Event: Carlsberg FY 2016 Financial statement conference call

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Speakers: Cees 't Hart, Chief Executive Officer
Heine Dalsgaard, Group CFO

Operator

Ladies and gentlemen, welcome to the Carlsberg Full-Year 2016 Financial Results. Today, I'm pleased to present President and CEO, Cees Hart.

For the first part of this call, all participants will be in a listen-only mode, and afterwards, we'll have a question-and-answer session. Just to remind you, this conference call is being recorded.

Speakers, please begin your meeting.

Cees 't Hart

Good morning, everybody, and welcome to Carlsberg's full-year 2016 results conference call. My name is Cees Hart; and I have with me our CFO, Heine Dalsgaard; and Vice President of Investor Relations, Peter Kondrup.

2016 was a good year for Carlsberg. We are satisfied with our financial performance and we took significant steps to become a more successful company. An important milestone in the year was our new strategy, SAIL'22. Our new strategic priorities are now well integrated in the plans for 2017. Funding the Journey is an important element of SAIL and we are, of course, pleased to deliver the fist benefits of the program which we realized faster than originally anticipated.

Please turn to slide 3 and the Golden Triangle with the key KPIs we use to measure our performance: market share, gross profit after logistics margin, and operating profit. We continuously aim to strike the optimal balance between these KPIs as we believe this is key to drive sustainable value growth.

For 2016, achieving the balance meant that volumes declined organically by 2%, partly due to some deliberate decisions to go out of margin-dilutive volumes. On the other hand, we delivered a very solid GPaL margin improvement of 140 basis points, which was mainly driven by favorable price/mix. On organic operating profit growth, we also saw a solid delivery of 5%.

This was actually higher than anticipated at the beginning of the year for which reason we upgraded our guidance in November.

Please turn to slide 4 and a few comments on the status of SAIL'22. Overall, SAIL'22 got off to a good start. Execution of Funding the Journey was the main priority for 2016. It is progressing very well and we are on track to deliver the full benefits of DKK 1.5 billion to DKK 2 billion. We are determined to achieve the substantial proportion of the remaining Funding the Journey benefits in 2017, as this will allow us to grow earnings organically and invest in SAIL'22-related activities to support the future growth of the company. With respect to the other elements of the strategy, we are well on track, and we will see the priorities come alive in 2017.

Let me give you some more color on this. Please turn to slide 5 and Strengthen the Core. Leverage our Strongholds is about successfully leveraging our strong brands and market positions. We want to improve our performance in the 24 markets where our international and local power brands give us a number 1 or number 2 position.

To do so, we will focus our resources on fewer activities, step up our commercial capabilities, drive a cost and efficiency agenda across our business and dispose of non-core assets.

In 2016, we began the development of a new commercial approach to identify new sources of value growth and make the right portfolio and channel choices. This new approach is now being implemented across the Group.

We also evaluated and redirected spending on fewer brands and activities to make these more impactful. In this connection, I would like to highlight some of our local power brands such as Zatecky Gus in Russia, which grew 2%, and Beerlao, which grew 3%. For the international brands, Tuborg grew 9% and Carlsberg grew 5%.

In 2016, Russia accounted for 16% of Group operating profit. It does remains our largest market, and becoming more successful in Russia will be impactful on Group profits. In 2016, we executed on a well-defined and much sharper commercial agenda with clearly defined priorities, including the repositioning of the Carlsberg brand and an intensified focus on the growing segments and channels, not least the modern trade. In the years to come, we will build further on this commercial agenda.

Excel in execution covers a wide range of areas, such as embedding high-quality point-of-sale capabilities and standards and step-changing within digital. In 2016, we implemented our internally developed point-of-sale excellence program in all our Western European markets and carried out an assessment in a number of markets to determine areas for improvement. By the end of the year, we had also initiated the implementation in India, and more Asian markets will follow in 2017.

Within digital, we focused on building capabilities. The first task was to hire a head of digital, and she is now busy designing our future digital strategy. With respect to Funding the Journey, Heine will come back to this in a moment.

Please turn to slide 6 and our growth priorities, where we in 2016, but even more so in 2017, are investing in the long-term growth opportunities for Carlsberg. Within craft & speciality, our ambition is to deliver great brands for the many. In 2016, we further strengthened our longstanding cooperation with Brooklyn, opening the E.C. Dahl brewery in Norway. From 2017 January onwards, we took over the distribution of Brooklyn in the UK.

With respect to our international speciality brands, we are increasing the availability of Grimbergen and 1664 Blanc. In 2016, Grimbergen continued its strong performance both in existing and in new markets, and the brand grew 11%, reaching the 1 million hectoliter milestone. Revenue of 1664 Blanc grew 15%, mainly as a result of strong growth in Asia.

Within non-alcoholic beverages, we believe that our strong R&D capabilities, which includes the largest and world-leading yeast library give us a competitive edge. In the coming years, we will continue to develop our non-alcoholic beer portfolio. In 2016, we already saw solid growth of some of our existing powerful NAB brands such as Carlsberg Nordic, Baltika 0 and Tourtel Twist.

On big cities, the team became operational in August 2016. Since then, it has concentrated on carrying out analyses to determine the relevant cities for pilot entry in 2017.

In Asia, Tuborg had another year of success. We launched the brand in Vietnam, Cambodia and Laos to tap into the growing premium category in these markets. In India, we saw another year of good growth and we are building a new brewery to support our positive momentum. In China, we achieved value growth on the back of the ongoing premiumization.

Please turn to slide, 7. A critical enabler for the long-term success of our strategy is to develop a winning culture which will foster the right team and performance way of working. To develop a team and performance-based culture, we rolled out our triple A concept – alignment, accountability and action. By living this concept, we will create a strong sense of ownership and accountability for delivering results, and this will be further supported by a close connection between incentive schemes and financial objectives. Our incentive schemes now include targets which are clearly aligned with our key priorities and foster a team orientation on results. Across our markets, we introduced rigorous tracking and monitoring.

Another visible action has been the change in the top leadership team. Heine joined us as CFO; Michiel Herkemij joined us as EVP for Western Europe; Chris Warmoth was appointed as EVP of Group Strategy; Graham Fewkes took over Chris' role as EVP, Asia; and most recently, Philip Hodges joined us as EVP, Supply Chain.

