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Heineken

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Cost for Revenue

Alberto Toni, Senior Director France

Good morning everyone. Not an easy task, you had three very strategic and commercially oriented presentations, and between you and lunch now you have finance guy talking about cost for revenue. So I will try to be -

All talking together

Laughter

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Alberto Toni, Senior Director France

Yeah maybe. I hope you will like.

So why cost for revenue? I think you have heard it - first of all let me introduce myself. Alberto Toni. I am a chartered accountant. I started my career as a consultant, nobody is perfect. But then I joined Heineken a few years ago. I held various finance positions in the Group, first in Italy then in the Netherlands at Group level. Lately I was Finance Director in our operating company in Brazil, and I joined the management team of Western Europe in September last year.

So the subject of the next presentation is cost for revenue. Why cost for revenue? I think you have heard it a couple of times. We are convinced that a sustainable profit growth comes from both top and bottom line. As Alexis said, we think that cost should be embedded in a strategy and should have a purpose. In our planning cycle we have decided to aggressively target cost savings, not only to contribute to our bottom line but as well to fund initiatives that can expand our top line, and therefore creating a more sustainable source for bottom line growth.

I will focus basically on three areas where we are extracting cost, what are our cost saving areas, how we are reinvesting the savings behind our top line initiatives, and finally I will take you through some preliminary but very encouraging results that we are achieving. Then I will hand over to my colleague Wiggert Deelen who will focus on how our supply chain organisation is evolving in order to support our strategy, not an inch back strategy.

As you all know Heineken has launched over the last few years a number of cost saving programmes where Western Europe has substantially contributed with more than 700 million which is a third, almost half of the cost savings. This allowed us in full fairness to deliver still operating profit growth as you have seen already in the presentation of Alexis, in a period where our top line growth was definitely challenged by the economic and demographic struggles that we had in Western Europe. That is exactly the reason why we decided to move to a cost for revenue strategy. Again, sorry to repeat myself, by my ancestor Latin says repeat it if you want, we are convinced that healthy bottom line, sustainable bottom line comes from top and bottom line.

So we target - we focus our cost saving agenda in order to invest in commercial initiatives. Commercial initiatives are supporting the growth of the category, are supporting the market share growth, are helping us to improve our mix and price strategy, and at the end are delivering sustainable value growth. In this context we have decided to make cost management a cornerstone of our strategy to embed it in our strategy. In essence moving away from the logic of cost programmes. Cost programmes very often are starting and finishing, are reacting to a situation, are facing a negative economic cycle or a crisis. Cost for revenues is a permanent governance. It's one of the cabinets of the strategy cabinet that Alexis mentioned to you before. It is proactively and continuously focusing on identifying cost savings in order to invest behind the top line initiatives.

Very often cost programmes which are not embedded in a strategy target indiscriminate cost saving across the whole cost base, very often proportionately across all the cost categories. With the cost for revenue strategy we want to discriminate between good cost and bad cost. Bad costs are very often the effect of inefficiency. Those costs need to be eradicated as soon as possible and as fast as possible. But what are good costs? Very often in cost saving programmes like I said that are going proportionately across, you affect also commercial initiatives that are strategic to your agenda. We want to maintain the good costs, and if possible even increase it then. Again with the ultimate purpose to be able to focus both on bottom line and top line.

So what are the areas that we have decided to focus on in order to drive our cost management agenda? Very clear choice, two main areas of focus. One is cost of goods sold and logistics, with the main ambition to improve our gross margin. The other area is support functions with the ambition to have them at least aligned with the global benchmarks. So in 2014 we are delivering €18m savings in the area of COGS and logistics. Around a third of this saving will come from supply chain based on the core productivity and the efficiency initiatives. Around another 10% will come from consumer value engineering which are initiatives aiming at eliminating from our product any feature that does not give any value to our customers or to our consumers. Circa 40% of it will come from procurement, product related and non-product related saving. And the remaining will come from our wholesale business, mainly through the logistics space.

I will not go through the details of the supply chain and consumer value engineering part because this will form part of the presentation of vigour. I will give some more colour on the product related and non-product related procurement saving later in my presentation.

Our support functions will contribute in 2014 with another €20m of savings. 40% of it will come from IT, around 10% from HR, I would say another 15% again from non-product related spend in the area of support functions, and the remaining part will be driven by our operating companies with local initiatives still in the area of support functions.

