8 September 2014

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 full year results, 52 weeks to 13 September 2014, which are scheduled to be announced on 4 November 2014.

As previously indicated, adjusted earnings per share for the full year are expected to be ahead of last year. Strong operating profit performances from Primark and Grocery, and improvement in Ingredients are expected to offset the adverse effect of lower sugar prices and the impact of some £50m on the translation of overseas results arising from the strengthening of sterling. The net interest expense will be well below last year's charge following the retirement of expensive long-term debt and a much lower level of borrowings throughout the year. The underlying tax rate will be lower than last year reflecting a further reduction in the UK corporation tax rate and a change in the profit mix.

Net Debt

The cash inflow before financing will again be substantial this year driven by strong profit generation, a good working capital performance and lower interest costs. Capital expenditure will be close to last year's level with a larger proportion of the total spent on new stores and refits for Primark. Year end net debt is expected to be further reduced from last year's £0.8bn to some £0.5bn this year.

Sugar

Revenue and adjusted operating profit for AB Sugar for the full year will be substantially lower than last year driven by declining European sugar prices, lower volumes in north China and a currency translation impact on operating profit of some £20m. The world sugar price continues to be unsustainably low at an average of 17 cents per pound which is well below the global average cost of production. In Europe, prices were driven down by competition amongst producers positioning for growth in new markets ahead of the removal of quotas in 2017, and a higher than normal level of quota stock across the EU as a consequence of exceptional measures taken by the European Commission in the prior year. In China, domestic prices were depressed by the continuation of low-cost imports of raw sugar for refining, and Illovo's results will be affected by low-cost imports into Tanzania and the impact of lower pricing on Least Developed Country (LDC) exports to the EU.

British Sugar produced 1.32 million tonnes of sugar compared with 1.15 million tonnes last year. Good growing conditions extending into the mild winter resulted in a higher beet yield and sugar content than last year. All UK factories performed well with further progress achieved in health, safety and environmental metrics and in performance improvement initiatives.

The current crop for the 2014/15 campaign has made very good progress with early estimates suggesting that it could be well ahead of that produced this year. We have the capacity to deal with a larger crop and are confident of our ability to process higher volumes than in recent years, which will be a particular advantage in a post quota environment.

The beet price payable to growers for the current crop was agreed in summer 2013, at a substantial increase over the price for this year, and at an increased cost to British Sugar of some £30m. Negotiations for delivered beet costs for the 2015/16 campaign have now been concluded with a reduction of some 20% on the prior year. This will make a major contribution to ensuring a more sustainable UK beet sugar industry reflective of the new commercial environment for EU sugar.

In Spain, sugar beet volumes will be lower than last year as a result of a reduction in the area planted due to waterlogged fields in the north during the spring. Total beet sugar production was 338,000 tonnes, down from 405,000 tonnes in the previous year. 200,000 tonnes of imported raw sugar was refined at Guadalete and a further 59,000 tonnes was co-refined at the northern beet plants.

Contract negotiations with our EU customers for the 2014/15 marketing year are well under way with much weaker selling prices than the current year being realised.

Illovo has continued to perform in line with our expectations. Sugar production of 1.72 million tonnes this financial year compared with 1.87 million tonnes last year primarily as a result of lower production in Zambia and Swaziland where the phasing of the campaign is slightly later than last year. The profitability of exports of raw sugar to the EU market under LDC tariff-free import arrangements was adversely affected by the lower pricing in that market. Domestic pricing increased in line with local inflation with the exception of Tanzania and South Africa which were affected by low-cost imports. However, import tariffs have now been introduced in South Africa which has resulted in some improvement in local pricing.

In China, profitability has improved with the success of a number of overhead and efficiency initiatives. In the south, excellent growing conditions and a higher sugar content in the cane resulted in an increase in sugar production from 500,000 tonnes last year to 560,000 tonnes this year. However, flooding in Heilongjiang province led to a significant reduction in beet supplied to our factories which resulted in much lower sugar production in the north, at 116,000 tonnes. The campaigns at Qianqi and Zhangbei were excellent with good factory throughput and a high sugar content in the beet following our success in working with the growers over a number of years. A significant level of imports and increased domestic production resulted in domestic prices being depressed throughout the year.