In addition, there has been a number of changes in some of our larger markets and in central functions such as IT and sales and marketing. These changes have been a healthy mix of internal promotions and external hires. We believe these changes will drive us to deliver better performance and improved results.

I will now hand over to Heine who will comment on the Funding the Journey progress, the 2016 financials and the outlook for 2017. Heine, over to you.

Heine Dalsgaard

Thank you, Cees. And good morning, everybody. Please turn to slide 8 and Funding the Journey. First of all, the program is well on track. In 2016, we delivered slightly more than expected at the beginning of the year. Approximately DKK 0.5 billion was achieved out of the full DKK 1.5 billion to DKK 2 billion to be realized by 2018.

Let me give you a few comments on each of the four areas within Funding the Journey. On value management, the concept is rolled out in all markets. It is based on the Golden Triangle that you know, and we track progress rigorously and fine-tune when and where necessary. It is working well and the price/mix of plus 3% is proof of this.

On supply chain efficiency, savings are coming through in several areas including procurement, production and logistics. We are working on improving our processes to ensure that we capitalize on the BSP1 system and the BSP1 investments in prior years.

On SKU reduction, we have reduced the number of SKUs by 1,200 net. In 2017, we will continue to work on further complexity reduction. Within operating expense efficiency, more than 2,200 white-collar people have left the company and that marks the end of this part of the program.

Operating cost management delivered substantial savings in Asia and in Eastern Europe. In Western Europe, we are still in the process of implementation. Consequently, the execution of OCM in Western Europe will be high on our agenda in 2017.

The outsourcing of shared services in Poland and China is progressing and about 300 people were transferred to Genpact, which is our external service provider. We're now doing more intense work on addressing our indirect spends where we also see opportunities for further savings.

In terms of right-sizing, we concluded a number of initiatives. In 2016, we divested the Danish Malting Group, Carlsberg Malawi and the VungTau Brewery in Vietnam, the Sejet plant breeding company in Denmark and we completed the asset swap in Xinjiang. In addition, in the first one-and-a-half months of

2017, we have divested Carlsberg Uzbekistan and United Romanian Breweries. We are still working on divesting a small handful of activities.

Please turn to slide 9 and the final pillar of SAIL'22, which basically measures the outcome of the strategy. We have defined three key measures for delivering value for shareholders – organic operating profit growth, ROIC and capital allocation. As already mentioned, we delivered 5% organic operating profit growth, return on invested capital developed very positively, being up 110 basis points to 9.2%.

If adjusting for the impairment done in 2015, ROIC would have improved by 60 basis points. The improvement was the result of lower capital employed which was impacted by disposals, impairments, currencies and the fact that CapEx was below depreciations.

Net interest-bearing debt was reduced by DKK 5.4 billion in 2016 to DKK 25.5 billion. This has led to a net debt-to-EBITDA ratio or financial leverage of 1.96 compared to 2.34 at the end of 2015.

Based on the solid results, the strong cash flow and the leverage, the board will propose an increase in dividend per share of 11% to DKK 10 per share. This equals a payout ratio of 39%. When the SAIL'22 strategy was announced, we promised to start increasing dividends towards the 50% payout target when leverage came below 2 times net debt-to-EBITDA. As we want to see leverage come further down, the increase in the payout ratio is done gradually.

Please turn to slide 11 and a few comments on the P&L. Net revenue grew organically by 2%, driven by the positive price/mix of 3% and as the result of a positive development across all three regions. In reported terms, net revenue was adversely affected by currencies and disposals, and ended the year down 4% versus the previous year. Reported gross margin improved by 140 basis points. This was the result of both the positive price/mix and efficiency improvements in the supply chain.

OpEx was up organically 3%. This was due to a number of factors with the most important ones being sales and marketing investments, investments in SAIL'22 priorities such as the launch of Tuborg in several Asian markets and the establishment of central teams for big cities, non-alcoholic and digital. On top of this, we saw higher costs of the short-term and long-term incentive programs and higher IT amortization costs.

Central costs, or what in the accounts are called not allocated were DKK 1.7 billion, representing an increase of DKK 265 million. This was due to investments in SAIL'22, the Euro sponsorship and cost of incentive programs. All in all, we delivered a solid 5% organic growth in operating profit, a currency headwind of minus 6% and minus 2% from disposals meant that reported operating profit was down 3%.

The currency impact was broad-based, with a particularly strong impact from the Eastern European, Chinese, British, and Norwegian currencies. The disposal impact was mainly due to the divestment of the Danish Malting Group and Carlsberg Malawi.

Slide 12 please. Further down the P&L, net special items amounted to plus DKK 251 million. There was a significant positive impact from the disposal of non-core assets, but there were also offsetting items, many of which were related to Funding the Journey, in addition to further brand impairments in Chongqing and in Russia. Net financials were positively impacted by the reduction of net debt and lower interest rates.

Other financial items were down due to FX gains partly offset though by write-offs and interests related to the Finnish tax case that we lost earlier in 2016. Our tax rate was also impacted by the Finnish tax case and was, therefore, somewhat higher than in previous years but in line with our revised guidance. It is worth noting that the tax case was a one-off expense and had no cash impact in 2016. Minorities or noncontrolling interest were DKK 371 million, largely at the level of 2015. Both years were impacted by brand impairments in Chongqing, which is a 60% owned company.

All in all, this has led to a net profit of DKK 4.5 billion and a reported EPS of DKK 29.4. Adjusted for special items, net profit was DKK 3.9 billion, and adjusted EPS was DKK 25.4. The decline in adjusted EPS was the result of organic growth in operating profit and lower financial expenses, which, however, was offset by currencies and the higher tax rate.

And now, some comments on the cash flow on slide 13, please. Free cash flow was DKK 8.6 billion, corresponding to DKK 57 per share. Free cash flow was positively impacted by disposals of non-core assets, a good trade working capital development and CapEx below depreciations. The change in trade working capital was plus DKK 1 billion. We continued last year's strong performance and as a percentage of net revenue, trade working capital reached an all-time low at 9.5% minus. We're very satisfied with our trade working capital performance.

