DS Smith Half Year Results
Conference Call Recording
04.12.14

<u>Speaker Key</u>

MR Miles Roberts
AM Adrian Marsh
FL Fabio Lopes
PB Paul Bradley
BD Barry Dixon
UM Unidentified Male
OP Operator
CO Catriona O'Grady

MR It's just after half nine, it's when we're due to start. I think all of the lines are open. Firstly, welcome. I'm delighted to see so many of you here today. I'm joined by Adrian, our Group Finance Director, and various other members of the team - Rachel, Hugo and Jonathan Nicholls, are here today as well. Welcome to our half-year results for six months to the end of October, and we're delighted with the performance. We're delighted to see another period of enhanced performance right across the Group.

But why do we have that delivery? It's because of our focus. It's our unique approach to our customers in how we help them sell more product. How we help our customers, like Nestlé, Unilever, Reckitts, Procter, how we help them sell more product at the point of sale in a retail environment that's changing very quickly, and how we reduce their costs. So we add value to our customers, and therefore, we've seen the growth in volumes, up to 2.3% in this six months.

That added value means we've increased our return on sales by 130 basis points to 8.9% in the half year. We've increased the return on capital by 170 basis points, so now getting towards that 14% figure. The free cash flow, conversion of profit into cash, saw a 44% increase on last year. And on the back of that, the earnings per share are up 24%, all at constant currency.

Thankfully, the only number that didn't go up was debt, and debt fell from over 800 million to less than 700. But very importantly, we've also continued to reshape the business, reshape our portfolio with the entry into the Spanish market, the fourth largest market in Europe, our first entry into it, which I'll talk more about later. And the announcement today of our entering into an exclusive arrangement under a letter of intent to acquire into Turkey and Greece, and that gives us a positive outlook for the future. Adrian.

AM Thank you, Miles, and good morning, ladies and gentlemen. I'm delighted to report that yet again, DS Smith has met all of our financial KPIs. Corrugated box volume grew by 2.3%, ahead of last year and in line with our target of GDP plus 1%. This was, again, achieved in challenging economies in Europe with positive momentum in every region, and notable strength in Italy and Central Europe, where our business is benefiting from previous investments.

Return on sales is near the top end of our target of 8.9%, a significant 130 basis points increase on constant currency. And return on average capital employed is up 170 basis points to 13.8%. The focus on cash we described at the year-end has resulted in a reduction of net debt of some £133 million, with resulting leverage of 1.6 times.

As we previously advised, our financial highlights have now been expressed in constant currency terms, which more accurately describe our business performance. Clearly, the year on year strengthening of sterling has had a big impact on the translation of our results, with some 80% of operating profit arising outside of the UK. We have, again, given guidance to try and help deal with this in the round.

On a constant currency basis, revenue has been flat, reflecting a greater integration of paper in the business, whilst operating profit has increased by 17%, resulting in the improved margin I have previously described. Profit before tax has increased 21% and EPS 24%, reflecting the overall higher operating profit and a reduction in our interest charge. We have, again, grown our dividend and have declared a 3.7 pence per share interim dividend.

Asset turnover and return on average capital employed are important measures for a manufacturing company, and whilst we're pleased with our progress, having an asset turn of 1.7 times and an increase of 170 bases points on return on average capital employed to 13.8%, we know there is more we can do to improve these. We believe this has been a good performance and demonstrative of our sustainable business model.

Going through the detail on revenue, the headline figures show a 5% reduction, but this actually masks some decent organic growth. We have used, as a starting point, the reported revenue, less the same adjustment we made at the year-end to strip out the zero margin revenue from sales of tooling, to customers and waste. And if anyone needs the specifics on that, I can describe that in some detail. But in essence, when customers ask for us to do certain projects and pay for the tooling for that, we charge them for the tooling, but we make no profit on it. So we have stripped it out of revenue and we did that at the year-end. This just makes it consistent with the previous half-year.