Let me emphasise the reason why we are able today to step up our cost saving ambition. I would say probably one of the most important reasons is that our global business service organisation has done remarkable progress in the recent years. GBS is now a reality in Heineken, is up and running and is now giving us the ability to finally

leverage our scale by centralising activities. And I will now go through the three areas where GBS is operating, associating it to the area where we are able to deliver savings.

So let's start from IT. Our global IT organisation in the last three years, over the last three years, has been able to reduce our IT running costs by 25%. Three main areas to deliver savings. Infrastructure. We are moving towards new technical standards in - basically in servers and in networks, and we are leveraging managed service through outsourcing a lot more than in the past in this area.

In application support we are now much better in control of our licences through a very advanced asset management tool that we are utilising. But also we have been able to optimise our consumer base - our supplier base. We now basically have only one supplier both for maintenance and for application support.

Finally voice. We have been able again to rationalise our supplier base through a European tender on mobile. We are also reducing the number of phones through focusing only on mobile instead of mobile and fixed, and we are making stronger utilisation of the internet voice services that are becoming more and more effective.

Moving to procurement, we have - procurement is now playing an increasingly important role in our cost saving agenda, and you see why. Basically 94% of our purchases in the product related area are today directly under central contracts. That is scale, that is centralisation. And we have been able to achieve saving in the area of glass, of cans and also of moulds by negotiations but also by reducing the cost of transformation of glass into bottle with the help of our suppliers.

In non-product related spend 75% of the spend is either centrally contracted or contracted under central governance. And here we still have important areas of saving which materialised in supply chain, in transport and warehousing, but also in cleaning and disinfection, and for example in the support base area mainly from integrated facility management and for example car leasing. In this area through this we have been able to deliver savings between 10% and 20% compared to previous year. So the global procurement organisation for Western Europe is playing a crucial role in this.

Last but not least I think probably the most transformational initiative that we have undertaken recently in the support function area is our financial shared service centre in Krakow. The centre is now fully up and running. We have 700 colleagues in Krakow in Poland who are servicing Europe, for the whole Europe. For Western Europe we have nine operating companies in scope. They are all serviced by the centres in various stages of migration to the centre. Already simply by consolidating and concentrating the four processes scope in the centre, we have seen already efficiency materialising. We have been able to increase the productivity and invoice processing by 40%, and that resulted in a reduction of 25% of the cost per invoice.

Now the emphasis is on continuous improvement and in standardisation. So we are just at the beginning of the journey. The saving potentials are all there. Having said that we are definitely feeling very well on track in the achievement of our target which is to reduce our transactional cost of finance by 30% by 2019.

So now I think I have elaborated a bit on where we are saving and now I would like to spend the next few minutes on how we are investing. Some will be a repetition. I think you have already seen we have stepped up our marketing and selling spend in 2014 by 14%, and we have been able to increase our draught beer outlet base by 3%, also thanks to that ability to increase the investment in successful outlet assets like the draught extra cold. I think then later on David will give a practical example in the UK of what the extra cold investment means for business.

In addition to that we have been able to step up our investment behind premium brands, global premium brands like Affligem and Desperados by 25%, to double the investment behind Radler, and we have been able to implement our excellent outlet execution programme in 100% of our market.

Again also this you have partly seen. While stepping up our investment we have been able to become more efficient in our marketing spend. So in four years we have been able to increase our consumer facing spend and in practice to reduce the non-consumer facing spend by eight percentage points.

So I think you have already seen it, is this delivering tangible results? Yes. Alexis showed that year to date we are growing revenues by more than 2%. We have already seen that we have been able to increase our gross margin by 60 basis points. The other positive news is that we have been able to reduce our support cost function, our support cost as a percentage of revenue by 50 basis points. So I hope that this shows to you how we have been able to reinvest our saving behind our commercial agenda.

To conclude, we are convinced that by consistently applying our cost for revenue strategy we will be able to drive sustainable growth in the region. First of all we think that cost for revenue is creating a virtuous cycle. You target savings; savings are giving you the opportunity to step up your investment in key commercial initiatives, the key commercial initiatives are giving you the opportunity to increase your top line growth, you earn scale and you are able to deliver a much more sustainable bottom line growth.

Summarising what I have presented to you, cost for revenue is our strategy. We have two main focus areas for cost saving, it's cost of goods sold and logistic and support cost functions. We are reinvesting largely the saving that we generate behind our commercial initiative. That can take many forms, however with the main purpose to deliver sustainable value growth and the preliminary results are positive and encouraging.

With that I would like to close and hand over to my colleague Wiggert Deelen to discuss a bit more in detail the supply chain agenda, and we will take questions together at the end of the presentation.

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