Other working capital was impacted by extraordinary payments to the UK pension fund of £100 million, and consequently, the change in other working capital was minus DKK 1.1 billion. Net interest paid were positively impacted by the lower net interest bearing debt. 2015 net interest were impacted by the settlement of financial instruments of around minus DKK 0.5 billion.

Tax paid in 2016 was DKK 1.752 billion which was DKK 388 million lower than last year. The decrease was mainly explained by phasing of tax payments between 2015 and 2016. Net CapEx was DKK 3.6 billion, gross CapEx was DKK 3.8 billion, well below depreciation of DKK 4.8 billion. We will continue to drive a strict focus on CapEx also going forward. The positive contribution from financial and other investments was mainly due to the aforementioned disposals of non-core assets.

Please turn to slide 14, and outlook. 2017 will be another important year for the Group as we will focus on the delivery and execution of majority of the benefits from Funding the Journey and we will invest in SAIL'22 priorities to drive the long-term growth of this company. We maintain our assumption that approximately 50% of the benefits will improve EBIT while the other 50% will be reinvested into our business to strengthen brands, portfolios and capabilities to ensure that we drive long-term value for shareholders.

When looking at the market dynamics in 2017 versus 2016, we don't see significant changes. We are assuming a relatively flat market in Western Europe, declining markets in Eastern Europe as a result of the PET restrictions in Russia and the general challenging macro economy and in Asia, a slightly declining Chinese market in volume terms but growing in value terms due to continued premiumization and volume growth in the non-Chinese markets in Asia.

Our key priorities per region are as follows – in Western Europe, it's margin and operating profit improvement; in Asia, revenue and profit growth; and in Eastern Europe, organic operating profit growth. Based on this, we expect to deliver a mid-single-digit percentage organic growth in operating profit in 2017. In addition, we will continue to reduce our financial leverage.

A couple of other assumptions for the year, which are worth mentioning here, are that we assume a positive FX translation impact on operating profit of around DKK 350 million based on the spot exchange rate as of February 6. So, for the ruble-euro, this implies an exchange rate of RUB 63.2.

Net financial cost, excluding potential currency losses or gains, are expected to be around minus DKK 1.0 billion to minus DKK 1.1 billion. The tax rate is expected to decline to just below 30%, and we expect to keep CapEx at around DKK 4 billion.

We are making smaller changes to our reporting. As you can see in the appendix to the announcement, we will move the costs for our central supply chain function from the not allocated part to Western Europe. This is around DKK 500 million in 2016 and this impacts margin in the region, so Western Europe, by minus 130 basis points to 12.9% for 2016. There is, of course, no impact on the Group numbers.

Cees, back to you.

Cees 't Hart

Thanks, Heine. And now to the regions. Please turn to slide 15 and Western Europe. We estimate that the overall beer market in our Western European region grew by around 1% for the year. Our regional market share declined mainly due to the reduction of margin-diluted volumes in the UK, Finland and Poland.

We delivered a solid 2% price/mix largely driven by value management and less low-price volumes. We are pleased with the value management efforts in Western Europe and how the Golden Triangle is being adapted across our markets.

Our volumes declined by 2%, mainly as a result of the aforementioned contracts. Excluding these, volumes would have been flat. In quarter four, volumes declined by 4%, which we are not pleased with. We will monitor the volume development closely to ensure the right balance of the Golden Triangle. However, to be clear, volumes are important, but we don't want to hunt for volumes and market share at the expense of the healthy development in earnings and margins. For the year, we delivered a solid 3% organic operating profit growth and 50 basis points operating margin improvement.

Slide 16, please and a look at key businesses in Western Europe. The Nordic markets grew 2% to 3%. We grew volumes in Norway, Denmark and Sweden, but our total Nordic volumes declined by 3% due to the withdrawal from the margin-dilutive supply contract in Finland. All markets delivered very solid price/mix improvements following growth of craft & speciality and value management efforts.

All four markets delivered operating profit improvement with particularly strong improvement achieved in Norway and Finland. In France, our volumes grew by 1% while the market grew by approximately 3%. We gained market share in the on-trade, while we lost share in the off-trade. Our volume growth was driven by Carlsberg, Tourtel and Skøll and by craft & speciality brands such as Grimbergen and Brooklyn. Our share loss was mainly attributed to the mainstream Kronenbourg brand and 1664 as we did not engage in steep discount activities during the summer to the same extent as the competition.

The Polish market grew by an estimated 2%. The market remained highly competitive. Our volumes declined by approximately 12% mainly as a result of the decision to pull out of certain low-priced volumes at the beginning of 2016.

In the UK, the turnaround is progressing well. We are strengthening our portfolio with more premium offerings. With respect to the outsourcing of the porterage and secondary logistic business contracts, this is on track. Switzerland delivered another set of very solid results. Most other markets in the region delivered top and bottom line growth for the year. We saw particularly good market share and profit development in markets such as Bulgaria, Germany and Greece.

Slide 18 please and Eastern Europe. The Eastern European beer markets remain under pressure because of the ongoing macroeconomic challenges. Our volumes were flat for the year, as a result of easy comparables with 2015, especially in the beginning of the year and very favorable weather in Q3. Price/mix was solid at 7%, mainly driven by price increases across the region. Operating profit grew organically by 12% and operating profit margin increased by 60 basis points. The strong earnings growth was driven by a number of factors, including easy comparables and improved commercial agenda in Russia and Funding the Journey benefits.

Slide 19, and a few comments on our major markets in Eastern Europe. The Russian beer market declined by an estimated 1% to 2% for the full year and an estimated 5% in Q4. The market development during the second half of the year was helped by very warm weather in Q3. Although some macro indicators have started to show improvement throughout 2016, the market remains negatively impacted by the macroeconomic challenges in the country.

Our Russian shipments grew by 1% for the year due to easy comparables, warm weather in Q3 and market share gains in the second half of the year. For the year, our market share declined by 30 basis points to 34.5%.

