

DANONE

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8:15 AM ET**

Susanne Seibel:

Good morning, ladies and gentlemen. My name is Susanne Seibel. I am the European Food and Household and Personal Care Items. And it is my pleasure to again and thankfully again work on the Danone team here today. We've got the CEO, Franck Riboud; Pierre-André Terisse, who's the CFO; and Antoine Guttinger from Investor Relations.

So since last year's conference, a lot has happened for Danone, the acquisition of Unimilk, probably the biggest (inaudible) as well as the continued and accelerated expansion of the company and in particular of its dairy franchise. What has not changed is the pursuit of a growth strategy that is rooted very deeply in Danone's early insight that the world has changed.

We look forward to hearing more about where Danone is now and where Danone is going to go. And with that, I'd like to hand over to Franck. Thank you very much.

Franck Riboud:

Go back to school. When I was children that's not something I really loved but I will try to do my best today. You explained that something change in Danone and basically nothing change. We continue the same strategy that we'll try to summarize for those who don't know the strategy about Danone.

First of all, we drive a unique model. There is a very simple vision which is to bring health through food to the largest number of people. And the main important items of this mission is not health. The main item is to the maximum number of people. If you understand that, you understand all of our emerging country strategy, which is not to focus just on the one who can pay for our product but for the total pyramid of the consumer.

You look at our four businesses. We are as you know in the fresh dairy product, the water, the medical nutrition and baby nutrition, what is very something new for us is we can really to measure of that there are a lot of interaction between the different businesses. Even if it's not obvious to think about interaction between the marketing of a dairy and the marketing of medical nutrition. Trust us, there is a lot, especially the way we understand the consumer. On top of that on the right, you can see our positions, number one, number two, number two, number three. Our vision is to be locally number one with a big gap with number two. That is the only thing we are running after.

We are a growing company. True, I just listened to the presentation from my colleague from Kraft. I saw that on his positioning. I have to say that being in baby, being in

medical, being in dairy, being in water, that you can see it's easier. I'm not saying that the people in Danone aren't doing nothing, but it's easier to deliver growth when you are working in that kind of growing category than when we are not. Even if we have also the tools to develop growth if we are in difficulty, if there is a global difficult economic environment we are never looking at that. We are doing our job, we are focused on our brands and we are not running after excuse or whatever to explain situations.

If you look at the geographical portfolio, it seems totally natural now to be a company in the consumer goods having more than 50%, it's not 49, it's more than 50 in the emerging country. The guy in charge of the company built this split between geographies. That was definitely not the case 10 years or 15 years ago. So it's really something we implement and that's a result of a strategy. It's not something we find like this.

And I didn't split North America and the emerging country because I don't want you to think I'm thinking badly about the country. But for us, if you look at the definition of a market and I will focus on the US market, US is an emerging country for us. You will see that the consumption per capita is around 7 kilo per year per capita, which is exactly what we expect from an emerging country. France is 30 in fresh dairy. So you can imagine the potential we have.

If I look at the slide we are on the fermentation business, so we call MICRUB. MICRUB means Mexico, Indonesia, China, Russia, USA and Brazil. It means in 2006, 30% of our total sales. Now, it's 37%. Obviously it's the big part of our growth. It represents more than 60% of our growth and very important also for company like us. It's now more than 60% of the people working for Danone.

If I look at the figures, H1 you have in blue our target, 6 to 8, which is the target for the year, which is a target for the next following years. So a difficult 6 to 8. As you can see, we achieved the target. We even explode the target because at the end of H1, so it was 8.7 in terms of sales growth. So it's a very good performance. I will not go through all the categories and all the geographies but you can imagine that to deliver this, it means that all geographies and all the categories are growing on top of what we expect. Obviously and just one comment, as you know water was a real growth driver in H1. But because I know that you love to make calculation, don't think that water will continue to grow like this in the future. But I will come back on that. Because water was really bad by huge seasonality in spring and a huge, huge effect because of a sad situation for the population that grew the water business especially in Japan.