The largest impact on revenue is a translation back into sterling, which accounts for some 5.5% of the half-year movement. The £10 million taken out for acquisitions and disposals, principally relates to the disposal of a non-core phones business, which took place before the start of the period, plus the positive benefit from Italmaceri, our Italian business, where we took full ownership during the period. On a like for like basis, we've grown revenue broadly in line with volume growth, with a small positive from mix and non-corrugated volumes.

As with revenue, operating profit has had a big impact from currency translation, with around a 6% reduction on a like for like basis. Sales price mix versus input costs is broadly zero in the period, which reflects the way that paper prices have moved. Paper prices are broadly unchanged, period on period, although there have obviously been some small movements both ways in between. The £36 million revenues from increased total volume has dropped through to £12 million of EBITA, a similar ratio to prior periods, demonstrating the good organic growth that I mentioned earlier.

Lastly, you can, again, see the benefit of synergies. As a reminder, this is the final and third year of incremental synergy benefit from the SCA Packaging acquisition. There is a further €20 million to be delivered in the second half, and that will complete the programme. The effect of the organic growth, plus synergies, on the constant currency base after M&A, is an increase of 18%.

I've now cantered through the Group's revenue and profit, and you've seen the drivers for the Group wide improvement in margin by 130 basis points, compared to the prior half-year period. You'll no doubt remember that our profit does tend to be half one weighted, so it's typical for the half one margins to be slightly higher than that for the full year.

In the UK, the business has benefited from the turnaround programme at our Kemsley Mill. This has been a great benefit from the SCA acquisition, as we've gained some individuals with strong paper making skills, and this team has taken Kemsley from being loss making to profitability. Alongside this, our UK packaging business has continued to deliver market leading innovation for our customers, resulting in another good result.

The Western Europe region, for us, France, Benelux and Spain, has seen a decline in margins, but it's worth noting that they've improved from the full year. This broadly reflects the tough conditions, which we now feel have eased somewhat as the year's progressed. In the remainder of the business, margins have continued to improve, despite conditions remaining competitive, as always. We've seen the benefit of greater integration of our paper operations, and the reduction in use of kraft liner in our packaging business.

When we come to plastics, our US operations are doing very well, as are our rigid plastic operations in Europe. Our flexibles business in Europe is still in transition from the UK to Eastern Europe, although this phase of the restructuring has finished and we expect margins to progressively improve over the next 18 months.

Turning to cash flow, we have, again, stepped up our focus on tight cash and capital management, as we talked about at the year end, and our results are bearing witness to this with average monthly working capital to sales at an all time low of 3.4%. The benefits of our focus on cash are also represented by the £133 million reduction in net debt, which now stands at £694 million at the period end. Restructuring and integration costs are running slightly ahead of the P&L charge, as these mainly relate to the items booked in a prior period and a cash impact in this period.

As Miles will go on to describe, we actioned a number of small acquisitions and disposals, with a net £9 million inflow from proceeds in the period. The impact of Andopack acquisition will fall in the second half, which, coupled with the payment of a final dividend, will result, most likely, in a small increase of our year-end leverage from the 1.6 times we've delivered at the half-year, although our focus on cash won't lessen.

This is the slide most of you are familiar with, and for the majority, it hasn't changed since the full year. Depreciation is now expected to be in the range of £115 million to £120 million, a little lower than we thought at the start of the year. This is principally due to the FX translation impact, combined with a slightly lower spending on CAPEX in the first half of the year than we'd anticipated when we gave the guidance.

Our interest costs have reduced, due to the refinancing we undertook at the start of this half-year, resulting in an improved average interest rate. We expect the interest charge in the second half to be similar to that in the first half. The exceptional costs are unchanged, although if the disposal of the mill goes ahead, there is likely to be some additional charges.

Our dividend is a key measure of our returns to shareholders. This year, we'll have paid out in the order of £100 million in dividends, and today, we've announced an interim dividend of 3.7 pence per share, consistent with our progressive dividend policy. So to conclude, this has been a financial period where we've continued to deliver a strong and sustainable financial performance, despite tough economic conditions persisting in Europe.

