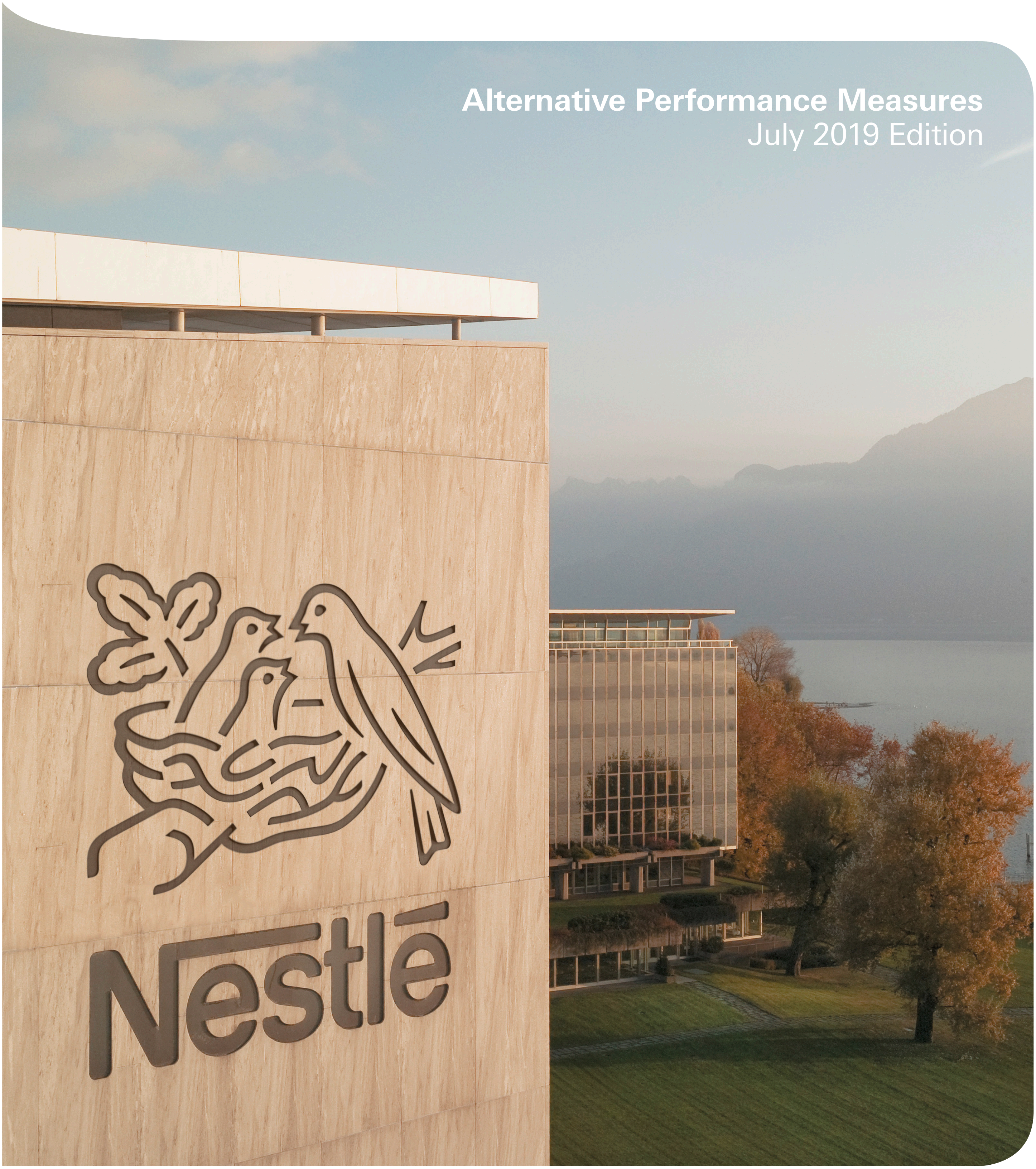
Nestlé

Good Food, Good Life

Alternative Performance Measures

July 2019 Edition



Definitions of Alternative Performance Measures

The Annual Report, the Half-Year Report and other communication to investors contain certain financial performance measures, which are not defined by IFRS, that are used by management to assess the financial and operational performance of the Group. Management believes that these non-IFRS financial performance measures provide useful information regarding the Group's financial and operating performance. Such measures may not be comparable to similar measures presented by other companies. The main alternative performance measures used by the Group are explained and/or reconciled with our IFRS measures (Consolidated Financial Statements and/or Condensed Interim Financial Statements) in this document.

