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## PRESENTATION

**Operator**

Good day and thank you for standing by. Welcome to the Danone Third Quarter 2021 Sales Conference Call. (Operator Instructions) Please be advised that today's conference is being recorded. (Operator Instructions)

I would now like to hand the conference over to your speaker today, Mathilde Rodie, Head of Investor Relations. Please go ahead.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you. Good morning, everyone. Mathilde Rodie speaking, Head of Investor Relations at Danone. Thank you for being with us this morning for Danone's Q3 sales. I'm here with our CEO, Antoine de Saint-Affrique, who will make a quick introduction; and our CFO, Juergen Esser, who will go through some prepared remarks before taking your questions in a second step.

Before we start, I draw your attention to the disclaimer on Page 2 related to forward-looking statements and the definition of financial indicators that we will refer to during the presentation.

And with that, let me hand it over to Antoine.

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**Antoine de Saint-Affrique** - *Danone S.A. - CEO*

Thank you, Mathilde, and good morning to everyone. It's good to be with you at the start of our third quarter results call. It is not customary for the CEO to join the quarter three sales call, and I have no intention whatsoever to break the tradition. But I thought it was important, as I have now been around for about 5 weeks, to spend a few minutes with you this morning to introduce myself, to give you a sense of what I have been doing so far and to share what my immediate priorities are. After this, I will hit the road again, actually, I'm back from Moscow this morning, and leave you in Juergen's more than capable hands to go through the quarter three prepared remarks and Q&A.

As I said to my Danone colleagues on my first day, I'm proud to be a Danoner again and to be given the opportunity to lead a company with unique DNA, being, at the same time, very entrepreneurial and sustainable. Danone is a company with an amazing stable of categories and brands and one which has consistently been showing an incredible ability to pioneer and to reinvent itself.

While the last month has allowed me to learn a lot and build some views on our business, it is definitely way too early for me to formulate a structured and credible path forward. Right now, I am focusing on 5 areas which will serve us as a base as we relook at our strategy to help bring Danone to the next stage and consistently create value for all.

My first priority, and I said it, is to deep dive into the business, to meet Danoners from all around the world, I told you I was yesterday in Moscow, to understand the current state of affairs, to look together with the teams at how we can accelerate what works, but also start doing things differently and better when needed. And as I do that, form a fact-based view which will nourish our thinking on the way forward.

My second area of focus is our sustainability. I said it many times since I joined but also in my professional past. I am convinced that sustainability can be and should also be a source of long-term competitiveness. As an "Entreprise à mission", which we are, with a strong purpose and having been a pioneer on all sustainability fronts - socially, environmentally - Danone should be in a unique position to create value in a sustainable manner.

My third area of focus is people and culture. We have historically been a talent magnet and a talent grower, a company where passion, purpose and performance culture go together. There, I think our leadership has eroded over time. This will clearly be front and center on the agenda of our new Chief HR Officer, but also a place where I will certainly spend some of my time.

Fourth, and as you would expect with my background, I have quite some passion for categories, for brands and for innovation. Keeping differentiating ourselves through brands and product quality, leading innovation, developing new business models are at the heart of who we are and how we create value.

And fifth but not least, the best strategy has no impact if it doesn't shine wherever the consumers are meeting our products. Flawless execution of our business across channels is certainly top of my agenda.

So, 5 areas of focus in the coming weeks as I get acquainted with the business and as we work on our strategy.

I must say I have been quite encouraged with what I've seen across the business, certainly, by the openness of the discussions I had and by the teams I've met not shying away from challenges. But as I said, I'm only on week 5, and there is still quite a bit of ground for me to cover.

So you'll hear more from me in a few months when we release our full year results and at the occasion of the capital market event, which, as you've seen, we will organize on the 8th of March next year. So I'm very much looking forward to meet as many of you as possible then.

But for now, I'm leaving you in the very capable hands of Juergen for the quarter three remarks and Q&A, and I'm hitting the road again. So goodbye, a very good day to everyone, and speak to you in February.

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Thank you, Antoine. And also good morning from my side to all of you. I hope you are all safe and well.

Let's start our review on Slide #5 with a few key highlights of our quarterly performance. Global message for this third quarter is, certainly, it has been another quarter with focus on execution and delivery for us. First of all, and importantly, this is translating into another quarter of growth with, again, a broad-based contribution from all categories. We will delve into the details of the performance later, but we are pleased to deliver +3.8% of net sales like-for-like growth at company level, with a very solid contribution from EDP growing +4.1%, Specialized Nutrition delivering +2.9% and the Waters division growing +4.6% versus last year.

Secondly, we have crossed another major milestone in the implementation of our Local First project. Since beginning of this month, we have started to implement Local First in Europe with countries like the U.K., Spain or Germany already shifted to this new organizational model since October 1st. We are going to progressively implement Local First across all Europe as we travel through the remainder of this year and are, hence, on track to deliver the saving targets with the timelines that we announced.

