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Speakers: Cees 't Hart, CEO
Heine Dalsgaard, CFO

PARTICIPANTS

Corporate Participants

Cees ’t Hart – Chief Executive Officer, Carlsberg A/S
Heine Dalsgaard – Chief Financial Officer, Carlsberg A/S

Other Participants

Michael Vitfell-Rasmussen – Analyst, ABG Sundal Collier (Denmark)
Sanjeet Aujla – Analyst, Credit Suisse Securities (Europe) Ltd.
Trevor Stirling – Analyst, Sanford C. Bernstein Ltd.
Jonas Guldborg Hansen – Analyst, Carnegie
Hans Gregersen – Analyst, Nordea Bank AB (Denmark)
Edward Mundy – Analyst, Jefferies International Ltd.
Tristan van Strien – Analyst, Redburn (Europe) Ltd.
Fernando Ferreira – Analyst, Bank of America Merrill Lynch
Søren Samsøe – Analyst, SEB Enskilda (Denmark)
James Edwardes Jones – Analyst, RBC Europe Ltd. (Broker)
Olivier Nicolai – Analyst, Morgan Stanley & Co. International Plc
Simon L. Hales – Analyst, Barclays Capital Securities Ltd.
Matthew Webb – Analyst, Macquarie Capital (Europe) Ltd.

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, welcome to the Carlsberg H1 2017 Financial Statement Conference Call. Today, I’m pleased to present CEO, Cees ‘t Hart; and CFO, Heine Dalsgaard. For the first part of this call, all participants will be in listen-only mode, and afterwards, there will be a question-and-answer session.

Cees ‘t Hart, please begin.

Cees ’t Hart, President & Chief Executive Officer, Carlsberg A/S

Thank you very much. Good morning, everybody, and welcome to Carlsberg’s first half year 2017 conference call. My name is Cees ‘t Hart, and I have with me CFO, Heine Dalsgaard; and Vice President of Investor Relations, Peter Kondrup.

Let me first briefly summarize the key headlines for the first half year. We delivered strong financial performance. We are on track to deliver a large proportion of the Funding the Journey benefits. We are accelerating investments in SAIL’22 activities to drive long-term growth; and we are maintaining our full-year outlook.

I will go through the highlights of the first six months and the regions, and Heine will talk you through the financials and outlook.

Please turn to slide two. We delivered a strong set of results in the first half of 2017, and we are pleased that we are also delivering against our key SAIL’22 KPIs. We grew both top and bottom line. Net revenue grew organically by 2%, and 2% in reported terms. Organic operating profit grew strongly by 15%, and adjusted net result grew by 63%.

The cash generation of the group continues to improve. Free operating cash flow increased by 37%, which resulted in a substantial net debt reduction bringing net debt/EBITDA down to 1.57 times.

Slide 3, and a few words on our Golden Triangle. We achieved strong performance when it comes to GPaL margin improvement and organic operating profit growth, whereas volumes declined by 2%. The GPaL margin improvement was driven by a solid 4% price/mix and cost savings in supply chain. The operating profit progress was a result of improved GPaL, cost efficiencies which were positively impacted by Funding the Journey and different phasing of some costs between H1 and H2 compared to last year.

In terms of volumes, we are not satisfied with the decline that we saw in the first half of the year. The decline was primarily caused by the PET downsizing in Russia, which impacted the market and the competitive environment negatively. We lost market share due to the fact that we choose to pursue a value approach by which we took the opportunity to further drive price/mix in contrast to some of the other players in the market. I will elaborate on this later in today’s presentation.

Slide 4 please, and a brief update on our strategic initiatives. The two group priorities for the year are to deliver a large proportion of the benefits from Funding the Journey and by this enable the second priority, namely, to accelerate our investments in SAIL’22 in order to drive the long-term top and bottom line growth of the company.

The Funding the Journey program is well on-track and we expect to deliver a large proportion of the DKK 1.5 billion to DKK 2 billion net benefits this year. We follow our plans within all buckets of the program. We have on earlier occasions commented on operating cost management in Western Europe being a bit behind plan, but I’m pleased to report that the program is progressing well in all three regions.

It is very important that we ensure that the governance structures and processes established in connection with Funding the Journey are embedded in our daily routines and operations. While Funding the Journey is a program that will terminate by the end of 2017, the principles, standards and processes will remain a vital part of how to do business in Carlsberg in the future.

With respect to SAIL’22, we are accelerating our investments in our strategic priorities in order to strengthen our core business and change the growth profile of the group. A few examples of the first half year are the relaunch of Carlsberg’s export in the UK and the subsequent rollout in new markets of the popular new marketing campaign modified to Carlsberg Green Label. We saw good growth of the DraughtMaster system where we are successful in winning new outlets and converting existing customers from steel kegs to the DraughtMaster system.

Within our defined growth areas, craft & speciality grew by 25% underpinned by Grimbergen growth of 23%. Brooklyn was rolled out in more markets. And recently, we decided to establish new micro breweries in the Baltics and Hong Kong and acquired London Fields Brewery.

Another growth priority is alcohol-free beer. And in Western Europe, we grew our volumes in the category by 13%. In June, we launched our new sustainability program, Together Towards ZERO, where we have set industry-leading targets. These targets were very well received both internally and externally. To mention a few of the targets, we want to reduce water consumption in our breweries by 50%. We want to be CO2 neutral by 2030. And already by 2022, we target 100% use of renewable electricity at our breweries.

With that, I will hand over to Heine for the financials. Heine?

Heine Dalsgaard, Chief Financial Officer, Carlsberg A/S

Thank you, Cees; and good morning, everybody. Please turn to slide 6 and a few comments on the P&L. Net revenue grew organically by 2% due to a very solid price/mix effect of 4% with positive price/mix in all three regions. In reported terms, net revenue also grew by 2% as the impact from disposals was offset by the positive contribution from currencies.

Cost of goods sold per hectoliter increased organically by almost 3%, as a result of general inflation and the volume decline in Eastern Europe. Nevertheless, reported gross margin improved by 110 basis points positively affected by price/mix, efficiency improvements and currencies.

