Company Name: Kellogg
Company Ticker: K US
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Event Description: Deutsche Bank dbAccess Global Consumer Conference

Market Cap: 25,507.22
Current PX: 72.82
YTD Change($): -.89
YTD Change(%): -1.207

Bloomberg Estimates - EPS
Current Quarter: 0.931
Current Year: 3.919
Bloomberg Estimates - Sales
Current Quarter: 3156.000
Current Year: 12617.529

Deutsche Bank dbAccess Global Consumer Conference

Company Participants

- Rob Dickerson
- John A. Bryant
- Fareed A. Khan

MANAGEMENT DISCUSSION SECTION

Rob Dickerson

All right. I'll get started. Everyone could have a seat. Once again, it's a pleasure to welcome the Kellogg Company back to our Global Consumer Conference this year. Kellogg is currently focused on maximizing it's growth and profitability potential with its 2020 strategy, geared towards improving performance in cereal, increasing its global snacking presence, doubling the size of its emerging market platform and investing in high velocity channel positioning. Kellogg has directed its comprehensive efficiency efforts towards revenue growth management, ZBB and Project K which includes its current US-based DSD exit.

With us today, we have Chairman and CEO, John Bryant; Senior Vice President, CFO and Principal Financial Officer, Fareed Khan, along with Vice President Investor Relations, John Renwick and with that, I hand it over to John Bryant to take off today's presentation.

John A. Bryant

Thank you, Rob and good afternoon everyone. It's a pleasure to be here today to give you an update on the Kellogg company. We are committed to return into top-line growth and driving margin expansion over the next several years. And we'll give you a sense of how we're going to do that, how we're going forward.

Before I start, I'll draw your attention to our forward-looking statements disclaimer, hopefully, there we go. It's our forward-looking statement disclaimer, please take a moment to read this and refer to our SEC public filings online if you have any further questions.

In terms of the agenda today, three areas I want to go through. One is top-line growth, how we're going to do that, how we're navigating some of the change in the marketplace around us. The second is, financial visibility which Fareed will take you through and Fareed, as Rob said, is the Chief Financial Officer of the Kellogg Company and a relatively recent add to the Kellogg Company. And I'll come back and talk about our core values because in this period of transformational change in the food industry is essential for companies like Kellogg to go back to the core reasons why we've created and hold those in the palm of our hand, to help us navigate what is it incredibly rapidly changing environment that we're operating in.

And the Kellogg Company has been transformed over the last 15 years. If you go back to the year 2000, we're 70% cereal, 20% snacks, even though we call that portable foods at the time, was largely cereal bars on-the-go cereal and 10% frozen foods. Today the company is more than twice the size. We're still the world's largest cereal company with cereal being roughly 40% of that business, but today we're also a global snacking company, with over 50% of the company sales in snacks. We're the world's second largest savory snacks company with the Pringles acquisition, and second largest cookie cracker company both with our U.S. business as well as the number of acquisitions around the world including Russia, Egypt and Brazil, and we continue to have a successful and vibrant frozen foods business in the U.S.

So what are the some of the changes that are going on in our industry, but I think rapid changes in food beliefs. We have a ever expanding snacking, we're seeing the media landscape changes, with changes, how have we to deal with brands. We are seeing dramatic changes in the retail landscape and there'll be even more changes to go through the next 5, 10 years, and the defining event in our lifetimes in the food industry is the emerging markets, and being in a position we continue to participate in the strong growth of those markets.

I'll take you through each of these five trends, including about how we're positioning ourselves to take advantage of these changes. First, in terms of food beliefs, we've seen dramatic changes in food beliefs and this had an adverse impact unfortunately on our business. We had a portfolio that was well suited to the traditional definition of health and wellness, which is low fat, low calorie. Today, consumers particularly in the U.S. are no longer are as concerned about that, they're they are not interested in counting calories. And that's adversely impacted one brand in particular in our portfolio and that is Special K.

So looking at our portfolio, Special K is over 100% of the decline in our business over the last couple of years. Special K saw a double-digit growth from in 2003 to 2013, as low fat, low calories are very much on trend. As our [indiscernible] change unfortunately we've seen a double-digit in the decline in this business over the last couple of years.

