DANONE

2017 -2020

Shaping the growth model

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Transcript

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After all this rich discussion, in this session I will focus on sharing with you how we would like between 2017 and 2020 to continue to strengthen our economic model, the agenda and the actions, and finish with the metrics for 2020.

Before I do that, I think it is important to come back on our ambition for strong, profitable sustainable growth and that this should lead into EPS sustainable growth. We are continuing exactly on this same agenda. In 2015, I shared with you that the journey included some steps. The first step was to make sure we were delivering profitable growth. The level of the margin was not satisfactory and neither was the imbalance of the model towards growth. We said we would make sure as the first step that our growth is profitable and that we focus on rebalancing the model between growth and profitability to ensure that we build a more robust model. I will share with you the results of what we delivered on that first step.

The second step will start this year and is about sustainability. It is about making sure that while we are accelerating on growth, the profitable growth equation is delivered in a sustainable manner year after year. I will spend most of my presentation on that. In addition, continuing to prepare for strong profitable growth.

Let us come back to 2014 to 2016, which were a very major transformation and important progress was made to build a more resilient growth model. There has been a consistent year after year improvement in margin, 120 basis point cumulative. It has translated to consistent recurring EPS growth with a CAGR of 8.8%. When we stood there and said that we needed growth to be more profitable and the model to be more resilient, this is what we have delivered. We have also improved returns. We had a discussion in New York 2014, on the level of ROIC, where Emmanuel said that we were not satisfied by the level and would make sure that we improved it continuously. We said that the reason why the ROIC had deleveraged was about the dairy performance of the past years. Dairy ROIC has now stabilised around 10% and we have improved ROIC 110 basis points at constant exchange rate, or excluding the FX impact. On cash, when I started my journey with you, the first year of guidance was 2015 and we did not guide on cash. Some of you were very worried that it was not a priority on our agenda any more. I think that the results here show that has always been a very strong priority and we have always focused in making sure that the NOPAT was converting into cash and that we were keeping a best in class level of working capital. Therefore, despite not having it in the yearly guidance, we have delivered a strong improvement in cash delivery in this year's. How did we do that? We continued the agenda that had started and on top of that, we started to transform.

We have discussed the One Danone organisation before but hearing some of the comments in the corridor, I will take a few minutes to explain because I am not sure it is totally clear for everyone. Before we set up the One Danone organisation, in each country where we operated, each category had a full business unit with, for example full HR and finance functions. At the end of 2014, we decided to mutualise these functions, together with ISIT, and not only mutualise them in each country but decide very precisely on the good point of leverage to have this good service unit. We decided on about 30 clusters of country. It is not by chance that we picked three locations, it is to make sure that we were balancing the efficiency of the model, which is about mutualising four functions in our operations to be more efficient, to get senior competencies and capabilities, but also that we always kept a view on the markets, category management team serving the business. This is what we did and it is now fully in place.

Beyond organisation we had another major transformation, which is the way we monitor performance and allocate resources. We went from a typical and classical 12-month budget exercise, into a dynamic process that includes three times horizons. The first one is a three-year mandate for each business unit, including strategic priorities and KPIs. The second one is that translates into rolling forecasts where we make sure at any point that at every quarter, we had another quarter to ensure permanent visibility over a four-quarter horizon. Third, supported by this rolling forecast, we have introduced resource allocation conversations every quarter where we start by looking at the performance and then we share relocation of resources, allocation of new resource, behind what initiatives and make sure that we balance the time horizons. It is not only allocating resources to secure short term, it is allocating resources on building the model for Danone. It is about agility, because we do it regularly and strong discipline to ensure that we invest behind initiatives with the right return and impact and sustainability of impact.

