%, growing across all our three segments. In fact, aside from Italy and Nigeria, where Sparkling volumes were down slightly, we grew Sparkling volumes in every single market in the first half. Volume growth, combined with healthy price/mix, resulted in revenue growth of 7.4% for the category. We are very pleased to see that our innovation pipeline of new reformulations, flavours and packages are meeting the consumers' preferences and adding value to our customers by accelerating growth in this important category.

Trademark Coke is doing very well with a 5.3% rate of growth in the first half. Within this, the fastest growing brand continues to be Coke Zero, which grew by 24.9% with excellent contributions from every market in the business.

We are also particularly pleased by the 10% growth in our Adults Sparkling portfolio, which includes brands such as Schweppes, Kinley and newly launched Royal Bliss, and we are encouraged by the strong growth rates we are seeing from the Adults category in the more developed markets. For example, Adults Sparkling grew by low teens in the Established segment and high teens in the Developing segment.

We are also seeing good growth in our Still drinks portfolio.

Water grew by nearly 5%, driven by growth in Emerging and very strong growth in the Developing segment, where volumes increased by 20%, while the Established markets volumes were broadly stable.

Juice volumes were flattish. Volumes declined in the Established segment, mostly due to large declines in Ireland from the decision to reduce distribution of dilutes. Developing and Emerging segments grew driven by good performance mainly in Poland, Romania and Serbia.

Energy continues to see very good growth and the first half was no exception with volumes up 33.5%. We saw strong growth from both Monster and Burn and in all three segments.

RTD Tea declined by 0.6% in the first half but volumes were up by 0.5% in the second quarter; it's still early days in our territories with the FUZE brand, but I can say that at this stage we're very pleased by what we're seeing.

Established markets - Focusing on innovation and value

Turning now to our performance by segment and focusing on some of the bigger countries.

In our Established markets segment volume was up by 0.9% in the first half of the year.

In Italy, the main drivers of the small decline were Water and full-sugar Sparkling. We are encouraged to see growth in our strategic areas of focus, such as lights and zeroes. Coke Zero grew 13% and we are also seeing good growth from Fanta Zero and Sprite Zero. Our glass bottle for the HoReCa channel is doing well and we saw good indications from our launch of Royal Bliss. RTD Tea is seeing remarkable results with volumes up 30%; and Energy grew by over 30%, as well.

Volume in Greece grew by mid single digits in the first half, driven by good volume growth in Water, Sparkling and Energy. Within Sparkling we are seeing growth from our no-and-low sugar variants, Coke Zero grew 17% for example. We are also seeing good results from some of the new innovations in that space too, such as Sprite Zero Lemon Mint launched in April and Fanta with Stevia launched in June. Schweppes also benefited from innovation with a new glass bottle and new Lemon and Mastic Mint flavours, contributing to the overall 16% volume growth for the brand.

In Switzerland, volume declined marginally. We saw good performance in Sparkling and particularly in Trademark Coke which grew by 4%. This growth was more than offset by declines in Water, where we took the decision to de-list at a large QSR chain where pricing was undermining profitability, thus not creating value.

The Established segment saw a 1.1% improvement in FX neutral revenue per case, driven by favourable price, category and package mix.

<u>Developing markets – Continued good growth in all markets</u>

In our Developing markets, volume grew by 8.9% with growth in all the markets in the segment and strong volume growth in Sparkling and Water.

In Poland, volume increased by 10% with Sparkling up high single digits and volume growth from all of our brands. Kinley, our Adults sparkling brand in Poland grew by nearly 50%, following the successful launch of a premium bottle. Water volumes were particularly strong in the first half; we have taken the decision to support our Polish water brand Kropla with additional promotion and that has proven very successful.

In the Czech Republic, volume grew by low single digits, with all categories growing except for Water. Sparkling delivered mid single-digit growth and Energy grew by double digits on a strong growth from Monster.

Hungary continues to see very strong growth. First half volumes were up high single digits. Sparkling volumes grew high single digits and we saw particularly strong growth from Coke Zero, which was up over 30 percent, boosted by new flavours like Coke Zero Lemon and Coke Zero Cherry. RTD Tea was also strong with volumes up double-digit.

Overall in the segment, favorable price, category and package mix resulted in a 0.9% increase in FX-neutral revenue per case, while channel mix was unfavourable.

Emerging markets – Medium-sized markets driving growth

Volume in our Emerging markets grew by 5.1%, an acceleration from the slight decline in the first quarter, as we saw the anticipated return to growth in Russia and Nigeria in the second quarter.

Volume in Russia was up low single digits in the first half. The NARTD market has returned to growth in Russia in 2018 as the economy shows signs of recovery, and the second quarter saw an acceleration in the growth in the underlying market aided by good weather and the excitement created by the FIFA World Cup. Strong execution and increased promotional activity in a competitive environment supported our growth. Sparkling volumes were up by mid single digits, with Trademark Coke up by high single digits and Fanta up by double digits, helped by the success of Fanta Pear. Our Adult portfolio is also doing well in Russia, with Schweppes up by double digits. RTD Tea returned to growth in the second quarter, but was still down by low single digits for the first half.

Volumes in Nigeria in the first half were down by 0.7% as the strong volume growth in the second quarter recovered nearly all of the volume lost in the first quarter. Sparkling volumes were stable in the first half, and we saw very good growth from our PET packages, as availability of these packs improved. We also benefited from strong demand for Coke Zero and our local brand, Limca. Water volumes declined by low single digits in the first half but grew in the second quarter.

Volume in Romania grew by 11%, with strong results across all categories. Sparkling grew by double digits, with Coke Regular up by high single digits and Fanta up nearly 20%, supported by new flavours like Fanta Grapefruit. Innovation also underpinned the strong results from Schweppes with the launch of new premium bottle and Ginger Ale flavour in April. Water grew high single-digit and Juice double digit with strong growth from both Cappy and Cappy Pulpy.

Currency neutral revenue per case grew by 3.8% in the period, with price/mix growth slowing in the Emerging markets, as expected, as we cycle price increases taken in Nigeria in 2017, and as the inflationary environment in Russia remains benign. Category and package mix also supported currency neutral revenue per case.

Looking ahead

In conclusion, we expect the scaling up of the innovations in the second half to continue to support our growth. We are also expecting a better balance between volume growth and price/mix improvements in the full year.

Looking ahead to the second half, we expect volume in the Established markets to grow slightly faster, while Developing and Emerging markets moderate their growth compared to the very strong first-half performance.

Our revenue growth management initiatives, selective price increases and lower promotional activity in certain markets are expected to deliver an acceleration in currency neutral net sales revenue per case growth in the second half of the year.

Our full year expectation for input costs, on an currency neutral per case basis, is for flattish year-on-year outcome, which is slightly better than our previous guidance of very low single-digit increase.

We also expect the impact of currency movements to be approximately €45 million for the full year. This is in line with our previous guidance.

Overall, we continue to make good progress against the 2020 targets and expect to deliver another year of revenue growth and profit margin expansion.

Q&A

With that, I will now hand over to the operator, and Michalis and I will take your questions.

Thank you

[Q&A transcript will be available on the Company's website on Friday 10th August]