And then third, we have also seen this quarter our leadership on ESG topics reiterated. For instance, in this July, we were awarded by MSCI for the third year in a row with a AAA score, with Danone being part of the only 6% of companies reaching this leading score worldwide. We were also rated recently by Vigeo Eiris as one of the leaders in ESG. And last but not least, we were among the top 3 out of a total of 350 companies in the food and agriculture space of the World Benchmarking Alliance, and we were hence the first one on governmental topics.

Now I could, of course, not go over the highlights of the last 3 months without talking about the challenging external environment that we are navigating through on next page, I think Page #6. You remember, we mentioned back in July that we experienced COGS inflation of around 7% in the first semester of 2021 and that we expected this inflation to sequentially increase by another 100 to 200 bps in the second half of the year. What became very, very clear over the last months is that the increase will be at the upper side of that corridor, leading to a COGS inflation of around 9% in the second half of this year.

This sequential acceleration has been driven by a number of elements. First of all, we observed a further increasing inflation in raw materials, with some of our hedges that we benefited from year-to-date phasing out at the back end of this H2. In addition to that, logistics and transportation inflation continued to accelerate over the summer, the reflection of trucking capacity shortage across some key geographies for us, like in the U.S. or in the U.K. And last but not least, we now observe sharply increasing energy inflation, but more importantly, challenges to our supply chains. This has, unfortunately, in some geographies, impacted our ability to produce and serve customer demand, something I will come back to in a few minutes.

In that very challenging context, we are clearly putting a greater focus on the delivery of additional productivity and pricing in the second half. On productivity, by accelerating the cross-category synergy programs, which we already launched end of last year; and on pricing, by sequentially moving from selective pricing into broad-based pricing or revenue growth initiatives in all of our geographies.

Let's now take a deeper look at our net sales growth in Q3, turning to next slide, Slide #7. As said before, sales were up +3.8% on a like-for-like basis in the third quarter. The -0.8% decline in volume was more than offset by an increase of +4.6% in value, thanks to significant pricing, but most importantly, by a strong contribution from mix, with improved country mix linked to a better performance in China and with product mix benefiting particularly from the recovery of small-format bottles in Waters.

Outside of the like-for-like, "currency and others" had a positive impact of +1.7%. Currency, within this box, had this quarter a positive impact of +0.8%, reflecting the appreciation of the Chinese renminbi, the Mexican peso and the British pound against the euro, while the U.S. dollar and other emerging currencies remained broadly stable versus last year.

Next to the currency, you see scope had a 0.3% positive effect resulting from the combined effects of the integration of Harmless Harvest and Follow Your Heart and the disposal of our Vega brand, all in the U.S.

All in all, reported growth stood at +5.8% for the quarter, bringing our quarterly net sales to roughly EUR 6.2 billion, up from EUR 5.8 billion in Q3 last year.

Let's go a bit deeper into the performance by category, and I will start on the next page with the Essential Dairy and Plant-based division. This division continued its strong momentum, posting +4.1% growth on a like-for-like basis this quarter. When analyzing the global performance by segment, it's great to report that the Dairy part of our EDP portfolio delivered another quarter of very solid growth, while on the other side, our Plant-based portfolio delivered strong mid-single-digit growth, definitely not at the level of our expectations. This Plant-based performance was indeed strongly penalized by the before mentioned supply and logistic issues, and here especially in U.S.; I will come back to that in a second.

When looking at the overall EDP performance through the geo lens, Europe and Noram both delivered another solid performance, delivering a combined growth of 4.3% over the quarter. In Europe, our Essential Dairy portfolio delivered solid growth this quarter with another strong contribution from our Probiotics and Protein platforms. Our Probiotic portfolio continued to benefit from the health and immunity growth trend, led by Actimel that registered another quarter of double-digit growth while gaining market shares, while Activia continued also its strong momentum in the U.K. as well as in Germany. The Protein segment maintained also its growth momentum, especially the High Protein segment, thanks to the continued geo expansion of our YoPro brand, but also thanks to the replication of this high protein concept into other existing dairy brands.

Moving to Plant-based in Europe. Alpro delivered another quarter of double-digit growth, notably led by a strong performance of the recently relaunched Oat range that registered another quarter of strong growth, and here, I think worth mentioning, again, grew its market share in this very dynamic segment. It's probably also worth noting that our recently launched plant-based blend under the name of This Is Not Milk shows promising early signs in Germany, having been able to attract new consumers to the category.

Switching to North America. Our Essential Dairy portfolio performed particularly well this quarter, posting strong growth, notably led by the Yogurt but also by the Coffee Creations segments. In Yogurt, Oikos and Two Good brands delivered both an excellent performance, growing well into double-digit territory and gaining share within the Greek segment. In the Probiotics and Wellness segments, Activia delivered mid- to high single-digit growth, leveraging its unique and winning proposition on key consumer trends. In Coffee Creations, International Delight and Stok delivered high single-digit growth with resilient share performance also in this quarter.