Operating expenses were down organically by 1%. This was driven by good execution of operating cost management and also phasing of costs partly offset by normal cost inflation. The ratio of OpEx to net revenue declined organically by 110 basis points to 38.3%.

In reported terms, operating expenses were also reduced by 1% as a small negative currency impact was offset by net acquisitions. The not allocated cost line increased by DKK 97 million due to phasing of costs between the first and the second half of the year and higher investments in SAIL’22 priorities.

In total, we delivered 15% organic growth in operating profit, and we are pleased that all three regions contributed with double-digit growth. In reported terms, operating profit grew by 20% because of a positive contribution from currencies of 6%. The most significant contributor to the currency tailwind was the Russian ruble. The impact of disposals on operating profit was minus 1% and was primarily because of Carlsberg Malawi and Nordic Getränke in Germany.

Slide 7, please. Further down the P&L, net special items amounted to plus DKK 38 million and were particularly impacted by measures related to Funding the Journey. Again this year, this included a positive contribution from the disposal of non-core assets, which in the first half were Carlsberg Uzbekistan, United Romanian Breweries, a Russian malt producer and Nordic Getränke in Germany.

Net financials were minus DKK 351 million, which represented a significant decline over last year. Net interest costs were down DKK 89 million as a result of the repayment of the £300 million bond that matured in November last year, and a reduction in the average net debt. Currency gains and fair value adjustments were DKK 167 million versus DKK 211 million last year, and remaining other financial items were minus DKK 164 million. The effective tax rate in the first half was 29%, in line with our expectations.

Non-controlling interests were back at the normal level compared to the last year when they were impacted by impairment and restructuring in Chongqing, related to the brewery closure program. Therefore, non-controlling interests amounted to DKK 403 million in first half 2017.

The Carlsberg Group’s share of consolidated profit was DKK 2.3 billion, an increase of 23%. Earnings per share was DKK 15.1. Adjusted for special items, the increase in net profit was 63%. Adjusted net profit was DKK 2.3 billion, and adjusted EPS was DKK 15 versus DKK 9.2 last year.

And now some comments on the cash flow on slide 8 please.

Free cash flow was DKK 5.9 billion, which represented an increase of DKK 632 million. The progress was driven by stronger earnings and a positive contribution from trade working capital and achieved in spite of last year's significant proceeds from disposals. The change in trade working capital was positive DKK 1.2 billion. We continued past years' strong performance, and as a percent of net revenue, trade working capital reached an all-time low of minus 12.9%.

We are satisfied with our current trade working capital performance. The change in other working capital was also positive, amounting to DKK 192 million. Net interest paid was actually positive by DKK 95 million which may be slightly counterintuitive, but was due to the settlement of certain financial instruments including currency swaps. Tax rate was DKK 891 million which was at the same level as last year. Net CapEx was DKK 1.8 billion, well below the depreciation of DKK 2.5 billion.

In the first half of 2017, we continued the disposal of non-core assets and therefore saw a positive contribution from financial and other investments of DKK 654 million. This compares with plus DKK 1.4 billion last year.

Slide 9 please and a few words on leverage which continued its fast decline as we reached a net debt to EBITDA ratio of 1.57. Net interest bearing debt was reduced by DKK 3.7 billion versus year-end 2016 and as I've just been through the P&L and cash flow, the reasons for the decline are straightforward; namely, improved earnings, continued working capital improvement and disposals of non-core assets.

As you may recall, we have clear capital allocation targets set in the SAIL'22 strategy where we want net debt to EBITDA to be comfortably below 2 times, which means we are targeting a ratio somewhere between 1.5 and 2 times. The stronger earnings and lower capital employed led to an improvement in ROIC of 60 basis points taking it to 6.5%. ROIC improved in all three regions.

Please turn to slide 10 and the outlook for the year. Based on the first half performance, we keep our 2017 guidance unchanged and therefore maintain our outlook of mid-single-digit percentage organic growth in operating profits.

As said earlier in the year, we saw a stronger year-on-year operating profit performance in first half than we expect in second half as we will have tougher comps in the second half of the year. In Eastern Europe because of a very strong Q3 last year, and in Western Europe, because of bad weather in Northern Europe so far in Q3 this year. In addition, there is a different phasing of costs this year compared to last year, and lastly, we are right now accelerating investments in SAIL'22 activities.

In terms of benefits from Funding the Journey, we still assume that approximately 50% of the DKK 1.5 billion to DKK 2 billion will come through this year and the remaining part in 2018. In addition, we expect to reduce financial leverage for the full year compared with the last year, and this will be driven by solid cash flow from operations as can be seen from the deleveraging by the end of June; we are very well on track on this expectation.

Based on the spot rates on August 14, we assume a positive translation impact on operating profit of around DKK 50 million for the full year compared to DKK 300 million in May. The decline is mainly due to the weakening of the Russian ruble during the summer. Excluding currency and fair value adjustments, we now expect the net financial costs to be around DKK 1 billion due to a faster reduction of net debt versus DKK 1 to 1.1 billion previously.

That is it on the outlook. Back to you Cees.

Cees C. Hart, President & Chief Executive Officer, Carlsberg A/S

Thank you, Heine. Please turn to slide 12 and Western Europe. Net revenue in Western Europe grew organically by 2% due to volume growth of 1% and price/mix of 1%, the latter achieved in spite of a negative country mix. Price/mix was positive in most markets. Other beverages grew by 4% following good performance of non-beer products in the Nordics. Reported volumes declined by 1%, and this is explained by the divestment of the German wholesaler, Nordic Getränke in April. In Q2, volumes grew by approximately 1% despite of tough EURO 2016 comparables.

The region achieved strong organic operating growth of 14% and an improvement in operating margin of 160 basis points. The earnings improvement was driven by a stronger top-line, Funding the Journey benefits and lower marketing investments compared to last year, which was impacted by the EURO 2016 investments. Within Funding the Journey, value management, supply chain savings and operating cost management, or OCM, all delivered good results.

Slide 13, please, and some market-specific comments. The Nordic markets declined slightly for the first six months. Our total volumes grew by 1%. Price/mix continued to develop favorably mainly as a result of growth of our premium propositions. Our non-beer businesses in Sweden, Norway and Finland delivered solid growth while we lost market share in Denmark.