I'm now going to hand you back to Miles, who's going to talk a little bit more about some of the particular commercial successes and actions in the period, and how that positions the business, as we move into the second half of the year. Miles.

MR Thank you, Adrian. We were going to talk about four key themes; commercial success, developing our offering, expanding our capabilities, and very importantly, about how we are focusing our capital and our investment and disposal strategy, to have the right mix of business. It's so important, what's underlined the success that we've achieved. But just before getting into these areas, I just want to reflect a little bit on what's been behind the half year, because the economic environment that we work in is pretty much unchanged from what we said at the full year.

It's challenging. We don't expect that to change over the foreseeable future, but of course, the challenge is; how do we thrive in that environment? Because packaging has never been more relevant to our customers than it is today, that's why you're seeing the improvement in the results. Because we're helping our customers sell more product at the point of sale, and we're reducing the cost that our customers face. And why is that important? Well, the retail channels in which our customers are selling their products are changing very rapidly.

So if you're a major brander, you can be very focused on the final consumer. The brand is the brand, the product is the same, but suddenly, instead of selling most of your product through a supermarket, suddenly, you're finding that I'm selling it online. I'm selling it through discount. I'm selling it through convenience. I'm selling it through big box. I'm selling it through supermarkets. And it's changing rapidly. So the format of the packaging has to support them at the point of sale; that is why we're winning with our customers.

And then how do they organise their supply chains to minimise the total cost of supply in a more complicated and changing environment? DS Smith has never been more relevant to our customers, that's why we're seeing the growth, that's why we're giving the confidence for the future, based on our unique focused supply cycle thinking. So behind that, we continue to invest in our company. And I'll talk about our M&A, it's all customer led. It's our customers saying; we want you in those regions because we're simply not getting what you have today.

And I'll talk about the growth in the regions and why we've been successful there. Leading packaging, a short paper position, one that's getting shorter. And a long, long, successful recycling position. So what has that meant? 2.3% growth in the six months. Difficult six months for many European economies, but growth higher than we had last year, so we're consistently growing, we're very focused, particularly in the food and drink sector.

And you think about that FMCG business, our volumes have never gone down from the year 2000. On any six month period to where we are today, right the way through the crisis, our volumes never reduced, so we're growing in that sector. It's resilient growth. It's growth that doesn't just turn on and off with the economic cycle. So we're building resilience into our customer base.

And the growth? All regions are in growth. In the UK, Western Europe, Central Europe, Eastern Europe, they're all in growth. So we're growing in France. We're growing in Germany. We are, particularly, growing very strongly in Central and Eastern Europe. But the markets that we've really enjoyed growth were the markets that came to us with SCA, because our customers wanted us to go there and they've rewarded us with more business. The growth is coming from those new regions, giving a totally unique supply to our customers, and that gives us the confidence to go into these new regions.

What is does commercial success look like? At our capital markets day we talked about this at some length, but it's worth just repeating. We have a company called Mondelez. It's one of the few that will actually allow us to talk very openly about this. I think they are just delighted with the progress and the difference that we've made to them. It's an exclusive deal with them. What they're saying is; we won't work with any other corrugated supplier whatsoever across Europe, in any market. Even in the markets that you're not in. We just want to work with you. Five years, and it ramps up over the year, continues to ramp up over the next 12 months, so by September next year, we'll be fully operational.

But the way we're selling to them, the way we support them, is on the total cost of their production, how we help them increase sales. And we're so confident of this, it's on a gain share basis. So we're very pleased with progress, and I have to say, it's very closely watched by many other customers as to the value we're adding them, and indeed, our whole communication and discussion with other customers is very encouraging.