Moving to Plant-based Noram. And as I mentioned a bit earlier, the performance was penalized this quarter by supply and logistic issues that impacted our ability to produce and serve customer demand on a number of product groups. It did also limit our ability to execute some of our restaging initiatives to the extent we initially planned. Those combined effects led to subdued growth over the quarter at low single-digit level. Last few weeks have shown sequential improvement on both service level and market share so that we should expect to progressively recover over the next weeks and months.

To conclude our EDP review, our platforms in the Rest of the World delivered solid growth. Latin America and Africa continued their sequential recovery, while dynamics continue to be soft in CIS amid a challenging macroeconomic and sanitary environment.

Looking at the remainder of the year, we expect EDP to maintain its growth momentum driven by Europe and Noram, while other markets should progressively recover.

I suggest we now turn to Slide #9 and look at our Specialized Nutrition business. Specialized Nutrition continued its recovery this quarter and posted +2.9% growth on a like-for-like basis. When going into the segments, the Adult Nutrition portfolio delivered another quarter of growth, around mid-single digits. Growth was led by China and other emerging platforms in Southeast Asia notably, growing well double digits, both the oral and tube feeding platforms continue to grow, fueled by winning propositions and a strong go-to-market.

Moving to Infant Nutrition. Our Infant Nutrition portfolio delivered moderate growth this quarter. And as expected, growth was led by China, which grew double digits, with a broad-based contribution from all channels. Aptamil reiterated its leadership position in the market, staying very resilient with its leading market share position.

Looking deeper at the dynamics through the lens of our 3 key channels. First, the domestic label business sustained its strong performance and delivered another quarter of mid- to high single-digit growth. Second, international labels sold through cross-border e-commerce platforms delivered another quarter of strong growth at steep double-digit levels. And third and finally, indirect channels, which mostly include the Daigous and the Friends&Family, were back to growth this quarter after having declined by approximately minus 60% on the previous last year, as you may remember.

Outside of China, Europe delivered flat net sales in a declining category that is still penalized by decreasing birth rates and working from home, while our platforms in the Rest of the World delivered a soft quarter, notably due to some phasing effects with Q4.

In a context where the IMF category suffers from birth rate decline and other COVID implications, the premiumization and specialization trends are still very dynamic, and our leadership remains strong. Across geos, we delivered a strong performance in the pediatric specialties and value-added propositions like on organic, A2, goat or the recently launched tablet format, to name a few.

Looking at Q4, we expect Specialized Nutrition to sequentially accelerate driven by another quarter of growth in China, while platforms in the Rest of the World should sequentially recover. Europe, however, is expected to remain soft on the back of a slowing category.

Let's now conclude our category review with the Waters division on next slide, Slide 10. In Europe and Latin America, category dynamics were strong in this quarter. This benefited both our plain water and aquadrinks business, although a relatively cold and rainy summer hampered a bit the out-of-home consumption.

In Indonesia and China, categories became, unfortunately, again, under pressure over the summer, penalized by restrictions to mobility during the holiday period. In that volatile context, we are focusing the teams on competitive growth and are happy to report that we delivered an excellent performance from a market share perspective across many of our geographies.

What does it mean in numbers? Waters net sales increased by +4.6% on a like-for-like basis in Q3. This represents a further step in getting back to 2019 levels, mostly driven by Europe, while other geographies still remained more or less disrupted over the quarter.

Zooming a little bit more into the geos. To be specific, Europe delivered strong mid-single-digit growth despite the unfavorable weather conditions I mentioned during the summer. This performance was led by recovering mobility, but also by broad-based market share gains. Notably, we are glad to see another strong competitive performance from evian and Volvic across all Europe, Zywiec Zdrój in Poland and Font Vella in Spain.

Turning to Mizone. Sales declined low single digits in Q3 after 3 quarters of positive growth. Sell-in was momentarily penalized by the resurgence of localized travel restrictions, as I mentioned earlier. This had a significant impact on summer holidays and out-of-home consumption, which are indeed important seasonal drivers to Mizone. Having said that, execution remains solid. Mizone continued to recruit younger consumers and saw further improvement in distribution and velocity, while market shares resisted well.

In the Rest of the World, Latin America delivered double-digit growth in Q3, thanks to an improvement of mobility during the summer despite infection rates remaining pretty high. Finally, the performance in Indonesia was penalized by strong mobility constraints linked to COVID, including the reimplementation of some local lockdowns over the summer, which led to flattish growth over this quarter.

Looking at the remainder of this year, we expect Waters to deliver another quarter of growth on the back of solid market shares and a dynamic category. While it's difficult to predict what will be the market conditions in Latin America and Indonesia, we believe that Europe, but also Mizone in China, are poised for growth.

Let's close these prepared remarks on Page 11 with the outlook. As I explained in my introduction, we are navigating through a very challenging and volatile cost and supply environment, with COGS inflation reaching for us around 9% in H2. This makes us increase our focus on productivity, explore additional pricing and revenue growth opportunities across all geographies, but also manage our business with the highest level of agility and flexibility to limit supply shortages and to permanently adapt our brand and commercial support to the actual service situation.