Foreword
Evolution of the Net financial debt and Return on Invested Capital are presented only on a yearly basis as not relevant at the end of an Interim period.

Organic Growth (OG)

OG combines Real internal growth and Pricing and represents the growth of the business after removing the impact of acquisitions and divestitures and other changes in Group scope of activity, and exchange rate movements. This provides a "like-for-like" comparison with the previous year in constant scope and constant currency, enabling deeper understanding of the business dynamics which contributed to the Evolution of sales from one year to another.

In order to limit the distorting effect of hyperinflation, pricing in excess of around 2% per month (the level at which hyperinflation generally occurs) are excluded from OG calculations in hyperinflationary economies, with a corresponding adjustment in changes in exchange rates. The exception to this is Venezuela, which the Group excludes completely from RIG, Pricing and OG to eliminate the volatility due to this extreme business environment.

For purposes of calculating OG (a) the sales of an acquired business are excluded for the 12 months following the business combination, but incremental sales generated by post-acquisition expansion of the business are generally included; and (b) sales of a divested business are removed from comparatives for the 12 months prior to the divestiture. Supply agreements related to the divested business are included in acquisitions and divestitures during a transitory period. The pricing impact of changes in the way that a business is transacted in an entire country (e.g. establishing a local operating company instead of exporting to a distributor, or vice versa) are included in acquisitions and divestitures, respectively.

The effects of changes in foreign exchange rates are calculated as the current year sales' values converted at the current year's exchange rates, less the current year's sales converted at the prior year's rates.

Real Internal Growth (RIG)

RIG represents the impact on sales of volume increases or decreases, weighted by the relative value per unit sold. It is calculated at the level of the individual product reference (stock keeping unit) per distribution channel, by comparing the weighted sales (this year's volumes valued at the prior year's prices in local currency) to the prior year's sales. At the product level, it is therefore primarily driven by changes in volume, while when aggregated at operating segments or Group level, it embeds the impact of the evolution of the product mix.

Sales of newly launched products are included from the moment of launch which tends to increase RIG, while products which are discontinued have a negative impact on RIG since the historical sales continue to be included in the prior year comparatives. This reflects in a balanced way the impacts of renovation and innovation and the impact on sales coming from ongoing product rationalization efforts. In hyperinflationary economies, the sales of newly launched products are deflated to the price level of the prior year.

As RIG is a component of OG, it excludes the impact of acquisitions and divestitures, and exchange rates.

Pricing

Pricing is part of OG and represents the portion of sales growth caused by changes in prices over the period. It excludes the impact of RIG, as well as the impact of acquisitions and divestitures, and exchange rates.

Analyzing pricing allows management to assess the degree to which inflationary (but not hyperinflation, see Organic Growth above) or deflationary factors have contributed to sales evolution, and the degree to which cost changes have been passed to customers.

Evolution of Sales

The Group uses OG (including RIG and Pricing), exchange rate impacts, and the effects of acquisitions and divestitures in order to understand the Evolution of sales from one year to the prior year (either the increase or the decrease in the current year's sales compared with the prior year's sales, expressed as a percentage).

Total Group

	January–June 2019	January–June 2018
Sales (in millions of CHF)	45 456	43 920
Evolution vs prior year (in %)	+3.5%	+2.3%

The reconciliation of OG to the total Evolution of sales is as follows:

Total Group
In %

	January–June 2019 vs January–June 2018	January–June 2018 vs January–June 2017
Real Internal Growth	+2.6%	+2.5%
Pricing	+1.0%	+0.3%
Organic Growth	**+3.6%**	**+2.8%**
Effect of exchange rates	–1.2%	–0.5%
Effect of acquisitions, divestitures and other changes in Group scope activity	+1.1%	+0.0%
Evolution of sales	**+3.5%**	**+2.3%**

Underlying Trading Operating Profit Margin

Underlying Trading operating profit margin is when Underlying Trading operating profit is calculated as a percentage of sales. Underlying Trading operating profit is Trading operating profit before the impact of Other trading expenses and Other trading income (mainly restructuring costs, impairment of property, plant and equipment, and litigations and onerous contracts). See note 4 of the Consolidated Financial Statements of the Nestlé Group 2018 (www.nestle.com/asset-library/documents/library/documents/financial_statements/2018-financial-statements-en.pdf) for more details of Other trading expenses and Other trading income.

