Kerry Group: Interim Management Statement

30 Oct 2013 - Kerry, the global ingredients & flavours and consumer foods group, issues the following Interim Management Statement for the nine months to 30 September 2013 and confirms outlook for full year.

Key Highlights

9 months to 30 September 2013

- 2.9% increase in continuing business volumes (Q3 +3.2%)
  - Ingredients & Flavours +4.1% (Q3 +4.3%)
  - Consumer Foods -0.2% (Q3 +0.1%)
- 1.7% increase in pricing
- Group trading margin up 80 basis points
  - Ingredients & Flavours +80 basis points
  - Consumer Foods +30 basis points
- Continuing progress in 1 Kerry Business Transformation
- Earnings guidance in a range of 8% to 10% growth for full year, notwithstanding currency headwinds

BUSINESS PERFORMANCE

Kerry Group achieved a good business performance in the three month period to 30 September 2013 and continued to invest in enhancing the quality of Group businesses. This performance was achieved against a background of significant currency headwinds and a challenging overall market environment in developed markets. Despite weaker economic conditions in some developing markets, Kerry continued to achieve solid growth and business development – particularly in Asia and EMEA developing zones. Performance was assisted by successful integration of acquisitions and good results to date from continuing deployment of the Group’s 1 Kerry Business Transformation Programme. Development of the Group’s Global Technology & Innovation Centres supported by Regional Development & Applications Centres, continues to drive successful product innovation and
partnerships with key accounts – enabling the Group’s ingredients & flavours’ taste & nutrition systems and functional ingredients & actives businesses to outperform market growth rates. The Group’s consumer foods’ sectors in the UK and Ireland remain highly competitive where Kerry Foods continues to focus its business model on its core offerings and on strategies to improve the quality of its business portfolio.

Sales growth sequentially improved during 2013. In the nine months to 30 September 2013 continuing business volumes grew by 2.9% and pricing increased by 1.7% broadly offsetting input cost inflation of approximately 3.5% to 4%. Continuing business volumes grew by 3.2% in Q3. Reported revenues in the nine months to end of September decreased by 0.2% reflecting significant currency headwinds (~6% in Q3) and discontinued volume of 3.7% arising from restructuring programmes to optimise the Group’s manufacturing footprint and withdrawal from Kerry Foods non-core business activities.

Added value business development and the positive impact from exiting Kerry Foods non-core business activities, coupled with the benefits accruing through the 1 Kerry Business Transformation Programme, contributed an 80 basis points improvement in the Group trading profit margin for the nine months. The continued positive margin momentum reflects an 80 basis points improvement in Ingredients & Flavours and a 30 basis points improvement in Consumer Foods.

**BUSINESS REVIEWS**

**INGREDIENTS & FLAVOURS**

In the nine months to end of September continuing business volumes in Ingredients & Flavours grew by 4.1% (Q3 4.3%) outperforming market growth rates. Pricing increased by 1.9%. Reported revenues increased by 2.7% reflecting 3% LFL growth. Divisional trading profit margin increased by 80 basis points. Discontinued volume as a result of manufacturing footprint optimisation amounted to 3%. Good growth was recorded throughout the Group’s taste and nutrition platforms in food processor and foodservice accounts – in particular in developing markets.

**Americas Region** performed well with strong innovation through key customer accounts delivering 4.5% continuing business volume growth. Good growth was achieved in the foodservice channel through major chains and through Kerry’s branded offerings. Performance was also assisted by successful integration of recent acquisitions in the region and strong business development in the beverage sector. Big Train was successfully integrated, which coupled with the integration of the Cargill’s flavours business, has significantly advanced Kerry’s beverage flavour capabilities, product development and branded portfolio dedicated to the foodservice channel. Continued business development was also achieved through the division’s aseptic beverage platform. Performance in the meat sector was assisted by good growth in coatings’ applications. The Millennium Foods business acquired in 2012 contributed to continued growth in culinary applications. Performance in the ready-to-eat cereals sector was impacted by competitive issues and reduced sales in breakfast cereals. The nutritional bar segment again grew satisfactorily. Overall sweet sectoral industry performance was sluggish but Kerry innovation continues to drive development through major accounts - in particular through shelf-life extension technologies in the bakery and confectionery sectors. Pharma applications maintained strong global market development, in particular through cell nutrition applications.
EMEA Region developed markets remain relatively weak but regional developing markets provided good growth opportunities, particularly South Africa and Russia. Kerry recorded good progress through its strategic customer alliances throughout the region. Continuing business volumes increased by 1.6%. Market conditions in the savoury, dairy and culinary sectors remained relatively weak due to industry sectoral issues and constrained consumer demand. Good progress was achieved through global accounts in the sweet and cereal sectors and an encouraging product development pipeline is expected to lead to further new product launches in 2014. South Africa based Orley Foods acquired in March performed well, providing a strong boost to Kerry in meeting customer requirements for sweet ingredients solutions in regional developing markets. Good progress was recorded in beverage markets in particular through beverage flavours and new foodservice product launches. Proteins, enzymes and nutritional ingredients achieved solid growth. Pricing in primary dairy markets continued to increase into Q3 due to increased demand from importing countries. Construction of the Kerry Global Technology & Innovation Centre in Ireland is progressing well and scheduled to open in Q1 2015. To support development needs of global and regional customers in the Middle East, North Africa and Turkey, a new Kerry Regional Development & Application Centre was opened in Dubai, UAE.