Having said that, we are reiterating our guidance, to deliver profitable growth in H2 driven by the overall positive momentum of our categories, a positive geographical mix and a more balanced category mix. We also continue to expect recurring operating margin broadly in line with that of last year.

Last but not least and turning to the next and last page. Let me please confirm what Antoine already mentioned earlier on this call. We'll be holding a capital market event early March next year, to be precise, on the 8th of March, which will be just a few working days after the presentation of our full year results we just scheduled for the 23rd of February. We will, of course, share further practical details as soon as available and are looking forward to those milestones, hoping that we can meet as many of you as possible at this occasion.

That concludes my prepared remarks, and I now hand it over to Mathilde, I believe, to launch the Q&A session.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, Juergen. So now it's time for the Q&A with Juergen. (Operator Instructions)

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## QUESTIONS AND ANSWERS

**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

And we will start with Guillaume Delmas from UBS.

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**Guillaume Delmas** - *UBS Investment Bank, Research Division - Analyst*

So only one question. So I guess I'll go for Specialized Nutrition and more specifically on your performance in Europe and North America. On a 2-year stack basis, there seems to have been a sequential deterioration in Q3, particularly if I compare that to Q2, but even the first quarter of this year. You've been mentioning in the presentation a declining market. So my question is, is this just a lingering impact from COVID, and as a result, maybe there is a scope for some rapid improvement? Or is it, for the time being, the kind of market conditions you will be facing for potentially not just Q4 but also the whole of 2022?

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Well, let me try to give you some insights into that. Obviously, what we are seeing in Europe is what we are seeing around the world, which is the decline in birth rates and hence a lower demand for the IMF sector. What is probably a little bit more particular for Europe is the fact that we have a quite significant first diet business, which means that we are also exposed to the fact that the moms are staying longer at home and cooking themselves the meals for their babies and young children rather than buying our products in retail, which means also that the recovery dynamics in Europe and in North America, knowing that North America in absolute size in terms of business is not as important as our European business, may have a different dynamic than the return to growth which we are seeing in China or the Rest of the World.

So in other words, I think that the team is doing a pretty good job managing the mix in Europe because you said that the category is declining, we have been posting flat growth. I think that the category will stay a little bit under pressure for the next couple of quarters for as long as home consumption stays at the level where it is, but there will be a moment we will mechanically rebound back to growth. When is that going to happen in 2022, that's probably too early to say because for the moment, I think home consumption stays at a quite stable level.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Next question from Bruno Monteyne from Bernstein.

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**Bruno Monteyne** - *Sanford C. Bernstein & Co., LLC., Research Division - Senior Analyst*

My question is regarding your last slide about sort of reiterating margin guidance, and you call it broadly flat. I just want to make sure I understand broadly flat is a stretch up to minus 40, 50, 30 basis points potentially. And linked to that, you keep talking about sort of ever higher inflation expectations, but the margin guidance sort of doesn't really change. What is it that allows you to keep this stable, that margin guide, despite commodities getting worse? Is that just a 2021 phenomenon and actually it could get worse in 2022? Or is there anything you can really highlight why you can keep the line so straight on your guidance despite the worst picture?

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Look, when we were together 3 months ago, what I told you is that we see inflation 100 to 200 points higher in the second part of the year. And we are in this corridor, we are in the upper side of the corridor, but we are in this corridor. So in that sense, there is no surprise to us when it comes to inflation.

As we had already this corridor of inflation for the S2, we were preparing to increase our productivity. What I shared with you already in July is that productivities are coming quicker than what we initially were planning for at the beginning of the year, partially thanks to the fact that our SKU rationalization program is ahead of plans, partially linked to the fact that the duplication of our supplier platforms in many of our countries gives us incremental opportunities for synergies. So basically, we are banking part of the EUR 300 extra million, which we wanted from cost of goods sold productivity earlier and on to our P&L.

This is definitely helping us to sustain our guidance, unchanged vis-à-vis what we were discussing 3 months back. What I think is also important, we know is the fact that we are exactly in the dynamic we were expecting. And when I say exactly in the dynamic, I mean in topline dynamic. So we are benefiting in the H2 definitely from a more balanced category mix with SN back to growth, and with SN, which we expect will post a higher margin in the H2 than in the H1. We have been discussing that already in July, and this is what we continue to see for the remainder of the year.

China country mix is important. We are pretty happy with what we are seeing in China in SN. Very good growth and growth in all the channels, which, when you take the combined effect of all of those, makes me continue to be confident in our ability to deliver the margin, as we said, broadly in line with that of last year. So a number of moving parts, but I would say nothing which is coming as a surprise.

Probably last point on that one is that I've been pretty vocal on the fact that we are going for selective pricing. And this is what we did in H1, and you saw that coming through. And now with the increased inflationary pressure, we are now, I would say, gradually going to broad-based pricing. Many of the geographies are starting to implement or prepare. We see some more pricing initiatives in emerging markets, Mexico, Brazil, Russia and so on. We are doing incremental revenue growth initiatives in Europe and in North America, particularly, which is also an important component, one, to deliver what we are committed to this year; but also and importantly, to prepare 2022 as we do not expect inflation to be any less than what we are seeing in 2021.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, Bruno. The next question from Jon Cox, Kepler Cheuvreux.

