DS Smith Half-Year Results
7 December 2011

Miles Roberts

Good morning, everybody, and welcome to our interim announcement for DS Smith, that's the last six months to the end of October. I'm joined, as always, with Steve, Steve Dryden, our finance director, and also from the company we have Gareth Davis who is standing in as chairman for DS Smith due to the absence of Peter Johnson, our chairman, who's, should have made an announcement about, so thanks, Gareth, for coming. We do have a very strict policy in the company, as many of you know, on things like health and safety. We're not expecting any fire alarms this morning, so if one does go off you'll see the fire exits clearly signposted, and as the old joke goes – follow me out.

So we're going to talk about, obviously, the half-year and our three main topics. Firstly, as always, it's the numbers; the numbers do the talking, and we'll be spending a lot of time looking at the results. Secondly, about the strategy; the results are built on the strategy, the consistent implementation of that, and lastly, we'll come and talk about capital discipline.

So I'm sure you've already had a look at the results for six months, but the corrugated volume is up 3%. It didn't tail off towards the end, it just keeps on coming every month. That means we're taking market share, and that's market share in every one of our principal markets. The margin, due to improving mix of the business, and the efficiency gains that we're making, has improved to 7.6% – that's an 80 basis point improvement. And our primary measure – this is what we're here to do; we're here to make a return in excess of our cost of capital, and that's increased to 12.9%. All of these results exclude Spicers, which is treated as a discontinued item; if obviously you put Spicers in there that return on capital will go more towards the 15% – just to show what's happening in the company. The earnings per share, again excluding Spicers, up 44%; the debt fell: the debt as a proportion of our earnings is now at quite a modest level and that, in conjunction with our very clear dividend policy, has meant that we have announced an increase in the dividend of 40%.

And on the strategy, the results come from the strategy – we have made a lot of progress in improving primarily the mix and performance of the Group. And there's momentum building – you know we are a company that's built on people, and you hear this often trotted out, but 90% of strategy is actually implementation. It's about building confidence into the people that we have, getting this culture of people wanting to succeed, and I have to say momentum is building in the company. The people's tails are certainly up. And on capital discipline – Otor's doing really well for us. We knew it was good when we bought it; it's performed ahead of our expectations, but I have to say there's a lot more to come from that. And we're investing organically behind customer-driven investment; these are behind packaging, short paybacks, attractive returns. At a time when many others are pulling back on investment, we've invested substantially more than we have last year. And there remain significant opportunities in a highly fragmented market for us to respond to the pull that we get from our customers to grow and develop the business.

Make no apologies – it's the same tune in terms of our strategy. This strategy is as applicable today as it was when we announced it exactly a year ago. Markets are difficult, but we've set a stall out which will allow us to grow and develop within a difficult environment. And we said, as a Group we wanted to achieve consistent GDP-plus growth, and it is essential that we have that to have a growing business. And to address the issue of cyclicality – to markets turned down when paper cycles changed, DS Smith continues to ride ahead of that and go on increasing profits and returns on capital at a time that, perhaps traditionally, the Group would have had some issues. And drive margins –

margins are the sign of a value that we had and the resilience of the business and as our primary measure, consistently year in, year out achieve above our cost per capital.

And so we have looked at our business mix, as you know. We want to come out of paper as far as we possibly can. Paper today – for this year, not a bad year for paper, represents less than 10% of our profitability. If you go back to 2008, that was just under 40% of the Group's profitability, both excluding Spicers, although the current result does include the mills that we intend to sell, or have sold and are closing.

On differentiation – how do we add more value to our products that allow us to consistently capture any increases in raw material energy costs? Steve will take you through that, but you see again, because of the value we've added, we're consistently able to retain and indeed grow our margins. And on efficiency, how do we ensure we're disciplined in the use of capital and operation efficiency? And again, we'll take you through the improvements that we've made there. I say again, the culture – strategy is about implementation: it's aligning all of our people behind what we're trying to achieve as a company, for themselves, for our customers, for the environment and for shareholders and providers of capital.

And all of this – how do we manage risk in this environment? You're looking at a company where we have announced the disposal of Spicers, and that'll be completed shortly. We have disposed of a paper mill; we are closing another paper mill; we've closed two factories in France and we've implemented Otor. This is about managing risk, and to demonstrate to you today how we've successfully done that across a number of areas in difficult market conditions. But first, Steve, the numbers.

Steve Dryden

Thank you, Miles. I think most of you know me: I'm Steve Dryden, the Group Finance Director at DS Smith. I think over the next few slides I'm going to take you through, obviously, the financial performance, but try and show you some of the drivers to that performance and, importantly, show you how we're delivering against the medium-term financial targets that we set ourselves.

And really, these results are about a consistent delivery of strategy that's actually leading to another set of strong results. There's really five real underlying drivers for these results. First of all, growth – we're growing our, we're growing our corrugated products business by 3%, but at the same time we are improving our margins. We're getting faster cost recovery – that's reducing the time it's taking us to recover the input costs, and we see this as one of the key drivers to trying to reduce cyclicality within this business. Our margins, Miles has said, they're up 80 basis points. In there you've got Otor integration which is proceeding well. Our operational efficiency, but also as we grow, as we grow volumes, there's some operational gearing in there, and I'll show you how that breaks down across our profit growth later.

And returns – returns above our cost of capital, ever so important; we set ourselves a target of 12% to 15% return on capital, with 12.9% there; our cost of capital is about 10%, so adding real value. Finally, strong cash generation – it's all about capital discipline, strong free cash flow, but then that's giving us the chance to reinvest in the organic development of this business.

So the income statement that you see in the presentation and in your packs is worked on a continuing basis, so that means it excludes Spicers. Then returns – if you look to the far right there, underlined, that's like-for-like, taking out the effect of the acquisition, the Otor acquisition that we did last year

we're up 11% on revenue, 22% on profit. So the underlying business is performing very well. Then on top of that, if you put on the additional benefit for four months of Otor, our headline numbers are revenue up 26%, operating profit of 41%. Then in terms of our key medium-term metrics – our return on sales is up 80 basis points to 7.6% – you'll remember we're trying to target 7% to 9% – and our return on capital is up 300 basis points to 12.9%. Again, we're trying to target between 12% and 15% return on capital there. And the excellent profit growth of 41% – well, that's flowing through to our earnings per share showing an uplift of 44%.

I think the thing to realise is that with the Spicers disposal, DS Smith is really a focused packaging business, and we're showing you here that we're growing and improving across the UK, the Continent, and in plastics. This focus is allowing us to grow revenue, our margins; the capital good discipline, particularly on working capital, is further improving the returns on capital, and I'll just take you through some highlights for each of those three divisions.

