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Presentation

Jacob Broberg
Thank you very much and welcome once again to Cloetta Q4 Results. My name is Jacob Broberg. I am the head of Investor Relations and we have now Danko Maras, our CFO and Henri de Sauvage Nolting, our CEO. And I hand it over to Henri to start. Please go ahead.

Henri de Sauvage Nolting
Thank you, Jacob. You can see our brands and products that's in the end, what this business is about. Lovely brands, lovely products, our goal, of course, is to bring a smile to your munchy moments. Let see how quarter four went.

We can see that our net sales came up to 1.6, 43 million. Of course, there is the acquisition effect of Candyking in there. The organic growth of the existing Cloetta business was flat – 0% – and it's good to say that the Candyking business which is not in the organic, compared to previous quarter last year grow with 14% in the quarter.

If we then look at the adjusted operating profit, you can see that we're nearly flat versus last year at SEK 206 million, and operating profit a bit below. However, the profit for the period from continued operations came to SEK 20 million and there's a non-cash impact from the tax dispute which Danko will try to explain a bit more, further down in the presentation.

Also, cash flow at SEK 305 which was good, but we have to remember that we do not adjust for the Italian cash flow effect over here which has a negative impact on the like-for-like comparator. Net debt and EBITDA came under our target level, and that also means that we are proposing a special dividend of 75 öre very much linked to the disposal of the Italian business.

If we then look at the markets, it's again, very good to see that all markets except Denmark are showing growth, yeah, so the confectionery market is showing growth. This is not what some people are thinking. This is Nielsen growth which is mainly related to the packed, branded business; on top of that, we have the pick & mix business, which is not measured by Nielsen, which we can also see ourselves is growing in sales.

Organic growth was flat and we can see that our two biggest markets in Sweden and Finland were in growth, the Netherlands declined only in the quarter mainly due to promotional planning. And as I said Candyking grew 14% which is really pleasing to see after many years of decline, and also that meant that now, the full year of Candyking is showing a growth of 1.3%.

And again, when we look at the Candyking integration, it has been very much our focus in this first year of integration, the focus on the top line growth and keep that because that's so important for the Candy King business but also for our own investment case that we bring those growing volumes in our existing factory network.

So, if we look at the Candyking integration, it's in line with plan. The new integrated organisations are progressing in all markets. We've also decided to exit Poland. That's only a SEK 15 million business full year 2017. Loss-making and we did not see an investment case to make that into profit.

The insourcing activities are progressing well in line with plan and probably also important to mention that we've renegotiated all contracts from Candyking, apart from one, which is still under negotiation at the moment. Some of them one-year contracts, some of them three-year contracts; it's a mix. And the identified savings over SEK 100 million are still standing firm.

Then I would like to hand it over to Danko to take us into a bit more detail on the P&L.

Danko Maras
Thank you, Henri and good morning everyone.

I'll come back to the sales number, if we just go direct into our gross profit for the quarter. You can see that we have delivered SEK 45 million more in gross profit but we have a dilution of our gross margin of about 410 bps. And again, I said this a few times now, hopefully, it's becoming clear, it's dilution coming from the acquisition of Candyking. It represents approximately 250 bps out of the total and as we start realising synergies from the factory production, this business will start yielding and diminishing and come up to the margin that the overall company has in total. But that has yet to come but that's the core reason for the dilution of the gross margin.

We also have some forex effect in the quarter that is not only related to Euro. So the pound is still affecting us and US dollars, and that in total, represents approximately 60 bps. And the remaining part in the gross profit is supply chain cost that we have both which represent approximately 80 bps. Those are the three key ones and those 80 bps had also been part of the items affecting comparability. So when you look at the difference between operating profit and operating profit adjusted, that's the difference that we are taking out, because they are related to one-off supply chain costs.

And moving down to the P&L, you can see that we are fairly in line with last year on the operating profit adjusted, and the operating profit is about SEK 9 million below last year. The difference between the adjusted and operating profit of SEK 35 million, is Candyking integration costs, and those supply chain costs that I referred to before.

So we have all seen parts of this, obviously I have done a couple of quarters with our net financial items, but now we are starting to see comparators from last year when we got the benefit from the renegotiated refinancing that we did in Q3 last year. So you can see that we are low at SEK 27 million, but last year's comparator is 25; that is the approximation of some around the effective interest rate of 1%.