We are prepared for 2017 to 2020. You have seen the progress we have made. We are prepared to go to the second step of the journey and I will take you through it. Before I do that, I would just like to acknowledge where we are today, starting with 2017, which you know about because we shared that with you yesterday. First, is no news. We operate in a VUCA world, we shared that in Evian last time. We did not say it is a problem, it is a fact and we need to make sure that we live with it. There will be bumps on the road, but we need to be resilient enough to absorb them and continue our journey safely. The second thing is the accelerated transformation of our industry that you heard about yesterday, with numerous disruptions. These two things are creating a short-term transition in growth, which is led by a transition in some emerging markets and a short term slow-down of the food industry growth. It will recycle and start a new cycle and be back again. It is important to go through the short-term transition, because this is our starting point to ensure that we build and recraft the right journey for 2017 to 2020.

Danone is impacted short term because 40% of our revenues are in ALMA and from those revenues we have two big markets, China which is in transition in two of our categories and Brazil, which we have been hearing even more today. Excluding these two, the 2.9 of 2016 would have been 3.4, but for me this is not the most interesting message it is just to say that we are in markets we are forgetting that they were growing double digits for a long time and that they enabled us to build very strong platforms, that there is a transition, but they will come back.

The slow down and turnaround of Dairy Europe is taking more time. We need to be careful to make sure when we talk about Dairy Europe, there is Activia but there have also been successes in the way we have done our agenda. Remember that when we started this Dairy Europe turnaround, everyone was very focused on delivering the level of margin that was not satisfactory. We have been able to improve the margin in dairy outside the milk impact by 225 business points. We have been adapting our business model a lot to make sure we were on track with that business commitment and improving the level of margin of Europe Dairy. However, because this is the starting point of 2017, I acknowledge that the turnaround of Dairy Europe will take longer.

Two things, first we have what it takes in terms of portfolio, categories and geographies to reaccelerate. You have seen the categories. We have a very well balanced portfolio of geographies, which will increase our resilience further so we are geared to accelerate. However, today in Q1 we were on 0.7% growth and that is why when we issued our 2016 full year results we said that we were going for this short term and while we are taking the time to reaccelerate, we were going to decouple our agenda to maximise and accelerate efficiencies while accelerating growth to ensure that we secured our result and continued to improve margin and as a result, deliver consistent EPS growth. In addition, that we would unlock additional resources to fuel the transformation and the growth.

I will now focus on efficiency. Efficiency is a key part of going through that journey to make sure that we will continue to build a stronger model, deliver the results and have the right path for acceleration of growth towards strong, profitable and sustainable growth. When we talk about that it is first unlock efficiencies. It is not that suddenly we have started to look at efficiencies, it is first to continue and enhance the things we do every day in our business in terms of efficiencies. Second, it is about Protein programme. The reason we are very comfortable that we can do it and be sustainable is about what I showed you that we are fully organised and going about our process to allocate resources. Of course, a key pillar in starting the new Danone journey, is to make sure that we have a successful integration of WhiteWave and that we deliver the value creation plan. All that is to make sure that every year of 2017 to 2020 delivers the sustainability of profitable growth and consistent EPS growth.

On efficiencies, I would like to discuss three topics. First, there is the continuing improvement of productivities in gross margin. Second, is how we have always had and continue to have initiatives to optimise the fixed cost base and ensure that we adapt our organisation locally. Third, is about Protein programme.

Growth margin productivity is about three buckets: sourcing, manufacturing and supply chain. We have discussed many of these initiatives in the past. I just wanted to clarify the order of magnitude and make sure that you are clear that it exists, because we have not talked about it much recently and I heard that some of you were confused about what we were doing. We are delivering 600 million in savings in 2016; 4.8% on the total cost of goods sold base; increasing versus the previous year. This is productivities that are increasing year on year and that we extract in our growth margin. It is allocated to mitigate inflation, to reinvest in products and growth and in 2016 the 50 business point extra improvement in growth margin came from the extra net savings in that field.