So what is it about developing our offer? And I'm going to talk about those two areas. One about reducing total costs, and then we're going to come on to about selling more product. So developing the offer. One element of it we call performance packaging. It's a simple concept; you will hear other people talk about it generally. But this is about designing the box for the critical point of failure for the box, for its whole supply chain. So really understanding where the box has to perform at its maximum and where it doesn't. If you understand that point, you can design for it.

So it's moving away from selling a box on weight, which has been the traditional approach, specification on paper. That's the way that, by far, the majority, over 90% of our customers have traditionally bought boxes on that basis. And now moving along to a basis where it's the performance of the box. And because we have a short paper position, we're not trying to fill our mills. So we can change the paper grades to design the box according to the critical failure.

And then how do you manufacture the board, so that the board has exactly the strength that it should? This is built on all of the technology we bought from SCA. Technology it took them over ten years to develop. Two million tests to determine the correlation between the performance of the board and the way it's produced, two million tests over ten years, all IP protected. A live test on every single machine, so you know exactly the performance of that board. All the cost of this, the rollout, that's all in our results. And I can say, as one customer said; you've moved us more in the last year than we have moved in the last 30. That's about taking cost out of our customer supply chain. That's what gives us some of the confidence going forward.

But how do we get it to market? It's great having a good idea, absolutely marvellous, but if it's just sitting in people's heads, what's that route to market? So we said, when we bought SCA and we had the pan European footprint, we were going to set up a whole network of innovation centres, right across Europe. We said we're going to set up 40 of them. And to date, we've built 30. Unique, innovation design centres, all linked to a central development centre in Brussels that some of you have been to. So all the technology that we are developing through all of our systems can be applied to every local market.

So that's where we are today; t's actually 31, as we speak, today; and moving to 44. And you'll see there's a new one in Spain because our customers are saying; we want the same in Spain because we simply can't get it today. So if you're a customer, if you're sitting up towards the Artic Circle in the snow, or you're sitting down on a beach in Italy, you're less than two hours from an innovation centre. We know you get exactly the same technology wherever you are. There will be one in Spain. When we're in Greece and Turkey, you'll see the same platform in there as well; customer led innovation.

And then we talk about investing in our capabilities. This is an update on our plastics business. We said at the full year, we have a very strong plastics business. This is predominantly, not exclusively, but predominantly making the bags and the fitments that go inside cardboard boxes for the transportation of liquids with the world's number two supplier. The number one is based in the US, the world's largest market. We're in the US, Europe and the Far East.

We built a new factory in the Far East two years ago. We've announced three new factories in Europe, again, all customer led. We're closing two factories to roll into these. The new capacity is coming on stream, particularly in the second half of the year, reducing our costs, increasing our capacity. And if you look up in the top left, that's a new one facility in Chicago. It's just opened and the orders we have received get its capacity today to more than 50% of its ultimate capacity. All customer led, unique solutions, but we're really going to see the benefits of this come through in 2015. All on plan.

And what about management of the portfolio, the assets? I think this is one of the most important areas. Our strategy is long packaging, short paper, and a very strong recycling position. So everything that we're doing is around that. So how are we building into new markets? We announced the acquisition of Andopack. It's one factory; it's not far from Barcelona. It's a factory that's been built since 2003, so it's virtually a new facility. It's heavily under utilised. Spain is our fourth largest market. We've had it for a month, and I can tell you, from the customer feedback, we're absolutely delighted. And an innovation centre will go behind that new market for us.

We also announced the letter of intent to acquire into Greece and Turkey. We've had to announce this today because one of the businesses in Turkey is a quoted business, so they've made an announcement on their stock exchange this morning, saying they're in exclusive discussions with us, DS Smith, for us to buy this business. There are no other pan European suppliers there. There are none, none at all. Turkey, 80 million people, all of our customers going there. Our customers saying; please, go there, DS Smith, because we don't have a pan European player there. Please go. Support us in that market. 80 million people.