And at the same time, you can see the target in term of margin, -30 basis point as a target with -23 in H1. That many reason about that but the main reason are the impact of Unimilk and I will come back on Unimilk and obviously the negative impact of the earthquake in Japan. But at the end of the day, we are in the target and I won't comment on the free cash flow. As you can see, it's still growing in the same time our CapEx was growing 23% versus 2010. So it's a real, real good reason for us that we will achieve also the year target.

How do we deliver that? Always the same story, growing our categories and growing our brands. What about the context? Our job is to grow the category perhaps more than our brands. The first job for us is to grow the category. If you look at what happened in water, if you remember what I said many years ago when the category was declining, we decide to take care of the category. And I have built this. We take care of our brands because you have no brands growing if you are not taking care of the category on which your brand are working.

How do we do that? If you look at the different performance from dairy, without Unimilk or with Unimilk, next year we will never speak without Unimilk but only Russia. That will be done in Russia. But for the time being, we are building the platform so we continue to split and I think it's easier for you to understand as you can see the different performances of the different businesses and obviously the same performance for the different geographies.

What can I say on that is because I think you need to understand what is our vision in term of growth. As you know, the global target for the group is between 6 to 8. It means that if the baby is between 7 and 9, if the medical is around 10, if the water is between 5 and 7, I just need 5 in dairy. You can make the calculation. You will see that and if Dairy is doing well, that will be on top of 8. If everything is difficult because of all the question everybody has about the economy of world going to be 6. So basic question is 6 to 8 is an equation we trust in. And we think that all our businesses in all geographies can help us to achieve it.

So categories -- how do we grow? So I will not speak about the water division. I choose just within the water division a part which is called in our "jargon" as we said in French, aquadrinks, which is 21% of the total water division. And we can see the result of the growth. That's what we think is growing our categories and mostly growing the brand behind these categories. So, it's a good example. We have reached the category, we leverage our distribution systems. For example, in Indonesia where we are 70% market share, we leverage the distribution system of Bonafont in Mexico we sell the product and leverage also the maturity of our product because we are always, even if it is aquadrink we are talking about Volvic fruits or Bonafont hibiscus or Badoit fruit in France. We are leveraging also the brand. And the equity of the brand, which I used to play in the mineral water business. On top, we have specific aquadrinks, Mizone. Perhaps you don't remember, you remember we sold the company in New Zealand but we keep the product for China and Indonesia. So we keep the product and the brand Mizone for us. And Mizone in China is just booming by the time being.

How to grow the category in baby nutrition? You know normally it's a period of six months or eight months or nine months. So we are just developing product for ladies, pregnant ladies because we are supporting the breastfeeding. We are not against. We are supporting, we are recommending breastfeeding, but we also think that the quality of the milk is not exactly the same than mothers' milk. So we are preparing and we are already launching product to help the future mother to improve the quality of the breastfeeding when she will get the baby. Obviously, we address the baby period and we develop as you know specific food, because all the medical community now recommend a specific food until three years. So we are going to leverage this recommendation from the medical community.

Medical nutrition, again I told you we discover a lot of links between our classic marketing and the very specific medical nutrition marketing. Basic marketing, taste, texture. If you are in a difficult situation, it's not the reason why you have to drink or to eat something which is awful in term of taste. If you are in a difficult situation, you must understand from the packaging what do you have to do with the product. So we transfer a lot of competences from our classical marketing people to this category. And if you look at the way we build the product range now, it's fully becoming a consumer product. On top of that, we are testing in some countries a product through the OTX model, which is a product which is recommended by the doctor but not reimbursed. And obviously, our marketing skills are very important to develop this business.

In Fresh dairy, you can see on the chart yellow, what we add in term of per consumption capita growth between 2005 and 2010. And the most important thing is you can see the heterogeneity of the different countries. So we are not saying that the US citizen will eat 30 kilos per year per capita. But coming from 5 of 7, we think we can do something. And I will show -- because for the time being we are not the guy who is bringing that to the US consumer. The Greeks are bringing this. So we have to look at, but I will come back on that.

