CCH – Jefferies Virtual West Coast Consumer Conference
Fireside chat transcript – 18 November 2020

COCA–COLA HBC - PARTICIPANTS

Zoran Bogdanovic, Chief Executive Officer

Michalis Imellos, Chief Financial Officer

JEFFERIES - PARTICIPANT

Ed Mundy, Analyst

Ed Mundy, Analyst, Jefferies LLC

Good morning. Good afternoon everyone. My name is Ed Mundy. I'm the beverages analyst at Jefferies in London, a very warm welcome to our West Coast Virtual Conference. It's a great pleasure to have Zoran Bogdanovic and Michalis Imellos, CEO and CFO of Coca-Cola Hellenic; as well as Joanna Kennedy, Head of IR with us today. Zoran and Michalis, hello.

Michalis Imellos, Chief Financial Officer

Hi, Ed.

Zoran Bogdanovic, Chief Executive Officer

Hi, Ed, and greetings to everyone, who's connected on this call.

Michalis Imellos, Chief Financial Officer

Yes.

Zoran Bogdanovic, Chief Executive Officer

Thank you for having us.

Ed Mundy, Analyst, Jefferies LLC

Great. So for this fireside, I've prepared some questions, which we'll start to run through. I guess, it's been a very difficult year given the impact of COVID on the out-of-home business. What is your degree of confidence that the out-of-home business comes back post the pandemic? And can you just remind us why is this important from a volume, pack, channel, product mix as well as operating leverage perspective?

Zoran Bogdanovic, Chief Executive Officer

Yes, thanks, Ed. Actually, first of all I'm quite confident that the out-of-home eventually will restore sometime in the future whether it's two years or one year, it will reach its previous level. However, it may be in a little bit different shape given the fact that this pandemic really did have and it does have an impact on a number of our customers. We've seen before a situation that some of them usually disappear unfortunately. The new owners come in, but for us this is an important part of the business.

We consider that our approach with out-of-home part of the market is a competitive advantage that we have behind which we are continuously investing with the size of the sales force that covers that market as well as our marketing investments, equipment, programs, etc. Usually in the normal times the out-of-home business is just over 40% of our revenues. And as everyone can imagine, the majority of that revenue in that out-of-home business is coming from single serves. So that's a very high percentage. And yes, those single serves have a higher revenue per case.

Now logical next question is how are the margins, which actually they are more similar with at-home part of the business than sometimes people might think because of also the out-of-home part of the market requires more of a logistical effort, route-to-market is very different. There are more touch points, there are more returnable glass packages that also need some logistics in reverse way. However, net-net, yes, also margin is somewhat higher in the out-of-home versus the at-home. So this is in a nutshell. So I do believe that it's going to recover. And if I may say Q3 was a good indication that even when the market did not operate in a pre-COVID level and still there were a number of 10%, 20% of customers, which didn't work, with lower capacity, still we've returned to that level we were able to operate in a very, very good way.

Ed Mundy, Analyst, Jefferies LLC

And I can just ask on your out-of-home. I think roughly half historically is due to HoReCa and the other half is more immediate consumption, I think. Do you expect both to come back in a similar way? Or do you think that there will be some scar tissue on its side, for instance, people working from home on a longer duration basis in the aftermath of the pandemic?

Zoran Bogdanovic, Chief Executive Officer

Yes. Look – yes, I think that a number of, let's say, I see and there are types of quick service restaurants, which would operate sometimes in big hyper centers where people would just kind of quickly go for to grab a meal, a sandwich or something, there is going to be some impact in the short-term as working patterns will change. But we are already compensating that shift with our approach to how do we cover, how do we plan, how do we organize our marketing activities, execution in the store for at-home channel because the consumption remains, it's just that it's a little bit shifted between the channels. And I would like to emphasize that for at-home where there are – now even more drinking moments, we are actively and with strategic push promoting our single serve packages either as a single unit or even more as multi-packs because – and we do see that year by year this proportion of single serves that go to at-home is increasing.

Ed Mundy, Analyst, Jefferies LLC

And that brings into my second question. What are the opportunities to emerge fitter post the pandemic in terms of top-line and bottom line, you mentioned the opportunity to push more single serve into the off-trade. But what are the top and bottom line that should allow you to come out stronger post the pandemic?

Zoran Bogdanovic, Chief Executive Officer

One thing is that I think this pandemic also kind of even further sharpened the view on – of the best performing categories, where also more channel investment makes sense. That's clearly sparkling, that's energy, that's new Costa Coffee that we started in May and then certain value creating versions of the hydration space where there are functional flavored similar water propositions. One thing is that we will be paying attention on portfolio innovations going forward. We've also realized through these that it's better and wiser together with Coca-Cola Company. We have discussed and fully aligned to go after fewer things, but which are more scalable, which are stronger, more profitable, than spreading ourselves thin. I think that's a critical part.