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**Jon Cox** - *Kepler Cheuvreux, Research Division - Head of Swiss Equities and Head of European Consumer Equities*

It looks like a pretty decent print for Q3. I was just wondering if you can come back to the Local First and where are you exactly. You alluded that some of those savings may already be coming through on the COGS side, and that helps you on the inflation side. You mentioned EUR 300 million. Just wondering where you are on that, and also the bulk of it, the EUR 700 million on the overheads, where we are on that equation.

And as part of that, how should we view this? Because I know we have a legacy margin guidance, say, for around 15% next year, and a lot of that was really on the back of Local First. Should we just assume that it's all going to be absorbed anyway by the inflation, so we shouldn't be expecting anywhere near that figure next year?

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Look, on Local First, you remember, we implemented this organizational model in North America already early Q2. We went through the whole social consultation process as we planned in Europe, so that one was successfully closed. And hence, we are starting to implement in Europe as we speak. A number of countries went live on the 1st of October, and the remainder is to come as we travel through this quarter, which just means we are exactly on track to deliver what we said in terms of timing, and we are exactly traveling according to the timelines we had set end of last year, which is true in terms of savings, the overall amount of EUR 700 million; which is true about the phasing of the savings, with the majority of the savings kicking in next year; which is also true for the cost of the program of EUR 1.4 billion.

You are absolutely right, Jon, that we do not want to, I would say, change the course: we want to use part of those savings to reinvest into our business and to reinvest into our brands. It means that we are animating the teams in a way that there's inflation out there and the inflation is high. And this we need to counter by smart pricing, strong mix, and I think Q3 has been a good testimony for this, and an elevated level of productivity. That is the agenda for year 2021. This will be the agenda for year 2022 so that we can really make sure that the Local First savings are here to help the margin expansion, but also very importantly, to reinvest into our strategic battles and into our brands and businesses around the world.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, Jon. Our next question from James Edwardes Jones from RBC.

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**James Edwardes Jones** - *RBC Capital Markets, Research Division - MD & Analyst*

Juergen, Antoine's priorities don't include anything on financial performance. As CFO, what are your thoughts on that? And if I could just sneak in a second: Rest of the World Specialized Nutrition was impacted by phasing effects. Can you just say what they were and how big they were?

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Sure, James. I think you don't need to worry on the first part. My first interactions and discussions with Antoine were a lot on financial impacts. But of course, financial performance is a result of business performance. So I think that what is now very important is 2 elements. First, that we continue to deliver quarter-by-quarter on the dynamics we have started to produce since Q2 of this year, and at the same moment, Antoine was alluding to that, articulating a new strategy for our company and making sure that in terms of execution, every opportunity we identify, we are improving as we speak. So don't worry on financial performance, please.

The second point was on volumes in Specialized Nutrition. On this part - and I think that overall - when you look at it, we are pretty happy with the overall Specialized Nutrition volumes performance, which may be a bit counterintuitive. But let me give you the moving parts in that.

China, very happy with the performance across all the channels. We are growing in volumes. Aptamil is doing well in market share, domestic labels growing strong, controlled international e-commerce outperforming. And this is, I would say, a pretty good news. And with the uncontrolled international channels in growth this quarter. But just to state the obvious, we know that this is a structurally declining channel. And so this channel will represent at the back end of this year only 20% of our net sales after being 30% of net sales last year, and I remind you, being 70% of our net sales 6 years ago. So we are getting more and more controlled net sales in China, which I interpret as pretty good news for the short-term and long-term future.

Europe we have been discussing. Europe, flat in net sales, decreasing in volumes. Team is doing a good job on mix. And then Rest of the World, and here, we have a very particular phasing impact this quarter. You may remember that we had a good start of the year, very solid first half. This Q3 indeed is reported with pretty negative volumes. However, we expect a normalization to happen as early as Q4 this year. So here, it's really mostly about managing healthy inventory levels from one quarter to the next, while overall, we see the growth trends in Rest of the World broadly unchanged.

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**James Edwardes Jones** - *RBC Capital Markets, Research Division - MD & Analyst*

So is that phasing effect you're referring to really just a function of fluctuating inventory levels?

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

So it's really mostly linked to that, James. Absolutely. So you will see that Q4 performance will already look very different.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, James. Next question from Warren Ackerman from Barclays.

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**Warren Ackerman** - *Barclays Bank PLC, Research Division - Head of European Consumer Equity Research*

It's Warren here at Barclays. My question is on EDP growth. It was quite a big beat versus consensus on organic despite Plant-based growth slowing down. So my question is, what is going on there? Is the category elevated post COVID? Or is market shares improving? Maybe, Juergen, you can share some latest market share data. I'm particularly interested in what's happening to kind of Activia, your biggest brand, in terms of growth, if you can give us a growth number for Activia for the 9 months over the Q3 and what's happening to share.