We are taking aggressive steps to stabilize this business to reposition and get it back to growth. We're doing that by changing its position positioning from weight loss, or dieting, towards inner strength. We're also doing this by reformulating a large sum of the foods. Some of the cereals becoming more like a white granola such as Special K Nourish goals and launching through positive more in line with current food beliefs and food trends.

Where we've changed the food, we're seeing better progress. This is very much a work in progress for the Kellogg Company, but an area that we need to make additional progress in order to stabilize the business in terms of total company to growth. And we have confidence we can make this happen. We've had another brand with a similar set of positions, issues which is Kashi. Kashi is a leading natural food brand in the U.S. We are caught in a GMO discussion, we've had to reformulate the foods, take in GMO free, and invest even more aggressively back into the foods.

You can see on this page that we've returned the total Kashi Company's food business to growth here in the first quarter of 2017. And we're reformulating our snacks business and you can see that we're picking up additional points of distribution in snacks, which will help us drive the Kashi business back to growth over time. So, we have to keep reinvesting back in the food to just stay on trend from a food perspective, not just the Special K and Kashi , but across the portfolio. So we're removing negatives, artificial colors, artificial flavors, reducing salt, reducing sugar across the portfolio. Adding positives such as vitamin bundles and additional nutrients. But there is one thing to take away is the taste is still king. Nothing is growing in the food industry that doesn't taste good. We have to keep the taste credentials out there and keep driving taste in our portfolio. So we're committed to continue to identify changing food trends and changing the portfolio and investing back in the food. We've been doing that over the last three to four years and you should expect us to continue to invest in our food as we go forward. We are going through the largest renovation program in the company's history.

The next big trend that we're facing is snacking and this is a tailwind that benefit for our company. We're seeing every generation in the U.S. snack more than the prior generation. So the boomers are snacking more than the greatest generation, generation x is snacking even further, and millennials are snacking more than any prior generation in the U.S. This reflects the breakdown of three meals a day, reflects the movement to all day grazing in the U.S. and around the world.

As I said before, we've changed our portfolio to take advantage of this. So today snacks is over half our company and in fact our snacks business in 2016 is roughly the same size of the entire Kellogg company back in 2000. And we have a number of brands helping us drive this growth including Pringles. We've seen strong mid single-digit growth in Pringles since the date of acquisition. We've spent over $1 billion in capital expenditure to enable additional growth in this business. Early on we were capacity constraint, this is a business that not seen additional capacity since 1998 before the date we acquired it, it's 2012. And you can see here a lot of that business is in Europe.

In fact we have twice the level of market share in Europe than we have in the U.S. and the U.S. is significantly higher market share than we have in Latin America and Asia Pacific. We are still in the early days of the Pringles growth expansion and growth opportunity for the Kellogg Company.

As you go beyond Pringles we have other major brands in the U.S. including Cheez-It and Rice Crispy Treats. Both of these have seen strong mid-single-digit growth. Cheez-It has had over 20 years of consecutive growth. And Rice Crispy Treats is feeding off the very strong cereal equity. Another big change in our snack business is a decision to exit the DSD system. As a reminder, in the U.S. we got to market with cookies and crackers through the DSD system.

Today that 60% of our snacks business goes through DSD, 4% goes to business through warehouse – to market through warehouse. When we go to market through warehouse, our shares are higher, our in-stock performance is higher and our margins are higher, our growth is higher. We are confidence that we can go to market through warehouse system and be successful in this business. It's worth remembering, as we transition to warehouse that we're transitioning to the Kellogg Company warehouse system, with only services as cereal and pop-tarts. The merchandising levels in cereal are as high as cookies and crackers. We've already demonstrated the ability to run a very successful, highly merchandise category such as cereal through that warehouse system.

In addition as we move to warehouse, we will generate significant savings, which should be reinvested back into the business. We will increase our operating margins on snacks, be more in line with the company average in the U.S. We'll invest back in our brands and historically we've been investing in Pringles, Cheez-it, Town House crackers and Club crackers, Rice Crispy Treats and seeing good growth. But quite frankly the DSD system has constrained our ability to invest as much in the brand building as we'd like. So as we invest more into brand building, we expect to see good return from that investment. As we look at Keebler, we've had limited support behind Keebler last year. We saw a very early positive return, so we continue invest back in those brands. We also improved retailer margins on this business and there is very strong retailer support for this shift. Retailers recognized that they go to their stores virtually every day with full truck loads. Now DSD system is going to the back of their stores once or twice a week with less than full truck loads. We have very strong retail support for this shift and we are on plan at this stage with that DSD transition. We're seeing what we expected to see. We are making good progress in this area.

