27 February 2017

Associated British Foods plc

Pre Close Period Trading Update

Associated British Foods plc issues the following update prior to entering the close period for its interim results to 4 March 2017 which are scheduled to be announced on 19 April 2017.

For the half year we expect excellent progress in adjusted operating profit and adjusted earnings per share for the group. The trading outlook for the group for the full year is unchanged with progress expected in adjusted operating profit and adjusted earnings per share.

Cash flow and funding

We expect a stronger cash flow, before acquisitions and disposals, in the first half of this year compared to last year. This will be driven by a higher profit before depreciation and amortisation, and a lower working capital outflow. Capital expenditure will be higher, driven by Primark's expansion.

Acquisitions in the year to date amount to £60m and with the benefit of net proceeds of £0.5bn from the sale of the US herbs and spices business and the south China cane sugar operations, we expect a net cash balance of some £200m at the half year.

Phasing of profit recognition

We continue to expect substantially all of the full year increase in adjusted operating profit to be generated in the first half. This is for the following reasons:

- the benefit arising from the translation of overseas results in the first half is expected to be some £50m but, with the weakening of sterling in June last year, and at current exchange rates, there will be less translation benefit in the second half;
- the full effect of sterling weakness against the US dollar on Primark's purchases will result in a greater margin decline in the second half because our currency hedges were at more advantageous exchange rates in the first half; and
- last year's change in Illovo's financial year end has benefited the first half.

Grocery

Revenue and operating profit in the first half are expected to be ahead of last year at constant currency and substantially ahead at actual exchange rates. Margin is expected to make further progress.

Twinings Ovaltine revenues are well ahead of last year at constant currency and, with almost 80% of sales generated overseas, revenues at actual exchange rates are even further ahead. Twinings has achieved market share gains in the UK, the US, Australia and France. Ovaltine sales showed good growth in the developing markets of Vietnam and Brazil and with successful new products in Thailand.

Allied Bakeries volumes have been strong and the new Kingsmill pack design has been well received by customers and consumers. The market remains competitive and margins have declined as a consequence. Jordans and Dorset Cereals achieved growth in the UK supported by award-winning new product launches and particularly good growth in Australia, Belgium, the Netherlands and France. The rate of decline in Ryvita crispbread volumes has slowed with the launch of new variants and portion packs.

Trading from continuing operations at ACH in North America has been stronger than last year with higher consumer oil volumes and better margins. Home baking product volumes also increased resulting in share gains. As previously announced, we completed the sale of the herbs and spices business on 21 November 2016 for a gross cash consideration of $367m and the assumption by the purchaser of net pension liabilities which, at the last year end, amounted to $17m. Tax of some $100m will be payable on the transaction in the current year. Oil volumes in Mexico have improved but the weak peso has kept margin under pressure. Stratas Foods, our commodity oils joint venture, completed the purchase of Supreme Oil, based in New Jersey, thereby expanding its manufacturing presence in the northeast of the US. Supreme supplies a variety of oils, shortenings, mayonnaise and dressings to foodservice and retail.

At George Weston Foods in Australia, first half revenues will be close to last year at constant currency with market share gains both in the bakery and meat businesses. Tip Top achieved volume growth for its mainstream bread brand, 'The One', and the launch last September of Abbott's gluten free loaf has been well received. Further cost reduction and significant process improvement at the Castlemaine factory contributed to margin improvement for Don KRC.

Sugar

AB Sugar revenue from continuing operations will be well ahead of last year on a comparable basis taking into account the change in Illovo's year end. Higher sugar prices, increased production in Africa, and further benefit from the performance improvement programme will deliver a substantial increase in profit.

With 2016/17 forecast to be the second year of global sugar deficit, world prices are higher than last year. A tightening of EU stock levels has strengthened domestic prices across the region. Domestic and regional prices increased in Africa as a result of higher US dollar denominated world prices.

In the UK, the beet crop is smaller than the prior year and, with marginally lower yields, production is projected to be just under 900,000 tonnes. The UK campaign was delayed in order to maximise the growth of the crop with production at Newark running into late February. With sales fully contracted for the year, firmer prices have been confirmed which, combined with lower beet costs and a weaker sterling/euro exchange rate, will drive substantial improvement in British Sugar's operating profit. The new anaerobic digestion plant at Bury St Edmunds, which produces biogas from sugar beet pulp, became operational in the summer of 2016. The biogas is fed into a gas engine generating low-carbon electricity which then exports the renewable power to the national grid.

Azucarera in Spain is expected to produce close to 385,000 tonnes of sugar from beet. In response to strengthening customer demand and partly to compensate for a lower volume of beet sugar, the Guadalete refinery, which processes cane raws, is operating this year and is now expected to produce 295,000 tonnes. Operating profit will be much improved with the benefit of higher sugar prices and increased co-product revenues.