In France, we gained market share, and our volumes grew by 5% driven by our premium portfolio with particularly strong growth of 1664, Grimbergen and SKØLL, whereas Kronenbourg in the mainstream segment declined. Despite a very competitive pricing environment, we strengthened price/mix.

In a slightly declining and highly competitive Polish market, we grew volumes by 7%. Our brands in upper mainstream and premium segments such as Okocim, Kasztelan, Carlsberg and Somersby grew, while Harnas in the strong beer segment declined.

In UK, our volumes declined by 7% due to tough EURO 2016 comparables. We continued to focus on premiumizing our portfolio and delivered a very solid price/mix, thus, achieving flat organic revenue for the six months. The addition of Brooklyn to our portfolio, the rejuvenation of Carlsberg Export at the beginning of the year and the further expansion of our portfolio with craft and premium products, all serve as examples of our premium strategy in the country.

In Switzerland, we grew volumes in line with the market. Our core beer brands Feldschlösschen and Cardinal delivered good results as we grew our craft & speciality and alcohol-free beer offerings well ahead of the market.

In the rest of the region, we saw particularly good top line growth and margin improvement in markets such as Portugal, Italy, and Bulgaria. Furthermore the Baltics, Greece, and Germany reported solid earnings improvement.

Slide 14 and Eastern Europe. Net revenue in Eastern Europe was down organically by 1%. This was caused by a volume decline of 9% as price/mix was strong at 8%. Reported net revenue grew by 16%, supported by a significantly positive currency impact driven by the Russian ruble. The strong price/mix was the result of price increases last year and this year, as well as the introduction of smaller packed sizes in Russia following the PET size restrictions. Price/mix was less pronounced in Q2 than in Q1 as we took less price increases compared with the same period last year.

Organic operating profit increased by a healthy 17%, driven by the positive price/mix and strong execution of Funding the Journey. Supported by the positive currency impact, reported operating profit grew by 39%. Operating margin strengthened significantly, improving 320 basis points to 19.1%.

The volume decline in the region was driven by Russia as we delivered volume growth in Ukraine, Kazakhstan and Belarus.

And now please turn to slide 15. The Russian beer market declined by an estimated 5% for the six months, impacted by the downsizing of PET packaging, the continued challenging consumer environment and cold weather in parts of the country.

Profitability improved significantly, driven by solid price/mix and tight cost control. Our Russian volumes were severely impacted by the PET downsizing. Approximately 20% to 25% of the market volumes were previously in the 1.5 litre packaging formats and these had to be converted into smaller PET formats. In response to this significant change in the marketplace, we adopted a value-based approach to drive further value in the market.

In the chart on the slide, you can see the weighted average retail price for us versus our main competitors and the average of the market, as measured by Nielsen. As the chart indicates, some competitors have adopted a volume-based approach. Consequently, our products in the PET segment are currently priced at a premium compared to the average price points in the market.

In some cases even, the price gap on the shelf between our offerings and those of some competitors is up to 30% to 40% and this compares with 2% to 3% last year. This all resulted in market share loss and volume decline, particularly in the lower mainstream segments with brands such as Bolshaya Kruzhka and Zhigulevskoe.

Our value approach was a key driver behind our strong profit improvement, and we will stick to our value focus. Having said that, such a significant price gap of low-end beer key products where our consumers are very price sensitive is, of course, not sustainable in the long run.

Outside PET offerings, we saw good progress of our premium portfolio with brands such as Tuborg, Baltika 0, Baltika 3, Carlsberg and Zatecky Gus gaining market share. We further expanded our position in the DIOT channel, where we grew our volumes by more than 50%.

Our beer is now sold in 35,000 DIOT outlets and according to Nielsen data, our market share in the general expanded by approximately 5 percentage points.

In Ukraine, our business continued to perform strongly delivering volume growth and strong price/mix in a slightly declining market. We gained market share driven by compelling performance of our local power brand Lvivske, Carlsberg and Garage.

Slide 16, in Asia. Net revenue in Asia grew organically by 6% driven by a very solid 5% price/mix and flat volumes. Reported net revenue grew by 1%, impacted by last year’s divestments notably of Carlsberg Malawi in August 2016 and a number of breweries in China.

The price/mix improvement was driven by price increases and continued focus on expanding our premium offerings across the region with strong performance of Tuborg, Carlsberg, and 1664 Blanc. The volume development was mixed across markets with further growth in China, Nepal and Myanmar, whereas volumes declined in Cambodia, Vietnam and India.

Organic operating profit grew by 12% and operating margin improved by 200 basis points to 19.4%. The premiumization efforts and supply chain savings, especially in China, impacted gross margins very positively and along with operating cost management, key drivers of the profit improvement.

Slide 17 please. Our Chinese business is really continuing its very positive trajectory. Net revenue in China grew organically by 8% driven by 5% price/mix and 3% organic volume growth. Once again, the growth was mainly driven by our premium brand portfolio consisting of Tuborg, Carlsberg and 1664 Blanc with Tuborg being the most important contributor, delivering 10% growth.

The Chinese market continues to premiumize and we believe that we are well positioned to benefit from this trend due to our strong premium propositions in the market. Profitability continued to improve and operating margin grew by approximately 400 basis points. Following the restructuring of our Chinese supply chain network a total of 18 sites have now been closed or sold since 2015.

In India, our business recovered in Q2 and delivered double-digit volume growth following a challenging Q1 that was impacted by the highway ban. Our volumes outperformed the market and we further strengthened our market position in the country. Also in India, Tuborg was the key brand behind the growth. We expect India to remain volatile for the remainder of the year as a consequence of the implementation of the highway ban and GST.

In Indochina, we saw a strong financial performance in Laos which compensated for weaker results in Cambodia and Vietnam. Our business in Myanmar grew strongly albeit from a small base. In Laos, we saw a good progress of Tuborg that was launched last year in the premium segment. In Vietnam, our volumes declined in Q2 following a strong Q1.

We've changed the management of Carlsberg Vietnam and are carrying out a number of changes in order to strengthen our local commercial organization. In Cambodia, our business was under pressure and lost market share.

