



Dairy Crest – Final Results for year ended 31 March 2014

Interview with Mark Allen, CEO

Results

Q: Talk us through the key figures you're reporting today.

A: I guess there are four areas I'd want to talk about. Firstly, we've had a satisfactory year from a profitability point of view. Our profitability is up 31% to £65m; I'm very pleased with that. Behind that, our brands have performed pretty well. Overall, they're up 4% and that's against a 1% at the half year. We've been very successful in reducing our cost base, taking £25m out of the cost base during the year. That's particularly important in a climate that's quite difficult.

Finally, I'm particularly excited about the fact that we've launched our project to make demineralised whey powder. That's really exciting and it will improve our profitability by about £5m each year and gets us into the baby food market, which is fast growing and moves us to different continents around the world, particularly China.

Q: So how much of an impact have property disposals, particularly the sale of the Nine Elms site, had on these results?

A: This year, they've had an unusually high impact on the numbers and you'll be aware that we sold Nine Elms earlier this year and made a profit of around about £15m on that sale. That helps us, as we rationalise our doorstep business, to cover some of the costs of that rationalisation.

Q: Let's talk about your key brands, how have they performed during the period?

A: Let's start by talking about our spreads brands, Country Life and Clover. They've performed reasonably well in what is a very difficult marketplace. As far as Clover is concerned, Clover has seen slight value decline but pleasingly has got volume growth. That's good.

Country Life had a difficult first half where we constrained sales because of the high cream prices, but has responded better in the second half. Actually, Country Life Spreadable is the fastest growing of all the spreadable brands. We're very pleased about that.

Let's move on to Frijj and talk a little bit about Frijj. Frijj is a fantastic brand and has great potential, but over the last 12-18 months, we've constrained sales while we've been implementing new packing capabilities. That works' done now and we saw a much better performance in the second half versus the first. But we're really excited about the future of Frijj, since the capability is now there.

Then finally let's talk about the star of the show, Cathedral City. Yet again, it's had double digit growth in value terms and continues to outperform the market by some distance. It's a fantastic story and we're really proud of the brand.

Q: Now you've also introduced a number of new products this year. Why is that so important to Dairy Crest?

A: We are a consumer-led, demand-driven business. To be a business that focuses itself in that way, you've got to be able to match the ever changing needs of consumers. So a few years ago we set ourselves this challenging target that 10% of our sales should come from products that we've developed in the previous three years. I'm absolutely delighted this year that 29% of our sales, if we include the new milk bottles, actually come from new products. That's a great performance.

Q: Now you've made £25m of cost savings this year. How was that achieved and is there more to go for?

A: Cost savings are an integral part of our business, particularly so in the difficult trading environment that we find ourselves in at the moment where consumers are still financially stretched. We've achieved it through a range of things; by a real focus on trying to do things better tomorrow than we did yesterday. Examples would be the amount of money that we took out of our head office in the restructure, we've been very successful in buying better in certain areas. We've also invested in equipment to make us more efficient as we move product through our factories.

As far as the future is concerned, absolutely I can see way into the future that there are £20m each year that are capable of being delivered.

Q: So are you happy with your level of net debt?

A: The short answer to that is, yes. We are very comfortable with where we are. We've got some more capital spend over the next 12 months, then we'd start to expect debt to come down. That's a real positive for our business over the next three or four years, to get our debt even lower than it currently is.

Q: Now you've raised the dividend, but given the increase in our adjusted PBT, couldn't you have returned more to shareholders?

A: I think the first point I would make as far as that's concerned is actually there were a couple of one-offs this year. We've talked about Nine Elms as an example of that. So I think a 3% increase is in line with our progressive dividend policy but also gives us scope to carry on with that policy going forward.

Strategy

Q: Turning now to strategy, in what ways has the transformation into the single business structure of 'One Dairy Crest' benefited you?