Our sugar businesses are actively engaged in performance improvement programmes aimed at extending further our cost leadership in all regions to ensure that AB Sugar is well positioned as a globally competitive producer. All businesses have undertaken a review of overheads and substantial reductions have already been delivered although the programmes are ongoing. As previously announced, a £20m charge will be taken in the adjusted operating profit this year to provide for the costs of further overhead reduction.

Agriculture

Profit at AB Agri is expected to be ahead of last year with cash margins in UK feed maintained and growth delivered by higher margin businesses.

UK feed volumes remained resilient despite lower demand for ruminant feeds due to perfect weather conditions throughout the summer for forage. Strong growth was achieved by AB Vista driven by the success of Quantum Blue, its phytase feed enzyme, notably in Latin America and the Middle East but also in the EU where it was launched recently following its approval by the European Food Safety Authority. The new granulation facility at Evansville, Indiana, is operating successfully providing additional capacity to meet the increasing demand for these enzymes.

AB Agri China maintained margins through good procurement and a favourable product mix. As meat production in China transitions from small, family-run concerns towards large-scale commercial operations, there is increasing demand for high-quality feed supplied by modern, efficient feed mills. Construction and commissioning of our new feed mill at Zhenlai was completed to plan in August and good progress is being made with construction of another mill at Rudong, both of which will supply these large integrated meat processors.

Frontier saw strong demand for cereal and rape seeds with fine weather during the planting seasons. The mild winter and warm spring also encouraged disease which drove demand for crop inputs, such as fungicides and fertilisers. Encouragingly, the warm dry summer resulted in an early wheat harvest of excellent yield and quality.

Grocery

Grocery operating profit will show good growth with George Weston Foods in Australia, ACH Foods in the US and Twinings Ovaltine all well ahead of last year. Revenues are expected to be broadly level with last year at constant currency but will be adversely affected by the strength of sterling on the translation of overseas results.

Twinings Ovaltine delivered double digit revenue growth in tea both in the UK, where green tea and infusions were the main drivers, and in the US where we remain the fastest growing tea brand. Ovaltine again performed well in its developing markets, particularly Brazil and south east Asia, and the new Ovaltine packing plant in Nigeria is now fully operational. Tea manufacturing conversion costs were lower than last year with the benefit of higher volumes, further improvements in operating efficiency at the factory in Poland and more high-speed packing equipment at Andover.

At Allied Bakeries, revenues and profit will be ahead of last year with higher branded sales and an increase in market share driven by the launch of Kingsmill Great White, a white bread with all the fibre of a wholemeal loaf. The major capital investment programme is nearing completion with the installation of a new bread plant in Stevenage, which is due to be commissioned in November, and completion of the modernisation of the Glasgow bakery. The proposed closure of the Orpington plant was announced in August with employee consultation currently under way.

Silver Spoon's revenue and profit will be well below last year reflecting an especially competitive year for the UK packed sugar market which saw the loss of a number of granulated sugar contracts and considerably lower prices. Revenue and profit at Jordans and Ryvita will be ahead of last year with growth in our international business tempered by strong competition in the UK. At the end of May we exchanged contracts to acquire Dorset Cereals, a premium muesli brand, subject to clearance by the Competition Markets Authority.

AB World Foods made further progress achieving revenue growth in the UK for both Patak's and Blue Dragon. Patak's also performed well internationally, particularly in Canada and Australia. The core brands of Westmill Foods, Lucky Boat noodles and Elephant Atta flour, achieved further growth.

Sales at George Weston Foods in Australia were ahead of last year in local currency, driven by higher bread prices and meat volumes, and profitability was much improved. Don KRC achieved further improvements in factory efficiency and secured new business as a result of improved customer service levels and product quality.

Sales at ACH were ahead of last year, largely the result of demand for Mazola with positive consumer reaction to the plant sterols advertising campaign highlighting the lower cholesterol benefits of corn oil. Capullo, our premium oil brand in Mexico, increased its market share and profit further benefited from lower input costs.