In Malaysia and Singapore, our business delivered good performance for the six months. 1664 Blanc and Somersby achieved very strong growth rates, and we saw good progress of Funding the Journey initiatives.

That was all for today. But before opening up for Q&A, a few concluding remarks on slide 18. We delivered strong financial performance for the first half year with 15% organic growth in operating profit, 60 basis points of ROIC improvement, and a further decline in leverage to 1.57 times.

We are on track to deliver a large proportion of the Funding the Journey benefits. We are accelerating investments in SAIL'22 activities to change the growth profile of the company. And we are maintaining our full-year outlook.

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

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Michael Rasmussen from ABG Sundal Collier. Please go ahead. Your line is open.

<Q – Michael Rasmussen – ABG Sundal Collier (Denmark)>: Thank you very much. I would like to start up asking a little bit about Russia and this third quarter. You had a 16% comp from last year, and you talk about the 5% negative impact from the PET ban, and then you also talk about some negative macro impacts. So, I'm just thinking how we should model this in the third quarter if we see competitors acting the way they are at the moment, then we could potentially look at a worst-case volume development of 22% to 25% down, and also a few comments on how that could impact margins in the second half of the year, please.

My second question goes on Western Europe. Could you please tell us what price/mix would have been in Western Europe excluding the negative country mix from Poland because looking at 1% price/mix I think that's not very impressive given the numbers you give on craft and non-alcohol growth, please? And then the final question is a bit of a household. In terms of special items in the second half, how should we model that given about the positive effects from divestments fall out? Thank you so much.

<A – Cees 't Hart – Carlsberg A/S>: Thank you, Michael, for your questions. Maybe I should give you and all people on the line a bit more color on what has happened in Russia this year. So, let me spend a few words explaining the changes, but it will not lead to a kind of guidance for Q3 as you will understand, Michael. As you know, the ban on PET bottles above 1.5 liters came into effect on the 1st of January 2017. Our best estimate of the impact on market volumes from the ban was and still is around minus 5%.

In response to the PET ban, we began implementing the needed changes to our portfolio already in late Q3 and early Q4 2016 taking a value approach with the aim to improve the overall value of the market, as well as enhance our price/mix and our profitability. Consequently, we have increased prices on our 1.42-liter bottles.

One of our major competitors has followed the same approach while two other significant competitors have chosen a more volume-focused approach and actually lowered their prices in addition to increasing the promo pressure.

In the past, our offerings were typically priced a few percent above those of our competitors, but according to Nielsen, some of our 1.42-liter products now sell at a premium of up to 30% to 40%. And as a result of this significant price gap, we have lost around 5% market share, as just mentioned, in the PET segment.

On the other hand, we have seen some of the big size PET volumes move into DIOT channel, where we achieved very good results, growing our volumes by more than 50%, but this strong volume growth was not enough to offset the lost PET volumes and our Russian volumes declined by around 15%. Worth noting is that 7 of our top 10 brands are performing well and the 3 brands doing less well are brands in the lower end of the market that are typically sold in PET.

All-in-all, we believe that we have taken the right approach for the market and for ourselves, as it delivered a solid double-digit price/mix in Russia and, as you can see from the results in Eastern Europe, a very strong organic operating profit growth of 17% and an expansion of the operating margin of 320 basis points. That said, in the long run such a price premium is of course not sustainable, hence we will monitor the dynamics in the market closely. A bit of a long answer maybe but we get that there are many questions about Russia and we hope by this we have explained the situation there.

With regards to Europe price/mix, basically that's an answer that I don't have now on hand, what the mix would be if we would correct it, but the good thing is that we see price increases in most of the countries. Obviously as we said earlier, the mix has been deteriorating some of that despite the good results in most of the countries. So if you want to have more details you can come back to Peter on it. With regard to special items, Heine, over to you.

<A – Heine Dalsgaard – Carlsberg A/S>: Yeah, Cees. So, you're right. Special items, plus DKK 38 million in first half. We don't comment specifically on second half and we don't comment specifically on special items, but for the full-year you should expect sort of small negative numbers here due to the ongoing restructuring programs we have.

<Q – Michael Rasmussen – ABG Sundal Collier (Denmark)>: Great. Thank you so much, Cees and Heine.

<A – Cees 't Hart – Carlsberg A/S>: Thank you, Michael.

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

<Q – Sanjeet Aujla – Credit Suisse Securities (Europe) Ltd.>: Hi. A couple of questions on my side please. Firstly, can you just outline how much savings were delivered in the first half and how much was reinvested – or put it another way, what would your profit growth have been excluding those net savings?

Secondly, can you just allude to some of the comments on the price gap there in Russia? Is that something you could review then you would love to cut pricing there on the PET bottles? And just a broader question following the announcement of the ABI-Efes merger last week. How do you expect that to impact the market and potentially your business going forward? Thanks.

<A – Cees 't Hart – Carlsberg A/S>: Thank you. Heine, savings?

<A – Heine Dalsgaard – Carlsberg A/S>: Yes. So in terms of savings, let me – I suppose you mean in particular, Funding the Journey program. We don't comment specifically on periods within the year. What we can say is that we are comfortable and feel more comfortable as we progress throughout the program, of course, about the full benefits of Funding the Journey program of DKK 1.5 billion to DKK 2 billion. What we have said all along is that we expect the 2017 delivery of that to be approximately 50%. So, 25% in 2016, approximately 50% in 2017, and then the remaining part in 2018.

<A – Cees 't Hart – Carlsberg A/S>: With regard to the price gap in Russia, the current situation reminds us a bit to the situation of 2015. At that moment of time, we increased our prices just before the season. That was in hindsight, at that moment in time, not the right timing. And the competition could not follow us anymore. And as a consequence, we had a high price premium on the shelves during the season of 2015.

At this moment in time, we have a higher price premium on the shelf in Russia. As I said earlier, we're not going to make radical changes in our pricing policy. We'll see in the coming weeks and months what is going to happen in the dynamics in the markets. And only then will we adjust to that, except of course from protecting here and there our volume and having good promotions and actions with some of our key accounts.

With regard to ABI-Efes, well, we see a further consolidation in the market. We will have two formidable competitors now moving into one, which you see that across the globe is always encouraging for the development in the market. So, we're waiting for the developments from that.