And I come back now to grow the category in fresh dairy, obviously if I have to summarize and sorry because it's a little bit basic, but we have to go back to the basic. We have to think about how to connect the consumer with digital and iPad and everything and the community. But it's I think crucial for every consumer good company to go back to the very basic marketings, the packaging, the impact on the shelf, the color of the shelf. We are testing what we call a black shelf, which is a shelf black with a special light. We increases the sales by 5%. For us, it's a good news because it means that even in a country where the economy is not doing so well, we can continue to deliver growth. And if you look at France and Spain, which are not the easiest economic contexts of the world, especially Spain, we build a growth. And as you know, we were having trouble the last five years. How do we deliver this? New packaging, what we call a "kiss" cup, which is the one you can I hope see on the picture, the green one. So the color cup, differentiation, competitive advantage. The bottom of the cup and the spoon, because it's very important the consumer can measure with a spoon the texture of the product. So it's exactly what we are doing. And we are going to launch this cup everywhere. Obviously, we have to invest. So we have to make productivity also to justify the fact that we spend money. But we have to do our job. We all have to think about just reduce the cost of the packaging to save money to improve the margin. We have also to invest money to develop a differentiation for the consumer. So we have to focus on the consumer in terms of taste, in term of packaging, in term of quality of the advertising and so on and so on.

We have also to invent new channels. It's exactly what we are testing with what we call the Yoghurteria. I'm not sure you understand but it's a corner shop and you can ask for an Activia frozen yogurt or an Activia yogurt with in front of you and multiple type of fresh fruits. So we develop and we test this. We have also the milkshake machine. We are developing new benefits because we are not forgetting our health positioning. But you know, the limit for the Danone brand in term of health benefit, is health benefit you can measure by yourself. So Densia, it's helping your bones to become stronger. It's part of the brand territory. It's even part of the category.

We have also Danacol against cholesterol. Doing very well because you will make blind test and you will see that it's participating to your diets. Activia will not describe everything about trend. It is intestinal transit. So it's working.

After that, if we have to go much more further in term of health benefit, I think that another brand will take care. And the brand is Nutricia, because we are using Nutricia in the medical nutrition. So we are really going to organize the company with two brands, one really hard health, Nutricia; the other one more starting from pleasure to health with the Danone brand.

And YoCream, I'm sure you know because it's a new channel of distribution for us, especially in the US.

Fresh dairy product in Russia. Very interesting country, the biggest one for Danone today. As I said since we took over the company as you can see it's a very important

country because the purchasing power is growing. So it's an emerging country where people start and the middle class is growing. Is there a risk like in every emerging country except that they have petrol, they have gas. I don't say they have (inaudible) but they have all this. So I think it's a risk we can deal with. In the other side, as you can see, the fresh consumption per capita is growing. So, the thing is it's not going to be as you say, finger in the nose because it's a big country and so we will have up and down. We decide this year, 2011, to be down. And you will see. We decide to cancel a number of SKUs. We decide to build the platform because when you are in Russia like we are, we are not thinking short term. We are not thinking about the market share next week. We are thinking about what we are going to build for the next 15, 50 years. And I will try to explain what we are doing by the time being.

So I will not come back on this. You have Danone. You have Unimilk. Total different body. We are focusing on the long term. We are focusing on traditional. We are more east. We are more west. But they bring us the platform. Honestly, if we have to build a number of factories to develop the Danone brand, we will not do it. Not because we are afraid but because it's too risky. It's too difficult to do it. With Unimilk, we have the platform. So we are going to do our job as a classic one, distribution situation like productivity, become more efficient, find the right people and leverage the good brands.

You can see on this chart what we did this year. What was our job this year. First collaboration and Phase II integration, very strong one. We learned from China. So we decide to fire all the people and to put Danone people and loyal people at the end of the company. That destabilize a little bit at the bottom the company but that was for us the main things to do to be sure we will succeed.