The exclusion of these items allows tracking and better understanding and prediction of the results due to the day-to-day trading activities under the control of the operational management in the business units. It excludes the impacts of decisions (such as factory closures, disposal of a piece of real estate, or restructuring plans) made in conjunction with Zone or GMB management, or litigations and disputes or events which distort the underlying performance due to their frequency or the unpredictability of the outcome.

The reconciliation of Underlying Trading operating profit to Trading operating profit is as follows:

Total Group

In millions of CHF except for Underlying Trading operating profit margin

	January–June 2019	January–June 2018
Trading operating profit	**7 058**	**6 391**
Add:		
Other trading income	(89)	(19)
Other trading expenses	804	691
Underlying Trading operating profit	**7 773**	**7 063**
Sales	**45 456**	**43 920**
Underlying Trading operating profit margin	**17.1%**	**16.1%**

Trading Operating Profit Margin

Trading operating profit margin is when Trading operating profit is calculated as a percentage of sales. Trading operating profit is a subtotal in the Consolidated Income statement, appearing above Operating profit. It excludes Other operating income and Other operating expenses. The items excluded from Trading operating profit represent the results of transactions and decisions taken at Group level that are largely out of control of management of the operating segments (such as acquisitions, disposals or strategic alliances), or the impacts of events which are irregular in nature and difficult to predict (such as wars or natural disasters).

Underlying Trading Operating and Trading Operating Profit Margins in Constant Currency

Profit margins in constant currency are calculated as the ratio between profits (see above) and Sales, adjusted to eliminate the impact of changes in exchange rates.

When comparing the year-on-year change in profit margins, it is useful to eliminate the impact of changes in exchange rates in order to isolate the results generated by business operations from the effect of translation of these results into Swiss Francs. This is done by converting both Sales and profits of the current year at the exchange rate of the prior year. The resulting profit margins can therefore be compared with the reported profit margins of the prior year to understand fundamental business trends.

The reconciliation of profit margins in constant currency is as follows:

Total Group

In millions of CHF except for Underlying Trading operating profit margin and Trading operating profit margin

	January–June 2019	January–June 2018
Sales	**45 456**	**43 920**
Retranslation at prior year rates	419	188
Sales in constant currency	**45 875**	**44 108**
Underlying Trading operating profit	**7 773**	**7 063**
Retranslation at prior year rates	64	31
Underlying Trading operating profit in constant currency	**7 837**	**7 094**
Underlying Trading operating profit margin (as reported)	**17.1%**	**16.1%**
Reported evolution (in basis points)	+100 bps	+20 bps
Underlying Trading operating profit margin in constant currency	**17.1%**	**16.1%**
Evolution in basis points compared to prior year as reported Underlying Trading operating profit margin	+100 bps	+20 bps
Trading operating profit	**7 058**	**6 391**
Retranslation at prior year rates	73	42
Trading operating profit in constant currency	**7 131**	**6 433**
Trading operating profit margin (as reported)	**15.5%**	**14.6%**
Reported evolution (in basis points)	+90 bps	–50 bps
Trading operating profit margin in constant currency	**15.5%**	**14.6%**
Evolution in basis points compared to prior year as reported Trading operating profit margin	+90 bps	–50 bps

Underlying Earnings Per Share (EPS)

Underlying EPS is calculated by adjusting Net profit attributable to shareholders of the parent to remove the effects of Other trading income and Other trading expenses, Other operating income and Other operating expenses, and related tax effects. An adjustment is also made to eliminate Other trading income and other trading expenses and Other operating income and Other operating expenses included in the Income from associates and joint ventures.