<Q – Sanjeet Aujla – Credit Suisse Securities (Europe) Ltd.>: Thanks. Just a follow-up please on Vietnam. Can you just allude to some of the share losses that you've seen there, what changes you're making following new management coming in and perhaps an update on the situation with Habeco would be great?

<A – Cees 't Hart – Carlsberg A/S>: Yes. Thanks. Well, it's a bit – in Q1, we had, as you probably recall, pretty stronger volumes. In hindsight, we feel that there was a bit of trade loading. And as well there were very much price-focused actions from our competitors. So, that was a very weak Q2. It's too early now to say what the new incumbent general manager in Vietnam is going to do. But obviously, we have made a change for a reason that we were not satisfied about our performance in Vietnam.

With regards to Habeco, as you know, we are the sole strategic shareholder, and therefore, we have certain rights - the right of first refusal. We have had several constructive meetings with the Vietnamese government to discuss the privatization process of Habeco. We now see good progress in these meetings, and we will continue these discussions with the Vietnamese governments for the next steps. However, it's not possible to say more at this stage, and I do not want to speculate about the timing.

<Q – Sanjeet Aujla – Credit Suisse Securities (Europe) Ltd.>: Thank you.

<A – Cees 't Hart – Carlsberg A/S>: Thank you.

Operator: Thank you. Our next question comes from the line of Trevor Stirling from Bernstein. Please go ahead. Your line is open.

<Q – Trevor Stirling – Sanford C. Bernstein Ltd.>: Good morning, Cees and Heine. I suppose three questions from my side. One question on Russia. You've given a lot of color, Cees, but any signs so far that competitors three and four might be taking prices up as the season comes to an end?

Second thing is, your remarkably strong performance in the first half, and yet maintaining the guidance of mid single digits for the full year, which implies roughly a flattish organic EBIT growth from the second half. Is the biggest factor there the Russian drag in Q3 or SAIL'22 investments, and perhaps just a little more color about the relative weight of those two would be great?

And finally again, very strong cash performance. The net debt-to-EBITDA ratio is looking very good. As we get to the end of the year I guess much depends on Habeco. But if you do have an under levered balance sheet at the end of the year, have you any thoughts at all about what you do about that, about buybacks, dividend rate is, and – or is too early to talk?

<A – Cees 't Hart – Carlsberg A/S>: Thanks, Trevor, for your questions. The first one I will take, and the other two, Heine will take. With regards to signs of competition – competitors, as I said earlier, it all reminds us a bit of the season of 2015 when we were late with increase of our – just before the season of increasing our prices. Competition at that moment in time tried as well, but they were too late. Key accounts had not basically accepted that.

And we see some signs moving now to this year, we see some signs of those competitors trying to increase their prices in the PET segment. So, that question I can only answer is, yes, we see signs of competitors moving. Heine?

<A – Heine Dalsgaard – Carlsberg A/S>: Yeah. Hi, Trevor. Just if we start with the expectations for the second half. So, you're absolutely right that we maintain our full-year guidance of mid-single digit growth in our operating profit. We don't comment, for good reasons, specifically on periods within the year. There are three main reasons why we maintain our outlook for the year, and we don't sort of split in between those three parts.

The three reasons has to do with first of all tough comps in Eastern Europe in Q3 following last year's heat wave and also volume growth in Q3 last year. And then a poor weather in the beginning of Q3 this year, in particular in Northern Europe. So, that's one. Second has to do with higher investments in second half versus first half. So we are now accelerating exactly in line with our strategy. And the third reason has to do with typically the phasing in particular of certain marketing costs. So these are the three main reasons why we maintain our full-year outlook.

In terms of your question, Trevor, on some additional shareholder return, you are correct that we are getting closer to the 1.5 times, and as we have said, we feel comfortable somewhere between 1.5 times and 2 times. The decision on additional shareholder return is taken once a year by the supervisory board and announced at the Q4 announcement. As stated in our capital allocation principles, we have four sort of main priorities which are: one, to invest in the future growth of the business; two, to reduce debt; three, to increase our payout ratio gradually towards the 50%; and then four, after that, we will distribute cash either as higher dividends or buybacks.

So, the logic is that we will increase payout ratio before additional shareholder returns but, again, this is something that we will discuss with the supervisory board later in the year and come back to you in connection with the Q4 announcement. And you're absolutely right that it is clear that potential M&A activities like Habeco can postpone the sequence a bit.

<Q – Trevor Stirling – Sanford C. Bernstein Ltd.>: Thank you. Thank you very much, Cees and Heine.

<A – Cees 't Hart – Carlsberg A/S>: Thank you.

Operator: Thank you. Our next question comes from the line of Jonas Guldborg from Carnegie. Please go ahead. Your line is open.

<Q – Jonas Guldborg – Carnegie>: Yeah. Good morning, everybody. Two questions from my side. First of all, I would like you to talk a little bit about your craft strategy when it comes to these microbreweries. Now, you bought London Fields Brewery and are building a new one in Lithuania. If you could just talk about what we should expect from you in the coming periods, i.e. more M&A and more startups here?

And then second question is on full-year guidance and the effect from M&A. You've divested quite a lot of companies over the recent quarters. So, could you give a ballpark [indiscernible] (39:06), which effect we should expect on EBIT in 2017 from this? Thank you.

<A – Cees 't Hart – Carlsberg A/S>: Thank you, Jonas. With regard to craft, we have, in our view, a strong portfolio there with brands like Grimbergen, Brooklyn and 1664 Blanc and these are, these are like international craft brands which we want to further grow and you're seeing some signs of early success in our figures, talking about over 20% of growth in this category. So, in that respect we feel that our initiatives on SAIL'22 really work.

So, these are the international ones, then we have some, what we call, line extensions of our power brands, local power brands. We call that Crafty extensions and these are successful as well. And then we see here and there that we need some very local-specific brands in our portfolio and one of them you quoted is the one in UK and the other one in the Baltics.

But you should not expect from us, a big effort in acquiring small craft breweries. So here and there, we see that and basically have already investigated where we need or where we see some gaps in our portfolio, we'll do so but it's not that you should see a step-up in our acquisitions there.