So we want to have build a one company by 2012. So we give us, we give us one year to clean, to stretch the brand, to cancel SKUs, just to be sure we will be efficient.

So if you look at the product mix and you can see that the difference here. That's a translation of what I'm just explaining. Basically, we focus on gross margin because with that gross margin you can protect your brand. You can develop the business. So we need to correct as you can see the gross margin was -0.65. After that, that was -2 and going to be around 4%. That was the priority we have and I hope that we continue for the rest of the year through improvement and efficiency and through obviously synergies between our Danone Russia company and Unimilk. And we can see the result on the brand we are focusing on and the growth we can deliver.

But in the same time we can see on this job how the traditional and local brands are doing now. How modern brands are slowing down also. As you can see the result and for us again, you have to understand that it's not a question of market share. It's a question on which brands are we going to build our future. If we don't think in the future of our brand, we stop the brand and obviously we lose all the volume behind the brand. Obviously, we have to re-dimension the production and all the supply chain. But it's clearly the job we are doing by the time being.

I'm jumping on this one, explaining the potential of US. You can see where US is in term of consumption per capita. So see a lot of room on the left side of the chart. The result by the time being and it's funny because I was looking to the presentation of Irene and just before, but you can see that whatever the growth is in the US, if you look at from 2005 to 2010, the CAGR from the total Dannon including Stonyfield, our organic product, the CAGR growth was +10. So it seems very linear. But if you remember well what period we were minus something, period we were at double digit. That's account of the dairy market in the US. It's a very small market, very small. So sometimes we are

lucky, you're on the right way or not, but you have the right way and you fly. Sometimes somebody else, if you remember, low carb. We were not in the low carb. And we were down, somebody else was growing up. We were down. Somebody else grew it. We were on the light product. We grow very fast. We launch Activia. We grew very fast. We launch all the kids product, we grow very fast. This year, we grew less. Why? Because somebody launch Greek. And we have Greek. And Yoplait has a Greek, but the Greek of the guys launching the Greek obviously and performing better than us. And the Greek take, as you will see a big part of the market.

The sad story is nothing on top. So not developing the category and I come back to the category. Our job is to develop the category. And by the time being this week or last week, the market is flat. Not because of crisis. Not because of consumption declining. No, no. Because cannibalization from one category and the other. But the base business is growing down. Is it a sad story or a good story? It's a good story because it means that the consumption is moving, is changing. So new tastes are arriving, which is for a company like us, very good news. Because as I said, we have the portfolio. So you can see the different evolution in the market share. Why Dannon is resisting. Because of Activia, because of the kid product, not because of the basic fruit in the bottom. So and the one, don't have the right answer. Globally it's declining much more faster.

If you look at the US fresh dairy market, by the time being, you can see the blue line is the Greek. Taking something like 25% of the category. That was a huge cannibalization. Obviously, you know Dannon, we will react, which was tough. Switching, we have our friends guys from Stonyfield here, who's delivered with perhaps specific vision that he'll launch Greek called Oikos. And we decide to have an Oikos organic. And we can sell our Greek and we transfer our Greek Dannon under the Oikos equity brand. And we have an Oikos 3% fat, which is a revolution in the US. But you can taste it. It's pretty good because pleasure is part of this diet. You need one. But you need also something in top. So we launch a Greek 3 and a Greek 0% for the different consumer.

And what I propose to you, I will show obviously another chart to present the product, a transfer from Dannon to Oikos but it's a marketing. If we can see the video one, the advertising campaign we just launched but it's too early to tell you about the results. [VIDEO] As I said, basic marketing. But it works. The other thing, next time I would like they did it before, not after. Anyway, it's an internal discussion. Obviously, we will continue to invest a lot on Activia and the different product. We leverage the brand.

