11 September 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 full year results for the 52 weeks to 16 September 2017[1], which are scheduled to be announced on 7 November 2017.

Trading performance
In our third quarter trading update on 6 July we reported an improvement in our expectation for the group's full year underlying operating performance as a result of a stronger profit delivery from Primark. Since that time we have experienced an even lower level of markdown which has further improved our full year outlook. Adjusted operating profit for the group will be well ahead of last year.

Net interest expense will be at a similar level to last year and, as previously explained, an increase in other financial expense will reflect the impact of last year's fall in bond yields on our UK defined benefit pension scheme. The underlying tax rate for the full year will be slightly lower than that of the first half and, as expected, will be higher than last year which benefited from the revaluation of UK deferred tax liabilities following the announced reductions in the UK corporation tax rate.

In summary, we expect to report good growth in adjusted operating profit and adjusted earnings per share for the group for the full year.

Currency
The result of the UK referendum on EU membership saw sterling weaken substantially in June 2016 against all major currencies.

With some two thirds of the group's operating profit earned outside the UK, this devaluation will result in a translation benefit of some £85m this financial year, most of which arose in the first three quarters. Sterling weakness against the US dollar has had an adverse transactional effect on Primark's largely dollar denominated purchases this year, whilst the euro's strength in the second half has had a beneficial effect on British Sugar's margin.

Next year we would expect no material translation benefit at current exchange rates. Sterling weakness against the US dollar will continue to have an adverse transactional effect on Primark's margin in the first half although a benefit from the euro's strength is expected in the second half. At current exchange rates, we would also expect the euro's strength to benefit British Sugar's margin next year.

References to revenue and profit growth in the following commentary are based on constant currency unless stated otherwise.

Net cash
The operating cash inflow will be much greater than last year driven by the higher operating profit and a reduction in working capital achieved with significantly lower sugar stocks and the benefit of tight management by the businesses during the year. Capital expenditure will be higher than last year driven by a higher level of investment by Primark across all its countries of operation. Expenditure in the food businesses remained at the same level as last year.

Net proceeds from the sale of the south China sugar and US herbs & spices businesses amounted to almost £400m, including debt disposed. The higher operating cash inflow and these disposal proceeds will result in a closing net cash position which is expected to be some £650m and compares with net debt of £315m last year.

Grocery
Grocery revenues from continuing businesses are expected to be level with last year while adjusted operating profit is expected to be lower. Twinings Ovaltine has had another good year with further sales and profit growth at constant currency and a strong performance at actual exchange rates. Margins improved at ACH in the US and at George Weston Foods in Australia. However, margins declined at Allied Bakeries as a result of a very competitive UK bread market and inflationary cost pressures. Grocery revenue and profit will both benefit from favourable currency translation.

The Twinings brand performed well in its core markets, gaining further value share in Australia, the US and France. In the UK, where significant investment in tea packaging technology is now complete, black tea sales grew well although infusions and green tea came under some competitive pressure. Last year's return to growth for Ovaltine in Thailand has been sustained, driven by a strong increase in ready-to-drink sales, and margin has also improved.

At Allied Bakeries, the Kingsmill relaunch earlier this year, which saw many recipe improvements and new packaging, was well received by consumers. However, a very competitive market with low retail prices, a resurgence of lower margin own-label as retailers sought to differentiate their bakery offering, and inflationary cost pressures combined to result in a significant margin decline. Silver Spoon secured sugar price increases albeit at the expense of some lost volume.

Jordans and Dorset cereals continued their international expansion, now selling to 75 countries, with overseas sales of Jordans now greater than in the UK. Trading conditions in the UK were more challenging with an increase in own-label in the major retailers and a greater market share being taken by the European discounters where the focus is mainly on own-label products. Westmill Foods recently announced another expansion of noodle capacity at its Manchester factory, as demand has continued to grow, and a continued focus on overhead reduction saw the completion, in June, of the rationalisation of its distribution operations. Patak's and Blue Dragon both performed well and remain the largest brands in their categories in the UK.

Operating profit at ACH's continuing operations will be well ahead of last year driven by higher revenue and lower overheads. Mazola was supported by television advertising achieving growth in revenue and market share. Consumer yeast, corn syrup and corn starch all performed well both in retail and foodservice. Margins improved again this year at George Weston Foods in Australia. Tip Top launched Thins, a product new to the Australian market, with all three variants achieving strong listings. Cost management continues to be a focus area with inflationary cost increases being covered by operational efficiencies. The Don KRC meat business continued to grow volumes in both deli and pre-pack formats and has worked closely with key customers to develop and stimulate the category as exemplified by the re-launch of the deli ham range for the Coles supermarket chain.