And then we do see that the better we develop and stronger our fundamental core critical capabilities to drive growth, they equally play a role in the normal times as well as the crisis times. That's why our focus accelerated investments behind big data advanced analytics, revenue growth management, route-to-market, key account management capabilities, innovation and talent. Those are the ones where we – even this year when we prioritized things, we did not stop our progress in how we develop capabilities and I see that as absolutely critical thing. Also I think the Michalis can say a little bit more on the cost base because I think it's an important one. I see that as one of the success factors of this year, where we have reacted quickly, but obviously we take our learnings from there as well that embedding in our planning going forward that we will not be restoring to the same cost, the spending that we had before.

Michalis Imellos, Chief Financial Officer

Yes. I mean, if you look at this year savings, we said that we are shooting for $120 million as a minimum in terms of savings and around 75% of that was behind marketing expenses. Now as we go into 2021 and with a recovery scenario that we see for next year, a lot of that marketing spend will come back next year. However, still we are not going to be at the levels of 2019 in absolute terms. So, there is a little bit of, call it, saving that is coming from that. Having said that, particularly this year and to some extent also next year, there is some shift of marketing investments behind the promo activity. We found that this year was the most suitable and the most effective tool in the circumstances to be able to defend the volumes and gain shares.

Next year also we'll continue on this balancing act. And then the other 25% of savings this year, which came from what we call discretionary expenses and costs, travel and meetings and events and consulting and so on, and so forth. We feel that a good chunk of that is here to stay. It's the new way of working, introducing more digital into our processes, less traveling; gradually less office space will be needed as more and more people will be sharing the work between home and the office. So with all that, we feel that a good chunk of that pillar of savings is here to stay and set them into 2021.

Ed Mundy, Analyst, Jefferies LLC

Very clear. Thank you. It seems like a long time ago since you provided the investor event, the capital markets events back in June 2019. I think when you fleshed out a medium-term growth algorithm of about 5% or 6% on top-line and roughly 20 to 40 basis points on margin, having been through a very strong margin recovery period since 2015-16. Do you feel that that framework is still relevant on a medium-term timeframe once we're through the pandemic and all the volatility that it brings?

Michalis Imellos, Chief Financial Officer

Yes, I can start and maybe Zoran can build also. So, first of all, if you look at where we were at 2019 in terms of margins on an organic level, so excluding Bambi and various other accounting things that are going on this year. We were up 10.7% margin that had another 10 bps from Bambi, which we acquired mid 2019 and we reported that 10.8. So if you look at the base of 10.7 as an organic margin, we really feel that there's no reason why we cannot hit this level of margin next year. So next year is a special year, a recovery year, let's say, to get somehow back to the new normal. And from there we also feel that we can continue to grow organically our margin back to the guidance that we gave in June 2019.

On the other side, when you look at revenue, the guidance, as you said, in the mid-term, yes, it's absolutely valid. However, it's going to take a little bit more time for us to be able on a reported basis with all effects in and so on. It will take some time to get back to the 2019 levels simply because in 2020 and in 2021 we have significant ForEx impacts primarily coming from the ruble and the naira. So, on a reported basis, we'll take a little bit longer to get back to levels of 2019, by the way 2019 with just over EUR7 billion was the second highest year in terms of revenue, only second to 2012, which was EUR7.45 billion.

So, it is a big milestone and probably will take a little bit longer to get there, but on a currency neutral basis, absolutely we can see that after next year, which is a recovery year, fixing "the dislocating gap" that happened in 2020 with the pandemic. There is no reason why we would not continue also with a help of both the aggressive rollout of Costa Coffee, which obviously is a huge opportunity and, as we said in June 2019, almost doubles the addressable market size on top of NARTD.

Ed Mundy, Analyst, Jefferies LLC

Thank you. I think that brings on to my next question. One of the things that you highlighted back in June 2019 was your vision as 24/7 beverage partner. And as part of that journey, you continue to do very well with your core carbonates business, your core sparkling business, but an ambition was to really get greater exposure to some of these categories that are in a potentially higher margin, higher revenue per case and reweight your business towards those. Could you provide a bit of a feel as to how you've shifted the portfolio as part of that 24/7 beverage strategy?