To conclude, I would like to speak a little bit about productivities and cash efficiency. That being put the evolution of the input cost. As you can see, we have different peak in -- I'm doing this job for now more than 15 years. So, I'm not afraid by the evolution of the commodity curves or whatever. But I think we already illustrated that we know how to deal with that kind of situation and even the last two years. As you can see since there is a little slow down, we will benefit of it obviously. But if you ask me, my vision about that kind of curve. Do I think that the price of the raw material will go down the next 20 years? No, no. To make the inverse assumption is you have to pretty stupid to think this. It means that I have to drive the company thinking about how to deal with this. And that the reason why productivity, new recipe, milk cracking and all these things we presented for those we were in Evian are very crucial for us. Because with this, we will continue to support our brand and be affordable for the consumer. Otherwise, one day Danone will be Gucci or Vuitton or whatever. So, the answer which is pricing power, I can't transfer to the consumer. Obviously, we have to do this. But in the same time, we have to control our costs. We have to control our productivity and it's exactly what we are doing.

Talking about productivity, as you can see every year, making no noise. Every year we have an impact of something around 500 million Euros. Ongoing every year. And as you can see, we deliver 246 in first period for the year and we will achieve the 500 at the end of the year. And we are still having a lot of creativity to reinvent our model, to reinvent the way we organize the company. Not destroying the control of the company, but taking care of the way we spend the money. Again, very busy but very efficient.

A little bit more difficult, which is the example of Danette. You don't know the product but it's a dessert. It's an indulgent product all across the world. We do it with milk except that we don't need the milk because we don't need the protein. It's not a fermented product. So we decide to leverage what you have on the left starting from the skim milk. How do you crack the milk? Means that you are separate the milk and you take the part you need and you produce the same product. So the recipe is really cheaper and with the money, you reinvest behind the brand. And doing this, you can see also the other impact on the quality of the product and the nutrition and also on our future impact, which is something we are also focusing on. So we can leverage many things by doing this including improving the margin of the product.

Productivity, as you can see, whatever the context of the raw material, at the end of the day, we control and we have quite the same margin and including everything, every difficulties, just because of just what I just explained.

The free cash flow. As you know our target is 2 billion in 2012. We are on track. We will achieve the \$2 billion. We are even in advance in our program. And the main reason of that is also part of the DNA of the company. Because if I look at the situation of Numico before the Danone period of time, just by transferring what the people of the fresh dairy are doing, the technical thing to deliver free cash, which is easier in fresh dairy because you have a negative working capital. You have a shelf life. So it's easier for us. Within the baby food business, we also improved dramatically the situation of generating free cash flow in the baby food. It means we will continue to transfer all these best practices within the different company businesses.

The other thing which is the most important for you. You can put that in the computer. I will help you perhaps to make the calculation. Sales growth H1, 8.7, objective full year, as you know, 6 to 8. You make the calculation and we can imagine what we expect for the rest of the year. I made the calculation, Q3 between 5 and 6, no more. Mainly due to the water which is another situation than in Q2. So Q3 between 5 and 6 also because as you can see we are impacted by Russia in dairy. We are impacting by dairy US where we build a new platform. It is not exactly the same in Russia and Europe, but we have to react in US and we have to continue to really focus and perhaps destroy volume in Russia to build the future. So that impact us. So that reason why water, these two main engines, we are flat, 5 to 6. Now having 5 to 6 for Q3. And again I think you can make the calculation for Q4. But I'm really convinced we can deliver the 6 to 8. And as you said in English, well into 6 to 8. Not coming from me.

The margin, as you can see, 20 basis points as a full year objective, obviously we confirm very strongly the target. But being -23 at the end, if you make the calculation, it means we will be around 60 on the second part of the year. And perhaps you didn't see, but Unimilk is now around zero. And we're really badly impacted beginning of the year. We have this raw material impact and so at the end of the day we see no reason not to confirm the full year target. But especially in top line, it's important we understand how are we going to build this 6 to 8.

Free cash flow, as I told you, we are on track for our objective of \$2 billion. And whatever you think about the economic situation in the world, we are still very confident in the Danone model. We focus on our jobs. We stop to read newspaper and everything is doing well. Thank you.

And if you have question, I don't know if we have time. We have time? I was a little long.