<A – Heine Dalsgaard – Carlsberg A/S>: Hi, Jonas. The question on full-year effect on EBIT from divestment is not that significant but expect a negative impact on EBIT of around DKK 80 million.

<Q – Jonas Guldborg – Carnegie>: Okay. Thank you very much.

<A – Cees 't Hart – Carlsberg A/S>: Thank you.

Operator: Thank you. Our next question comes from the line of Hans Gregersen from Nordea. Please go ahead. Your line is open.

<Q – Hans Gregersen – Nordea Bank AB (Denmark)>: Good morning. Returning to Russia, I do expect that you should have the best cost structure across the Russian brewing industry. Can you clarify, if you were to apply the low price points you're seeing from your competitors, would you be profitable on those PET segments? That's the first question.

Second question, on organic EBIT, do you expect a positive organic EBIT development for H2 as such, no quantification, just whether it's positive or negative?

And then, thirdly, in terms of minorities, they were quite up compared to last year. What do you expect for the full year on this one? Thank you.

<A – Cees 't Hart – Carlsberg A/S>: Thank you, Hans, for your questions. With regards to the low price points, I think – or we know, indeed, that we have the lowest cost structure. We have investigated that, we see that it's very difficult to make profit at the price levels they are focusing on at this point of time in PET.

<Q – Hans Gregersen – Nordea Bank AB (Denmark)>: Sorry, Cees, can I just come back to this? If you were to apply those price points, could you turn or sell those products at a profit or would they be loss-making?

<A – Cees 't Hart – Carlsberg A/S>: I guess this very much depends on whether you're talking organic or reported. Reported is strengthening of the ruble is a bit different but in organic terms, we would make losses.

<A – Heine Dalsgaard – Carlsberg A/S>: So, Hans, your question on expectation for second half EBIT, first of all, we do not comment specifically on periods within the year. We maintain our full year guidance of mid-single digit, and then I'm sure you do your math yourself.

In terms of minorities, they are back now at a normalized level after having been impacted last year by impairment in Chongqing, actually over the last two years, and as we said at the Q4 call, all minorities would last year have been somewhere between [DKK] 600 and 650 if we adjust for the Chongqing impairment and restructuring. Full-year 2017, we expect slightly higher minorities than in 2016.

<Q – Hans Gregersen – Nordea Bank AB (Denmark)>: Thank you.

Operator: Thank you. Our next question comes in the line of Edward Mundy from Jefferies. Please go ahead. Your line is open.

<Q – Ed Mundy – Jefferies International Ltd.>: Morning, everyone. I appreciate you're not guiding specifically on the outlook for organic EBIT growth for second half, but could you perhaps provide a bit more color as to what the range of mid-single-digit is? Is it at 4% to 6%, or is it more than 4% to 6%?

Secondly, is there any benefit from the hedging of input costs in Russia in the second half? I know that you hedged till 12 months out or so, and then finally on interest expense, it looks like your guidance of DKK 1 billion for the year looks quite conservative, now with the DKK 300 million or so in the first half, perhaps you could extrapolate on that as well.

<A – Cees 't Hart – Carlsberg A/S>: Thanks Ed. Over to Heine.

<A – Heine Dalsgaard – Carlsberg A/S>: Yes. Good morning, Ed. So, what does mid-single-digit mean? It's what is in between low-single-digit and high-single-digit, probably translates into something like 4% to 7% in our book. In terms of the benefit from currency, you are right that approximately in Russia, you're right that approximately 30% of our COGS comes from euro and U.S. dollar purchases, so there is the benefit. You are right on that one.

In terms of interest for the full year, your comment is that the DKK 1 billion seems to be on the high side. Do take into account that the way guide now is on net finances excluding FX and if you have the first-half number of a net number of 351, then you can also see in the details that DKK 167 million from FX. So, if you add that on top, you come to a number of about DKK 500 million which makes the full-year guidance look a bit more logical. So, the reason is that our guidance on net financials is excluding FX.

<Q – Ed Mundy – Jefferies International Ltd.>: If we do include FX, what would the financial items be assuming spot momentum as it is today?

<A – Heine Dalsgaard – Carlsberg A/S>: That's why we don't guide on – so what we say is only – and that's the reason why we don't guide on FX because we simply don't know what FX will do for the rest of the year. What we can say is that for the first-half of the year, there is a plus of DKK 167 million, we do not guide specifically on FX impact for the second half.

<Q – Ed Mundy – Jefferies International Ltd.>: I mean, if we've seen that that spot remains unchanged, should we take that DKK 1 billion, less by DKK 160 million, or should we just multiply the DKK 350 million by two?

<A – Heine Dalsgaard – Carlsberg A/S>: That's something we don't comment on. We don't know where we're – and this is the reason, exactly the reason why we don't guide specifically any longer on net financials, including FX. It simply doesn't make any sense.

<Q – Ed Mundy – Jefferies International Ltd.>: Okay. Thank you.

Operator: Thank you. Our next question comes from the line of Tristan van Strien from Redburn. Please go ahead. Your line is open.

<Q – Tristan van Strien – Redburn (Europe) Ltd.>: Good morning, gentlemen. Just three questions. Two on Russia and one on working capital. The first one, you have share gains in DIOT. Can you just maybe expand on that what is your current share? How many outlets have you gained and how the split between modern trade and traditional trade, and how do you ensure you're delivering a brand experience in what is essentially an unbranded occasion? So, maybe a bit of color on that.

The second one is on pricing in Russia again. Last year you were actually the price cutter in the market. So, how would that graph on page 15 look, if we take it on a two-year stacked basis? I mean, you're in line with – the market now in line with you basically on a two-year basis and within that, what premium does Carlsberg brand and Tuborg brand enjoy over Baltika at the moment, versus last year?

And then the last question, Heine, on working capital; some very strong movements. How should we think about this in the full year? Is this kind of the running rate that we're looking at, or do you see some of that given back in H2?

<A – Cees 't Hart – Carlsberg A/S>: Okay. Tristan, thanks for your questions. First of all, we need to say that the DIOT channel is not very well covered by Nielsen. We estimate that the channel is probably some 15% of the market even though it has been growing by 20% CAGR the recent year, and we expect the channel will continue to grow.