Profit before tax, SEK 144 million versus 155 last year, is just a trickle down of the effects of the operating profit. But then we have a one-time charge in our tax line of approximately 20 million which is non cash in nature. We will look at how that actually impacts us in the future. That depends on the streaming flows but we are assessing that we can actually reduce the cash effect for this one. But this is a late incomer from us, we received a note from the Slovakian government and we are doing a recognition of evaluation allowance on a deferred tax asset that we will dispute strongly. But because we want to be conservative about the booking and the advice we received, we have actually booked it now in the fourth quarter. And we will come back to you on this point going forward to make sure that we have complete clarity on it. But we feel confident that we have an ability to drive these issues.

If I then go back into the sales part, you can see 20.8% is the structural changes in the quarter. We have a slightly negative impact in exchange rate of minus 0.6% but overall, full year, the euro has continued to be stronger versus prior years, while the full year effect is still there at 0.6%.

The organic growth is flat in the quarter, but then full year, you are seeing a year of decline of 1.2%. But if we look at the total for the quarter, it's quite a large number of 20.2%. And as Henri was saying, a very nice delivery from the like for like comparators on Candyking versus last year with 14% growth. So great work from the Candyking business.

On the cash flow, also this slide is not unimportant perhaps to see it in the right light. We don't restate Italy in the cash flow. The cash is what cash is and therefore you see cash flow from operations as 406 million. And always in the fourth quarter, the Italian business was cash generating because of the seasonal business. So if we extract that out of the comparator, the cash flow from operating activities is similar to last year and a very good cash flow delivery in the quarter.

If we then move down to investing activities, you can see that we have 23 million in total versus 105 million last year. This is the second instalment of the payment on our Italian business, so the 69 million result in the second instalment from the business we have and had sold in Italy. So, if we combine those two together, we are at full year delivery of 690 million and in the quarter, 328. And those 690 million are to be compared to last year of 567.

But if you then going and look at the metrics – maybe I'll just take a moment here to give you an indication of a good cash delivery. Our net working capital as a percent of sales is, today, 5.5%. So those of you who have been with our journey knows that we have been up to 15%. So that's a significant reduction and obviously part of the disposal of Italy for factories and the acquisition of the more asset-light Candyking business making a good effect on the capital efficiency.

Our CapEx is about 2.4% of sales which we have as a target of 3% and our cash conversion is 83% in the quarter versus 82% last year. So all metrics on cash delivery are very good. And because of that I'll come back to this in relation to the dividend.

But if you go to the next page, you can see that our net debt EBITDA has now reached 2.39. We are below the target level. It sounds like the wrong word. We are better than the target level of 2.5 times. And this part then also relates to the one-off effect of the disposal of Italy. Because of the cash proceeds received, we have a lower net debt.

So with that in mind, the dividend proposal from the Board is originating from a two-folded rationale. One is to give an ordinary dividend of 75 öre per share which is approximately 54% of the normalised net income excluding the effects of the disposal of Italy. And the reason to why we don't increase it is because we simply did not have a good year on our EBIT, and therefore, we retain the level at 75.

On the other hand, there was a good cash proceeds in the incoming disposal of the Italian business, and therefore, the board will propose an additional 75 öre as a special dividend for this year that totals 150. So, there is an ordinary dividend of SEK 0.75 and a special dividend of SEK 0.75 totalling SEK 1.50. And with that, I stop and I give the word back to Henri.

Henri de Sauvage Nolting
Thank you, Danko. If we then look at the focus areas we have at the moment, no surprise that our main focus is to drive profitable growth, sharper brand plans, more focus on working together across the markets and with the central marketing functions, so with priority number one.

The second one is the factory network. As communicated earlier, we'll get this new line in the beginning of Q2. Our focus is to be up and running but also the reallocation of production over the moulding network has been done and we also can see that we have more stable production coming from the moulding network. But, of course, we're still using as well some third parties to help us supply until the new line is up and running.

Third priority is the Candyking integration: two big chunks, of course. One is the commercial integration. But, also in Q2, we will go live in most of the markets with the enterprise system of Cloetta, so we can start to work as a single back office in all those areas. And the other one, of course, is the big insourcing activity which we already started last year but which is ramping up during 2018.

And then last but not least is the gross margin and cost improvement. Gross margin, very much, again, through supply chain efficiencies but also mix. And then we're working hard on the execution of the cost programme which we also announced before of the SEK 15 million towards the end of this year in run rate the combination of non-people cost and FTE reductions.