As mentioned earlier, we sharpened our commercial agenda in 2016. Part of this was to strengthen our position in the modern trade channel, which we achieved, while our market share was down in the declining traditional trade channel. We saw good performance of Carlsberg, Zhigulevskoe and Baltika 0, while Baltika 7 and Baltika Cooler declined.

In Q4, we reduced our PET bottles to comply with the 1.5-liter ban that came into effect on the 1st of January 2017. Our best estimate of the negative market impact in 2017 from the size ban remains around 5%.

The Ukrainian market continued to be difficult, declining by an estimated 6% to 7%, impacted by the challenging macroeconomic environment. Our business performed strongly with only a modest 2% volume decline, gaining market share and improving margin. Our market share growth was driven by our local power brand, Lvivske, and by Carlsberg.

Slide 20 please, and Asia. We delivered 4% organic revenue growth in Asia, driven by a solid 6% price/mix as our premiumization efforts were successful. This included both premiumization of local power brands and growth of international brands with Tuborg being the key driver. In addition, 1664 Blanc is becoming an increasingly important part of the portfolio. Although the brand delivered small volumes, its super premium pricing makes it a very attractive part of our portfolio. Volumes declined by 2%, mainly as a result of the Chinese brewery closures and the Chinese market decline. Our non-Chinese beer volumes grew by 2%.

In addition, we had an impact from the disposal of Carlsberg Malawi that happened in August. The earnings growth continued. Operating profit grew by 6% organically and operating margin improved by 90 basis points. In addition to premiumization, Funding the Journey benefits came through nicely. Moreover, our business in India started to deliver meaningful profits.

Slide 21 and some market specific highlights from Asia. Our Chinese volumes declined organically by 6% while the market declined by an estimated 4%. We gained market share in most of our key provinces while the restructuring of our Chinese business and subsequent brewery closures resulted in substantial volume decline in the affected provinces. During 2015 and 2016, our Chinese organization has been through a comprehensive restructuring and cost savings program resulting in the closures and disposals of a total of 17 sites by the end of 2016. Approximately two-thirds of the volume decline related to brewery closures.

Our premium portfolio grew by 8%, with particularly strong growth of Tuborg and 1664 Blanc. The positive development of our premium brands and the reduction of low-price products in Eastern Assets led to a positive price/mix of 5%. Operating margin in China improved by more than 300 basis points due to premiumization, tight cost control, and the closure of sites.

In Indochina, Laos delivered solid top and bottom line growth in 2016. Growth of our water and soft drinks business in Cambodia was offset by share loss in the increasingly competitive beer market. In continuation of the success of Tuborg in recent years, we launched the brand in Cambodia, Vietnam and Laos. Early results are very encouraging in all three markets. The brand has quickly established a leadership position in the international premium segment in Cambodia and enjoys a strong position in Northern Vietnam.

Our Indian business continues to grow, delivering volume growth of 16% in spite of the alcohol ban in the state of Bihar as of April. The Indian beer market grew by an estimated 2%, and we strengthened our market position further, reaching a 16% market share for the year. Carlsberg Elephant grew significantly and Tuborg continued its strong growth trajectory. Profitability improved considerably as a result of volume growth and tight cost control. 2017 could be a volatile year for India, as it is still expected that GST will be implemented; and in addition, there may come a ban on liquor sales near highways as well.

That was all for now, but before opening up for Q&A, a few concluding remarks on slide 22. 2016 was a good year for Carlsberg with earnings growth on track and strong cash flow. We delivered well on all our key priorities for 2016. Funding the Journey is slightly ahead of plan and timing, delivering a quarter of the expected benefits.

SAIL'22 has been well received by our people and the implementation is going well. And we delivered on our regional priorities for the year. Our delivery against the financial priorities of SAIL'22 were satisfactory with 5% organic growth in operating profit and a 10 basis point ROIC improvement and a further decline in leverage to 1.96 times.

For 2017, we are determined to achieve a substantial proportion of the remaining Funding the Journey benefits, allowing us to grow earnings organically and invest in SAIL'22 related activities to support the future growth of the company.

And with this, we are now ready to take questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] The first question comes from the line of Simon Hales from Barclays. Please go ahead. Your line is now open.

Simon L. Hales

Analyst, Barclays Capital Securities Ltd.

Thank you. Morning, everybody. A couple of questions first on the Funding the Journey program, please. You just talked about the substantial savings you're expecting in 2017 to continue to come through. In the past, you've indicated I think about 50% of the gross savings should really be coming in 2017. Is that what you mean by substantial or could it be above that now, given the momentum you've seen this year?

And then, related to that, in terms of reinvestment of savings, how should we think about that building in 2017? And I wonder if you could give us any idea as to how much of the DKK 0.5 billion of savings in 2016 were reinvested back in for the business.

And then, just secondly, if I can, just on Western Europe. Could you give us the Q4 volume number excluding the – or the decline excluding the contract impact? And perhaps give us a little bit more of a detail as to perhaps what you struggled with in Q4? What went wrong to drive that weakness in Q4 from your view?

Heine Dalsgaard

Good morning, Simon. If we start with the Funding the Journey part, then, you're absolutely right that we have said that a substantial part of the benefits will come through in 2017. Our sort of view is still approximately 25% in 2016, approximately 50% plus in 2017, and then, 25% in 2018.

Reinvestments into the business in 2017 is going to be higher than in 2016 for the simple logic that we have not initiated that much in 2016, but have started a lot of initiatives that sort of will roll out and also incur costs throughout 2017.

Cees 't Hart

Simon, with regard to Western Europe, overall, the market was a bit weak, but it's a combination of a few aspects. First of all, the continuation of the withdrawal of some contracts. If we would exclude these, the minus in Q4 would be between minus 2% to 3%. We had as well some market share loss in Poland and we were suffering from delivery issues in the UK as a consequence of an incident in UK where we had an ammonia leakage. For that, the brewery was closed for almost three weeks and we couldn't deliver from there. So that's a combination of factors, but very specifically, without the contracts, it will be minus 2% to 3%.

Simon L. Hales

Okay. That's very clear. Thank you.

Operator: The next question comes from the line of Trevor Stirling from Bernstein. Please go ahead. Your line is now open.