Underlying EPS reflects the underlying earnings from trading operations for each share of Nestlé S.A.

Underlying Earnings Per Share (EPS) in Constant Currency

Underlying EPS in constant currency is used when comparing the year-on-year change in Underlying earnings per share to eliminate the impact of changes in exchange rates in order to isolate the results generated by business operations from the effect of translation of these results into Swiss Francs. This is done by converting the Underlying EPS of the current year at the exchange rate of the prior year. The resulting figure can therefore be compared with the Underlying EPS of the prior year to understand fundamental business trends.

The reconciliation of Net profit to Underlying EPS in constant currency is as follows:

Total Group

In millions of CHF except for data per share or number of shares

	January–June 2019	January–June 2018
Net profit attributable to shareholders of the parent	**4 972**	**5 825**
Add:		
Restructuring costs	306	299
Impairment of property, plant and equipment, goodwill and intangible assets	333	384
Net result of disposal of businesses	95	(1 400)
Other adjustments in net other income/(expenses)	305	80
Adjustment for income from associates and joint ventures	134	153
Tax effect on above items and adjustment of one-off tax items	157	311
Adjustment in non-controlling interests	(4)	(7)
Underlying net profit	**6 298**	**5 645**
Retranslation at prior year rates	63	(62)
Underlying net profit in constant currency	**6 361**	**5 583**
Weighted average number of shares outstanding (in millions of shares)	2 954	3 035
Underlying EPS (as reported)	**2.13**	**1.86**
Underlying EPS in constant currency	**2.15**	**1.84**
Evolution in % compared to prior year as reported Underlying EPS (unrounded)	+15.7%	+9.2%

Net Financial Debt

Net financial debt represents the net level of financial debt contracted by the Group with external parties (e.g. bonds, commercial papers) after considering cash and investments readily convertible into cash. As per the table below, it is composed of the current and non-current financial debt, derivatives hedging financial debt and liquid assets less cash and cash equivalent and short-term investments.

Total Group

In millions of CHF

	June 30, 2019	June 30, 2018
Current financial debt	19 250	15 756
Non-current financial debt	23 735	19 847
Derivatives [a]	381	(77)
Cash and cash equivalents	(4 535)	(4 615)
Short-term investments	(487)	(2 102)
Net financial debt	**38 344**	**28 809**

(a) Related to Net debt and included in Derivative assets and Derivative liabilities balances of the Consolidated balance sheet.

The reconciliation of the year-on-year Net financial debt evolution as published (see comment in Foreword on page 1) is disclosed in Note 16.5 of the Consolidated Financial Statements of the Nestlé Group 2018 (www.nestle.com/asset-library/documents/library/documents/financial_statements/2018-financial-statements-en.pdf).

See Note 12.2e of the Consolidated Financial Statements of the Nestlé Group 2018 (www.nestle.com/asset-library/documents/library/documents/financial_statements/2018-financial-statements-en.pdf) for more details on the monitoring of the Net financial debt.

Adjusted Earnings Before Interest, Tax, Depreciation and Amortization (Adjusted EBITDA)

Adjusted EBITDA is used as a measure of the ability of the Group to generate enough cash from earnings to repay its net financial debt. It is computed as follows:

Total Group

In millions of CHF

	January–June 2019	January–June 2018
Trading operating profit	**7 058**	**6 391**
Add:		
Net other trading income/(expenses)	715	672
Depreciation and amortization	1 864	1 943
Adjusted EBITDA	**9 637**	**9 006**

When Net financial debt is divided by Adjusted EBITDA, this yields a ratio which is used to monitor the Group’s financing capacity.

Free Cash Flow

Free cash flow represents the cash generating capability of the Group to pay dividends, repay providers of capital, or carry out acquisitions, if any. As per the table below it equals Operating cash flow less capital expenditure, expenditure on intangible assets and other investing activities.

Reconciliation of Operating cash flow to Free cash flow is a follows:

Total Group
In millions of CHF

	June 30, 2019	June 30, 2018
Operating cash flow	5 159	4 399
Capital expenditure	(1 079)	(1 158)
Expenditure on intangible assets	(222)	(251)
Other investing activities	192	(106)
Free cash flow	**4 050**	**2 884**

Working Capital

The Group monitors average Working capital to evaluate how efficient it is at managing its operating cash conversion cycle.