In China, we completed the sale of our five cane sugar factories to a consortium led by Nanning Sugar on 22 December 2016 for total proceeds, including debt assumed, of Rmb2.6bn (£297m). Tax arising on the transaction is not expected to be material. Our two beet factories in north China at Zhangbei and Qianqi, are operating well and will process a record beet crop. Adverse weather conditions experienced during beet harvesting and storage have adversely impacted sugar levels in the beet but, with the higher volumes and improved prices, this business is expected to deliver a much improved profit this year.

Illovo has made good progress following last year's weather-related crop shortfalls and, with further recovery expected in the new season production, this financial year is expected to improve to 1.7 million tonnes compared with 1.4 million tonnes for the same period last year.

Revenue increased substantially in the first half driven by higher volumes and prices, and benefiting from the introduction of new consumer pack sizes. Cost reduction from performance improvement initiatives in Zambia, Malawi and Mozambique substantially mitigated local inflation.

Agriculture

Revenue growth in the first half will have been achieved largely as a result of higher commodity prices but also with the benefit of last year's acquisition of a Danish producer of alternative proteins and other speciality feed ingredients. Operating profit is expected to be marginally down in the first half with a continued strong performance from AB Vista, particularly in Asia, almost offsetting the impact of margin pressure in UK feed.

UK ruminant feed volumes were lower than last year as a result of the smaller sugar beet crop and strong price competition in compound feed. Exports from our UK starter feed business were strong and production from the new starter feed factory in Spain is due to commence in the spring.

In China, further consolidation in the agricultural sector, leading to an increase in larger scale farms, drove higher demand for assured sources of high-quality feed. Further investment has been made by AB Agri in developing a value-added product range and operation of its new premix mill will commence shortly.

Ingredients

Revenues in the first half are expected to be ahead of last year at constant currency and substantially ahead at actual exchange rates. Operating profit growth for the half year will be strong on both measures, with further recovery in yeast and bakery ingredients and another excellent performance from ABF Ingredients.

At AB Mauri, this has been achieved despite challenging economic conditions in a number of countries especially its important markets of Argentina and Brazil. The trading performance in Europe has been in line with last year with notable success for the recently opened UK Technical Centre which enables the development of new bakery ingredient solutions and provides technical support and training to customers. Asia is delivering a stronger performance this year following last year's manufacturing rationalisation, and margin improvement in Australia has been achieved through overhead reduction.

Trading in North America has been good and in January we completed the acquisition of Specialty Blending, a bakery ingredients business located in Cedar Rapids, Iowa. The combination of this high-quality and well-positioned ingredients blending operation with AB Mauri's global technology capability will strengthen our North American business.

ABF Ingredients has had an excellent performance in the first half. Sales of feed enzymes were particularly strong and growth was also achieved in bakery, food and technical enzymes. Abitec in the US continues to strengthen its range of bioavailability enhancement solutions and we have also seen sustained growth in functional excipients and drug delivery systems in the US.

Retail

Sales at Primark are expected to be 11% ahead of last year at constant currency, driven by increased retail selling space, and 21% ahead at actual exchange rates.

Last year was a 53-week year for Primark and, as a result, this financial year started one week later than last year. On a comparable week basis, total retail sales at constant currency are expected to be 12% ahead, and 22% ahead at actual exchange rates. The increase in average retail selling space in the first half, compared with the same period last year, was 12%.

The UK has performed well with like-for-like sales 2% ahead of last year and market share increased reflecting the strength of our consumer offering. Like-for-like sales for the group were level but, excluding a decline in the Netherlands affected by a particularly rapid increase in selling space, like-for-like sales were 1% ahead. New stores opened in the period traded strongly and our business in the US continued to develop.

Stock was well managed again this period and markdowns were in line with the first half last year. As forecast, the operating profit margin in the first half will decline, mainly reflecting the strength of the US dollar on input costs. Foreign exchange contracts are now in place for the majority of the remaining purchases for this financial year and our expectation for operating profit margin decline for the full year is unchanged.

The new store opening programme in the first half was very strong. Retail selling space has increased by 0.8 million sq ft since the financial year end and, at 4 March 2017, 329 stores will be trading from 13.1 million sq ft. 16 new stores were opened in the period comprising relocations in Reading and Sheffield to larger, more central locations; new UK stores in Carlisle, Stafford, Truro, York and Colchester; Liffey Valley in Ireland; Mallorca in Spain; Mannheim and Hamburg in Germany; Lille and Paris, Evry in France; our second store in Italy in Brescia; an 89,000 sq ft store in the centre of Amsterdam; and our sixth store in the US in Burlington, Massachusetts.

Our store at the Tottenham Court Road end of Oxford Street in London was extended by almost 40%, increasing square footage to 114,000 sq ft, making it one of our largest stores after Manchester and Newcastle in the UK and Madrid, Gran Via in Spain.

We still expect a total of 1.3 million sq ft of new selling space in this financial year. 0.3 million sq ft of new space is planned to open in the next quarter comprising: Uxbridge in the UK; Charleroi, Belgium; Granada, Spain; Zwolle in the Netherlands and Staten Island in the US, and an extension to the Downtown Crossing store in Boston, US.

The new warehouses in Islip, Northamptonshire, and Roosendaal in the Netherlands are now operational.

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