Trevor Stirling

Analyst, Sanford C. Bernstein Ltd.

Good morning, Heine and Cees. Two questions on my side, please. One for Cees, I guess, you actually look forward to 2017 and you're looking at the brand developments that are underway, Cees. Where are you most excited? Which are the brands and countries do you think you're going to see the biggest uplift?

And second, more technical question for Heine. Heine, you mentioned all about the minorities interest is slightly flattered, because the Chongqing minority has basically picked up 40% of the impairment costs. If you looked at the underlying minorities charge without those impairments, what do you think that will be?

Cees 't Hart

Good morning, Trevor. Thanks for your questions. With regard to brand development, well, the good news, in my view, is that we have a broad portfolio with some exciting developments. First of all, of course, Tuborg in Asia, which is doing pretty well, as I said in the call, we started in Vietnam, for example, and Cambodia, Laos, and there we see a good start of Tuborg as such.

Further, we have in Europe, for example, Grimbergen and Brooklyn that we're going to push further. And the commercial agenda in Russia is picking up very nicely and especially Carlsberg after the repositioning is doing very well. So in that respect, we are comfortable with our current portfolio, the focus on some of these brands and the support levels behind these brands.

Heine Dalsgaard

Good morning, Trevor. And the question on minorities, you're right that 2015 actually also as well as 2016 are impacted by impairments on brands in Chongqing [Brewery] that we own 60% and then the minorities are 40%. The impairment in 2016 was around DKK 800 million. That means 40% of that is around DKK 300 million. So that means then our normal run rate is DKK 600 million to DKK 650 million on the minorities.

Trevor Stirling

Very good. Thank you very much, gentlemen.

Cees 't Hart

Thank you, Trevor.

Operator: The next question comes from the line of Jonas Guldborg from Carnegie. Please go ahead. Your line is now open.

Jonas Guldborg Hansen

Analyst, Carnegie Investment Bank AB

Yeah, good morning and thanks for taking my questions. First of all, I would like to try to understand your Russian comments a bit better. You're saying that you still expect a minus 5% from the PET ban, and then, you're talking about a negative impact from macroeconomic development. So should we expect the market to decline more than 5% in 2017 compared to 2016?

Then, India profitability, you say, has increased substantially in 2016. Are we at the double-digit margins now or still single-digit?

And then, lastly, if you could put some words on why the OCM program has not impacted Western Europe significantly yet, and then, of course, when we should expect it to do so. Thank you.

Cees 't Hart

Thank you, Jonas, and good morning. With regard to Russia, the PET ban will, in our view, have an impact of 5% minus in the market. And what we try to say in the call that on top of that will be the impact of the further market development and that's what we don't know at this moment of time.

If you put this, as you know, in historical perspective, two years, three years ago, it was a double-digit decline that moved slightly more positively into single-digit decline. And last year was basically only minus 1%, minus 2%. And so, we see that so far, the decline in the Russian market is bottoming out, but it's difficult, of course, to predict 2017. As you know, 2016 has been a bit more favorable because of a very good summer in quarter three, resulting the volumes there. So it's minus 5%, and then, plus or minus the impact of the further development of the market.

Jonas Guldborg Hansen

Okay.

Heine Dalsgaard

Good morning, Jonas. With respect to your question on India, you're absolutely right, we have increased our profitability quite a lot in India. And at the same time, as you can see, we've also been able to grow the business. Even though we have the ban in Bihar, profitability in India is up significantly compared to last year but still single-digit.

Cees ‘t Hart

The OCM in Western Europe?

Heine Dalsgaard

In terms of OCM in Western Europe, it's progressing well. We are planning forward, but in terms of sort of maturity, it is still behind Eastern Europe and Asia, in particular for good reasons, because it's only starting up right now. So it's a high focus area for us for 2017, and we have relatively high expectations for ourselves and for our Western European colleagues.

Jonas Guldborg Hansen

So we should see effects in 2017 from this?

Heine Dalsgaard

Yeah.

Jonas Guldborg Hansen

Thank you very much. Thank you.

Cees ‘t Hart

Thank you.

Operator: The next question comes from the line of Sanjeet Aujla from Credit Suisse. Please go ahead. Your line is now open.

Sanjeet Aujla

Analyst, Credit Suisse Securities (Europe) Ltd.

Hi. A couple of questions please on Russia. Firstly, can you just help us break down the volume performance in Q4 in Eastern Europe? It seems like volumes are down 10%. You talked about the Russian market being down around 4%. We know there was a bit of destocking in the quarter as well. But can you just help us break that down in the various components and also, perhaps a comment on market share development in the quarter there as well?

And then, just coming back to the outlook, again, can you just give us a bit more granularity on why you remain cautious on the market, underlying market development, despite the improving macro indicators? Thanks.

Cees ‘t Hart

Thanks, Sanjeet, and good morning. Well, let me focus mainly on Russia, because Eastern Europe, of course, is bigger, but Russia is the highest percentage of share of Eastern Europe as you know. We had a good quarter three. The volume in quarter three was up by 15%. And it was partly, as well, because we finished our production of the 1.5-liter plus PET bottles and, if you like, moved it into the market. That was followed by a relatively poor quarter four with minus 8.2%, and we started there the production of the 1.42 liter so the new PET bottle size.

The market as such was down by 4%. And with regard to our market share, we were up in quarter three, and we were down in quarter four. But in total, in Russia, we grew volumes for the second half of the year by 4.3%.

Sanjeet Aujla

Got it. And then, just on the outlook there on...

Cees ‘t Hart

And with regard to the outlook, yeah. With regard to the outlook, basically, we are close to the market. We see that the macro indicators are improving a bit. But at the end of the day, we are depending on the consumer confidence. And we do not see these kinds of figures changing at this moment of time. So we are depending on, let's say, the confidence of the consumer in the near future. And therefore, we are not – I would say, yes, we are cautious, not pessimistic, not optimistic, but I think just realistic. Again, double-digit decline in the past, single-digit bottoming out last year, so the question is now what the market is going to do. So we want to refrain from a precise estimation on that one.