A: Two ways it's benefited. Firstly, it's obviously taken a lot of cost out of our business, but secondly and probably the most important part of the business, it means that the company, instead of operating as two distinct divisions, operates as one business. You get the functional expertise that exists in those businesses being capable of transfer between the two. So it gives us real focus.

Q: So is Dairy Crest now in the shape you want it to be? Does it mean that investors will see lower exceptionals going forward?

A: Absolutely it's in the shape we want to be. If we look at our cheese business; a fantastic brand, well-invested facilities with an exciting project around whey. Great growth for the future. If we look at our spreads business; we've got a two factory position at the moment that will very shortly be one factory, and we've got lower cream prices which will improve the profitability. Then finally on our dairies business, we've completed our major investment there. We're investing additionally in Friji, or just about to finish that investment, and the prospects going forward look attractive there as well.

What all of that means, if you add it all together, is that you should expect lower exceptionals going forward.

Q: Now you still haven't made any significant acquisitions since the sale of St Hubert. Are you on the lookout or has your thinking around this changed?

A: We're always going to be on the lookout, but actually for us, or for me, the key criteria is are you going to get value from an acquisition? It's fair to say that we haven't found an acquisition so far that we think we can get an appropriate return from. What we have done though, is concentrate on our internal investments such as whey, where we know we can generate profitability and I would argue in a much safer way than you can with an acquisition.

Whey

Q: You've said you're excited about whey manufacturing. Are you still on track to start production next year?

A: We're absolutely on track to start production early in 2015. I think the thing that's really exciting me about whey is today, we're a UK-centric business, the vast majority of our sales are sold here in the UK. By having the whey venture, the demineralised whey, which is the base product for infant formula, it exposes us to new markets around the world. It gets us into the export market, it gets us into the growing economies of China, et cetera. It's very exciting for Dairy Crest's future.

Q: So what have been the developments in whey over the past few months?

A: I guess the first thing to say is the actual manufacturing development, the equipment is on track and we will be ready on time. The second thing and the exciting thing is we've chosen our partner. The partner's a well-recognised brand in this sector. They're already helping us with technical and engineering support and as soon as we've signed the contracts, we'll make a formal announcement as to who it is.

Outlook

Q: As competition in the supermarkets intensifies, do you expect increased pressure from your major customers to discount on price?

A: Well I think it's fair to say that the retail market has always been competitive. We've lived with our competition for many, many years now. We've talked already about our cost saving plans and those cost saving plans help us support that competitive pressure.

Q: Now you're in the process of rationalising the manufacturing of your butter and spreads into a single site in Kirkby, what's this going to mean of the business in the future?

A: Well two things. It means that we have one focus of expertise up in Kirkby and the second thing is it means it's an opportunity to lower our cost base. Therefore we're more able to compete in what is increasingly a competitive market.

Q: If we look at production quotas for milk, they're going to be abolished next year in the EU, what impact do you expect that to have across the business?

A: I think for us in Dairy Crest, a very limited impact. If I talk about the two main areas, so our dairies business and our cheese business I'll try and explain why.

The first thing, as far as our dairies business is concerned, it's very expensive to import milk into the UK. That's not a practical opportunity. I think it's also fair to say that British consumers want to consumer British milk. So I don't think it's a risk at all for our dairies business.

As far as our cheese business is concerned, actually there may be more commodity cheese produced in Europe, but that's why we've spent many years developing a strong brand in Cathedral City. That protects us from the commodity market and takes us out of that domain.

Q: So let's sum up. At this stage, what does the year ahead look like for Dairy Crest?

A: I think the thing we can't get away from is that the retail environment is going to be challenging. Having said that, if we concentrate on the things that we can do well, it should be okay. Now what are those things? Well firstly, developing our brands. Making sure we innovate. Making sure we advertise. Making sure we promote those brands.

Secondly, looking at our cost base, every day looking at whether we can do things better tomorrow than we did yesterday; be more efficient. Then thirdly, making sure we deliver the new projects that we have, the whey project, the project at Kirkby to close Crudgington into Kirkby. If we do those things and carry on doing those things well, the future looks good.

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