And then just continuing on EDP, the one area that is continuing to be weak is Russia. I know Antoine has just come back, but any kind of thoughts on what is going on in CIS given it's such a big weighting to EDP? That would be super helpful.

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Yes, Dairy, indeed, pretty decent performance this quarter, in a quarter where we saw higher level of out-of-home consumption, which I think we read as reassuring element because we had some comments over the last quarters doubting the sustainability of the Dairy performance when, let's say, home consumption would be a bit less stronger. So we read that as a good sign for the category overall.

When you look at the underlying drivers of this growth, good growth in Europe, and I will come back to Actimel and Activia, pretty good growth in the U.S. And in the U.S., Oikos is, I would say, accelerating: after the good signs, we saw already at the beginning of the year with the restaging of Oikos, we just see that this is really working for us. We're investing into it. And this is not only helping the category, the Greek segment in the U.S., to be, again, back to growth, but also us to win share. And I think this is a good sign for the next months to come. This is not only Oikos. I mentioned Two Good. So we are overall pretty happy with the dynamics we are seeing in that part of the world on Dairy.

Europe, Actimel, I was mentioning, flying double-digit growth, delivering, I would say, as much as of the last quarter. Activia, we are seeing pretty good results from the restaging, especially in U.K. and Germany, where indeed we are also winning share with Activia.

When we look at France, for example, we are not yet happy with the performance, to be very clear. So we are still working on getting that back to sustainable growth. But I think, overall, we are on a positive trajectory.

Russia is and has been, as you know, also last quarter, a more tough environment for us. Macroeconomic environment is not easy. It's one of the places where we have increased prices the most. So Q3, we were delivering a slightly negative performance.

When you read that in more detail, as we have been increasing prices the most on our traditional portfolio, this is also where the performance is less good, the modern part of the portfolio is doing much better. We now need to go through this moment because the pricing is important to sustain a healthy financial equation in Russia, enabling us to reinvest also in the future. And so this is part of the game. But overall, as you say, very positive dynamics in Dairy across the globe, including Latin America, which I didn't mention, where we also see consumption sequentially coming back.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, Warren. Next question from Celine Pannuti from JPMorgan.

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**Celine A.H. Pannuti** - *JPMorgan Chase & Co, Research Division - Head of European Food, Home, Personal Care & Tobacco and Senior Analyst*

Yes. So I want to come back on China Specialized Nutrition. Could you elaborate about your growth rate? How much market share you had in the Mainland China? And as well, how is the pricing environment in this category versus peers of maybe slowdown of pricing? You were talking about premiumization earlier, but I'm not sure whether that was still the case.

And then if we think about this quarter was very strong, you said, and there was probably a comp effect in the Family&Friends and Daigous business. What is the sustainable level that we should be looking overall for the China business?

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Yes. So overall, let's maybe start with the category in China overall, and there is no surprise and everybody is talking about that, that the category is, of course, under pressure in IMF because of what we are seeing in birth rates happening in China and happening around the globe. And so that makes that China category is negative in volume and also year-to-date, very slightly negative in value, still benefiting from penetration gains and from premiumization trends.

Now when I talk premiumization, I don't talk pricing because we don't see really pricing happening in the market. What we are seeing is a trend which continues, which is that consumers going to the premium, super premium, ultra premium segments. And this is a trend which continues and which is to the benefit of the majority of the big players and to the benefit of us because it's driving the mix in the right way. So it's not really about pricing.

When it comes to our growth within this category, you're right, in a way, we are decoupling our performance from the category performance. Pretty happy to report that Aptamil is sustaining its market share- the reality is when you look at the domestic label business, where we are growing strong, we are, in fact, winning market share with a pretty strong execution. What is reassuring also in that sense is that - and I was mentioning that - what we call controlled international e-commerce, which used to be a very small part of our business, becomes a very significant part of our business. And here, we are having very, very high level of market share, and we are continuing to increase.

And last but not least, there is this Family&Friends and Daigous channel, which, yes, I mean, last year has been under extreme pressure. This quarter is back to growth in a very mechanical way. It's very difficult to predict how this will look like for the quarters to come. We do not count on growth coming from that channel, to be very clear, just because it's a structurally declining channel. And so we are managing to make sure that we are shifting the demand from this channel to the controlled channels. So overall, we are pretty happy with the performance.

We see Q4 also in growth in China, which, to some extent, is, again, a base effect. But on the other side, we are also continuing to be confident on the competitive strength of the Aptamil brand.

**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, Celine. Next question from David Hayes, Societe Generale.

**David Hayes** - *Societe Generale Cross Asset Research - Equity Analyst*

One question. It's a short-term question, I guess, just in terms of inventory building and shipment levels. So I guess I'm thinking about particularly Waters, weak summer in Europe, Mizone also impacted in China. So just trying to understand whether there was some higher volumes in the quarter that maybe you see on the other side of that in the fourth quarter.