The third big trend out there is media. Consumers are changing how they consume media and we need to change how we build our brands accordingly. We've been through this before as a company. We've gone from print to radio, from radio to TV, and now TV to social, mobile, digital, and we'll continue to change our mix. We are absolutely committed to having strong brands with the Kellogg company. We spend well above the peer group average and brand building, advertising, consumer promotion things like toys in the box, movie tie-ins et cetera. And we expect that to continue in the future and thanks for the DSD transition, we expect to add even more brand building back into the Kellogg company's portfolio.

Brand building as a percentage of sales has come down a bit in the last couple of years. Quite frankly that's an impact to the zero-based budgeting program, savings in the agency fees and production costs, non-working costs as opposed to true working media. The other thing that's really important here is we have become significantly better at measuring the impact of that brand building programs. We remember the old [indiscernible] want to make it "half my advertising is waste, I just can't tell which half." The benefit of new analytics, big data is we can measure real time the impact of that brand building programs, pullback and was not working and invest more working. And so this is critical as you drive as well as to the new media mix, and over 50% of our media – over 50% of our media now in the U.S. is through digital media channels.

The fourth trend is a changing retail landscape. This is still very much in its early days, but we're seeing significant expansion of e-commerce around the world. Over 30% of our sales in China are direct-to-consumer, over 10% of our sales in markets in Europe are click-and-collect. In U.S., less than 2% of food sales go through e-commerce. This will be a fundamental transitional change in the go-to-market model around the world as e-commerce impacts retailers.

We're investing back in e-commerce, we have a number of programs around the world, so we can learn from this, we even have a program in the U.S. is direct-to-consumer. BearNaked.com where you go online, you create your own granola blend from raw ingredients, we make it for you and ship it to your home.

Also the company has evolved to being a global snacks company, we need to change how we operate. Historically, we've been a pantry based company, center grocery store pantry company. Now we need to be within our [indiscernible] desire. So we're investing more in like frequency store distribution systems around the world, convenience stores in modern markets like the U.S. vending et cetera and we're seeing good early returns from that.

To give you a sense of the size of opportunity for us, in our Snacks categories, around 11% of sales is from single-serve items. We've announced next portfolio only about 6.5% of our sales is through single-serve items. We have an opportunity to nearly double the size of our business in the single-serve area. Again reflecting the company's historical legacy focus on center store grocery. So we're confident in our ability to drive additional growth through high frequency stores. While all of these trends are impacting the food industry, there is no question the biggest impact on the industry in our lifetime is emerging markets. We've seen billions of people rise out of poverty into the middle class and look for the benefits of packaged foods. So we're taking advantage of that to position our portfolio for that long-term growth. If you look at the – amount of sales in the emerging markets in 2017 and compared to 2012, we sold about 80% more volume in the emerging markets in 2017 than we did in 2012. What's driving that growth? What's driving that growth is underlying growth in cereal and snacks. Obviously, the Pringles acquisition also helps. We acquired the number one cookie cracker company in Egypt. We acquired a biscuit company in Brazil which more than tripled the size of our business in Brazil. We've made the largest food company – largest investment of any food company in Nigeria with our Tolaram business and we have a very successful joint venture in China.

So as we add all that up through our acquisitions and our joint ventures, we'll sell 80% more volume this year than we did just five years ago. Similar to that, going back to 2010, as our 10% of our sales was in the emerging markets. This year we had operation of joint ventures and acquisitions over 20% of our sales will be in the emerging markets because a lot of that comes through acquisitions and joint ventures is often not apparent in our financial results. So we're committed to driving emerging market platform. So our industry is going through tremendous change. We're taking advantage of those changes and positioning ourselves for long-term growth, particularly top-line growth through snacking and through emerging markets and I will hand over to Fareed to take us through our financial visibility.