Zoran Bogdanovic, Chief Executive Officer

Yes, Ed, I think actually I'm very, very happy to say that since June of 2019, quite a few things have been happening, but in a planned, orchestrated, and in a way that fits what we had in mind with our strategic priorities. First of all, we always in all our calls very open, we make a reference how important is the segment of Adults within sparkling, and as a really high value segment, which has a huge consumer elements as a mixers, but also as a straight drinks. We've been innovating a lot and in orchestration with Coca-Cola Company, doing a focused marketing. And now for a number of years, we have excellent double-digit growth in this segment, which is – it has a price premium versus average of sparkling between 10% and 40%.

And then even this year in Q3 as the reminder that we grew 10% with adults sparkling. Then I think probably globally, I think we are the company that plays with most of the energy brands, strong strategic partnership with Monster also now with Coca-Cola Company for Coke Energy. And I think there is excellent stratification of various brands at various price points to hit the very distinctive consumer segments, so high tier Coke Energy, then you have Burn, then you have Monster, you have now Predator, which is a latest brand from Monster, which is hitting the more lower value affordable energy segment.

So that has been continuously growing and even in this year has a very, very solid growth and we are continuously gaining share. Then strategic big bet is our – if I can say, proper entry into coffee, as some of you know that last three years we've been with Lavazza in five markets only, but now with Costa Coffee, we really go full scale. Obviously, we will do that in waves, but entry into coffee, which in itself is a huge revenue and profit pool, is something that we take extremely seriously. We have very ambitious plans and targets. We launched in May, which was a regional plan when we want to launch it, because of COVID we didn't delayed it because we do see relevance, even in this type of times. And already since May we have launched in 13 of our markets and we will continue next year expanding it further.

Just to say for everyone, when you think about coffee, this does not mean ready-to-drink coffee. It is also ready-to-drink, but in our territories ready-to-drink coffee is actually very small. We talk about the full package mix with whole beans, roast and ground for at-home, and also the same similar bags for HoReCa. Then we are also talking about the capsules, like, you know, whether it's these types of things espresso compatible capsules, express vending machines, so that's with Costa. I did mention earlier that we are doing a targeted entry into hydration space. We are not going after segment which is only about gaining volume, but we are choosing together with Coca Cola Company, those innovations that have elements that are giving reason for something additional, functionality, flavors, and therefore Aquarius is a such product that we have been rolling out in a number of our markets, and we will continue to do that and that hits into this lucrative segment of functional water.

And the last thing that happened is that together with Coca-Cola Company, we enter now into this light alcoholic space, in the space of hard seltzers with a brand of Topo Chico. We already launched in five of our markets, which are the first wave. And we are very excited to be expanding also in these kinds of spaces with Coca-Cola Company. We do have experience already more than 12 years in the alcohol space, because we've been distributing high quality premium spirits brands in almost all our markets. Therefore, the addition also from Coca-Cola Company portfolio of a product like this already lanes in our teams who are experienced, who have credentials with customers. So these are a number of things that have been happening since June of last year Ed.

Ed Mundy, Analyst, Jefferies

Yes. There's a lot going on. I guess, just to sort of follow-up from that. I mean, on the one hand, you've got this very, very strong distribution network, which you can put more things into the pipes, but on the other hand, getting these adjacent categories allows you to do more cross promotions with the key retailers and it allows you to get into other strategic important channels that you might have historically under-indexed in. I mean, how do you think about the channel and the other sort of strategic opportunity as well as just putting more volume through the system?

Zoran Bogdanovic, Chief Executive Officer

Okay. I think first of all, for us the critical capability is route-to-market, whether that's a physical one or that's a digital one, which is now developing and accelerating more and more. So, for us it's in the essence of who we are and what we do in the market. We are that last mile in the system with us and Coca-Cola Company and other brand partners. It's our role that delivers and makes that last mile connectivity with customers to be the critical one. So constantly it is about expanding and increasing the capacity of our lungs to be able to do a wider portfolio. And doing that also to do some things that through their complementarity they can enhance each other; and therefore excellent tests that we are doing in Serbia is with Bambi, leading confectionary brand over there.

And we do see that these cross category promotions, leverage that it gives us with customers, actually proves to be working even better than we anticipated. And Bambi as such is delivering well ahead of the plan. Another thing is also complementarity of the premium spirits category, which helps to ignite our core portfolio because of that mixability. It also helps us to compete with various spaces where beer is playing. So that's another example how we are utilizing that, that route-to-market muscle and where we see that it's wise to do that.

So yes, these are some of the areas. And then obviously I already talked about the coffee, which requires within the route-to-market and sales expertise, it requires a dedicated knowledge and skills but this is where, we are very committed and keen to invest, so that we can do that properly. So I see these spaces as those that are critical ones. I don't see ourselves suddenly doing, something out of the field, but these type of adjacencies more and more we are keen to explore and leverage.