Asia Pacific markets again provided solid growth opportunities for Kerry technologies despite softening in consumer demand in some countries due to relatively weaker currencies. Demand for Kerry’s nutritional systems, taste systems, functional ingredients & actives delivered 8.9% continuing business volume growth in the nine months to end of September 2013. Nutritional ingredients including infant and adult applications achieved double digit growth in China. Savoury and dairy applications saw slower growth in line with consumer demand trends. Culinary development in Australia also proved more challenging. Beverage systems and flavours performed well throughout the region with strong growth in foodservice applications. Kerry Pinnacle maintained strong growth in the Australian lifestyle bakery sector with significant new launches in major retail chains. Plans for Regional Development & Application facilities to serve customers in Asia are well progressed.

CONSUMER FOODS

While the level of promotional activity eased slightly in some categories of the UK and Irish consumer foods sectors, both markets remain highly competitive. Sales through ‘discounter’ retail channels and private label offerings continue to grow, adding to competitive marketplace pressures and structural changes in customer service. Against this background Kerry Foods performed well – in particular through its branded offerings in the UK market. In the nine months to end of September continuing business volumes decreased by 0.2% and pricing increased by 1.2%. Kerry Foods’ restructuring programmes refocusing its business model on its core offerings impacted sales – in particular the direct-to-store service to the independent and convenience retail sectors in the UK and Ireland. However Kerry Foods’ core brand shares were maintained and sales progressively recovered during the year – with Q3 continuing business volumes reflecting 0.1% growth. Reported revenues in Consumer Foods decreased by 7.3% reflecting depreciation of the sterling/euro exchange rate of 3.8% and discontinued volume of 5.3%. Business optimisation strategies will continue to be reviewed in line with evolving consumer trends in the Irish and UK consumer foods’ markets.
The division’s UK brands performed well. Richmond maintained a strong brand share in the sausage category with strong growth in frozen lines. Mattessons achieved solid volume growth in meat snacks. Cheestrings volumes were lower due to reduced promotional activity.

Volumes in the UK chilled ready meals sector were lower in July and August due to hot weather conditions. While sales in the frozen category progressively recovered during the year, volumes remain below year earlier levels. Dairy spreads lost market share to heavily promoted branded offerings.

In Ireland Kerry’s Denny and Charleville brands faced intense competition from heavily discounted private label offerings. Galtee and Dairygold maintained solid brand shares. Cheestrings continues to develop its market positioning in France, Germany and the Netherlands, and was also recently launched in Poland and Austria.

**FINANCIAL REVIEW**

At the end of September net debt stood at €1.2 billion, similar to that reported at the half year stage despite ongoing investment in development capital expenditure and footprint optimisation. The Group continues development of its 1 Kerry Business Transformation Programme across all operations and functional areas to leverage global capabilities whilst optimising manufacturing, scale and efficiency benefits. Deployment of SAP continues with recent successful deployments in Ireland and Germany. Changes in the planned phasing of deployment have resulted in slightly lower than expected expenditure in 2013 on the Kerryconnect project.

The programme to integrate recent acquisitions (including Cargill’s flavours’ business, Millennium Foods, FlavourCraft, Big Train and Orley Foods) is nearing completion. While the final cost of this programme will be higher than originally envisaged, the benefits from integrating these businesses quickly and successfully are significant – including the realisation of business efficiency savings and the enhancement of the Group’s capabilities across a range of technologies as evidenced by the improvement in the Group’s trading margin.

The two year programme to optimise the Group’s manufacturing footprint will be completed by the end of 2013. Post year end there will be no further discontinued volume resulting from this programme other than the annualisation impact of actions taken in 2013.

Business disposals in 2013 include the Freshways sandwich business and the remaining liquid milk business in Ireland. Consistent with Group strategy to exit non-core businesses, the disposals will be margin enhancing but result in an accounting loss which will be reported under the non-trading items heading.

Construction of the Kerry Global Technology & Innovation Centre in Ireland is progressing well and scheduled to open in Q1 2015. To expedite capability development at the Centre, the Group has accelerated the integration of R&D teams in Europe and recruitment to a leased facility adjacent to the site of the new Centre. By year-end 300 people will be employed in the interim facility. Costs of approximately €35m will be incurred in 2013, earlier than planned in the investment programme.
FUTURE PROSPECTS

Despite currency headwinds, the Group is confident of delivering 8% to 10% growth in adjusted earnings per share in 2013 to a range of 253 to 257 cent per share.

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