Acquisition
We are announcing today that we have reached agreement to acquire Acetum S.p.A., the leading Italian producer of Balsamic Vinegar of Modena (BVM), one of the best known vinegars in the world, which has been granted European Protected Geographical Indication (PGI) status due to its unique manufacturing tradition and provenance, as well as its high quality. Completion of the transaction is subject to antitrust clearance in Germany and Austria.

Acetum was founded by Cesare Mazzetti and Marco Bombarda, both of whom will remain in the business, and is based in the Province of Modena in Northern Italy, the region traditionally associated with balsamic vinegar. Its brands include Mazzetti, which is the leading brand in Germany and Australia, as well as Acetum and Fini. It also produces a range of balsamic glazes, apple vinegar and other condiments and sells its products to more than 60 countries around the world. In the year ended 31 December 2016 the business generated net sales of €103m. We have ambitious plans to grow these brands and the acquisition will broaden our international presence in speciality foods.

Sugar
AB Sugar's revenue and adjusted operating profit will be well ahead of last year on a comparable basis adjusting for Illovo's change of year end in 2016.

Sugar production of 900,000 tonnes in the UK this year was abnormally low as a consequence of the reduction in the contracted growing area in order to reduce the high level of stocks brought forward from the prior year. EU stocks will be at a low level at the end of this marketing year and, with the abolition of quota and export restrictions from October this year, our contracted area for the 2017/18 season has been increased by a third. The crop is developing well, following recent favourable rainfall and temperatures, and the latest sugar production estimate for 2017/18 is in excess of 1.4 million tonnes. Looking ahead to 2017/18, EU sugar prices will be below those achieved in the current year. However, the profit impact of this is expected, to some extent, to be mitigated by the higher production volumes and the benefit of euro strength against sterling on euro denominated sales. Beet costs will be in line with this year.

In Spain, beet sugar production is estimated to be 362,000 tonnes, lower than last year's 449,000 tonnes as a result of adverse weather conditions which affected the growing area and sucrose yields. The Guadalete refinery produced 300,000 tonnes and imported raw sugars co-refined at the northern beet factories produced 30,000 tonnes. Next year we expect lower EU prices to reduce the profit at Azucarera.

Our sugar operations in north China, at Zhangbei and Qianqi, processed a record beet crop with 180,000 tonnes of sugar produced. Market prices have been stable and profit will be similar to last year. The crop for 2017/18 is progressing well and, with a smaller growing area to enable the optimisation of plant utilisation and processing efficiency, production is estimated at 175,000 tonnes of sugar.

Illovo's 2016/17 season, which ended in March 2017, finished strongly and this has been followed by better growing conditions in the new season. Sugar production for the financial year is expected to be 1.65 million tonnes, compared with 1.40 million tonnes last year on a comparable basis, which, combined with the continuing performance improvement activities, will deliver profit ahead of last year.

Agriculture
AB Agri revenues will be well ahead of last year with growth in all businesses and the benefit of a full year's trading from Agrokorn, the specialist protein business in Denmark which was acquired last year. Operating profit will be lower than last year reflecting strong competition and higher raw material costs in the UK and China feed businesses.

Overall demand for feed in the UK has been weak and the smaller sugar beet crop reduced availability of co-product feedstocks. The new anaerobic digestion (AD) plant in Yorkshire was commissioned during the year and sales of new AD products and services under the Amur brand have commenced. Smaller arable crops and lower market volatility adversely affected Frontier's grain trading performance, but the results from its crop inputs business were strong.

AB Vista performed well, increasing enzyme revenues. The Primary Diets starter feed business had a very good year, achieving strong export growth into continental Europe, and the new starter feed factory in Spain is now operational. Feed sales in Asia began the year well with strong demand particularly in Vietnam and Thailand. In China, we have increased finished feed capacity and our first standalone pre-mix feed mill is now operational.

Ingredients
Ingredients' revenues will be ahead of last year and operating profit will again be well ahead with a further increase in margin.