We are out-growing the market – the channel growth – but still under-indexed in the channel. Year-to-date we grew, as we said earlier, 50%. To your question, how many are those outlets, 35,000; I don't have the split between traditional and non-traditional, but at this moment in time, still the channel is dominated by the locals. According to Nielsen, we have 17% to 18% share in the channel.

When you talk about we are the price cutter, that really is not factual. The only thing we have done last year was reducing our price of Carlsberg because it was overpriced. I think on average it has a premium of 10% on most of the Baltika portfolio, but, as you know, Baltika 0, 3, 7, they have their own price points. So, we continued, over the last three years, continuously to add value to the market, and we have not cut prices at all except a repositioning of the Carlsberg brand.

When you talk about DIOT in terms of unbranded occasions, well, basically it's very branded; if you walk into a such a shop, there you'll see 10 to 15 branded offerings. So, basically we are able, with our strong portfolio of brands, to add value to that.

To your point, there are especially in key accounts of unbranded occasions, but that's a lower – a smaller part of it. The main part and the interesting part of DIOT, which is growing fast, is the branded that part in DIOT.

<A – Heine Dalsgaard – Carlsberg A/S>: Tristan, in terms of your question on trade working capital, you're absolutely right; strong performance in the first half minus 12.9%, all-time low. There is a phasing elements in this as well. So, for the full-year expect a big round zero.

<Q – Tristan van Strien – Redburn (Europe) Ltd.>: All right. Thank you. Very clear. Thanks, guys.

<A – Cees 't Hart – Carlsberg A/S>: Thank you.

Operator: Thank you. Our next question comes from the line of Fernando Ferreira from Bank of America Merrill Lynch. Please go ahead. Your line is open.

<Q – Fernando Ferreira – Bank of America Merrill Lynch>: Morning. Thanks for the questions. Two questions left for me, please. First one on operating leverage. If you could comment on how relevant is it for you to revert those volume trends and go back to growing volumes in order to keep delivering on the margin expansion, please.

And then the second question on SAIL'22, if you can tell us which part of SAIL'22 is going to see more investments in H2 of this year. And also if you could provide us an update on your target of big cities project, please.

<A – Cees 't Hart – Carlsberg A/S>: Yeah. With regard to the volume we need for the margin expansion, I think we're having this kind of a Golden Triangle. That's a concept which we stick to. And, obviously, especially in Russia, it's very clear that we're extremely satisfied with the gross margin and the EBIT performance, but not with the volume performance. So it means that the Golden Triangle in Russia, for example, is out of balance.

Total company is influenced in terms of the Golden Triangle due to the Russian lower volumes. But, in total, when we talk about Russia and Europe, and then we see Asia, we are more or less in balance, but it's a tweaking process and that is what it'll continue to be in the coming quarters and years.

With regard to SAIL'22, when you talk about the big investments, the investments will be behind alcohol-free beer, behind as well craft & specialities. We see, as we said earlier, some first signs of success, alcohol-free beer in Western Europe was growing by 13% and we quoted earlier a 20% growth in craft and specialties.

With regard to the big cities, the project is going on. As we said earlier, don't expect early signs of success there as we see that this craft and alcohol-free beer. It's more that we have now established small enterprises in the two big cities. Again, we will not comment on it. But by next year, around May, we think we will be in total in four cities. And around that time, probably it's the right time to get you update on that.

<Q – Fernando Ferreira – Bank of America Merrill Lynch>: Okay. Perfect. Thanks, Cees.

<A – Cees 't Hart – Carlsberg A/S>: Thank you.

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

<Q – Søren Samsøe – SEB Enskilda (Denmark)>: Yes. Hello, gentlemen. Just firstly, a question on your gross margin, which improves 110 basis points. If could just say how big that improvement would have been if you adjust for the PET ban?

Secondly, you had a very strong momentum on free cash flow on first half. Can we expect this to continue in the second half or are there any sort of big CapEx investments waiting in second half and then what are they and are there any big working capital swings we should adjust for?

And then, finally, if you could just confirm in terms of your future financial costs, you have a bond, big bond, €1 billion running out here later this year, right? And what's the interest rate on that one? Thank you.

<A – Cees 't Hart – Carlsberg A/S>: Thanks, Søren. Heine will answer the three questions.

<A – Heine Dalsgaard – Carlsberg A/S>: Sure. Hi, Søren. So if we start with the gross margin and the effect of the PET ban that's something we comment on specifically. We're very satisfied with the 110 basis point up. Cees has already been through the effect of the PET ban, which mainly is a volume sort of effect short term.

In terms free cash flow, extremely strong for the first half in terms of the trade working capital, which is the big one we comment on here. Expect, as said before, a zero for the full year. We don't comment on the other ones. In terms of the €1 billion EMTN bond we have maturing in October, you're absolutely right. We will look into how to refinance that and the interest level on that one, the coupon is 3.375%.

<Q – Søren Samsøe – SEB Enskilda (Denmark)>: Okay. Thank you.

<A – Cees 't Hart – Carlsberg A/S>: Thank you, Søren.

<A – Heine Dalsgaard – Carlsberg A/S>: Thank you.

Operator: Thank you. Our next question comes from the line of James Edwardes Jones from RBC. Please go ahead. Your line is open.

<Q – James Edwardes Jones – RBC Europe Ltd. (Broker)>: Yeah. Morning. Could you just say what happened to marketing expense in the first half? Were they down as a percentage of sales and what component of the margin growth was marketing expenses?

<A – Cees 't Hart – Carlsberg A/S>: Heine, over to you.

<A – Heine Dalsgaard – Carlsberg A/S>: Sure. So marketing investments are down in the first half, which mainly, as said, is a phasing point because it has to do with the high investments in EURO2016 in first half 2016. For the full year, we don't expect marketing spend to be down versus last year.

<Q – James Edwardes Jones – RBC Europe Ltd. (Broker)>: But what about in the first half specifically?

<A – Heine Dalsgaard – Carlsberg A/S>: So the effect is a few hundred million lower than last year.

<Q – James Edwardes Jones – RBC Europe Ltd. (Broker)>: Okay. Thank you.