So there are five factories across the western seaboard there in Turkey, so a very nice position for us, customer led. It's the market leader in Greece, there are two factories and it nicely comes up under our Eastern European business. It's early days. We've still got to go through the due diligence, etc, but we feel very positive about that. And then we bought Italmaceri as well. In Italy, recycling, it's very important for our customers there; we developed that whole closed loop. It's a very strong player there; 500,000 tonnes of fibre collection per annum. It's completed, and again, we're very pleased with that.

But then on the disposals, disposing of non-core assets, the foams business, within plastics, part of SCA. We got a great price for it. Adrian talked about the proceeds, so we're out of that. We've received an offer for our Nantes Mill, paper mill, in France. We've gone to discuss it with the Works Council, and we'll see how that goes. That's 60,000 tonnes of capacity and as we said, we're looking to reduce the overall paper relative to packaging. So good moves to date.

So in summary, I hope our results are showing that we're winning with our customers, getting it right for them. And packaging has never been more relevant, and DS Smith never more important to our customers. That's what they're telling us. That's why the added value has improved, that's why the profits and the return on capital has improved. And that gives us the confidence to continue to invest and reshape our portfolio according to where we see the profit pulls of the future. That confidence has led us to increase the dividend by 16% for the half year.

Thank you. I'm happy to take any questions that people may have. I'll start at the front and come to the back.

FL Hi, good morning. Fabio Lopes from Bank of America Merrill Lynch. I have three quick questions. One on the dividend, 16% increase year on year. Should we be thinking about a similar rate of improvement for the full year? Is that the message underlying behind that? The second question is one related to your medium-term targets. 120% cash conversion. It's a pretty strong target and you've been doing it. What period in the future would it cover and what is the underlying driver behind that, because it looks again very strong? And the last question is; the increasing margin that's driven by the synergy, could you just give us a little bit more colour on physically where it's coming from, what measures are being taken? Thank you.

MR If Adrian takes the dividend and the medium-term, and I'll just talk about why the margin is improving, because there's a lot of churn underneath that. Do you want to take the dividend and the medium-term targets?

AM The dividend policy is that we will grow dividend in line with earnings for the year. We look at it at the half-year and we assess the interim dividend, and then when we come to the full year and we have the final year earnings, we'll look at it again, on that basis. So it's a very clear message. We have our cover measures, as well, but particularly what we're trying to do is to make sure that as we grow earnings, the shareholders participate on a similar basis. So it's nothing more complicated than that. So if you look at the way we expect the year to be earnings wise, you look at the growth rate there, you can have a pretty good proxy where you think our commitment will be.

In terms of the cash conversion target, you're absolutely right, 120 is an ambitious target. You tend to be able to achieve it and to deliver that when you have a big programme in place. Classically, as we went through the SCA acquisition and we were able to manage and really look closely at all the arrangements we had there. On a business as usual, it's ambitious to keep it. Something closer to 100% is probably more sensible on a business as usual. As you are, and as we are, looking at acquisitions, we think it's a reasonable target to set the business and to keep the focus.

Keeping a cash discipline and a tight cash focus is really important to us, so having stretching measures, not only Miles and I will stand up and describe, but equally, what each of our businesses will have to achieve is really important. It's covered in monthly trading with all of our divisions, we look at every aspect of working capital. It's a big, big measure for us.

MR Just on the margin, it is 8.9. There are a number of things. You've got to really look at the return on capital, I think, because frankly, anybody can generate margin at the expense of your balance sheet. And I think this industry has been a feature for this industry over the last 20 or 30 years. So we've improved the return on capital on more than the margin. It's a very important discipline. Why is it the 8.9? Just as a company, if you look at the portfolio of margins and customers, there has actually been quite a churn in our base.

And what we're finding is it's focusing on that added value and moving more towards this gain share. You've got to be confident of what you're doing, but we are. And you're moving away from selling a box on weight That doesn't do anything for our customers. It doesn't do anything. What you have to do is identify the value that you're adding to them, and then work on a basis where you've both gained from that, and that's quite a driver.