If we then look a little bit at our strategy into action, we talked about the eight essentials in the last update; the eight priorities for the company to start delivering versus our goals. One of the eight essentials is to offer consumer's choice. And we've launched now successfully in the Netherlands a range with lower and no sugar products which is under Red Band brand. We're doing very well. And simultaneously, we're also in the choice to do offering more portions controlled back, so smaller back and the bigger back, again, to give people in this case, particularly parents also, a possibility to work with portion control. So this is an example of one of the initiatives coming from the new strategy which will be rolling out across the markets.

And with that being said, we open up for questions.

Q&A

Operator
Thank you. Ladies and gentlemen, if you wish to ask a question, please dial 01 on your telephone keypad now to enter the queue. Once your name has been announced, you can ask your question. If you find it's answered before it's your turn to speak, you can dial 02 to cancel. So once again, that's 01 to ask a question or 02 if you need to cancel.

Our first question comes from Michael Hall of Danske Bank. Please go ahead. Your line is open.

Mikael Holm
Hi, this is Mikael at Danske. First, a question on the renegotiated contracts that you basically have closed all of them except one. Could you say something about the price level of this compared to what we did see in 2017? That's the first question.

Henri de Sauvage Nolting
That's very difficult to talk about prices. I think that's even probably not legally allowed to talk about the prices we agree with our customers versus the competition: competition law. But let me say, we're happy with having those contracts overall. So, as I said, negotiating the last contract with one retailer and, of course, this is very important for the volume. You can also see that in the projections we're making on the earn out instrument. So, the ship is on course in that sense.

Mikael Holm
Okay. And also, on marketing investments, you mentioned some 15 million higher in Q4 this year than last year. Is that something that should increase in 2018 as well because we noticed that the level has decreased in recent years?

Henri de Sauvage Nolting
So, what we have said in our new strategic plan is that we want to strengthen our brands, and one – only one of the things we want to do, is to competitively spend behind what we call 'working media'. So yes, we will be spending more, but what is the source of this, there's basically two sources, one is to be more efficient with the existing media budget and to move money from non-working media, which means research cost, agency cost, etc., into working media, which will then give us a benefit in the strength of the brand. And the other one is that, we said, okay, we will fund any additional investments in media, from cost savings, and particularly in the indirect line, on top of the programs we have like the Candyking insourcing.

And that we will be doing, we'll not do it blindly, and we'll do on good, justified business cases where we investigate the uplift. That's what I would have to say on that question.

Mikael Holm
Okay. And my final question is just on this somewhat higher production cost due to the thing that happened in Belgium. You mentioned there were higher earlier quarters, but is it fair to say that these issues were solved at this quarter, and 2018 will be basically –

Henri de Sauvage Nolting
I think we could, yeah, we could say that after Q2, when we have our new line up and running, we can take back all the production which we had to outsource, but we also can then optimise again, across the factory network; as we explained it, that we're running on five shifts now, in most of the factories, and sometimes, it is better to decide to run in three shifts, because you pay less.

So when we have our line in turnout up and running, we will start to come back to the original trajectory of our cost in the moulding network.

Mikael Holm
Okay, thank you.

Operator
Thank you. Our next question comes from Nicklas Fhärm of SEB Research, please go ahead, your line is open.

Nicklas Fhärm
Thanks, operator, and good morning to everyone. I would also like to start follow up from the first question on the call, regarding the marketing cost. So obviously, I realised you spent some additional

money, and in addition to that, you also write that you reduced some campaign activities in the Netherlands, you saw some impact in terms of falling volumes and sales in that market.

And it would be really, really helpful if you could elaborate a bit more on the relationship between marketing expenditure, and sales growth. And what I'm alluding to is also, if you could touch a little bit on sort of the structural implications, perhaps affecting the markets you're operating in going forward, please.

Henri de Sauvage Nolting
Yes. So, there are two questions in one. So if we look at the Netherlands, what we can see, there's some promotional phasing, the promotions which we used to have in Q4, maybe now, we're in Q1, but it's also a conscious choice to actually withdraw a number of promotions where we said, 'Well, we don't do that anymore in this channel, because it doesn't give us the margin, which we would expect from this branch,' yes.

All these kinds of cost are booked in our sales line, right, so it will give discounts to sell products on promotion, you look out for that in our sales figures.

Then the other question is about the brand support, and that's it in the SG&A line; so that is media, or advertising money, which tends to work much for long term, so you could say the first effect in the Netherlands, that's the promotional part, is short term, the media money is to build, you know, a preference for our brands.