AB Mauri delivered another year of significant improvement with growth achieved in both yeast and bakery ingredients. North America benefited from successful bakery ingredient product launches while the market for bakery yeast remains highly competitive. The EMEA region delivered profit growth despite the maturity of the European market and Asia's results improved following last year's rationalisation of production facilities in China. Although the economic climate in South America remains challenging, operating performance was robust. In January 2017 we completed the acquisition of Specialty Blending based in Cedar Rapids, Iowa. Integration has progressed steadily and its cake and doughnut mixes have benefited from the application of our ingredients' technologies.

ABF Ingredients will deliver strong sales and profit growth for the full year with a further improvement in margin. Sales of feed enzymes to AB Vista were well ahead of last year which drove high factory utilisation and better overhead absorption and in the second half we completed a 40% increase in enzyme production capacity in Finland. Abitec, our speciality lipids business in North America, had another year of double digit sales increases driven by the significant growth in generic pharmaceutical drugs. To meet increasing demand and to improve our research capability, further investment has been made this year at the Janesville, Wisconsin plant.

Retail

Sales at Primark for the full year are expected to be 13% ahead of last year at constant currency and on a comparable week basis, driven by increased retail selling space and 1% growth in like-for-like sales[1]. On the same comparable basis but at actual exchange rates, sales are expected to be 20% ahead.

Primark has performed particularly well in the UK where full year sales are expected to be 10% ahead of last year on a comparable basis and our share of the total clothing market has increased significantly. After a good first half, third quarter trading was particularly strong in the lead up to Easter, benefiting from comparison with prior year results that were affected by poor weather and an earlier Easter holiday. Favourable weather in the fourth quarter and the strength of our consumer offering resulted in markdowns at lower levels than normal. Early trading of the new autumn / winter range has been encouraging.

In the US we have continued to fine tune our ranges, opened three stores during the year and extended the Downtown Crossing store in Boston by 20% increasing it to 92,000 sq ft. Our ninth store is scheduled to open next year in Brooklyn, New York.

The first half operating profit margin of 10% declined from 11.7% in the first half last year, reflecting the strength of the US dollar on input costs. In our interim results we explained that the full effect of sterling weakness against the US dollar would have a greater impact on margin in the second half because currency hedges maturing in that period would be at less advantageous rates. However, with the benefit of input margin mitigation and lower markdowns we now expect the full year margin to be better than the first half.

With most of next year's first half UK purchases contracted at the weaker sterling/US dollar exchange rate than the same period last year, there will be an adverse effect on margin in the first half. However, the strengthening of the euro against the US dollar in recent months will have a beneficial transaction effect on Primark's eurozone margins particularly in the second half of next year if these rates prevail. With some cost increases and markdowns returning to a more typical level, we expect full year margins to be similar to this year.

This year's increase in the scale and breadth of the Primark estate was very strong: 1.5 million sq ft of selling space and 30 new stores were opened across nine countries. This brings the total estate to 345 stores and 13.9 million sq ft at the financial year end. Eleven stores were added in the UK; three in each of Spain, France, the Netherlands, Italy and the US; two in Germany and one each in Belgium and Ireland. The fourth quarter saw the addition of 0.3 million sq ft with four stores added in the UK, our fourth Italian store in Verona and one in France in the Val d'Europe shopping centre close to Disneyland, Paris. Our city centre flagship store at Oxford Street East was extended by 40% during the year, increasing it to 114,000 sq ft. The stores in Sheffield and Reading were relocated to bigger, better locations and two stores have been temporarily relocated while their existing sites are redeveloped.

In the next financial year we are planning over 1.2 million sq ft of additional selling space. France, Germany and the UK will see the most space added and overall we will open 19 new stores together with a number of relocations and extensions. The larger stores will be in Stuttgart and Munich in Germany; Toulouse and Bordeaux in France; and Antwerp in Belgium. Following the investment in warehouse capacity over the last few years, no further investment in distribution is planned next year.

For further enquiries please contact:

Associated British Foods John Bason, Finance Director Flic Howard-Allen, Head of External Affairs	Tel: 020 7399 6500
Citigate Dewe Rogerson Chris Barrie, Eleni Menikou	Tel: 020 7638 9571
Jonathan Clare	Tel: 07770 321881

[1] 2016 was a 53 week year for Primark, British Sugar, Agriculture and the UK Grocery businesses. The effect on reported sales growth for British Sugar, Agriculture and UK Grocery was not significant but for Primark the reported sales increase at constant currency is expected to be 11% (13% on a comparable week basis), and 18% at actual exchange rates (20% on a comparable week basis).