I should also say that the other added benefit from that is the operational leverage that comes through from it. So the margins start to improve because you're not just sucking in all this extra capital. That's back to that point of capital discipline in the company, so you really can get that operational leverage coming through. So 8.9, we're pleased.

PB Thank you. It's Paul Bradley at Citi. Just a couple of questions. The first one, just following up a bit on earnings. For the full year, should we be looking at the same sort of split as last year, the second half, the first half? In terms of the pricing environment you're facing, you commented that Western Europe is still rather challenging. What sort of pricing trends are you seeing in the other regions? And finally, your net debt to EBITDA is looking fairly strong. Even allowing for second half cash to be a bit weaker, the Andopack acquisition and such, aAt what level does it get to before we can start thinking about any additional returns to shareholders?

AM In terms of the earnings split, I think if you look back, historically, we're about 52% first half; 48% second half. When we look at our numbers and how we assess things, there's logic to that split, so I would be surprised if it wasn't broadly similar to that going forward.

Net debt, EBITDA, what level do we consider returns to shareholders? We're asked this question a lot. At the moment, our focus is on driving de-leverage as hard as we can, which allows us to participate in opportunities, like Andopack, like Turkey. There are a number of others, as we've previously described, at various stages of discussion. They come, they go, they come back again. We're very disciplined in what we will pay and these things take a while to unfold.

If we did nothing else and the business continued to de-leverage, clearly, from an efficient capital structure perspective, we believe around the 1.9 two times leverage on an ongoing basis is sensible to have, from an efficient capital structure, without looking to generate capacity to grow. So if we de-leverage significantly, then we would look to restore that through some sort of reallocation of capital, but that's not in the plans at the moment. Certainly, our corporate plan doesn't envisage it, because we've got so many opportunities at the moment.

MR There is a lot of opportunity, all customer led - it's always encouraging to see that. And on the pricing, if we look at Western Europe, the big market here, in France, the margin in the first half was below the margin in the first half of last year. It's actually above the margin in the second half of last year, so I think last year was a particularly challenging point in Western Europe. We're seeing those margins improving. As I say, we've been growing there; we're the market leader, and we expect those margins to improve.

But as you can see, the margins that we are generating are pretty healthy across the Group. There is no doubt, the pricing environment, just generally, is challenging. I'm just talking about the general environment with retailers. But we are confident in all markets that cost, etc, that we get, and the added value we provide means that we can be compensated for that. That's why performance packaging is so important. The same solution, in terms of performance; using less paper, great. We don't have to buy so much. So it's just thinking differently.

I think the old days of a paper focus are changing. It's the customer understanding, adding value to the customer in all those regions, progress to date and where we are. We have always recovered and we anticipate that going forward, it's as simple as that.

BD Thank you. It's Barry Dixon from Davy. Two questions, please, Miles. The first one; just run us through the assets that you're acquiring in Turkey and Greece, in terms of paper and corrugated assets. And the second question, maybe it's a follow-on in terms of the whole pricing environment. As you described the changes in the retail channels, if you think about a box that one of your customers puts into a discounter, where it is shelf ready, it's coloured, it's fantastically designed, all of that, versus a box that you might have traditionally bought your TV in, what's the differential in terms of the price of that box? And should we see a structural improvement in the corrugated box price over time, so that even though volumes might be flat or falling, you're going to get the revenue improvement by the actual price per unit, if you like, going up?

MR It's a very good, important issue. Firstly, Turkey and Greece. What we have are seven box plants. There is one modest paper mill in Turkey. It's not the biggest site, but there is a mill there. So when we look in that market, we've seen Greece come right down, but it's certainly returning. The Greek economy is starting to move forward. A lot of things with labour and the costs there have been restructured. So we have two box plants in Greece; one near Athens and one near Thessaloniki. Two very good plants. It's the market leader with 20% market share. It's well invested; we know the assets very well.