Now, UK's had a strong performance – revenue up 14%, profit up 25%, and importantly for this division which has historically struggled to achieve its cost of capital, we are now above our 10% cost of capital. Corrugated and recycling are doing well, and the paper business has been flatter, but that more reflects that our paper business is becoming more focused on internally supporting our packaging business. In corrugated we're starting to see the continued benefit of innovation, so volumes of R-Flute® were up 6% period-on-period, and the margin growth is due to a mix of some of our self-help or operational efficiencies which I'll talk about later, but also in terms of the procurements savings that are starting to come through, as well as what has traditionally been a very disciplined approach to input cost recovery.

And in this division, working capital is an absolutely major focus, if you actually think year-on-year we've managed an absolute reduction in working capital in this division, and that's despite us growing our revenues by 14%; I think that's a great achievement. In Continental Europe the largest influence in terms of growth is obviously the full year effect of Otor, which has been consolidated for a full six months. But the underlying business has performed equally well, particularly in Poland and in Italy, and it's all about putting through the necessary price rises to recover the input cost increases. The return of sales in capital – obviously both within our targets, but they're now on a… clearly on an upward trend, but we're also investing in new capacity to expand this business. Particularly, we're putting in a large printing capability in South-West France.

And finally, Otor – that had integrated well; I think you know the ultimate test is what's the return on investment for the last 12 months, and that's 14.8%, so in terms of the Otor acquisition, in terms of cash expended profit return, we've delivered 14.8%. And I guess that's a combination of several things. There's obviously the… it was a high-quality business we purchased; we're delivering on the cost synergies that we're committed to, but also, I think, it's true of the positive customer and employee reaction that we've had to this transaction.

And plastics – in terms of revenue and profit it's a solid performance, you know, it's incremental growth. The largest business in plastics is LP&D or Liquid Packaging and Dispensing or bag-in-boxes where you'll see it commonly, and really there we've got some really good new products coming on stream for customers like McDonald's and Starbucks, and that's really starting to come through in the business. But I think the interesting thing is to look at return on capital, so we've got a business of… it is growing, consistent margin delivery, but by focussing on the amount of working capital in this business, we've improved our return on capital year by 120 basis points to 15.7%.

I know it's discontinued, but I thought it was just useful to give you a quick update on Spicers. Firstly, in terms of the disposal process, if you remember, it was back in July we announced the potential disposal of the Spicers business. Since then we've received Workers Council approval; we've entered into a binding SPA with the purchasers; we received pension clearance, and we're now approaching the conclusion of European competition clearance, and we expect this to be, the transaction to be completed by the end of this calendar year.

Actually, meanwhile, the businesses continued to perform well in the first half of the year, but it's worth noting, behind that £9 million discontinued profit there's £1 million benefit by which we've stopped depreciating on the Spicers business when it becomes, when the disposal… we announce the disposal.

This is a familiar chart, really, where I'm just trying to show you the drivers that take you from last year's revenue or continuing revenue in our packaging business of £822 million to on the right here where we've reported for the first six months revenue of £1035 million. Really, you can see how just over half the revenue uplift is coming from the full year effect of Otor; the rest is all about sales price and sales mix. I think price is obvious – obviously, we're trying to recover our cost increases in full and quickly, and I'll show you that in the next slide. But mix is really about how we're trying to supply more complicated products that offer real value to our customers. I'm seeing here volume for corrugated boxed products is up 3%, or the £20 million here. Paper is down, but that's more as paper is sold internally into our business as we increase our integration levels and make sure that was supporting our packaging business.

So, really, same format for profit in the sense, on the left, our profit last year of £55.5 million; operating profit we're reporting here on the right, £78.3 million. And I think what stands out is just the scale in the first half again of the cost increases, you know, some 82 million of input cost. But again, we've achieved full recovery, and it's all about being incredibly disciplined in this area to make sure we recover our input costs. In addition, there's some volume benefit flowing through there of £2.5 million, and operating efficiencies, that's a mixture of the deficiency programmes we've got in the UK which are starting to come through, but also in terms of procurement. As you know, we announced on our procurement team, we're delivering savings and synergies there – that's really what's coming through into the operated efficiency. And lastly, obviously with acquisitions, that's the additional four months from Otor coming into the results, so finishing the first half at £78.3 million of operating profit.

Again, just trying to give you some perspective of how the return on sales has improved across the divisions, and hence for the Group, really, we've got a packaging Group here that's focused on profitable growth, cost recovery, and efficiency. Now this, I think, as Miles said in the introduction, the most important measure for us – return on average capital employed; averaged because it's the average of every single month in the year, not two data points; as you can see here across our three divisions and the Group where we're well ahead: we're into that target range of 12.9%, we're in that target range of 12% to 15%. Return on capital is a key measure for the organisation and it's a key measure in terms of our managers' incentive programmes, and that's why it gets real focus. And really I'd draw your attention to the UK: you know, 12.2%, I think, for the first time in quite a long time the UK is exceeding its cost of capital and adding real value to the Group.

So just really focussing on, just to give you some explanation on the bottom half of the income statement because we covered the operating profit drivers, net interest is higher – that's obviously the debt taken on to acquire the Otor acquisition last year, but it's also benefiting from the lower monthly working capital that we have. Pension finance charges lower, obviously reflecting a lower opening deficit, and that's really following the actions we took last year to close the scheme. Amortisation's

increased – again, that's largely flowing through from the Otor acquisition. Tax is around 28%; well, that's in line with the guidance that we gave you in June. Exceptional items – in here, there's basically the closure costs of the two paper mills that we announced in September and back last June.

I think the key thing here is there's a charge in the income statement but the actual cash effect is zero, because we've got disposal proceeds on the one mill we sold of £4.5 million to offset the cash closure costs of the mill that we're exiting of £4.2 million. So, yes, there's exceptional charge in the income statement; in terms of cash flow, it's cash neutral.

And just looking at that cash flow, net debt is really coming down progressively due to that healthy free cash flow. We're now down to a net debt EBITDA of 1.3 times. And if you think that will have the Spicers proceeds in before the end of the calendar year – you know we're estimating about £160 million there – that clearly puts our balance sheet into a very strong position: net debt EBITDA could be about circa 0.7 times. And then if you combine that with the new five-year credit facility that we announced in September, the sum is just over £600 million; you can see there why we feel that DS Smith is in a very strong financial position.

One area of cash flow that's particularly important to us is obviously working capital, and we've got, as you know, we have a target to reduce working capital to 5% of revenue, and actually we are, we're getting there – we're showing 5.6% here. And actually if you think about it – I'll show you on the cash flow – you know, an £8.5 million inflow on a business that's organically grown its revenue by 11%, just gives you an idea of the scale and the effort that we're putting in our working capital. In terms of the programme that we previously announced, we actually saved about £40 million on working capital.

And here's the cash flow which I alluded to earlier, you can see there the first red circle, that's the working capital inflow in the first half. In terms of capital expenditure, we're investing in a packaging business. We think we've got a great packaging business with really strong growth opportunities, and we're really confident about investing. We're putting in about £20.6 million of investment CAPEX. And really, what we're trying to do is provide our customers with the latest printing technology and box design, and it's supporting their requirements for more complex retail-ready packaging. Looking below that on taxation, it's higher than last year, obviously due to the higher profits, but also last year, you'll remember, we were utilising the tax losses that we acquired with the Otor acquisition. Dividends are higher, of course, reflecting the substantial increase in our full year dividend last year, and that's really just as we implement our dividend policy.