Fareed A. Khan

Thanks, John. And good afternoon, everybody. It's good to be here. So you've heard a little bit of our strategy and some of the changes that are occurring in our marketplace. What I want to do is give you a little bit of our perspective from a financial lens.

Really three takeaways. The first is, top line growth is our number one strategic priority as a company. I want to give you a sense of why we are confident that we can return the business to top line growth. Secondly, you've seen us implement a number of productivity and efficiency initiatives that are underway, that drive significant operating profit margin expansion. I want to show you and give you an update on some of those initiatives and how we're progressing towards a target of a 350-basis point improvement off a 2015 baseline. And the third point is, this business has strong fundamentals and that allows us to continue our commitment to a growing dividend, selective acquisitions, buybacks as well as investing strategically into the business.

So let me start with top line growth and there is really four elements. And we hit these four levers, the company returns to top line growth. The first is around stabilizing the two brands that we've seen significant top line erosion, largely because a brand that has been on-trend has now come off-trend and we've seen consumers shift their preferences, they moved around Special K with a strong growth driver for us, it's been a strong headwind in the last couple of years. But the Kashi business serves as a great example of what happens when we renovate the food, we reposition the business against consumer preferences and we see particularly in the cereal business, sales coming back in and on the wholesome snacks business, points of distribution increasing.

Special K bigger brand, earlier in the process, but we are deep into the food renovation. We've just launched in the U.S. the repositioning strategy, so we're confident that that business will get back to stabilization and then grow. So those two things alone really put the rest of the business in growth mode. Second factor is with the DSD transition that generates a significant supply-chain savings. Some of those, we're going to take to the bottom line pretty significantly in snacks. Some of those will enhance the margins that retailers get, which supports them – which gives them support with the initiatives. And the big part of that allows us to reinvest back in the snacks portfolio, both in terms of brand-building and product innovation.

Snacking is very much on trend, we see that across all demographics groups as John pointed out, and we now will have more resources to put against that portfolio. So while it's a significant bottom-line margin improvement lever, internally we really view the DSD transition as a long-term top-line growth engine. Third, we have a number of brands that John pointed out that are already in growth mode and making sure that we keep those brands healthy, product innovation strongly in those and essentially driving growth in those areas, whether it's Cheez-Its, Frosted Flakes, Froot Loops or others.

And the last area is around the emerging markets. We've made investments in capacity, we've made target acquisitions that give us market access, scale and distribution access. And it will be all about leveraging those investments to continue to drive growth in those areas, and we're seeing that already in our businesses. So if we put that together we feel, we can return to low single-digit growth and all will see the business like ours with our economics that's a significant long-term value creation lever.

The next area is around more of our efficiency initiatives and you've heard us talk about those we launch these as part of the 2020, each one has its own – set of financial levers, but essentially we're targeting sort of three to four window, new your window to implement these. The first is Project K. And it has a number of some sub initiatives, but we're targeting $60o million to $700 million in savings reaching a full run rate by about 2019. Part of this is network optimization where we are looking at our supply chain globally, closing higher-cost facilities, optimizing supply chains, also making strategic investments in new capital.

Second is around global business services. So we have a multi-business model, that's a mix of categories and geographies. We've taken a lot of a transactional services that support those businesses whether it's order to cash or record to report, those types of processes, and we moved those into a shared service infrastructure. Low cost locations, some of them in-house, some of them outsourced, and that obviously drives significant savings for us.

In an organizational design, in different geographies and different businesses we take in aggressive steps to make sure we have an efficient organization. We're focused focus on talent retention and development, and feel continue to allow us to be a nimble organization. So, there is some go-to-market changes that we made. The most significant of which was the DSD transition, which if you take each of those four levers, that gives us full line of site, on Project K savings, and that's a major contributor to a 300 basis points of margin improvement.

So, second major area is ZBB, and we're implementing pretty much textbook ZBB, it started about two years ago in the U.S. markets, where we basically piloted it, put in place the tracking, the programs, the ownership of the initiatives. And we've now scaled and rolled that out internationally. So each of our regions is implementing ZBB program essentially structured the same way, but being implemented in different markets. In both Project K and ZBB, we're delivering the savings in line with the targets that we set with our 2020 strategy and are encouraged by the progress.