And then similarly, in the China Infant Formula business, those gray market traders seem to be quite volatile with their inventory levels. It seems like, as you say, they come back into operation a bit more. So was there kind of a shipment build again in that indirect channel in the third quarter that maybe won't be there into the fourth quarter?

**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Look, in this very volatile environment, one of our focus areas is indeed to make sure that we are having healthy inventory levels. And so what I was describing on Specialized Nutrition Rest of the World is a testimony to this.

You were talking about Waters. It's true that the beginning of the summer has not been easy because July and August, both from a weather point of view, and I think we all experienced that, particularly in Europe, but also from a lockdown point of view, in Asia was not easy. September has been already much more dynamic, which has also helped us to make sure that we are leaving the quarter with healthy inventory levels across the geographies, so which is true for Europe, which is true for Asia. And so we do not expect any impact in Q4 from overstocking in any of those channels.

**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, David. Now we have the question from John Ennis from Goldman Sachs.

**John Ennis** - *Goldman Sachs Group, Inc., Research Division - Equity Analyst*

My question is on the early signs of inflationary pressure for next year. So this year, you've been able to mitigate a large part of the headwind through productivity savings, but of course, raw material and energy prices have increased throughout the year. So I guess, what do you see is the COGS inflation figure for next year at this stage? And can you give us the expected productivity offset roughly for 2022? And maybe you could also talk us through your hedging policies when it comes to energy prices, which, of course, have become a bit more of a problem since we last spoke at the 2Q stage.

**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

So when it comes to inflation, so 7% H1, 9% H2, so an average 8% for us this year. We do expect nothing less than that for next year and maybe even more. It will depend, to a very large extent, to what happens in global supply chains because what we are seeing today is that transportation rates, particularly, and also I talk about truck capacities but also shipping from Asia to Europe or the U.S. and back is under high tension. If this is going to continue over the next quarters, and I think we need to assume it's going to continue over the next quarters, we could see even higher inflation rates next year.

An important aspect in this is our ability to serve demand. I talked about the tensions we're having in Plant-based. So for us, preparing for next year is, I would say, threefold. It's making sure that we are avoiding any kind of service issues, which means anticipating all the needs we have in terms of trucks and transport to the extent possible. It's making sure that we are stepping up productivity. I was sharing with you in S1 that we had almost 5% of productivity delivered, which was a step-up versus a year ago. And we expect the second semester of this year to be higher than the first semester in productivity, and we continue that growth because in front of higher inflation, we need to put higher productivity. Here, again, the EUR 300 million program we launched in November 2020 is the lever. And then we have everything about pricing, which we have been discussing going through broad-based pricing.

When it comes to hedging, so especially for everything which is about plastics, we are usually hedging something between 9 and 12 months. We continue to use these kind of tools to lock part of our exposure, depending also on the windows of opportunity this year, which is different depending on the geography. But it will not give us the same level of protection as we had it this year. That's very clear.

And maybe a last comment which is important, which is that there's now a number of, as we talk, pricing. We have obviously different tools of pricing between list price increase and managing revenue growth, including promotional activities. We have been quite, I would say, smart in doing these pricing initiatives so far this year, avoiding where we could avoid list price increases. Obviously, when I talk broad-based price increases for next year, we also need to do more list price increase, which is also true for Europe and for the U.S. And here, we are starting to prepare our dialogues with our retailers in order to get to the level of pricing we need to get to and to translate it into a win-win situation.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Okay. So thank you very much. Next question from Martin Deboo from Jefferies.

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**Martin John Deboo** - *Jefferies LLC, Research Division - Equity Analyst*

Yes. Juergen, I just want to pick up on John Ennis' question. Can we just be crystal clear about this inflation statement? You're expecting inflation in 2022 not to be any less than the 9% you're seeing in H2. Do I understand that correctly?

And just an observation, Juergen, if you had 7% inflation in H1 and there doesn't seem to be much incremental inflation entering the system, just mathematically, why is it going to be at least as bad as FY '21?

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Well, look, I mean we go from 7% to 9%, so average 8%. When I say we do at least expect 8% next year, very clearly, part of the inflation we are seeing in the H2 of this year is because of the transportation tensions. Let's be extremely clear because we see spot rates for trucks in the U.S. at a record level never seen before. We see at least 8% for next year. If we will continue to see tensions on global supply, including truck capacity, it will be more than 8% next year. It may be 9%. It may be more. This is why we are preparing for the higher end of the scenario with all the levers I was mentioning.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, Martin. Next question, Jeremy Fialko from HSBC.

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**Jeremy David Fialko** - *HSBC, Research Division - Head of Consumer Staples Research of Europe*

Jeremy Fialko, HSBC here. So one other question relating to the inflation and the pricing. So first of all, as you have been putting the price rises up, particularly, in emerging markets, how is the demand for your products holding up? And I guess, what is your view as price rises become more prevalent across your different categories and the effect that this might have on consumers' disposable income? So some perspective there.