Ingredients

Ingredients' revenues will be ahead of last year at constant currency but with the strengthening of sterling and most of its businesses being located overseas, sales at actual rates are expected to be lower than last year. AB Mauri built upon its much improved first half profit performance with a strong recovery in the second half.

AB Mauri made progress in all of its regions and in both the yeast and bakery ingredients businesses. Good revenue growth was achieved in South America where cost inflation was either recovered through pricing or offset by improvements in efficiency. Higher volumes and a focus on business development drove growth in North America and the new yeast factory in Mexico is now supplying the markets of North and Central America. In China, the site of our Meishan yeast factory in Guangzhou City is to be redeveloped by the local government, the factory has been closed and provision for the small associated cost has been made. Customer requirements will be met from our modern facility in Harbin.

On 31 January 2014, AB Mauri completed the acquisition of a small bakery ingredients business operating across western Europe which offers craft and industrial customers a range of high-quality bakery ingredients. Its integration will broaden our product offering and our ability to respond to customer needs in a number of key markets.

At ABF Ingredients, growth was achieved in enzymes and the next phase of development at the manufacturing facility in Finland is under way. The new cereal extrusions factory at Evansville, Indiana in the US is now in production, providing increased capacity to meet the growing demand both for extruded rice products and AB Vista's granulated feed products.

In view of the complementary product portfolios and common customer base, the Australian and New Zealand yeast and bakery ingredients businesses of AB Mauri have been integrated with the flour milling business of George Weston Foods in Australia. This will reduce overheads and allow the combined business to bring its technologies to market more effectively. Reflecting this change, the results of the Australian milling business, which were previously included within the Grocery segment, will be included within the Ingredients segment. When the results for the current year are presented the comparative results for 2013 will be restated resulting in £272m of sales and £5m of operating profit being transferred from Grocery to Ingredients.

Retail

Sales at Primark for the full year are expected to be 17% ahead of last year at constant currency and 16% ahead at actual exchange rates. This excellent result was again driven by an increase in retail selling space, like-for-like sales growth, which we expect to be 4.5% for the full year, and superior sales densities in the new stores. Good like-for-like sales growth was driven by highly successful autumn/winter and spring/summer ranges. Sales over the Christmas period were excellent and were boosted in the third quarter by warm weather, especially in the spring and early summer, which led to good trading across the group and outstanding results in Spain. Early sales of the new autumn/winter range are encouraging.

The operating profit margin of 13.1% in the first half was higher than last year reflecting the benefit of warehouse and distribution efficiencies and lower freight rates. These benefits continued in the second half and, with the strong trading over the summer resulting in a low level of markdowns, we expect the margin for the full year to be slightly higher.

During this financial year we will have opened 1.4 million sq ft of selling space in 28 new stores, the most recent being Alexanderplatz in Berlin, Bath in the UK and Enschede in the Netherlands. We closed seven smaller stores, primarily where larger, better located, premises became available in the same city, resulting in a net increase in selling space of 1.2 million sq ft. This will bring the total estate to 278 stores and 10.2 million sq ft at the financial year end. We have a very strong pipeline of new stores in Europe extending over a number of years. We expect the increase in selling space in the next financial year to be a little less than 1.0 million sq ft, to be followed in the autumn of 2015 by a strong programme of openings.

Responding to the increasing scale of our business in continental Europe, we doubled the size of our warehouse in Torija, Spain this summer and the Mönchengladbach warehouse in Germany, which services the stores in northern Europe, is being extended by 60% and will become operational early in 2015.

We announced in April that, after extensive research, we had decided to take the Primark concept to consumers in the north east of the US. A lease for some 70,000 sq ft of selling space at Downtown Crossing in the heart of Boston, Massachusetts has been signed and we expect this store to open in late 2015. Negotiations are under way to secure further stores in the north east with the intention of trading from up to ten stores by late 2016. The US stores will be supported by leased warehousing in the region.

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