Fixed cost base and organisation, has both global and local organisation and I have examples of both. First, when we presented one Danone in 2014, your first question was how much saving and where is it going. We said that one Danone is not about saving it is about efficiency and investment. Efficiency coming from the mutualisation of functions and investment, because of the model of One Danone we structured and built a very strong GS function that was not yet fully structured. There are saving to One Danone and annually from 2017 to 2020 it will generate 50 million.

The second bucket is everything the teams are doing every day in their own businesses. For example, in Russia you have the European organisation and everything that the Chinese teams have done in my zone, to ensure that despite the slow-down in growth they were keeping up the margin level. We probably do not share this enough with you. You do not see it in restructuring costs, because most of the restructuring costs are going into the recurring part of the margin and these examples will generate more than 70 million yearly from 2017 to 2020.

I will not come back to how we do protein, I just want to say that is not about getting the 1 billion, it is about getting the 1 billion and making sure that it is an efficiency that is sustainable in our model. Again, it is about making our model more resilient.

There is only one thing that you want to know and that is what we do with the 1 billion. First, we have decided to keep EUR 300 million to put in the recurring operating margin, at about EUR 100 million per year, starting in 2018. As you know, we have said that 2017 is about the pilots, learning and making sure that we are fully ready, so that we can go full blast in 2018. The EUR 700 million we will invest in our growth and continued efficiency, to secure at any point of time our sustainable profitable growth, through our resource allocation process. All that will contribute to secure the sustainable profitable growth and consistent EPS growth, while we are preparing for strong, profitable, sustainable growth.

Yesterday, one of the questions was why now? Why are you clear that you can do it now? On top of what Susanne shared in terms of the way we are going for it and the organisation and the processes we have put in place to do it and to track it, again it will be about the fact that we have One Danone organisation in place, with support functions and business services unified for 30 clusters of country. They will run the processes, make sure that everything is done in a sustainable manner and then in re-implementing the regional organisation we make sure that all the businesses have the same region, which will also help in looking for more cross-growth and efficiency opportunities.

How do we allocate the extra resources that we would get beyond what we put into the margin? We will leverage our budget process to the maximum to make sure that we maximise the investment efficiency and the quality of execution. When we talk about resource allocation, we talk about any type and nature of resource that we put to work. It is promotion, A&P, talents, R&D and quality. The objective is to build an activate our brands and having the right product, in the right place, at the right price and the right promo. It is also about continuing to build our capex for future growth. We prioritise on business impact, sustainability of business impact on returns. For example, if you look at our capex plans for extra capacity in 2016, we decreased capacity investment for dairy and increased it for ELN. Beyond operational resources there is also the question of how we make sure we use our capital and set up our business models in countries with the right discipline. We are looking, adapting our business models very regularly, if we believe that the balance between the capital intensity and the business impact and what it will create as impact for Danone in terms of value creation, is not the right one. For example, recently we divested our investments in Columbia and Chile because of capital versus the business size impact and time of return was not the right one for us. When it comes to acquisition, Emmanuel told us that we have made four acquisitions in Africa. We have also looked at two assets in Nigeria, which in the end we did not pursue because the price was too high. Capital discipline is important to us and I wanted to make sure that we are not only looking at P&L, but we are allocating capital with the same discipline as the same of the resources.

WhiteWave is now part of new Danone and an important part of the agenda is to start it efficiently and, of course, deliver the value creation plan that we put to you last year and that we confirmed. That started with the EUR 300 million synergies, but that is not all. I will not go back to that because we spent the whole morning on WhiteWave, but I would like to show you why we are confident that we will do it, because we have already done it with Numico, 2007 to 2016. This is ELN plus Advanced Medical Nutrition, with an operating margin plus 500 basis points, working capital from positive level to minus 5% and we multiplied cash by two, EUR 900 million last year, which is more than dairy.

We have done it. We are committed on WhiteWave. You have seen the synergy plans. Then I took another example, which is a different acquisition and integration we carried out, which was Unimilk in Russia. In the recent past the context has been volatile and complex, however, since the acquisition the margin has gone from 0% to 9% and working capital from plus 6% to minus 9%. I will not elaborate more on WhiteWave, which was covered this morning, but illustrates why we are comfortable that we can make it.