I talked about, at the start, about our strategic financial targets –though they are in terms of what we set out, we said we wanted volume growth of 3%, again, in our core business, our corrugated business, we're achieving 3% growth. I think the important thing there, as Miles said, that 3% wasn't just earned in the first month; it was delivered consistently month-on-month throughout the first six months of this year that we reported. Return on sales – at 7.6% that's up 80 basis points seeing a return on capital of 300 basis points to 12.9% – firmly within that range there. And operating cash flow to operating profit we want to be greater than 120%; we're 125%. And it's all about our focus on cash generative business model to allow us to invest and grow. Finally, net debt EBITDA 1.3 times, and that's, you know, that is a strong balance sheet and a great platform to go forward.

This is really just an update on the self-help programme; we really do call it self-help, because we view this as very much… in what can be an uncertain world this is absolutely within our control, to go out and deliver; and you can see the benefit of some of these programmes coming through in the profit slide. But we're on track; UK, we're on track to deliver £3 million this year. Procurement – we

upgraded that in the pre-close to £9 million; we're on track to deliver that. Otor cost synergies – another €6 million; we're on track to deliver that this year, and then compared to the £75 million working capital target we want to achieve, we're £40 million there. So I really feel, across those measures, which is self-help within our control, we are delivering.

And, hopefully, this is what it's about; this is why we're here: you know, we are implementing a strategy to deliver sustainable dividends, and as a result of the performance in the business and the delivery of that strategy, we're announcing a full-year dividend of 2.8 pence… sorry, a half-year dividend of 2.8 pence, and that's up 40% compared to last year. Dividend per share is up 40%, and that's after the dilution effect of Spicers coming out, and hence is on a lower continuing earnings basis, so we see that as a strong progression.

Miles Roberts

Thank you, Steve. As I said, we're going to talk about three things – the results and, as Steve, as always, has given you a very, very comprehensive review; we review these weekly, monthly, together, and I spend more time with Steve than I do with my wife, but… it's the nature of the job. And now we're going to talk about the strategy and the capital deployment, going forward.

So this is our strategy – just a brief reminder, we're talking about being the leading supplier; not the largest, but the leading supplier of recycled packaging for consumer goods. This is what we said a year ago. The reason it's recycled, so we're not talking about kraft mills; we're not talking about any of that stuff about plastics, woods, metals – we're not interested; it has to be recycled, because that's what consumers want. The consumers, not our immediate customer; it's our customer's customer. So it's the person Procter are selling their products to; they want to be recycled – it's a format of choice. And as Europe - I think the currencies devalue against other currencies, not only today, but probably over the next five to ten years – Europe simply will have to use more of the material it already consumes, and that's where DS Smith is focused.

That's why we want recycled packaging, and why consumer goods, particularly fast-moving consumer goods, is because it is the Procter & Gambles, it is the Danone's, it is the Reckitt Benckiser, it's these companies – they're fabulously demanding, and demanding means differentiation, which means profitability. But it also means very, very consistent demands; people don't stop eating and drinking. That's why we're focussing DS Smith as recycled packaging for consumer goods, and it does mean building the packaging and the recycling business. The recycling, not because you want the fibre to go into a paper mill, because it means we own the relationship with the retailer and how corrugated in the retailer… but the retailer's using more corrugated, improves their profitability.

And we own that relationship; it's so important to our packaging business, and we feel real opportunity to grow, not only where we are today, but in new markets, with… where we want to enter. So we have a long position there, packaging and recycling, and we are significantly reducing paper in absolute and proportionate terms to the minimum paper possible. It's not that it's a badly-run, it's just, for a shareholder it will never give you the attractive returns we feel our investors want to see, so we're coming out of it. Streamlining the Group – that does mean we have to be focused; we can't be all things to all people, we don't therefore… we can't build on the success of Spicers with the rest of the Group, and we've announced that disposal. And we believe, as we become more streamlined, there are significant opportunities to improve operational and capital efficiency in the Group. And as I said already, everything must be built by engaging all of our people across Europe, different cultures, different backgrounds, towards our shareholders' and capital providers' objectives.

But let's just look at the slightly wider picture. Because our customers want to serve them across Europe, so just surveyed all our customers – we had an outstanding response rate. I was quite taken aback just how many of our customers responded in full to our survey, and it wasn't all because they wanted to say some perhaps less positive things, but absolutely fantastic feedback. What that's telling you is, they want a packaging company, which they're using to sell their products, to be more engaged; that's why they've taken the time; over 70% response rate, and they've come back and said, you know, DS Smith, you've got great positions in the UK and France, you really have, and we really value the service and the responsiveness and the interaction of your people. But, you know, we are looking for more innovation and we don't think you're big enough at the moment, and you need to be more Pan-European. We want you to come into these other markets and give us what you've got in the UK and France in the rest of Europe. We had very good positions in Italy and Poland, etc, very profitable, but they are smaller, so our customers want more recycled packaging and to use our expertise much more across Europe.

And why do our customers, the Procters, want that? Well, it's because the, our customers are selling their product much more at the point of sale. Years ago our customers would sell much more of their product spacing through advertising, but as we know today, the power of advertising we have on television, billboard, etc, is being diluted because there's so many more mediums which they can use. Therefore, they can't spend as much on each one, and therefore the power of it reduces. You've seen this in the results of some of these companies that are reliant on advertising income, and it's much more about the point of sale. So when you go in as a consumer to the retailer, you're choosing what product you want to buy much more at the point of sale. So it's positioning, it's price, the promotion, the product; the packaging is much more important, and this comes into shelf-ready packaging. And that's where we are very strong; the retailers are demanding more shelf-ready packaging; they can take cost out and they can improve the rate of sale of product that is well-presented on the shelf.

And in Morrison's recent results, new CEO – first thing he said: I really want to get this company working. What did he talk about? He talked about shelf-ready packaging – that's in his presentation. We need to improve our efficiency, not just in our cost, but in the rate of sale through using more shelf-ready packaging. That's in his presentation, but I'm not surprised it shows as one of the first things he said because he knows that's what he needs to get Morrison even better. And we can see here Carrefour, we're growing very well with Carrefour; Tesco continues to grow very well in terms of their use of shelf-ready packaging, and it is growing as we predicted.

And when we look at these major retailers, the economy is obviously in a very difficult position, and everybody's looking very closely at like-for-likes, but we've just put here on the left-hand side of this slide just how the absolute sales are going. What we're seeing here with Tesco and Sainsbury's last results is that they're taking market share. So when you look at our results and people say, gosh, you know, your volumes are up – yes, because our customers are taking share. Our customers, the big retailers, they use shelf-ready packaging and they're taking share in this market because they have the customers to support it. So you're seeing the highest presenting at the smaller stores, but the bigger stores become more powerful because they have the purchasing power, and that's been more important in the economic environment. That's why their sales are holding up so well in absolute terms, and we are focused behind them.