Then, the third area is really looking more around capabilities, revenue growth management whether that's making sure that we build the value into our products. We're positioning them appropriately with customers, price pack architecture model down, slopes are right across different channels, there is a number of factors that come and play on that – and that's a significant area that we've been building tools and capabilities in our business and then, John talked a little bit about the new marketing model and how we're looking at ROI on our brand building efforts with increasingly new analytics, shorter cycle times, so that we can make bets on brand building, see the results and cycle those in a much more efficient and rapid way.

So if you put these initiatives together, they drive the 350 basis points of operating margin improvement and we set a target from 2015 baseline to 2018. You've seen the improvements in our first year with 100 basis points of improvement and we are very much on track against those initiatives and again, this is in an environment where we've had slightly declining top-line growth and generally, deflationary environment. So not the optimal conditions to drive margin expansion, but we're pretty much on track to deliver that and we put guidance out as far as 2018, but we're going to remain committed to improving efficiencies.

Last area is around cash flow and with growing net income , with incremental working capital improvements as well as most of the heavier lifting around restructuring behind us, we're going to generate plenty of cash flow. Our CapEx requirements are pretty much in line with what we've done in the last couple of years. So about 3% to 4% of sales and that's going to leave ample cash for deployment of strong commitment as I mentioned to our dividend, to bolt-on acquisitions. You will see that play out in emerging markets like the Parati acquisition we made in Brazil or biscuits producers in Egypt that give us scale and market presence and access the distribution in future growth markets, but also looking at emerging snacks, health and wellness areas in our core markets as well. So it will be a mix.

And then balancing share repurchases and optimizing our debt. We feel good about our capital structure. We can flex up and leverage should an attractive acquisition come along. We'll also balance that with share repurchases. So with that, I'd like to turn it back over to John, for some concluding comments. Thank you.

John A. Bryant

Thank you, Fareed. As I said early on, we're going through a transformational change in the food industry and the Kellogg company is over 110 years old. We've survived two global wars, a depression, and numerous recessions. And as we go through these changes, we need to go back to the core beliefs of our founder and the company, of why the company was created in the first place to help us navigate these changing times. We have a strategy house. It has two sides of the strategy house. The left hand side is the one that you normally see from us, breakfast, snacks, emerging markets, win where the shopper shops. That's what we normally share externally.

In addition to that internally, we have the right had side of the strategy house, which are our values who we are, why we exist. And it starts with nourishing with our foods recognizing that where we sell based on health and wellness, we do everything we can to ensure that our foods help people live a better healthier life. When we sell on fun, we're doing everything we can to make it was more fun, people's lives are more fun and enjoyable and have to deliver against those promises. That means we need to keep investing back in our food and we're doing that in the last four or five years in an ever accelerating rate. Reducing sugar, reducing salt, removing artificial flavors and ingredients, et cetera from our foods.

The second big one is feeding people in need. We've recognized that everybody can afford our foods. We give away a lot of food. We've given away nearly two billion servings of food over the last three to four years to people who needed the most when and where they needed.

The third one is nurturing our planet. Climate change is reality. Climate change is a significant risk to agricultural-based companies such as Kellogg company. We've a wide range of sustainability programs to reduce our impact on the environment with a goal of leaving the world in a better place when we found it. Our commitment is through our entire end-to-end supply chain. If you look at greenhouse gas emissions and food production, it overwhelmingly echoes back on the farm. So our commitment is to reduce greenhouse gas emissions all the way from the farm to consumer's homes. To do that we set very aggressive long-term goals in our greenhouse gas reduction that includes working with farmers. We've a commitment to work with half a million farmers, institutes, climate smart agricultural practices. To do that they will set to be economically smart practices. A lot of this focus on increasing yield and reducing postharvest losses. So we have a goal of reducing greenhouse gas emissions by as much as 50% across the entire end-to-end supply chain by 2050 and we have a series of goals leading into that end date.

That whole reduction includes recycling of packaging at the end of the process as well, and as a core belief of that company and core area of focus for us. And then finally, living our Founder's values, Mr. Kellogg believed in investing in people and creating an environment where people could bring their best every day, I'm happy to say we continue to be recognized that progress and diversity inclusion, one of the top 50 companies for diversity and inclusion equivalent to Diversity Inc. in the U.S.