Ed Mundy, Analyst, Jefferies

Thank you. I guess, the story of 2020 with the pandemic has been, a, big supply-driven shock to your business with the away-from-home channel partly closed, it was certainly impaired. As you think about the demand picture on the other side of the pandemic, Hellenic has got pretty good experience of operating in a quite volatile environment following the sovereign debt crisis. Could you provide a bit of a feel as to how sensitive your business is to GDP growth? And if GDP does take a bit of a temporary dip, what tools do you have disposable to ensure affordability of the product and that you remain relevant to consumers' minds?

Zoran Bogdanovic, Chief Executive Officer

Yes. Let me start and Michalis please jump in as well. First of all yes, we have such a variety of territories, and I think that's actually the interesting and rich and beautiful part that all the way from Switzerland to Nigeria, and then in the middle Poland, Romania, whatever. First of all, the breath and such a wide portfolio with which we play, that means that, that gives us the opportunity that we can emphasize more categories and certain subsections within categories for the markets, where whatever may be relevant, that kind of thinking comes through our revenue growth management capability that over the last four years we have really fired up significantly. I believe creating a strong knowledge, systems, tools, methodology, that we started and then actually the global Coca-Cola world started also taking over.

And that helps us to come up with solutions and architecture that takes into account and balance both affordability situations, which are – let's say more relevant for Nigeria and lower GDP per capita markets. Also to premiumization solutions that are more relevant in higher GDP per capita markets. Even through big data and advanced analytics, which we are now using more for better insights to inform our thinking in the revenue growth management for exactly these types of situations is showing us that even in the low GDP per capita countries, like Nigeria, you have those socio economic segments that to which you also in a segmented way, you can cater, serve and sell premium solutions. So that's something that, those are the critical elements.

And then there is a continuous work on the cost structures. Nigeria is an excellent example where it's a very competitive market. However, every single year now, for a number of years, we always find ways how to take cost out, how to increase productivity, improve efficiencies, and our focus and discipline behind continuously looking into cost structure and making ourselves more competitive is critical in all types of markets. Michalis, anything that you would add?

Michalis Imellos, Chief Financial Officer

Yes. All I would say is that GDP is not, I would say, the best indicator and it is relevant, but it's not the best. I mean, we always start with the disposable income. Sometimes there's a strong correlation between the two, but sometimes also when the economy is a strong exporter or we have situations like now with COVID where you can see GDP declines, but then you can see also governments jumping in and supporting with fiscal packages the overall disposable income. So I would always start with disposable income because it has a direct link with the disposition of the consumer to spend and that also affects our industry quite significantly.

Ed Mundy, Analyst, Jefferies

Thank you. The Coca-Cola Company recently announced some changes, started looking at the different brand portfolios, as well as their structure. I mean, how would you characterize your relationship with the Coca-Cola Company at the moment, and what does the portfolio rationalization process that they're undertaking mean for your business?

Zoran Bogdanovic, Chief Executive Officer

So, look on – let me start. This portfolio rationalization that they started, initiated, I think it's a really strategic way of doing it, where I think in – they've been doing a brutally honest exercise to see what brands and which products are really not contributing to serious revenue and profit generation. And those, that's such a necessary breadth of a portfolio was an obstacle to be able to operate faster, leaner and smarter. So we are fully on the same page in relation to that, I already mentioned that even with our counterparts, for the territory that we jointly cover, we had an exercise in May, June, July, where we were looking into that prioritization, and we emerged fully aligned for the rest of the year, but more importantly going forward where we want to put our bets, what are the priority brands for each country. And consequently, what will be the resource allocation and the investments.

So I think that also a relationship with Coca-Cola Company, I really think it's on a very high, effective, fruitful level. I think this year has even more surfaced the quality of us working together, being closer than ever. And I really mean when I say closer and it's reflected in the speed of how we made decisions. As a reminder, as two separate companies, which work so close together, I think the way we have made decisions in Q2 and to prioritize investments and eventually achieve the results that so far we achieved, I think speaks as a concrete example and evidence of how the relationship works.

And I will just conclude to say that at all levels from both sides of the organizations we have very honest, trustworthy dialogues, conversations, discussions, and I'm very much personally motivated and encouraged by that level – that kind of a relationship.

Ed Mundy, Analyst, Jefferies

And we've seen one of your sister bottlers within Europe and so more large-scale M&A. How does that opportunity set for Coke Hellenic? Just more broadly, how does the M&A pipeline look?