And the exposure to Eastern Europe, where customers like Tesco or Metro sector are going; they're going into Central Eastern Europe where packaging, use of packaging is much less than Eastern Europe. So we have our customers wanting it, our customer's customers growing and moving into regions of Europe which are growing even faster than Western Europe. That's the opportunity that

we have at DS Smith. And let's look at then how we have started to deliver that – where we have moved more onto the Continent we do have this acquisition of Otor; we bought it from Carlyle, the American PE specialist who owned it for ten years – we are delighted. We've… the reception from our customers in the award of new work, that's part of DS Smith and we're part of Otor – there's been significant contract wins there. Work to our employers, in this, in France, and France has, as you know, a very distinct culture and it's working with people. And we've had a really, an excellent alignment with everybody there. The health and safety… our health and safety records since we've bought the company – one indication, it's down over 30%, just working with people to get it right. Putting in the talent management processes, the opinion survey, all the staff surveyed remuneration structures aligning to shareholders' interest have all gone in. It was owned by Carlyle, but Steve's work has halved the working capital – halved. And we've taken a lot of cost out as well, and there's a lot more to go for as we integrate more and more. And as we've said already, in the last 12 months, a 14.8% return on capital invested.

nd how do we continue this momentum in the business? Well, we have expanded the recycling to Poland; we've started in Czech; we acquired a small packaging business in Western Russia close to our joint venture in the Ukraine – we acquired it from SCA and paid €6.5 million; it's in the Krasnodar region. The return on capital in the first, since we bought it three, four months ago, has been absolutely outstanding. It's small, but again, a superb reaction from our customers. And we continue to invest: our capital investment is significantly ahead of last year, still below depreciation. As we said, it would be aligned behind strategic investments; we got some outstanding capabilities coming on in printing, die-cut and improving the performance, particularly of some packaging grades, more on white top to take share from kraft into recycled papers, all with very attractive paybacks, and really looking forward to them coming online.

And then how do we build our margins in terms of focussing on our customers? Commercial differentiation - our service levels, we believe, are the best in the industry for on-time in full. We've improved them significantly; we're good at quality, but we are not where the industry needs to be. It's very interesting to get positive feedback, but I know how these FMCG guys work, and they are at a different level in terms of quality and service. We're very good in the industry, but there is substantially more to go for, and frankly, they will pay for that as well.

So we know we can improve here; we are putting the coordinated management of Pan-European customers, we've started – we're good, but there is substantial opportunity to improve that. I'm looking at our sales and marketing plans for our customer. For the industry, they're good; not really done, not really presented before – new; so very positive response from our customers, but, you know, I know how our customers work, and I still say we're in the bottom half of performance relative to what our customers are doing. If we look at how we sell and market our products compared to how Procter sell and market their products, we're good for the industry, but there's a substantial amount of improvement we can make, and that we are making.

We're rolling out another impact, an innovation centre into Poland, building on the success of France and the UK. We are starting a new technical centre in the UK as well – all aligned behind our customer's requirements. We continue to roll out R-Flute® 6% period-on-period volume growth in the UK despite the substantial market share gain that it's already taken. We're good for our industry, but we can be a lot, lot better here. And as, of course, you'd expect to see if we are that good, then we should be seeing our market shares go up, and here we are: corrugated volume we grew 3%, the market grew 1%, and that's again a sign of how we're doing in a difficult environment.

We've already touched on this, but I think many people are wondering, well, we're in a different situation, the paper cycle is going down – I mean, frankly, goes up, down and sideways – who knows where it's going to go. All we can do for our shareholders is make sure we have the minimum exposure to this type of business. And this shows where our profits were made this year – paper's not having a bad year, and we're seeing about 10% of the Group's profits. Go back to 2008, that's just under 40%; we are closing a mill; we have sold a mill, started consultation, reduced further to the minimum paper we need to support the packaging business. So we expect paper prices… they've fallen slightly, we think they'll probably stay there – I don't think there'll be any major collapse, but from a profit point of view, it's not a big issue for our shareholders.

Again, with our cost-savings, we've talked about improvement in our efficiency. This isn't efficiency in terms of improving run speeds and our labour efficiency and weighted – that's just being in the game. This is about structural cost change in the UK as we bring it together, working in a way that we haven't worked before, working in a way that will fall to the bottom line and we're well on track with that for April 2014. Significant further progress we've made this year; procurement is working extremely well; the key to the procurement, putting the team in place – we've got an excellent head of procurement who joined us six months ago, we built the team behind him, but getting the organisation aligned behind this is working very well indeed. We've talked about the Otor synergies, again, all coming as planned, and on capital efficiency, working capital, the teams around that again all occurring very nicely and on track, as we've announced.

And the strategy implementation, as you know, it's, it is about our people, and we've done an enormous amount of work here. You know, just getting the right degree of trust and support and challenge with everybody who works in the company, communication – what I'm telling you today has been broadcast throughout the company. We've written to everybody today already; it all falls into their one-, two-, three-year plans, getting a lot of buy-in for that. The way we appraise people with the talent management promotion reward I think is working very well, and this is building our new structure which we announced last year – that's now all in place. This is a much more robust business structure; people management, it is one that is very scaleable as we proved with Otor, and how it'll enable us to grow further with a minimum risk in the future.

So our outlook – confident about the remainder of the financial year; we said it today, we said it two months ago, four months ago, eight months ago, and a year ago. People, it seemed, thought it was quite bold when we said it to begin with, but we were confident, and we still are. Some things are very important when we look ahead, because the markets are very difficult, but for us we're saying most of our business is in FMCG; people don't stop eating and drinking; we do have a lot of improvements coming through in our packaging business. Yes, paper's coming off, but we think that we can position the Group very well, that we continue to develop towards our financial objectives that we've already outlined this year and next year. And the reason is, we do have good market positions; there's real momentum in the business; our people and our infrastructure are being heavily invested in today to ensure we have a good future. We have a very clear strategy for growth and there's increasing capability being built into DS Smith every day that goes past. Thank you for your time.

Questions and Answers

Myles Allsop – UBS

Yes, Myles fromUBS, there's a couple of quick questions. Obviously it's a very sort of positive story, so maybe the first question is, what could go wrong? What do you see as the kind of key risk here? And when we're looking at the cycle, clearly that's rolled; waste paper costs maybe point to further

downside risks with some test liner prices. You've got the SAICA machine starting up at the second half of this year – what do you see as the biggest risk to kind of the earnings?

Miles Roberts

I mean, we… no company is immune from the macro issues, and as everybody knows, the whole sort of Eurozone issue is an issue every company has to reflect on. As I said, most of our business is in Northern Europe; we don't have anything in Spain or Greece; we have a business in Italy – it's less than 5% of our investments, so we are principally Northern Europe. But clearly a breakdown in the European monetary union would be difficult for any company, because now just don't know how that's going to work out. Our fear is their, the trade barriers they've built between various countries in Europe because we're heavily reliant on buying paper from Germany, and if their input duties… now these may seem a little extreme, but, you know, when you look at long-term investment, these are the sort of risks that you start to consider. But I don't think we're any different to any other company.