And the company received the series of recognitions for the work that we've done. Obviously Diversity Inc. is one. Oxfam and other NGOs recognize the progress that we've made in the area of sustainability, even though we recognize it's a lot further for us to go and more for us to do. We're one of the most [indiscernible] companies in the world and one of the most ethical companies in the world.

We prove this under our Kellogg's Breakfasts for Better Days program, which is a commitment to create 3 billion better days over the next four years. So we are committed to living the Founders values and navigating what is extremely turning and changing environment. We had committed to return to top-line growth, we're committed to doing that around the world, driving snacks, driving emerging markets and driving cereal. We have very strong visibility to opportunity programs in the profitability and driving cash flow, and we are absolutely focused on committed to building a stronger Kellogg Company for the future.

And with that, I'll take pause and hand it over to Q&A

Q&A

<Q>: Hi, great. Thanks John. We'll open it up for questions in one minute. I myself have a question. So, John, I'm just curious if you think about the pricing pressure, right, in the U.S. in traditional grocery and mass just for the expectation of the pressure of building driven partially by incremental investment from the discounters, hard discounters what's happening online.

Do you believe you – Kellogg is actually be ahead of the game so to speak in terms of the structure is being build with the retailers, the incremental margin that they are gaining. Basically if this works for you – works for the retailers at the end of the day, right, it would seem as if those retailers they have such buy in will look to others?

<A>: All right. So I think the DSD transition particularly what you're focusing on the – firstly on pricing and margin questions from retailers in the U.S. Retailers have always asked for more margin, yes, they will continue to ask for that. And it's probably a little bit more focus on that right now because of concerns about other channels getting bigger in the U.S. We'll continue to navigate that way through that, we do that through pack price architecture. You saw the big opportunity, we have in single-serve often retailers at higher price per kilo than pantry packs. So number of things that we can move to improve our price realization over time.

On DSD, obviously, exiting DSD is a major decision by the company. We are doing that because we have absolutely confident that's the right thing to do long-term. 40% of our sales today in the snacks business goes through DSD and works very, very effectively.

To give you a sense of the size and magnitude and this is indicative numbers. Illustrative numbers, I'm not suggesting these are our exact numbers. But a DSD system on average cost about 20% of sales to maintain. And warehouse system is more like 5% of sale. So it's 15 points of margin in there, between those two systems. Some of that is used to help improve our operating margins up to the portfolio average, some of that is used in best packing brand, and some of that will help our retail margins. I think it's important to recognize that not all of our retailers see DSD as a positive . And that, they already deliver product to the back of their stores. They can do it very effectively, very efficiently and in some respects this system is unnecessary. So we believe warehouse is the right way to go. We have a very strong retail support for doing that and we have confidence that this is the right way for us to run our business and to grow our business long-term. Any other questions from the audience?

<Q>: Okay. I will ask one more. In terms of Europe, you said on your – on the Q1 call that there is simply like a bit more work to do in Europe, I guess to renovate or return to a higher rate of growth and margin profitability. So could you just expand a bit as to exactly what you mean by a bit more work?

<A>: So, Europe has had a very strong performance behind Pringles over the last four, five years. Pringles has been growing mid to high single-digits in Europe. That's stalled out in Q1. So we took pricing, we had some disputes. Those are now behind us. They'll have some impact on Q2, then we're back to a normal run rate, in the back-half of the year and we see good long-term growth behind Pringles in Europe. We had bit more of a challenging situation with cereal in

Europe. Europe was the most overdeveloped region for Special K, in particular the UK. So we see more impact on that brand in these markets, but our kids brands is still doing well in Europe.

So if you're looking at the reported UK in-market data, for sure we actually see our numbers are getting better here in Q2. So we think we're making good progress in Europe, but Q1 was more of an anomaly and we expect to get back to that long-term growth behind Pringles as well.

Question over here?

<A>: Thanks. Currently it seems a marked declines across the number in the U.S. core categories and brands. So it's more of an industry issue rather than we used specifically. But do you think the whole industry is just way too focused on margin? I mean, I understand from your strategy [indiscernible] of the growth underpinning both sides, but there's a marked absence of that. And I appreciate, your advertising spend is well above the industry average, with 3.5% as the industry average, most FMCG categories only are operating at 10% plus. So doesn't it need to double and some to get growth back into the whole industry?