And in Turkey, we've got five plants going across the western seaboard, so really coming from Istanbul, down the western seaboard. That's where most of the economy is based for the rest of the country. To give you an example, the population of Istanbul today, just today, 18 million. It's growing at over a million a year. The projections of that city are to be 40 million people. It sounds a lot. It's just the same as the projection for Cairo.

Some of these cities are growing at an extraordinary rate, and these box plants are really particularly around that. As you know, Turkey is a big food producer. We know the assets very well, and our customers want us there. And when we go there, there will be some investment in there in the innovation centre, our technology, and also improving the asset base. There are some big companies there, but there's no other pan European. And this pan European supply capability is extremely important.

On pricing, it's so interesting, this change in the retail channel, because I'll say again, if you're a brander, you just don't know where your product is going to go. What's that channel and how are you going to understand the shopper at each one of those points, when you could be very focused on the consumer and how they use your brand? They've got to understand much more about the shopping habits of a person in each retail channel.

And here is an example of the discount. If you go into a discount store on your way home, because of their very low in store costs, their overhead is less than half the traditional UK retailer. Well, that's an 8% price difference to start with in the selling price, the product. 8%. Same brand, 8% less, simply because their overheads are 8% less. And the way they get that cost is using self-ready packaging and a few other bits and pieces, but it's mainly because of the shelf-ready packaging. So you go in there, everything is in shelf-ready packaging. Everything.

Now, if you understand the discount very well - they're very challenging on the prices, but the volumes are fantastic. The packaging is extremely high quality. So we focus on return on capital. The margin on that business is around about the average because of the quality, but the asset utilisation, it's just to dream of.

And that's the issue for this industry, over years and years. It's the asset turnover. Anyone can drive margin, but you've got to make the return on the assets. That's why it's so attractive. That's where you can get into online as well. So the pricing's okay, but the asset turnover, the operational leverage that comes from that, is extremely encouraging. The more people go to discount, the more boxes are sold. It's as brutal as that. I think the response from the majors will be to go more shelf-ready packaging, and we're already seeing that. We're starting to see that growing.

Looking at convenience. How do you serve a convenience store? You've got a full range of product in; but they've only got a very limited amount of space. So your shelf packing display has to be very precise, and you've only got moments to reload the shelf. So shelf-ready packaging is never more relevant than it has been today. That's discount and that's convenience. And obviously, with online, everything comes in a box. You've got all the different products that are going through it.

So how do you design a solution for every product? How do you send one of these – there's that very fancy plant with a long stalk?

AM An orchid.

MR Orchid. You get this great, long plant, don't you? And it comes, you buy it on the internet and a box comes, and it supports a stalk all the way down. Or you can buy a book. It can be thrown around; a hardback book, but you need packaging. Everything on-line comes in a box. So long answer to your question, Barry, but an important question.

BD Thanks. One final one. Just in terms of OCC pricing and maybe containerboard pricing. Given your exposure to the recycling market, what are your thoughts on OCC pricing and the impact that that might have on paper prices? Thank you.

MR Well, OCC, this is the old corrugated cases, this is fibre. It's been flat for two years now? We're heavily influenced by the Chinese market. The dollar's strengthening, so we don't expect OCC to change. It's been flat for two years and we see that being flat going forward. Coming back to this performance packaging issue, using less fibre in the paper, so you are reducing the demand for OCC per box; this is keeping that overall demand pretty flat, so pricing is flat. That's where we expect it to be, we're not seeing any real pressure on that.

And in terms of paper prices, they've come down, they've gone up, etc. At the moment, we've just had an extra 30 on testliner.

MR Kraft pricing has fallen because customers want recycled paper; they don't want kraft paper. So we're seeing falls there. So we've had an increase in paper costs in the last two months or the half-year, there were some reductions in the first couple of months. But we're not getting quite the volatility we've had in the past. Who knows? That's what we've seen.

AM Another question at the front, Miles.

MR One more and then we'll call it a morning.

UM Thank you. A lot of raw material costs have been coming down, as we all know. Is that important for your cost base?