Sanjeet Aujla

Just a final one on Russia there. Can you just comment on the pricing developments in the market more recently and the outlook there for 2017. As I understand, you'll have some mix benefits from that PET transition. And again, just trying to understand if you're now focusing on perhaps improving affordability in that market or how you see pricing playing out.

Cees ‘t Hart

Well, we had a small price increase in quarter four. We will have a different portfolio, of course, because the 1.5-liter plus is out. That is replaced by 1.42 liters. That SKU will have a slightly higher margin.The price per liter is lower for the PET bottle 1.5-liter plus and consequently higher for the 1.42 liters. The margin is slightly higher on the smaller bottle as well. So as a consequence of that, we should have a slightly better mix impact. With regard to pricing for next year, we will follow more or less the consumer inflation and we take it from there.

Sanjeet Aujla

Great. Thanks.

Operator: The next question comes from the line of Andrew Holland from Société Générale. Please go ahead. Your line is now open.

Andrew Holland

Analyst, Société Générale SA

Yeah. A couple from me, please. Firstly, your unallocated costs spiked up and you referred to EURO 2016. Can you give us an idea of where that might be in 2017? Is that going to actually come down or are there other factors that will keep it at that level?

And secondly, can you just give us a bit of an update on alcohol regulation in Russia? I think there was talk earlier in the year of possibly removing beer from the same sort of legislation that covers vodka. But also, maybe an update on the implementation of the alcohol reporting regime which came in last year.

Heine Dalsgaard

So good morning. So, if you start with the unallocated costs, you're absolutely right. They're going up from DKK 1.426 billion in 2015 to DKK 1.961 billion in 2016, so up DKK 265 million as mentioned. The increase is due to a combination of the EURO sponsorship, incentive programs, and that's actually both short-term and long-term, and also SAIL'22 investment, and this has more than offset the savings.

We expect approximately the same level in 2017. So savings will be coming through from Funding the Journey, but we do also see, as mentioned, some quite heavy investments into SAIL'22 initiatives fully as planned. So approximately the same level.

Cees 't Hart

Andrew, good morning. Thanks for your question. With regard to regulation, we see no other changes in regulations to be discussed at this moment of time. In general, we have a better dialogue with regulators than some years ago. And we are now seeing discussions about rolling back some of the rules put in place some years back. However, there's nothing concrete. And as you know, discussions like this can take a long time. And sometimes, predicting the outcome is difficult.

Personal observation is that everything is anticipating 2018 Soccer Championship and in that respect, I think nothing concrete will happen in the coming 18 months, but again, this is Russia.

Andrew Holland

Okay. But in terms of the sentiment, would you say that the sort of approach is more conciliatory towards the brewing industry than it has been in the last five years?

Cees 't Hart

That's what I would like to feel, but you can be surprised at the moment that you become a bit more optimistic on this one. The discussions are good. The discussions are at a very high level. There's a feel that the Western industry needs – or basically the investors [indiscernible] (47:29) to be positive towards the Western industry as well. So in total, at this moment of time, we are slightly more optimistic. But again, that can change every minute almost in Russia.

Andrew Holland

Okay. Thank you.

Operator: The next question comes from the line of Hans Gregersen from Nordea. Please go ahead. Your line is now open.

Hans Gregersen

Analyst, Nordea Bank AB

Good morning. Three questions. Administration cost, as admin to sales ratio picked up quite significantly in H2 compared to H1, are there any specific reasons for that? That's the first question.

Second question, in terms of net debt outlook and capital allocation, at what time will you start to address that? And in that regard, you mentioned you sold Carlsberg Romania and Uzbekistan. How much cash is coming in from those two divestments?

And then thirdly, Heine, you mentioned before SAIL'22 initiatives. What are you specifically targeting in 2017, perhaps not country by country, but more overall, and what will the cost spend be? Thank you.

Heine Dalsgaard

Chief Financial Officer, Carlsberg A/S

So if we start with the administration cost, it's basically more or less the same reasons as mentioned earlier. It's the reason why administration costs are going up is SAIL'22 investments. There are SAIL'22 investments also in administration cost and building up some of the central teams. And then, it is the further cost of the incentive programs, both the short-term incentive programs and the long-term incentive programs.

In terms of the net debt to EBITDA, where are we taking that? Yeah, we closed 2015 with 2.34 times. We're closing 2016 with 1.96 times. We have a target to go below 2 times. We've always said, Hans, that we are not targeting 1.9 times something, but something probably between 1.5 times and 2 times. So expect something approximately in the middle, so 1.7 times to 1.8 times.

In terms of the divestments. You're right, we have just in 2017 announced the divestment of Uzbekistan and of Romania. Cash is not something we're commenting on, but the net effect in cash from these two is not very significant.

Hans Gregersen

So like DKK 0.5 billion?

Heine Dalsgaard

Yeah.

Hans Gregersen

And will there be any major EBIT impact?

Heine Dalsgaard

No.

Cees ‘t Hart

With regard to our SAIL'22 Program for 2017 and our investments in that, we continue to have good support of our strongholds and we'll focus more on those brands. We will have the rollout of some of our craft & speciality brands. As you remember, some of these very strong brands were only in a small number of countries. We're now going to roll these out to more countries. As well, we will have an emphasis on non-alcoholic beer.

Then, we have launched our Tuborg brand in Asia, which we, after a very good start, obviously, want to continue. We will do some investments in further development of some of the teams. And we will develop our plan on big cities. The big city plan is more or less ready. And we are going to start mid this year in some cities.

Hans Gregersen

How many? Three to five cities or...

Cees ‘t Hart

Closer to three than five.

Hans Gregersen

Thank you.

Cees ‘t Hart

Thank you, Hans.

Operator: The next question comes from the line of Tristan van Strien from Deutsche Bank. Please go ahead. Your line is now open.

Tristan Van Strien

Analyst, Deutsche Bank AG

Good morning, gentlemen. Three questions, if I may. Just on the first one, as you balance out the Golden Triangle in Europe, what proportion of the volumes you have purposely lost this year do you expect to come back particularly in Poland, UK and Finland?

Then the second question, in India, just how many outlets right now in your distribution footprint, how many outlets do you serve in India and what proportion of those outlets sit within that 500 meters of highways and will potentially be impacted by the ban coming in April?