<A>: The U.S. food sector has been relatively softer beginning of 2017; January-February was very soft, March-April was better. So a little bit hard to read because of the timing of Eastern move year-on-year between those months. As we look to the future we expect the business to get a little bit better as we go through the year. We gave guidance at the end of Q1 that it will remain relatively softer and that's basically what's happening.

There's all sorts of potential reasons and element is timing of tax returns, you could argue where that's having an impact or not. There is some suggestion that immigration is falling down in the U.S. and illegal immigration, in particular, which is hard to read is slowing down. And a defensive position being taken, given some of the policies in the U.S. right now. So there is a number of factors there. I do believe ultimately as an industry, we need to drive growth, we need to do that through innovation, through investing back in our foods and investing brands.

Our brand building spend that you see is really just advertising. We have a lot more than just that. We have the consumer promotion spend as well, not trade spend here. But movie tie-ins, toys in the box, all those sorts of things doesn't fall in the advertising line, falls into a different part of the SG&A line. So I do believe there needs to be an increasing focus on growth in the U.S. food sector. It's probably not so much volume growth so much as price mix, R&D growth. It is a relatively low-population growth market.

Increasingly – we're seeing increasing snacking snacking growth and you can can't growth in U.S. business. We're growing our Cheez-It business 20 consecutive years, growing Rice Krispies Treats, Pop-Tarts have grown 26 of the last 28 years, there is lots of pockets of growth within that segment.

<Q>: Can I just back to DSD for a minute, please. I think I heard you said – you said your market shares were higher outside of the DSD, if that is right, can you just explain why that's the case?

<A>: So the channels which we deliver warehouse today are higher shares. We get good retail support in those channels. I think rather than talking about why there is share differences across channels, talking a little bit about our confidence in holding our share in the channels, which we're moving out of DSD. The DSD system if it comes today is different to what it was 20 years ago. 20 years ago you go in with a DSD system, you could change the shelf around, you can change displays et cetera. Today for most customers, the shelf is set nationally, set a sensor. DSD operators can't just walk in and move the shelf around.

Big end of displays tend to be set as part of our national calendar. So you cannot be able to move those around. Secondary displays absolutely. So we'll probably lose some secondary merchandizing here, and some of that compares might take that up, but is that worth 15 points of sales in difference. And by investing back in the brands, by working with their retailers are now making a higher margin with that products, we believe we can achieve growth in other ways that will offset that and help us gain share over time.

<Q>: Just to follow up on that point. You're giving money back to the retailers, which is not something we hear very often from companies, what explicitly are you expecting, I mean, you said you expect to get growth on the back of it, but what does explicitly have the retailers told you they will give you in return for that higher profit share?

<A>: Oh! It's worth remembering. What's happening here is we're transferring activity to the retailers. So, today our folks going directly to the back of the stores, in the future we'll ship to their warehouses, [indiscernible] ship to their stores and they have to bring it out onto the shelf. So, there is real activity going on that. Some retailers are in a better position than others who take that on just because of where they are with their systems. We've seen very good support from retailers and there is opportunity for retailers since little bit of cost a fix to make a higher margin as a result of this shift. So, it's not so much that we're giving them higher margin in return to certain things so much as we're moving activity, but what I will say is over 95% of that retailer base has bowed into the size of the price reduction in return for that activity as well as the SKU count on shelf and the shelf layout.

<Q>: Yeah. I have one question.

<A>: Question down the back end?

<Q>: So, in e-commerce we've seen select categories really resonate with the consumer thinking like pet and diverse. What do you think about cereal and cookies? and do you think that will see much higher penetration going forward in your key markets?

<A>: If I look at cereal, and I look at some markets here in Europe, we see an over-indexing in cereal going through click and collect type programs and e-commerce type programs. So, I do expect that to continue. I will also say that often we see a higher market share and all sorts of opportunities because we are on the shopping list as we have very strong brands. So, I do expect we see over-indexing in some of that categories and we do hope to benefit from that shift.

<A>: Okay. I think that's all the time we have. Thank you, John, Fareed.

John A. Bryant

Thank you very much.