MR We have seen oil prices fall; we've seen energy costs fall. It hasn't particularly affected us this year, but we are big users of energy. Not much effect this year as we hedge. But looking out over the following 12 to 15 months, then we expect those low energy costs could come through, if they hold. It depends what the weather does, etc.

AM and what happens in Russia.

UM It makes a meaningful difference to the bottom line?

MR Well, it hasn’t been in the half-year, but obviously, if this stays low we're big users and that will have a benefit, but we won't see that for 2015. We hedge forward because of the volatility.

AM So this year's pricing, substantially all of our input or non-paper input costs, are hedged and managed. So neither does the big spike costs us, likewise a big forward doesn't benefit us. We have a rolling three-year programme, so it's graduated. So we're starting to look out, going forward. At the moment, forward prices would imply a small year on year benefit at the moment, but the forward prices will come down and will change. If we have a milder winter, if Russia doesn't do anything crazy, then we could start to have potential benefit next year and the year after. But at the moment, we're looking at it flat.

MR Apologies, is there anybody on the telephones? There is.

OP Yes. We have two questions coming through on the phone lines. The first person is Catriona O'Grady from UBS. Please go ahead with your question.

CO Morning, Miles. Morning, Adrian and the team. Just three very quick questions from me. The first one is; can you give any numbers around the strong growth you delivered in Eastern Europe, in terms of volume growth, and define any particularly standout countries within this region? The second one relates to the paper mills. Obviously, you've signed the agreement, potentially, to sell one. Are there any more disposals in the pipeline in the back end of this year or early next year, or is it going to be a more longer term process? And thirdly, to build on Barry's question. Could you give us any colour on what percentage of your volumes are into online retail at all? Thanks.

MR Just in terms of Eastern Europe, we've talked about this before, about a target of getting up at the medium-term, getting up towards the 8%. And our growth in Eastern Europe is really incredible; it's been extremely strong. And we have, basically, built a new plant in Poland. And, frankly, we need another, it's as simple as that. Poland has been a strong economy. We're the fastest growing in that region. It's all customer-led.

It's all pan Europeans, and we're absolutely delighted with that support that we get. And again, that's why it gives us so much confidence into that whole region. We're talking about Hungary, we're talking about Czech, Romania. It's new for us with the SCA acquisition, so hence, we're just getting this whole step-up in performance. And as I said, that leads into the confidence in these other regions.

On the paper mills, we do have a stated objective. 70% of our paper needs come internally. That's been reducing. This is a further announcement, but our objective remains to get down towards that 50% level. It's so important for the flexibility for our customer solutions in this performance packaging. So we're not where we want to be, and that remains an ongoing target; either growing the packaging or reducing some of the paper.

And with online with some of the largest internet companies, we are, by far, the largest supplier. It started off quite small, but as you can imagine, that's growing very rapidly. And again, the European solutions, we actually have a slightly wider impact in the work we're doing here. It's being looked at further overseas, outside of Europe, in the solutions we're providing. So it's a reasonable part, in terms of a pure online, growing fast. Of course, a lot of online, particularly in grocery, is picked from existing stores.

So when you look at online retail, when you look at the growth there, if it's picked from store and it comes from the shelf-ready packaging, and we don't know exactly what that is. We know it's a proportion of overall sales for that retailer, so we have an idea, but for us, it can be the same channel. But on the pure online, it's growing very fast. It's a meaningful amount, but it is much more… a lot of the online is masked by that issue of picking from store.

Look, I think that's probably it. I'm very conscious of everybody's time. Just to say that we're pleased with the results. We're pleased with our progress. Strong profit volume and cash. It's because packaging has never been more relevant to our customers than it is today, and we don't see that going away. And we're supporting it with that rollout of the innovation centres. 30 built today, sorry, 31 built today; another 13 coming, to be completed into 2015. And on the back of that, we're very pleased to announce Spain, and the move now, subject to due diligence, into Greece and Turkey. I think our customers are as delighted as we are. Thank you very much for your time today.