And that is work which we're doing, for example, on some of our key brands, to reassess, well, the position of the brand, why do people like it, how do we communicate that towards people, what is the most effective way to do that. And we are making changes over there, we're also reaping more benefits across the market; it would take a brand like Läkerol for example, running across four markets, coming to the same kind of advertising, look at cost in having four agencies, rather than one, and then that money we can use to support the brand, meaning, money we spend to buy advertising on social media, or outdoor, or even TV, which over a period of let's say, two years, should start to strengthen the brand, meaning the people are – they're more preference to buy Läkerol as a brand, rather than one of its competitors.

Nicklas Fhärm
Okay. So what's your key message here, Henri? Is it that you're not that concerned that you spend that money, you didn't get any organic growth in the quarter, but we fixed that gap to generate some medium term, your support for organic growth rates? Is that what you're saying?

Henri de Sauvage Nolting
Yes, exactly.

Nicklas Fhärm
Okay.

Henri de Sauvage Nolting
Actually, you could say that you have lagging indicators, and spending in media is always – go in long term investments, you can see we do see that when we evaluate our brand strength, we have areas where we are very strong, but also areas where we have to improve. They're always lagging, and then on the sales investments, you can see that basically in the month, in the quarter, when you are investing or not.

Nicklas Fhärm
And I guess the true question here is of course, if we – I understand perfectly, that you have deliberately decided to quit certain campaigns, and volumes, which are obviously less profitable; but if you adjust for that, and you look at their organic growth prospects, why is it that the trend has been fairly sluggish over the past year, and more importantly, what do you think will be the drivers for you to return to growth in 2018?

Henri de Sauvage Nolting
There's really two questions in one. Of course, we have – we have as a company, an organic growth challenge. I mean we also have stating, as one of our objectives, that we want to grow just above market growth, and we have not been able to do that. And if you look at 2017, given the strain we had on our production facilities, the problem has been aggravated. You could say, that we're now seeing quarter four, at least, that we are more back to where we were before the fire, but the challenge on the organic growth is still a challenge, and that's also why this is our first priority.

And when you say, 'Well, how are we going to address that?' Well, it's very simple, it's by having stronger brands, and having more consumer focus, and the second part is customers, yes, because in the end, it's customers who are selling our brand. So that's the whole strategy, is built around these two pillars with many activities, which is probably a little bit too detailed to talk about it today, but it is about strengthening brands, because we focus on consumers; customers like to sell our brand, because they see they're strong, and there's a good off take. And then the fourth pillar is cost, yes, because these things could potentially mean that we have to invest in those brands, so that money has to come from our own cost base, so that's why we're focusing on that. It's not rocket science, but that's overall what we are doing.

Nicklas Fhärm
But long story short, you expect to drive organic growth by increasing costs in 2018 onwards?

Henri de Sauvage Nolting
No, no, that's not what I said. I said we will reduce our indirect cost price – so that's the cost of offices, people, travel, etc. – and we'll use part of that money to invest in our brand. And also, where I would like to have that money, because it's much easier to move money around when you have it in what we call advertising, media, than if it sits in indirect cost.

Nicklas Fhärm
Sure, sure. Got it. Thanks. Final question, could you give us some idea of the part of pick & mix in Poland in terms of 2017, I don't know, sales, and maybe, EBIT or losses before interest and taxes? Just to get a feel for that type of –

Henri de Sauvage Nolting
Full year 2017 was SEK 15 million, and it came as a loss. And we looked at the price points of pick & mix versus the packed business and we could not see that we were able to turn it around in a decent timeframe. So we decided to exit that market.

Nicklas Fhärm
Thank you so much for taking all these questions.

Operator

Thank you. Our next question comes from Mikael Löfdahl of Carnegie. Please go ahead. Your line is open.

Mikael Löfdahl
Yes, hi. First on organic growth, first, just to be clear how you calculate the group's organic growth. I guess Candyking is completely excluded from that growth, so the organic growth within Candyking is not included in the group. That is taken out as structural growth. Is that right?

Henri de Sauvage Nolting
Correct, yeah. So 0% organic growth means the business we had last year in Q4, excluding Italy, of course, versus the business we have now. And if we make the comparator on Candyking, if that will be the next question, Candyking in Q4 grew with 14% versus their Q4 last year when they were not owned by Cloetta.

Mikael Löfdahl
Okay. And next on organic growth, could you say something about packaged versus pick and mix organic growth in this quarter?

Henri de Sauvage Nolting
Well, what we have said is that as from Q1, we will start to state a P&L or at least on the top line for packed versus pick & mix. And that's also the way we're starting now to manage this business and we look at it as if we have two divisions because also the value driver in those two divisions are so different. So as from Q1 report, we will communicate on the top line between packed and pick & mix.