When you come down to where we are specifically, the market is difficult, volumes in terms of industrial packaging, I think are, you know, flat to 1%. And whilst…therefore what's going to happen to companies that are within those markets? Are they going to come and, try and come into FMCG sector because the volumes are so strong? That's why we're investing; that's why we're pushing innovation and building the barriers to entry. You've mentioned about the paper cycle – you know, I don't want to sound, sort of, in any way take this issue lightly, but, you know, we're working hard to make sure that DS Smith is a converter, and frankly, if the price of paper goes up or down, we're looking to pass that on either way. We have shortened our contracts – if it comes down it comes down, eventually that goes back to the customer; if it goes up it goes up, and we recharge the customer. The issue is our exposure to paper ourselves, and as I said, that's less than 10% of the Group, but there is clearly an issue there that we have to deal with.

You've mentioned the SAICA machine – you know, in a funny way, that increases the supply of paper, and for a company that's extremely short of paper that's actually not a bad position. We have fully factored in there any effect that we think it may have in the short term in the UK; they're in our numbers. And, in fact, they're also in the numbers in the half-year because they've already started to build their position in importing paper from Spain. The issue for our shareholder is, how exposed are we to paper? That's the fundamental thing. We are not out of it, we still have a path, but this is where we're clearly affected, but we still feel we can deal with it.

Myles Allsop – UBS

Two quick follow-up questions. First of all, I mean, the, you're obviously confident in the next sort of five months, sort of financial year 2012, I mean, how confident are you in making further progress in 2013 when you kind of… we're obviously just touching your target range in terms of retirement capital employed and EBIT margins. I mean, are we going to just touch and then fall back down, or do you think we can actually push further towards that 15%, I suppose?

Miles Roberts

I mean, what we can say to our shareholders is that markets obviously are difficult, just generally. We have a very clear strategy, and we think we're positioned to deal with those challenges. We're not over-stretched on the balance sheet, we've got a lot of improvements coming through, and today the City is expecting us, this year, to have a significant improvement in profitability and return on capital, and next year the City's expecting us to make further improvements. Now, if we had any concern

about that, we wouldn't have those targets out there. So what we're saying is, yes, it's difficult… now, this is groundbreaking for DS Smith, to get this sort of rate of improvement when we will be in the depths of a, probably a margin squeeze on paper. But that, as a company, is where we are. Steve, would you add anything?

Steve Dryden

I would. Yes, we stand behind those medium-term targets. You can debate the financial metrics of a falling selling price, but in the past that actually helps margin. You know, you can… there, but ultimately that's 79%, 12% to 15% return on capital. We think we're positioned in markets that will let us in there providing we give out the service and the quality.

Myles Allsop – UBS

So you're still confident in that kind of 2013 progress?

Steve Dryden

Absolutely.

We measure the progress that we're making on the UK efficiency, on the procurement. The working capital has more to do there that will help the return on capital you can see in terms of the Otor synergies coming through. There's more… there's three last year, another six this year – the overall target is still there at 13. So that's why I quite like that self-help because we can all wonder about what will happen to Europe with the paper cycle and, frankly, it's quite hard to guess that, but we do know what's within our control on costs and working capital; and those are the things that will help underpin, frankly, us getting and staying in that 7% ROS and 12% to 15% return on capital range.

Miles Roberts

It's quite interesting talking to our customers and these, one-, two-, three-, four-, five-year sales business plans, because they're new for the industry, and certainly new for us. Our customers are very surprised when we're turning up with them. And it's quite… it's a very interesting response, because if you're a big company, that's involved big FMCG, I have to say I think they are equally as concerned about the security of supply and the quality of supply for their brands. That's what we're talking about, their brands, not just about the next six months, can you check your price and have a couple of pence? It's a different… I mean, you have to be competitive, of course you do. I mean, you know, it's never been any different and it never will be. But actually what they want are good quality suppliers who are genuinely aligned behind the packaging and will continue to invest.

You know, we've just announced some investments in our half year... I mean, just that capita saying you're increasing investment, yes, when most people are backing off. No, we're increasing it, at least in areas that we think are right for you over the next few years, and they're prepared to give us longer-term… we've got short-term pricing, but much longer terms in terms of visibility. And I think it's quite interesting when you look at our customers and how they are seeing the economic environment. And, yes, they need competitive pricing, but what they want are secure, long-term suppliers who they can build a genuine relationship with, which will always be challenging.

And what they're very concerned about are companies with high debt, high gearing, who haven't been investing, and are they going to be here in one or two years' time? Because if they're not, will they

have a problem? And if you want to see how that problem manifests itself as our big customers come into fewer and fewer, but larger facilities – we have 80%, 90%, 100% sole supply – it's… I think this relationship's going to change further. And we are, as a company, determined that we grab this degree of trust with our customers because that will mean security of volumes and returns to our capital products.

But it's a different way, because we don't want to sell paper, we don't want to sell it. We don't go, oh; we don't say, look how many tons of paper there – we don't want to sell the stuff. Now I've got to be careful – we've got a few of our paper guys listening in with us, but we don't want to sell it – it's not in our interests. The minimum we can sell, the better we are because we have to buy less; so a very different relationship.

Myles Allsop – UBS

It's the very last question – on the sort of acquisition from obviously the balance sheets in a strong position, you're ready to make moves, you're talking about going to be customer-led. Are customers wanting you to have a Pan-European footprint, or are they more focused in terms of particular regions? Are you seeing acquisition opportunities at sort of prices coming down, the right sort of opportunities? Are we kind of on for a fun 12 months ahead?

Miles Roberts

Our customers are pulling us into new regions, and the big region is Central Europe, that's the big region for us. We have very clear financial targets. It's true to say there's a lot around in the Press; we have walked away from some, couldn't comment on them, but where we feel we just can't make the right return interests, and those businesses haven't been sold. It's up to the seller what they want; we're always very clear. I think in this environment opportunities could come out, but, you know, we're very clear where we want to go and what our customer would want to do; our ability and returns we want to make, and frankly, if things happen, great; if they don't, they don't. You know, there's nothing more I can really say at this stage.

Myles Allsop –UBS

When will you decide whether… and your balance sheet's too strong and you should return more cash to shareholders? I mean, what's that kind of waiting period of kind of looking for the right opportunities, what should we expecting.

Steve Dryden

12 months.

Miles Roberts

Tell us before we thought of it. The… look, you know, we're a fully responsible company, we understand capital discipline, balance sheets, strengths of balance sheets, etc. We have no desire to run a long-term inefficient structure, but I have to say for DS Smith and our shareholders, when we post up those sorts of returns from Otor, shareholders, they say to you, you keep the money. So if you can get those investments, you invest, we're very happy with that and there's no plan for immediate returns.