All this will ensure two things. First, now that we have delivered the first step, we will make sure that this is sustainable. We will make sure that we deliver on our commitments every year and at the same time, accelerate our growth.

What does this mean in terms of numbers? Starting with no news 2017. In 2017, I used an illustration that I think I shared with you in Q1. For 2017 there are three major things. The transition in growth in some of our emerging markets. It is the start of the decoupling agenda and the start of protein programme and, of course, the year of New Danone with the integration of WhiteWave. In terms of guidance, no news, moderate sales growth like for like, a sustained recurring operating margin improvement and double digit recurring EPS growth at constant exchange rate.

Let us now go to the rest of the journey and the objectives and metrics we are setting for 2020. Growth will accelerate. We are going for strong, profitable sustainable growth. We are going for strong growth. We acknowledge where we are. We have decoupled. We need to take the right time to make the right change and adaptation to accelerate, so we have an objective of 4% to 5%. If you look at this objective, there will be three strong categories with more than 5% and one will be 3% to 4%. To be precise, the first one will be ELN plus Advanced Medical Nutrition, the second is water and the third Dairy and Plant-based in NORAM, Danone, Dairy and WhiteWave. These are the three categories that have strong growth of 5%. Then there is plant-based international, outside NORAM, growing 3% to 4% and I will take the opportunity to answer a previous question, in that 3% to 4% the old dairy part will be a bit less than 2%. Overall, the pillars for this second acceleration are what we shared with you. That is, a unique and completed portfolio, now with WhiteWave in terms of 100% health categories well-positioned for growth. It is the continuation of making sure we choose reason and sustainability over speed. In the end, it is sustainability that will enable us to have long-term value creation. It is important that we make sure that we have a reason that will fit with safely reaching our journey.

Margin: margin improvement is a strong commitment. We have made the first part of the journey and started the second step. We are taking a recurring operating margin of more than 16% as our objective in 2020, equivalent to a 300-basis point improvement on a like for like basis. That will be built by everything that I shared before and was shared in the last two days. To clarify, the 200-basis point commitment for Dairy made in 2014 is part of that. We are not changing this objective, remember at the end of 2016 we were plus 82 and we will continue to drive the journey to improve to 200-basis points and it is part of the objective for 2020.

Deleverage: when we acquired WhiteWave we increased the debt on our balance sheet, which we had at optimised and great conditions. However, it increased the debt on the balance sheet and we have a strong commitment to deleverage. We have made an objective for 2020, to have a net debt to EBITDA ratio that is less than three times, acknowledging that one of the commitments is that we maintain a strong investment grade raging and for that there will be milestones along the way, which we are committed to reach. We will make it happen mostly through free cash flow from the model, making sure that we continue to improve and deliver fully on our free cash flow. It is about discipline in investment and there is no change in dividend policy to make this deleverage plan.

ROIC: when we announced the WhiteWave transaction, we said it would have an impact on ROIC of around 200 basis points. It will be in fact 150 basis points over two years, linked mostly to the time-lag of the closing and we continue to have a very firm commitment to improving our ROIC yearly. We have an objective of ROIC at 12% in 2020.

To recap on the 2020 metrics: like-for-like sales growth 4 to 5%; recurring operating margin above 16%; net debt to EBITDA ration less than three times; ROIC around 12%; making sure that we deliver consistent EPS growth each year.

To finish I would like to return to our journey. I know that some of you will say that we have changed the numbers and others that it does not change, at the end of the day we have not changed. That is, we are keeping our agenda, it is the same route that we shared in 2015 and we have made the first steps. We are in 2017 and have acknowledged the starting point. We have decided to decouple the agenda, going stronger on efficiencies and we have put a milestone in 2020 on metrics towards strong profitable sustainable growth. We are focused, committed and equipped to drive this journey safely. I am sure you now have many questions.

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