Mikael Löfdahl
But you cannot say something about Q4 outlook?

Henri de Sauvage Nolting
No, we haven't really disclosed that for Q4.

Mikael Löfdahl
Okay. In Norway, could you say something – is it possible to say how much volumes were impacted by some sort of inventory build-up ahead of the sugar tax in Norway?

Henri de Sauvage Nolting
Yeah. So we saw – so here I come back to your previous question. So we saw very little impact on our packed business but we saw an impact on our Candyking business in Norway where customers where buying more in December in anticipation on the sugar tax introduction as from 1st January.

Mikael Löfdahl
And do you think we will see a similar decline in volumes in Norway as we did in Finland?

Henri de Sauvage Nolting
Well, we don't know yet how this will pan out, and that is to be seen in Q1.

Mikael Löfdahl
Okay. Otherwise Norway, you've mentioned before on the pastilles side mainly that you've lost market share and in an overall declining market. Well, you don't mention that in Q4. How has that progressed, and I guess that's part of where you have put some more marketing spend in work as well?

Henri de Sauvage Nolting
Yeah. Well, we're focusing very much on getting the basics right in the pastilles business in Norway, which – and I don't want to disclose too much because my competitors could be listening as well. But it is basically focusing very much on the core business, on the core products which are strong, recognised and very much liked in Norway, and that means both getting better distribution but also getting more promotional and as we go at floor space or this place ballots up on the floor. And we see that that – whether that works. So that's – but that's a guess, something which will take place during the whole of 2018. And then I already mentioned that we're looking at the brand positioning of Läkerol and how we can work together across the four markets to get more cutting through advertising based on joint consumer insight, and that's something which will also be implemented during 2018.

Mikael Löfdahl
Okay, thanks. A final question on the tax. Just – I didn't really catch what you said. How much of the reported tax was a one-off related to Slovakia. Was it 82 million in the quarter?

Danko Maras
Yes.

Mikael Löfdahl
82? Okay.

Danko Maras
82. That was in the breakdown.

Mikael Löfdahl
And going forward, could you say something done given this revaluation than of deferred tax assets? How – in the future, could you give some guidance on tax for 2018 as your business looks right now?

Danko Maras
We continue to say that we work under 24%. And clearly, if you remember perhaps with the Italian business included, it was higher because there was a lot of non-deductible tax expenses from Italy. So, we think we can work on an objective of 24%. And this event that we were booking in Q4 is really a one time event that we will work hard on trying to eliminate.

Mikael Löfdahl
Okay. Okay, thanks.

Operator
Thank you. Our next question comes from Nicklas Skogman of Handelsbanken. Please go ahead. Your line is open

Nicklas Skogman
Yes, hello. Thank you for taking the question. Could you say anything about the contribution from Candyking to EBIT in the quarter, both from the underlying contribution but also in the synergies you read so far?

Danko Maras
It's Danko here. It's still too early to see the synergy realisation. As you know, we've talked about the majority of that coming now as we start into 18/19. So the contribution from Candyking on the profit

level is relatively minor and it doesn't deviate too much from what you are familiar with from the previous periods. And the contribution is yet to come.

Nicklas Skogman
Okay, thank you. And the impact from the fire on EBIT, do you have some estimate from that – for that?

Danko Maras
We are still in assessment of it. We have booked premium from an insurance on – or let's say, the discount of half a million euros, or SEK 5 million in the exceptionals. But then you have these knock-on effects that are difficult to determine now, and it's better that we come back to you when the issue is closed and then we can give you an impact of it in total.

Nicklas Skogman
Okay. But what is smaller in the quarter than you perhaps thought a couple of months back?

Danko Maras
Yes, it's moving in the right direction and that's the point that Henri also is saying is it's great that the team, even though there's a lot of strain in the supply chain network, are actually becoming more and more effective on the remaining parts. So – but some cost, you cannot avoid. The third-party costs are not as low as our own internal costs for obvious reasons because we have our fixed cost to cover, but we are gradually coming out of that. And out of those eight factors we have today, we can get a better utilisation when we move it in, and therefore, also lowering the cost. So let us come back on this point a little bit more when we have clarity on the total when the line is in.

Nicklas Skogman
All right. Thank you very much.

Operator
Thank you. Once again, if there are any further questions, please dial 01 on your telephone keypads now.

As there are no further questions at this time, I'll hand back to our speakers for the closing comments.

Jacob Broberg
Okay. We will then just say thank you very much from Cloetta and Stockholm Solna office. Have a good day. Thank you and goodbye.