Robert Eason – Goodbody

Hi, it's Robert Eason from Goodbody. Just a question on volumes – you're saying the volumes are up 3% - can you just give us a bit more colour on that in terms of how different it was between the different markets, number one; how it's evolved through your first half and maybe, you know, if you can just give us an indication how it's continued into, you know, the second half. And also, in relation to volumes, how your market share gains have varied by markets? Like, has it been better on one than the other? And just on the pricing issue again, coming back to earlier questions, you know, we've got container board down €80 per ton approximately, and you know, a good rule of thumb has always been, you know, every €10 per ton is a percent of box pricing. Have you seen box pricing already come under pressure from your customers, or are you holding onto a better than in previous cycles because you are moving your customers up the value chain?

Miles Roberts

You know, if we just cut this up a bit on… I know Steve will have some views. If I just talk about the volumes, and if you can perhaps pick up on the pricing – the pricing, Steve. We've made 3%, and there are some differences in there as you'd expect. We've always said that 3% is GDP plus 1% – that's what… that's where we came from; when we set that GDP we thought it would be closer to 2%, maybe it's more like 1% to 1.5% now. And the reason for that is the growth of shelf-ready packaging, growth from major retailers, etc. And, pretty roughly, the way we've seen the business is pretty much expected: FMCG has grown very well, way ahead of that 3%. But industrial, which is about 25% of our turnover, of our volume, that's been more like a 0% to 1%.

Now, during the six months, at the end of the six months or the start of the six months, the volume like-for-likes were pretty consistent in terms of that 3%; there wasn't any major move from that, but it is that mixture. And then you look into there, and there's no doubt that on the Continent, where Carrefour is so far behind France, we've seen higher growth on the Continent than we have in the UK, simply because the penetration levels are lower and we're able to give France much more of the expertise, frankly, that we've developed in the UK working with customers like Tesco. It's given us a real first-mover advantage in France, and we know it's there in other parts of Europe. We have a joint venture in the Ukraine, and we're being pulled very hard in terms of support from there.

Now, coming to November, we look at things on a regular basis – you know, one month is always difficult to judge, but at the moment it's been pretty much that we've seen in the first half. The Continent has remained strongly improved, and the UK's been a bit behind, but FMCG has been very strong. Looking in the Press, I mean, it starts getting to weeks then, and then, you know, you get to a level of detail which is I think for shareholders probably misleading, because you can't put it into context. But we haven't seen… to date it's been pretty consistent. But we do work in an uncertain environment. What about pricing, Steve?

Steve Dryden

Yes, I guess the first thing is, you've got to be very careful in taking a very peak price, and was it ever really paid at that to a drop-off? So €80 at ten percent is not something I necessarily recognise, but paper has come off. But ultimately we're sort of quite pleased with that because we're net buyers. You know, that's the thing; we're net buyers of paper, so there's an input cost coming off – that helps us in the short term; it's a pass-through as customers see indices are put pressure. Our issue is to just to keep re-quoting and re-pricing on new and different products, and that's the thing about the FMCG versus the industrial: in the industrial you're designed to be locked down for months or years,

and they've got the opportunity to go out and re-quote, and it's not changing. And the FMCG, it's changing with promotions, pack sizes, etc, all the time.

So you've got the opportunity to re-price based on the value you think you're adding and, you know, cost is just but one component of that whole pricing debate. So I don't actually recognise the €80 but, equally, or this 1% on box prices, but we're not focused on whatever the box price per thousand square metres (KSM) is – it's how much value that we're making for a different box. How much printing are we putting in, and what's the box design, etc? Frankly, the more complicated it is, the better.

So that's not really our driver, I'm afraid, in terms of those rules of thumb which I think more apply to industrial side, which is, you know, a minority part of our business. And then, hence the other thing is this view of paper buys – that's why they put that guidance in our statement about it being about 10% of our expected profits for this year, just so you can see the effect of it on… you know, the impact on the Group, and obviously you can judge that that impact against the… some of the self-help that we've got to keep giving us momentum in the next year.

Miles Roberts

See, if you're fully integrated, the box price determines the profitability, because you start at the source and you produce all the paper and so the box, so your final selling price box, so price per KSM is very important. But if you've broken that and you're on the conversion, the price per KSM isn't so important because the KSM is a pass-through and it's the value added. So again I think this is the issue that we are, that everything's really central to our strategy and that's why suddenly a relationship with a customer is so important because you're converting and you're not looking at boxed price per ton of paper, whatever it is, because you're not making the paper; you don't really mind. It has moved that value added and it's a different way… And I have to say, it's an issue which we've spent a huge amount of time on in DS Smith about pricing and value add and getting these, so we've brought some people in from the FMCG sector to help us with the whole pricing and selling.

The reason we didn't have all these customer sales and sales plans is because, if you're trying to sell paper, you just want to sell the paper through, whereas that real innovation, etc, and that… it's just not so much part of the company and that's the challenge for us over the next few years. We're starting to see it in the results and I think you'll see it again and again and again, and I think that's when investors will look at the rating and look at our relationships from other companies and where you can actually… perhaps you've got some different dynamics here, but, you know, it's up to us to prove it and that's what we're going to.

Steve Dryden

Just to say again as well, we're trying to sell less paper, we're light-weighting; so actually our box price per unit is going up because we're trying to sell a lighter product and that's when the problems with this poor ton-type measurement methodology – it doesn't actually reflect what's happening in the business. And actually, in fact, what the customers want, because they want something that's lighter and more colours and that's a complete congruence to a producer methodology of measuring on tons.

Robert Eason– Goodbody

Sorry, just one last question just in relation to the cost savings. In the presentation, especially in relation to Otor, you've kind of used the words there's more to go for – is that… how conservative are,

you know, the targets you've set yourself especially in the context of, you know, the next 12 to 18 months are probably going to be a bit tougher than we saw at, say, six months ago, even? And, you know, how much more headroom are there on those specific targets which you've set on cost savings?

Steve Dryden

Well, I think the reality is we always say we can do more on cost, but we've set out a plan to, you know, deliver €13 million – did three last year and another six this year; we've got another four to go after. Let's focus on delivery of that as a plan and then, you know, we'll see who reacts specifically with the environment. I think it's very important to say to people, that was your commitment, €13 million – deliver that supply. Now things get tougher, we can always, we can review and revise that. You know, there's always a scope to react. But ultimately, I mean, if that was important, have people stick to the plan and deliver it than almost have a moving set of targets that you're not quite sure who's the chief, what and where. So we're really clear – we'll set out and delivery those and I think we're making great progress – a 14.8% return on capital is… I don't feel as if we are being slow or a slouch on this, I think that's a great set of returns. Let's deliver that and then we can always review.