Michalis Imellos, Chief Financial Officer

Yes. Look, nothing has changed here, Ed. We first of all look at the organic growth of our business with CapEx behind revenue generating initiatives, whether it's coolers, whether it's production equipment. Now there is acceleration of investments behind digital as well and we talked a lot during this meeting about it. From then on, obviously, our progressive dividend policy and then there is the M&A, first of all, bolt-on acquisitions either in the Stills area or some niche sparkling, Adults, maybe sparkling, locally relevant brands.

And with the flexibility that we have in our balance sheet and the capacity that our balance sheet has, we are open for any geographical expansion opportunity that makes strategic sense, meaning that it's a growth opportunity and of course comes at the right price. Now we know that this is something that is initiated by the Coca-Cola Company, so whenever there is a small or a big opportunity, and we are called to the table, we will definitely be interested to examine. As I said, if it's a small one, we have ample firepower in our balance sheet. If it is a much bigger one, we believe we can flex the balance sheet with a low gearing that we have currently to be able to accommodate even bigger deal.

Ed Mundy, Analyst, Jefferies

Thank you. And then just more of a sort of near term question. How does the second wave that we're seeing in Europe, how does that compare to the first wave from what you're seeing across your markets?

Zoran Bogdanovic, Chief Executive Officer

There is a difference, first of all in this second wave, a fewer number of markets are affected because first time it was literally all markets except for Belarus that were in a very severe lockdowns, and markets go frozen. Now, you will have various degrees of measures and things imposed where only in half of the markets, or let's say markets that give us half of the volume are in those that we would call a more strict – with most really strict measures. And within that half of the volume; half of them are with lesser impact or a contribution of out-of-home in that volume.

Second thing is that, second wave is happening now when we are in Q4 and possibly might extend to Q1, and these are the quarters where we are less exposed to the out-of-home, whereas Q2 and Q3 were quarters where out-of-home is a much more important. And then another element is that because of the whole psychology that happened end of March, April, beginning of May, even at-home channel was in decline. However from July onwards, we do see that at-home channel has been in the positive trajectory and that's an important difference because it helps us to compensate for those declines that happen in out of home.

And then I would say that a number of learnings that we have accumulated quickly from the start of outbreak, which we have used to prepare for Q3. Q3 was excellent example and good evidence of how well we did adopt or not. I believe it was done fairly well. And also in a similar way, we've done lots of adjustments for these Q4. So even though there is a wave two, fundamentally there are a number of differences that characterize them in such a different way.

Ed Mundy, Analyst, Jefferies

Thanks a lot. We've got maybe a time for maybe a couple more. I just want to probably leave it with a very broad open question. I think Hellenic has a very wide range of markets with good natural growth opportunities. What is it that you're most excited about as you look to the next three, five, and possibly 10 years across your businesses? Is it the natural growth? Is it the opportunity to do more with price mix? Is it the opportunity to get more things in through the pipes? What is it that gets you most excited Zoran?

Zoran Bogdanovic, Chief Executive Officer

Excellent question. So listen, I really reflect and I think that we are in an excellent industry that has so much potential. I think that our starting position where we enter into this new decade that's ahead of us, I think that industry itself has already very, very good growth potential. There is so much innovation that's driving it, and evidently there is a potentiality for more value. So all that boils down that I'm personally very excited about the growth prospects, primarily I mean by that pushing the top line incremental driving our top line, meaning revenue, and then as we work constantly on continuous productivity efficiency elements, I can see how this company has every potential to become bigger and then smarter and more capable to do more things.

I just told you a few questions ago when you asked me what's different versus 2019 June? Only in a year and a half so many things have happened. When I think what can and will happen in the next one, two, three years, I think that opportunities are truly mind-blowing, and what keeps me particularly kind of alert is that we do the fundamentally right things in how we make this organization stronger. That starts with securing, that we have best talent, capable talent, and motivated people who then really work behind prioritized capabilities. When you have that, then whether you have great years or you have tough years, I know that this is what makes a difference. And that gives me that type of focus, and work gives me huge confidence that the period ahead of us and years ahead of us have to be, and will be years of very good growth.

Ed Mundy, Analyst, Jefferies

Also Michalis, I'm afraid that's all we have time for. We are finishing right in the hour – on half an hour. Thank you so much for your participation and thanks everyone for listening in.

Zoran Bogdanovic, Chief Executive Officer

Thank you, Ed. And thank you all. Thank you.

Michalis Imellos, Chief Financial Officer

Thank you everyone.

Zoran Bogdanovic, Chief Executive Officer

Bye, Ed.

Ed Mundy, Analyst, Jefferies

Bye.

DISCLAIMER