And then third, maybe just a follow-up on Uzbekistan. Just wondering who you sold that to and also the Romania ones. And actually, more from an autopsy standpoint, what went wrong in that market? Because you used to be market leader, used to do 1 million hectoliter. Today, you seem to be doing about a fifth of that. So, what went wrong in the last five years in that particular market? Thank you.

Cees ‘t Hart

Sorry, which market, you mentioned? I lost that one.

Tristan Van Strien

Uzbekistan. Yeah.

Cees ‘t Hart

With regard to the volume within the Golden Triangle, we think – it's difficult to say, of course, but we think that even in the 1% and the 3% that we lost in Western Europe, as you know, it was the combination of the UK and Finland and Biedronka. We are happy to report that we will be back on better terms in Biedronka so that will help us for the volume development in 2017. Maybe not so much on the price/mix, but for sure on the volume development.

With regards to India, the outlets in India, as you know, it's a very regulated market, I think 66,000 outlets, most of them we serve. The issue is that the interpretation of the Supreme Court that in the national and the state highways, it's not possible to sell beer closer to 500 meters. That involves half of the outlets. So, that really would be an issue in India. That would reduce, of course, the number of sales points, it would reduce as well maybe the sales volume, but for sure as well then the income for the states. So, as said earlier, India for this year has two big issues, that is this outcome of the ruling of the Supreme Court as well the possible introduction of GST.

With regard to Uzbekistan, Heine?

Heine Dalsgaard

Just a few comments on Uzbekistan and Romania. So, the buyer of both is CBC from Israel. What went wrong? First of all, in Uzbekistan, that is an extremely difficult market from a macro point of view, and we have simply decided to focus our efforts somewhere else. For Romania, remember that we have a 23% stake that we have sold to the other owner of the rest of it, which is then CBC.

Tristan Van Strien

All right. Thank you very much.

Cees 't Hart

Thank you, Tristan.

Operator: Your next question comes from the line of Søren Samsøe from SEB. Please go ahead. Your line is now open.

Søren Samsøe

Analyst, SEB Enskilda

Yes. Hello, gentlemen. Two questions from my side. First of all, on the Funding the Journey program, where you say you are ahead in terms of value management, but maybe you could elaborate on where you are behind? Of course besides the OCM in Western Europe where are you behind in the Funding the Journey?

Second question is regarding your CapEx guidance of DKK 4 billion. Could you tell us what you have assumed in that guidance, is that pure maintenance guidance or have you assumed building of any new breweries or making investments in new coolers in any markets or something like that? Thank you.

Heine Dalsgaard

So, in terms of – good morning, Søren. You're absolutely right. We said that we are slightly ahead on value management. Where we're behind – I would emphasise that we are talking slightly here – where we are behind is perhaps in sort of the progress on OCM benefits coming through in Western Europe.

Now, we have the plans in place, we have the organization in place, we have the focus in place in Western Europe, also to drive OCM, so we remain confident that we will catch up in 2017.

In terms of CapEx, this is basically in line with previous years. We are building a new brewery in India in Karnataka.

Søren Samsøe

Okay. So, and no new cooler investments or something like that?

Heine Dalsgaard

There is always a lot of new cooler investments and also this year, but not significantly more than the normal.

Søren Samsøe

Okay. Thank you.

Cees 't Hart

Thank you, Søren.

Operator: The next question comes from the line of Olivier Nicolai from Morgan Stanley. Please go ahead. Your line is now open.

Olivier Nicolai

Analyst, Morgan Stanley & Co. International Plc

Hi. Good morning. I've got three questions please. For Russia, you made a comment saying that you were expecting to grow in line with the market in 2017. Could you perhaps make the same comment for Western Europe, what are the market dynamics into 2017 and is your target to just maintain share in the midterm or to actually gain share?

Second question is still on the Western Europe, your price/mix was at 2% in 2016. Now, how much of that positive price/mix growth was actually driven by the withdrawal from the contracts in UK, Finland and Poland and actually what is the underlying price/mix in your business exiting those one-off?

And just a follow up on the CapEx guidance. I think that's been the fourth year in a row that your CapEx is below 100% of the depreciation. At what point do you think that this becomes unsustainable and should we expect an increase in CapEx in the midterm? Thank you very much.

Cees 't Hart

Okay. Thank you very much. With regard to Western Europe. We think that going forward we would expect very low single-digit price/mix in Western Europe, between 1% or 2%. That, frankly, would be in more or less a continuation of last year if we would, that's your second question, if we would correct that for the dilutive marginal volumes.

So, in that respect, going forward, we don't expect that many changes in what we have started in 2016. It will remain to be a balance of what we call the Golden Triangle between volume, margin and the profit. With regard to CapEx?

Heine Dalsgaard

Yeah. Good morning. So, you're right. CapEx is below depreciation. But if you go back three, four years, it was the other way around. So, the logic basically is that this is a timing matter. Within a few years' time, there will be a better balance. We're certain it has to do with the historical investment level and we are certainly not in any way, shape or form, under-investing in our breweries and in our future.

Olivier Nicolai

Perfect. Thank you very much.

Cees ‘t Hart

Thank you, Olivier.

Operator: Your next question comes from the line of Ed Mundy from Jefferies. Please go ahead. Your line is now open.

Edward Mundy

Analyst, Jefferies International Ltd.

Good morning, everyone Three questions, please. First of all, on input costs. Could you perhaps clarify what your input cost guidance is for 2017? Second, again, on input costs. You had a negative transaction impact from hard currency denominated input costs in Eastern Europe. Assuming the ruble stays where it is, could you confirm what the potential margin tailwind for Eastern Europe could be for 2017?

And then the third one, in Vietnam, I think there were some Bloomberg headlines there that you expect development in the Habeco sales process in Q2. Are you able to quantify what you mean by that?

Heine Dalsgaard

So, if we start with the costs, we expect that for 2017 to be approximately flattish. With respect to the FX impact in general, you are right that there is a positive impact coming from the fact that Baltika does buy approximately 30% of its hops in U.S. dollar. That is included in our guidance for the year.