Miles Roberts

On the more to go through item, principally on the commercial side, 80 times more integrated and we knew when we bought the business that we could improve costs, we could improve working capital, but equally the amount of capital expenditure and it's all in our planning, we can still make done, you know, it's not… it's going to be a few factories. There were key investments which we felt the business should make and we are putting those in, and I think, commercially I think we're going to do very well from, that's where I meant the more to come from – it's more at the front end, more at their industrial footprint and capability, you know, all within depreciation. But we just think we can, we can prove that whole offer into the market. Ross?

Ross Gilardi – Bank of American Merrill Lynch

Yes, hi, Ross Gilardi from Bank of American Merrill Lynch; so I have a few questions. So, look, it seems very clear, you've got a balance sheet now where you can afford to invest in this business when most of your other competitors are not in necessarily the same position, mature near market which is, you know, it's been difficult to earn a return when you start investing in a business. So how do you make sure you get paid for this investment that you're making, a new printing technology in France and how do you… how are you just thinking about balancing growing this company versus just milking it for cash over the next three or five years?

Miles Roberts

You know, the question, I think is absolutely excellent and it goes to the heart of many companies and how many times this year can we say I've saved it and then the margin's been changed? Not that I was expecting that to come to bottom line – it doesn't. And it's very… it's margin retention. You know, DS Smith, we used to call it costing, so setting a price, it's called costing. This has nothing to do with cost, it's got to do with pricing and value added and what's the value of the product to the customer? How do you assess that and how do you charge it? You're no different in your businesses. Look how much it costs you, but then what's it worth to the customer and your competitive vision? This is what we've been working on in DS Smith across the whole Group, and we've got so many examples of where we've done some costing without understanding the value that

we've added. And that means you've undercharged some customers and, frankly, you've overcharged some others so you end up losing them. So you end up keeping the customers, but, frankly, you're not charging enough to because of the service you're providing. And it's a whole way of thinking about the commerce in the front end we've done a lot of work on.

It is a very strict discipline and we have put in controls and procedures to allow us to very, very carefully understand that. And you can see it on that margin recovery that Steve put up and we had the same graph six months ago and the same six months before that. It's absolutely fundamental, this price recovery and margin capture. So I think we have the processes in there. When you come to capital it's very important… this is partly what I mean by investing capital strategically – there has to be areas where you're confident you're going to get the returns and the shareholder's going to see that. That's why we're here, that's why we're investing. And when you look at that you've got to be sure that you're going to retain that competitive advantage. Now we know how competitive the markets are, so broadly, we've moved the company from looking at a discounted cash flow over ten years.

You name me a business that lasts for ten years – I mean, I don't really know one. You know, being perhaps a little bit provocative, I don't know one. When you invest, how many investments go that way for ten years? I just don't know. That's the way the company's investing in paper, assuming for ten years… No, it just never happens so you've got to cut those out and we're focusing much shorter term paybacks so you've just got much less risk from macro issues and competitive issues, you're going to lose them; plus the pricing discipline, I think we're going to get those returns. So the investments that we're making in packaging are, not in all cases, but virtually, virtually all less than three-year paybacks. And they're not racy in terms of, you know, huge sort of volume growth, etc, even where upgrading paper we… the paybacks are half the time that I would say with the traditional paybacks in paper or even less than half (overtalking).

Steve Dryden

Yes, four or five years on paper; box businesses three years. I think that's the interesting thing. I think we're up against where we've got a competitive landscape where people are struggling with their paper long and will not be investing. And equally, we have an opportunity to invest in line with, in markets that are resilient, FMCG, and we can see, you know, good cash payback returns. And I think that puts us in quite a unique position in terms of the competitive landscape.

Miles Roberts

It's a process on margin, the OPEX side or the P&L side and capital discipline in terms of payback of it. And I know that's right because I used to work for one of our customers. I know how that customer thinks inside out. They don't make investments for more than three years because you don't know what the consumer is going to be doing. How many people put us in a deep recession three years ago, even six months ago. You know, so you've got to be aligned where your customers are and you can't have these massive payback periods when your customer's on a very short term. It's very interesting. I'm not surprised the industry doesn't make its cost per capital, when I look at the way capital is allocated.

Steve Dryden

I think so, the other thing, Ross, these are very portable assets. You know, we're not in the major high end of fixed infrastructure. If it's not working out well in Northern France we can move it to

Poland, we can move it to Italy. You know, these are portable assets; the customer demand isn't there – we can move it to where it is.

Miles Roberts

Can you unplug it, put it on the back of a lorry and drive it over to Eastern Europe? The answer is yes, then they're more likely to say, okay, then, you know.

Ross Gilardi – Bank of American Merrill Lynch

What is the penetration of shelf-ready packaging at Morrison's right now? Is it significantly below Tesco's and what… can you just give some sense as to what your existing relationship is with Morrison's? Are you collecting all their waste paper now already, or…?

Miles Roberts

We are collecting a lot of the waste but it's not all of it, though. We've won all of Sainsbury's recently, all of Tesco's, all of Primark, Next, Lidl, Marks & Spencer's, but it's for various reasons we don't have it all. But let's see where we get to, let's see where we get to. But their level of shelf-ready is less than Tesco. We were hoping to have all the statistics, actually for this meeting, but we actually have to go and do all the store research ourselves because the industry data just isn't there. And for various reasons, unfortunately we didn't have it ready today to say exactly what it was by retailer just because we have to do it. But… so therefore, we only have our own internal estimates which we're not allowed to sort of put up, is seen as… But it is quite a bit below Tesco but the interesting thing is it's improving quite strongly. You know, there is a, I know there's a slight change where there's a new CEO – interestingly, he's looking at that business, focussing on the supply chains, talks a lot about efficiencies, about getting the cost out. And if you just go into Morrison and you look down the aisle you can see that it's significantly less than someone like Tesco.

Ross Gilardi – Bank of American Merrill Lynch

Just on your recycling business, I mean, you're going shorter on test liner, but you're going longer on waste paper for the last three years. How did your recycling business hold up in the last recession and the OCC price continues to get hit here – I mean, can you sustain the absolute level of profitability that you have in the recycling business?

Miles Roberts

But just putting it into two parts and Steve will take us through the finance. The reason for the recycling being so long – we collect over 2 million tons a year and yet our paper uses less than 1 million. It's because it gives us the relationship with the retailer. So we don't just sell on we'll buy your waste paper, we will work with you to improve the use of corrugated in your stores and that will take X amount of cost out. That will increase the rate of sale on your shelves and will free up space from the back of store from the back of store to the front of store. And that will improve your asset turnover for your stores which is critical to a retailer. That's why you have that business. We've seen people in paper dispose of those businesses, yet to us it's such an important part of packaging. And that's the feedback that we get – it's a different model. Now, financially, it's even better, Steve.

Steve Dryden

Well, we'll make 6% to 7% return on sales on very little capital, so a fantastic return on capital. If you think about the recycling business, frankly, a major retailer knows how much the market price for waste is so, I mean, that's just charging a transaction fee. When you get down to very small individuals, stores or locations, you end up with that interesting dilemma that when the waste price is high they'd like to be paid something for it. When it's very low, they're paying you because they want to avoid landfill. So, you know, historically, as you look back that business has made a very, very consistent profitability and obviously excellent return on capital.