And then secondly, linked to this view on volumes and the elasticity, is it likely that your volumes will stay negative in the final quarter of 2021?

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Yes. Thank you, Jeremy. Maybe to start with the second part of your question, volume is negative. It's true that this Q3, we are negative in volumes. But when you look at it, EDP is delivering positive volumes. Waters is delivering positive volumes on the back of sound underlying dynamics. The negative volumes of the company, as we discussed a bit earlier in this call, is really coming from the SN particular situation we are having in the Rest of the World.

When it comes to the impact from pricing on overall volume dynamics, of course, this is not neutral. Let's be very clear. Especially in emerging markets, it has an impact. It will have short term probably an impact. I was talking about Russia, which is one of those cases where we see that it has an impact.

The elasticities are not the same category by category. We have been starting to do pricing on Dairy across many markets just because mix inflation came in first. We have seen that a good part of our portfolio is holding well in terms of volume, especially everything which has an additional benefit, which is truly differentiated versus competition. This is true for brands which I was mentioning, Oikos, Actimel, Activia. So we are not worried on these ones. Where we need to be extremely smart in doing pricing is on the, let's say, lower end of the pyramid, on the low price part of Dairy, in order to make sure that we don't take too much hit on volumes.

On Waters, we have been discussing that, I think, in the July closing. On Waters, because we are hedged on a good part of our exposure this year, it gives us the ability to price slightly after some of our local competitors, which in a way helps us to mitigate volume impacts.

And then Specialized Nutrition is a very particular element because here, you saw the very important mix effects we have seen, which is not only coming from the country mix with China but also from very important product mix. And so here, this is particularly the division where we want to play these 2 levers to the max because we believe that there is still a good level of opportunity in mix when it comes to especially the pediatric specialties where we are archileaders and where we believe there's sort of growth there, which may help us to limit our pricing initiatives.

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**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Next question from Pinar Ergun from Morgan Stanley.

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**Pinar Ergun** - *Morgan Stanley, Research Division - Equity Analyst*

Actually, Jeremy just asked it, but maybe a quick follow-up on the supply chain challenges you're seeing. Do you have any expectations on how long these headwinds will last? Should we assume situation gets worse before it gets better?

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**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Look, for us, supply chain challenges, we had mainly in the U.S. from transport. It's true that when you are running a factory full speed every day, any delay in supply of packaging, any delay in availability of truck capacity is causing a service issue. So what we are seeing is, in the U.S. on that particular front, that things have been doing slightly better as we were traveling over the last weeks. I don't want to overpromise that things are solved because we need to be extremely attentive and vigilant on what's coming over the next weeks. From what we know today, things should improve as we go through the fourth quarter.

Another element of attention for us is the overall supply on packaging materials, which is not only U.S.-based challenge. I take an example, which is cardboard supply, which is an overall global challenge for the industry and not only for us. And so for us, it's important that we anticipate those possible shortages in the market to make sure that we avoid any service issues also in other parts of the world.

**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, Pinar. So we'll take the last question from Cathal Kenny from Davy.

**Cathal Kenny** - *Davy, Research Division - Senior Analyst of Food and Beverage*

Quick follow-up question on inflation. Would it be possible to disaggregate just by cost center, Dairy versus PET, the current rates of inflation you're currently experiencing? A related question then is do you anticipate running higher levels of inventory in 2022 just to give you security of supply across those key raw materials?

**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

So overall, obviously, when I say total COGS inflation is something around 9% in the H2, we are seeing that material inflation is leading the tables. Logistics picking up because of all what I mentioned before on transportation, overall manufacturing costs increasing but to a lesser extent than what we are seeing on logistics and manufacturing.

When it comes to milk and, I would say, plant-based ingredients, we are seeing mid- to high single-digit market levels. On milk, we are slightly protected because we have this privileged local sourcing of some of our milk. Remember that where we are contracting where we have mid- or long-term contracts with some of our farmers and the associations, which makes up for 1/3 of our global mix supply, which is, I would say, limiting the impact on us.

Plastic, on the other side, is now hugely under pressure. Market inflation on high double digit, and this continues and also translates into some shortages for some specific plastic packaging materials as we speak. True that our hedging allowed us to absorb part of this inflation in H1, but obviously, for 2022, we need to be prepared to take that into our P&L and have the right mitigation actions in place.

When it comes to other packaging, also under pressure. You take metal, I mentioned before cardboard, also in strong double-digit inflationary trends.

**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, everyone. And with that, I don't know if you want to say last word.

**Juergen Esser** - *Danone S.A. - Chief Financial, Technology & Data Officer*

Well, guys, thank you very much for your attention today. And I think you have seen that we have been delivering a very solid Q3 after the solid Q2. So stay tuned on what's to come, and especially stay tuned on the full year and then for the capital markets event on the 8th of March. Talk to you soon. Bye.

**Mathilde Rodie** - *Danone S.A. - Head of IR & Financial Communication*

Thank you, everyone. Bye.

**Operator**

This concludes today's conference call. Thank you for participating. You may all disconnect.