Working capital is the sum of Trade Net Working capital, composed of Inventories, Trade receivables and Trade payables, and other components such as some Other receivables and Other payables, some Prepayments and accrued income, and some Accruals and deferred income.

The average of Working capital for the last five quarters is divided by sales for the 12 months immediately preceeding the reporting date to determine the average Working capital as a % of sales.

The average Working capital as a percentage of sales is determined as follows:

Total Group

In millions of CHF

	June 30, 2019: 5–quarters average 2019	June 30, 2018: 5–quarters average 2018
Trade receivables	9 819	9 504
Inventories	10 064	9 740
Trade payables	(12 956)	(12 103)
Average Trade Working capital	**6 927**	**7 141**
Other receivables	2 321	2 403
Other payables	(4 202)	(4 361)
Other elements of Working capital (a)	(3 428)	(3 224)
Average of other elements of Working capital	**(5 309)**	**(5 182)**
Average of Working capital	**1 618**	**1 959**
Sales on a 12 months rolling basis (b)	**92 975**	**90 584**
Average Working capital as a % of Sales	**1.7%**	**2.2%**

(a) Mainly composed of prepayments and accrued income (assets) and accruals and deferred income (liabilities).
(b) June 30, 2019: from July 1, 2018 to June 30, 2019.
June 30, 2018: from July 1, 2017 to June 30, 2018.

Return on Invested Capital (ROIC)

Return on invested capital is a measure of performance which integrates both measures of profitability and measures of capital efficiency.

The numerator is Trading operating profit before Litigations and miscellaneous trading income/(expenses), net of tax. This figure is divided by average Invested capital during the year. Invested capital is a measure of the operational assets used to generate the results of the business, excluding financing, tax and cash-management activities. Further details of the definition of Invested capital can be found on Note 3 of the Consolidated Financial Statements of the Nestlé Group 2018 (www.nestle.com/asset-library/documents/library/documents/financial_statements/2018-financial-statements-en.pdf).

Return on Invested Capital before Goodwill and Intangible Assets

Return on invested capital before Goodwill (GW) and Intangible assets (IA) is used to eliminate the distortions caused by the different treatments of goodwill in the past and internally and externally generated intangible assets. This removes from the analysis the impact of varying acquisition activities over time.

This measure is calculated by removing the average goodwill and intangible assets value from the average invested capital (see above).

The calculation of Return on invested capital is shown below:

Total Group

In millions of CHF

	January–December 31, 2018		January–December 31, 2017	
	Before GW & IA	After GW & IA	Before GW & IA	After GW & IA
Trading operating profit	**13 789**	**13 789**	**13 277**	**13 277**
Add:				
Net other trading income/(expenses)	1 732	1 732	1 494	1 494
Underlying Trading operating profit	**15 521**	**15 521**	**14 771**	**14 771**
Less:				
Impairment of property, plant and equipment	(500)	(500)	(391)	(391)
Restructuring costs	(651)	(651)	(673)	(673)
Impairment of intangible assets (excluding goodwill and non-commercialized intangible assets)		(122)		(152)
Impairment of goodwill and non-commercialized intangible assets		(626)		(3 039)
Trading operating profit before litigations and miscellaneous trading income/(expenses)	**14 370**	**13 622**	**13 707**	**10 516**
Tax rate [(a)]	(3 420)	(3 242)	(3 701)	(2 839)
Trading operating profit before litigations and miscellaneous trading income/(expenses), net of tax	**10 950**	**10 380**	**10 006**	**7 677**
Average Invested capital (Note 3.2)	32 274	32 274	32 654	32 654
Average goodwill and intangible assets (Note 3.2)		53 656		51 931
Average Invested capital, goodwill and intangible assets		85 930		84 585
ROIC	**33.9%**	**12.1%**	**30.6%**	**9.1%**

(a) 2018 figures based on the Group Underlying Tax Rate (UTR) of 23.8%.
2017 figures based on the Group Underlying Tax Rate (UTR) of 27.0%.

Notes