Audience Member: Just one question if I may. Actimel actually, you had mentioned that you (inaudible) in the Q2 conference call that you had launched the reset in some of the countries. So would love to know how that went? Because we had seen the impact that it has had on Activia a few years back. So if you can run us through Actimel reset results, which countries, how do you feel about it? Thank you.

Franck Riboud: I think to answer to your question I don't have to speak about the reset. You know everything about the reset. Reset give us an advantage, especially now when the price of raw material is still going up. And it's now but that was true at the first part of the year. So the reset for all our product we apply the reset give us the flexibility. We recreate the room to keep the right gap between private label and our brand, which is 120 as an index.

The situation of Actimel is not due to reset or price or whatever. It's more linked to what I explain about health benefit. What can the Danone brand can carry. Honestly today, to explain to the consumer immunity is more difficult. Nothing to say (inaudible) whatever, but it's, you know, you have to explain to people in a good shape that having Actimel they will develop their immunity. When you have to explain to somebody, you have cholesterol. You take Danacol, they can measure. You have intestinal transit issue. You can measure by yourself and so on and so on. So, for me Actimel, which is not doing so well in major country but better in some other country. It's like in automobile business. We have the platform. We need to do something on top of what we did the last ten years. And it's exactly what we are going to launch in some countries. But I can't disclose. It's internal secret. But we will take care.

But managing is now more and that is the reason I explain to you that since now one year we move on the emerging side, especially if the world is entering in a crisis situation which is -- I don't know -- I don't want to comment but indulgent product will come back very important. If you can see what we do in Danette and soon the kids product, so that, the future for the dairy. But that will need some, let's say, reformulation. But as I told you, and I said that since many years now, since the Nutricia deal, the Numico deal, I think the smallest business of Danone is perhaps the most important for the future, medical nutrition. It's a highway for us in term of growth and margin.

Audience Member: As a company who operates in 50% in emerging markets, you have courage going into Russia, which in the books is the most difficult country. What's happen for China, Brazil and India?

Franck Riboud: Our plan for China?

Audience Member: China, Brazil and India?

Franck Riboud: What we call the MICRUB. India, we just, as you know, reenter. And we are very strong in India with a biscuit product we sold. So we went in India -- we are still there with a joint-venture with Yakult, just to understand the distribution system. Going at the Japanese speed, but we decide to re-launch our dairy product. But you have to understand that for the next years, it's a next one year, two years, I really want to focus

the company on the thing we know, which is really working, where we will get the very fast return. Not because I'm afraid just because I think it's more serious to be like this. And we have a lot of things working very well. Brazil, Brazil is one of our priority. First of all, Brazil was one of the only country resisting and I don't want to say, during the crisis, because I consider we are still in the crisis. So Brazil is doing well as a country. Our product category are doing well and we launch the same concept than Bonafont, exactly the same. And we leverage the distribution system of the fresh dairy division to deliver the water business. So as you can see, we just do exactly what I explain. Lowest cost and be efficient. The water could be a priority in Brazil and obviously to continue to develop the fresh dairy and as I said, medical nutrition. So we are growing and growing in medical nutrition in Brazil by the time being.

Russia, clearly it's a platform for us. China, we are booming with the baby food. Just to give you an example, we try to launch an affordable product in China in baby food. We failed. In Indonesia, we exploded. The difference is because in China the price is part of the quality of the product. So we are going to launch a super premium product in China in baby food and we already start to launch it or that will be within a few weeks.

Water, in China, we have Mizone which is exploding. How could we accelerate that? This is exactly what I explained. We invest where the return will be very quick because we know that we have a success. And Mizone is a success in China. But China is so big, how do we accelerate China? We don't have to grow 10% or 9%. China, we have to grow 25. In the same time, we continue to develop the fresh dairy, not making money. So perhaps we have to refocus that just on the Shanghai area all for the same reason. Focus where we will get the return as quick and very secure. And forget no countries now. Okay.

Okay, but we have a breakout session.

Audience Member: There's a breakout session so we can answer more questions during the breakout. Thank you.