Cees ‘t Hart

With regards to Vietnam and the remark on Bloomberg, basically the process as you know is going on. And in that respect, we know that the next steps will be taken in the process of privatization there. If everything goes according to the current planning as scheduled, the next step will be at the end of Q1, beginning of Q2. So, that's where we are. And we don't have more news than that you and I read in the newspapers on that.

Edward Mundy

Thank you. And Heine, just a follow-up. Are you able to provide a bit of color on margin progression by division? Given you're going to get more OCM benefits in Western Europe, probably even more investment in Asia, are you able to provide a little more color where you think the most margin impact is going to be for your businesses for 2017?

Heine Dalsgaard

The short answer is no. The longer answer is that we only comment on the Group. There are really a lot of moving parts here. So, we don't comment on sort of guidance for specific regions.

Edward Mundy

Okay. Thank you.

Cees ‘t Hart

Thank you.

Operator: The next question comes from the line of Alicia Forry from Liberum Capital. Please go ahead. Your line is now open.

Alicia Forry

Analyst, Liberum Capital Ltd.

Hi. Good morning, guys. Just a couple of questions from me. Firstly on China. Can you talk about the expected trajectory of that Chinese business over the near to medium term, when you expect it to stop losing share, et cetera? And then elsewhere in Asia, you mentioned volume weakness across a couple of markets, an increasingly competitive beer market in Cambodia. How long do you expect those weaker trends to continue over 2017?

And then on Western Europe, will there be any lingering impact in Q1 from that UK factory being offline in Q4? And the Brooklyn Brewery distribution in the UK, are there opportunities to take that brand to other markets in Europe where you are not yet distributing it as that seems to be a craft brand that resonates pretty well in Europe?

Cees ‘t Hart

Okay. Thank you very much, Alicia. With regard to China, what we say is that there will be a continuation maybe of the decline of the market in the coming year. However, the premiumization of that market is playing in our favor. There are only two big players in the market that have international brands. We are one of them. And we see a substantial growth in our international brand portfolio in China. So, the gain is not volume but value, premiumization, and we are very well placed for that and in that respect optimistic for China.

As you know, we are very much focused on the West, and that's where we drive our market share as well and so far, so good, and we continue that in 2017.

With regard to volume weakness – well, weakness, it's lower growth in some of the Asian countries than we had in the past. But still, a nice volume growth in many of these kind of markets. Indeed, some of the competition is heating up, but that's the name of the game. We are very happy with Tuborg. We have been very successful in the three countries that we mentioned earlier, with the launch of Tuborg, and we plan to continue that. And given the proof points in other countries, we are optimistic on the impact of Tuborg in Asia.

With regard to the UK, no, we will not have any impact of the incident that we had in December in UK, in January or further. And with regard to Brooklyn, yes, we have that as a part of our portfolio, the craft portfolio. We have further strengthened our relationship and partnership with Brooklyn. We started in the UK, and indeed, we will use that brand in other markets where appropriate.

Alicia Forry

Thanks very much. That's clear.

Cees ‘t Hart

Thank you.

Operator: Your next question comes from the line of Anthony Bucalo from HSBC. Please go ahead. Your line is now open.

Anthony Bucalo

Analyst, HSBC Bank Plc

Good morning, everyone. Just a quick question, or two quick questions on India. One is that I didn't really hear any sort of discussion about the impact of demonetization, whether or not that's having any impact on your business right now or possibly will in the upcoming quarter.

Second is, the GST increase or the assumed GST increase, do you have the capacity, the legal capacity to raise prices to offset that impact without talking to local governments, or would you need to petition a local government in order to take that increase?

Cees ‘t Hart

Okay. Tony, thank you very much. Good morning. With regards to the GST first. We will not have, autonomously, the possibility to raise prices. So in that respect, we are subject to a kind of price control, and we think that there will be some pressure on the margins especially because there is always a kind of time lag between the increase of the raw material prices, and later on, the increase of the consumer prices or list prices.

With regard to demonetization, we have not seen any impact now. Obviously, as you know, the situation is a bit unstable in consumer market and confidence of that, there has been a bit of a shock in the market. But frankly we have not seen any impact for now.

Anthony Bucalo

Okay.

Cees ‘t Hart

Can we have the last question, please?

Operator: The next question is from Richard Withagen from Kepler Cheuvreux. Please go ahead. Your line is now open.

Richard Withagen

Analyst, Kepler Cheuvreux SA

Yeah. Yeah. Good morning. Thanks for the question. First of all, on your push into Asia, I mean, what else is there than Tuborg? Will there be further channel development in Asia? What other brands to emphasize and do you see any changes in sales practices?

And the second question I have is on France. I think you were a little bit caught by surprise in France in the first half of 2016, but I think you did better in the second half of the year. So, what actions have you taken in the second half to stem your market share losses in France?

Cees ‘t Hart

Okay. Thank you, Richard. With regard to Asia, well, we have a robust portfolio of local brands which served us well in the past and continue to serve us well in the future. And we can spell it out per country.

But we have a good mix of international brands including Carlsberg. We have 1664 Blanc. So it's not only Tuborg in that respect, but we have a good mix.

However, we saw as well that we could gain from the excellent positioning of Tuborg. That's what we started last year and that will be an add-on. And therefore, we are confident about the further growth of our business in Asia with a multiple of brands, and they're now including Tuborg.

With regard to France, I think what we can say is that it was a very heated summer in that respect in terms of competition. There were very steep discounts in the market which we did not participate in. Now, the market in the second half of the year is back in a more balanced way including more, if you like, normal promotions, and participating in that setting we have been able to gain some market share back in the second half of the year.

So, we have strong brands. We have strong people on the ground. But indeed, we were caught by surprise by a very steep discount action at the moment of the Euro Cup.

Thank you very much, Richard, for your question.

Cees 't Hart

And that's, if you don't mind, the last question for today. Many of you we see in the coming days and weeks. Thank you for listening in and thank you for your questions. We're really looking forward to meeting some of you during the coming weeks, and we wish you a very good continuation of the day. Thanks.

Operator: This now concludes our conference call. Thank you all for attending. You may now disconnect your line.