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

<Q – Olivier Nicolai – Morgan Stanley & Co. International Plc>: Hi. Good morning. I've got two questions, please. First of all, in France, your volumes were up 5% in H1, which is very strong, considering you were lapping the Euro Cup last year. Do you think this strong growth is all weather-related, or is there a change in underlying trends? And also, will you be able to comment on your market share evolution, what it was in the on- and off-trade?

And just going back to Eastern Europe. Obviously, your H1 organic EBIT growth was up 17% in H1. Could you please quantify the potential of positive transactional FX impact on your COGS? And would you expect this to continue in H2? And just to stay on Russia, obviously, next year, you have the world cup, should we expect a step-up in marketing already in H2 this year, or should we see this step-up in H1? I know you're not the official sponsor, but I'm sure you're going to do some activations. Thank you.

<A – Cees 't Hart – Carlsberg A/S>: Thank you. Thank you, Olivier. With regard to France, we are very pleased with our performance in France this year so far. Year-to-date, we have gained market share in the off-trade, which is more than 70% of the market. We gained market share after last year's weak performance in Q2, which you might recall. We're gaining both volume and value share. Private label is losing out in France.

We think we have lost a bit of market share in on-trade, which is 29% of the market as we largely had significant sales in football stadiums and fan parks at the EURO. So basically all in all, very pleased with our start in France.

Maybe I'll take immediately the one on Russia, the step-up. We see that we'll anticipate early in the season so much more in Q1 than in the remainder of this year.

And for your second question, the last answer over to Heine.

<A – Heine Dalsgaard – Carlsberg A/S>: Sure. So on the FX impact, so you're right. Strong earnings in the first half. And it is also right that there is a positive effect from FX in first half in Russia because of the 30% of COGS being purchased in euro and dollar. There are so many moving parts in the total profitability that we do not comment specifically on the different elements.

<Q – Olivier Nicolai – Morgan Stanley & Co. International Plc>: Okay. Thank you very much.

Operator: Thank you. Our next question comes from the line of Simon Hales from Barclays. Please go ahead. Your line is open.

<Q – Simon Hales – Barclays Capital Securities Ltd.>: Thank you. Just a couple of quick questions please to round up. Just on India, could you talk a little bit maybe about what the impact of GST you're seeing is on your business from both the margin and from a sort of volume and sales point of view, how things have developed as we moved into Q3, and a little bit more as to how you think things may move with regards to GST versus the highway ban through the second half beyond your comments around just increased volatility?

And secondly, I may have missed this, so apologies if I have, just in terms of the Russian beer volume performance that you saw in Q2 in the first half, could you give us the absolute numbers please?

<A – Cees 't Hart – Carlsberg A/S>: Okay. Thank you, Simon. With regard to India, the GST. On GST, it's too early to make any comment now. We see, of course – well, we know about the impact on the market. We probably will get some increases in pricing. That's what we need to recoup in the different states. Some of these are price-controlled, so we need to do our utmost to at least keep the margins in India.

With regards to the highway ban, we see a mixed picture. First of all, it's improving significantly after Q1, as you've seen in our volumes, which are now around 20% up in Q2. In India, we are seeing that some find it difficult to relocate to new areas. And state by state, we see the recovery of the highway ban and the figures in terms of number of shops before and after is between – well, if you take Himachal Pradesh is 43%, and others like Uttar Pradesh 77% of recovery in point of sales.

So in that resepct that's the mix feature, but it will be – because of GST and as well the highway ban, it's difficult to predict the Q3, Q4.

With regards to the Russian numbers, I'm not sure which numbers you would like to have.

<Q – Simon Hales – Barclays Capital Securities Ltd.>: Yeah. Just the headline volume numbers for Carlsberg.

<A – Cees 't Hart – Carlsberg A/S>: Okay. So for Russia specifically, we have in the first half year 15% decline, and that's I think the number you're looking for.

<Q – Simon Hales – Barclays Capital Securities Ltd.>: Yeah. That's perfect. Thank you, Cees.

<A – Cees 't Hart – Carlsberg A/S>: Okay. Good. Thank you very much. We have time for one more question. Can we have the final question please.

Operator: Thank you. Our final question comes from the line of Matthew Webb from Macquarie. Please go ahead. Your line is open.

<Q – Matthew Webb – Macquarie Capital (Europe) Ltd.>: Thanks very much. Just two questions if I may. First, I appreciate you don't disclose the gross or the net cost savings at the half year stage, but would I be right in thinking that the reinvestment level in the first half was well below the guidance that it'll be over 50% for the full year, given how strong the organic EBIT growth was in the first half? But also, does that guidance for the full year still stand that you're reinvesting more than 50% of the gross savings?

And then, the second question, I think you said in the presentation that the Funding the Journey program will be at an end of 2017, but the principles will remain and continue to give you some benefit. But should I infer from that that there will not be an explicit second phase to that cost saving program with new target set? Thank you.

<A – Cees 't Hart – Carlsberg A/S>: Heine. Thank you, Matthew. Heine for the first question.

<A – Heine Dalsgaard – Carlsberg A/S>: Thank you. Thank you, Matthew. So you're right in assuming that the investment part in 2017 is higher in the second half than it is in the first half. In terms of the full-year expectations, yes, we still expect approximately 50% and probably a bit more than 50% for the full year in terms of full sort of benefits for the full program in 2017.

In terms of your comment on Funding the Journey, as a program, it is a program, as Cees says, that we have initiated for 2016, 2017 and 2018. But the logic and the principles in the program will continue as a new way of living. Whether there will be a step two, let's see. We don't know. For sure, the principles and the logic of Funding the Journey is something that will continue. We don't foresee a new program. We just foresee that that we have now a program that we are delivering on in 2016, 2017 and 2018, and then that will translate into a way of living in Carlsberg.

<Q – Matthew Webb – Macquarie Capital (Europe) Ltd.>: Super. Thanks very much.

Cees C. Hart, President & Chief Executive Officer, Carlsberg A/S

This was the final question for today. Thank you for listening in and thank you for your questions. We're looking forward to meeting some of you during the coming days and weeks at our Capital Markets Day in October. Have a nice day. Thank you again.