So we're not sat there worrying about the recycling business now. On top of that, it's, frankly, it's growing rather well for the reasons that Miles has said, that we're, you know, following our UK retail of customers out into areas like Poland and Hungary. If anything, we're in the numbers, we're taking an element of start-up organic because frankly, it's a pure model in terms of building. You've got exactly what you want with the processes and controls to meet what those retailers want. So we're very much now in a start-up cost; we may behind those numbers, but we're absolutely confident, we've studied profit progression, irrespective to how the fibre collection moves on a global commodity market.

Ross Gilardi – Bank of American Merrill Lynch

What do you do with all the waste paper? I mean, are you interested… have you got a paper producer that is short waste paper? Are you interested in locking into a longer term supply deal or do you like being more, you know, open to the volatility in the market? Those prices are going up and down, but you've got a lot of paper producers out there that are short waste paper, that will probably like more security of supply so how do you approach that?

Steve Dryden

I think people like security of supply in terms of the period of supply, but, frankly, most people reference to the external indices in terms of the price. And I think people do divorce period of price review to a period of supply. You know, we supply paper producers in Asia, Mainland Europe, private businesses, listed businesses. At the end of the day I think people recognise we're probably, because of our systems and processes, collect a high quality of fibre and hence, that helps them in terms of their products and processes, so we command a good price for that. But, you know, we're, effectively, we're happy to sell through, you know, the people that will use it other than China or Europe.

I think one of the advantages, if the retailer says I want to know exactly where that fibre is going, our systems give us that, good enough. If they say I want you to reuse all the fibre within a specific country such as the UK, we can do that, and I think that makes that model quite unique.

Miles Roberts

Harry?

Harry Philips – Evolution

Good morning, it's Harry Philips from Evolution. A couple of questions. In, just looking at your bridge charts, the… just looking at the acquisition contribution, it looks like Otor, the additional months hit a margin of 8.9% against sort of 9.4% last year. Is there anything sort of structural in all that or is it just a quirk of the few months that you had it in additionally for…? And then, second, in terms of the

paper business, I appreciate the comments that it's now less than 10% of profits, but clearly in terms of capital employed, I guess it's still 20%, 25%. Apart from obviously acquisitions diluting that is there anything more structural you can do to actually reduce that exposure or percentage content?

Steve Dryden

Well, first of all, as you know, we've got obviously pricing going through on Otor as it's recovering an input costs, so although the return on capital is over a fixed cash investment effectively, and I suspect that will be only the mathematical effect there, so we're not seeing any competitive pressure in terms of what Otor is doing and the products it's supplying, you know, it's very, very good in terms of those markets.

In terms of paper, yes, you're absolutely right about the capital investment. There's things I think we can do on inventory to bring down that capital base, and we'll probably have to challenge some of the receivables and returns that we're selling on relative to the margins we're making at different points on cycle and currently are very good on the procurement on the payable side. So there's things we will do; as you saw in the overall UK results, and they're driving down that working capital, it's something that we're doing across the UK and that's generally where our paper business is. So there's no… obviously, as you know, we announced what we wanted to do. We've completed, in terms of these results… you know, one of them's a disposal, the next one's a closure. So it's something, I think, that we're just continually working at, to follow that overall aim to improve our return on capital.

Hector Forsythe

Hi, a couple of questions; the first: interesting move, to see the acquisition in Russia. Clearly, that's thoughts in process of linking that to the Ukrainian business. Could you just give us a view, in terms of the state of the Ukrainian business, as to whether that might ever make a reappearance in the account?

Steve Dryden

Can I do that one?

Miles Roberts

Absolutely, and I'll be listening as well. We… just before we give that, we have bought that, and the idea is to tie them up, and it's worked extremely well. There's a big market there, the Ukrainian business is very profitable, 30% market share up. We own just under 50%, our partner owns just under 50%; he's been our partner for 15 years, he's the market leader in there, and, indeed, it supplies a lot of southern Russia, with a, you know, very good market position. So we have bought that. It's not a large investment; I wouldn't be surprised if there were some further investments, but at that sort of the scale, over the next one, two years, supporting Danone, Procter, BAT, Henkel, etc. And the…

Steve Dryden

…the financing. Yes, where we are… remember, we fully impaired the investment there back in '09 when the business in the Ukraine breached its local borrowing facilities. Those were, you know,

without recourse of DS Smith. So that was the background to it, and I guess we've been renegotiating since then.

A month ago we were there, in terms of everyone happy between the banks and the company, and then just before signing, the banks decided they would like to have an EGM where all the shareholders had the opportunity to comment on those financing arrangements, and that EGM occurs on 20 December, and we are looking to sign up soon after that. And that will enable us to revisit the amount of impairment we're holding against that as an asset, and from there we can then recognise the income on the… in the income statement. So we'll, you know, at the time we're doing that, that's the time to put out an announcement for people then to amend their models to include that.

But, you know, the business is doing really well. I think people should remember, although it's in breach of its covenants, it's… effectively, it's continued to make payments, generate cash and pay down the US dollar loan, and that's the agreement that we've reached with the bank. So it's cash-generative, profitable, strong market share growing, and, clearly, you can see the synergies from there. Buying a business in southern Russia and putting that into the Ukrainian business shows probably our confidence in that business, going forward.

Hector Forsythe – Oriel

Do you want to scale the sort of contribution that can make on an annual basis?

Steve Dryden

I think if you look back historically, which is the only forecast I can show… point you to, but if you look back historically, that was making, after tax, about £4 million.

Hector Forsythe

Our share?

Steve Dryden

Our share, in terms of our earnings per share. Now, what's actually happened since then – frankly, it's making more profit, but I think you'll find that the finance costs are higher in terms of what we're renegotiating with the bank. But the historical number's not a bad number for you to look at, and I think, from memory, about £6 million of after-tax profit's about 1p, so you can work through in terms of what that is, in terms of our earnings per share.

Hector Forsythe

Okay, thanks on that. Just, more generally, you made the point that, on the corrugated sector you've been taking market share. Have you been taking market share in the FMCG space? And can you just talk a little bit about customer experience: are you winning bigger take with customers? Are you winning new customers? Do you have new customers in your sights? What's the kind of rotation of those customers?

Miles Roberts

We're here to make… we're not focused on volume, we're to make money and therefore we have to add something; and it's not about getting into competitive auctions and stuff. You know, if it's just a straight fight on price, then you have to have something more. So the gains have principally come from expanding recycled into formats that have been… that other products have been occupying, plastics, tin, etc, but predominantly plastics, and that's where we're focused on growing the range of products. Because once you've expanded the whole sort of perimeter, the envelope, then you've obviously got more chance to grow again.

So it's actually been mainly a growth of our products taking share from other formats. And with some of our customers where, particularly with Otor, they said, well, we used to have those, but right now just take that over. But that's been the main way, because, frankly, that's the most profitable for shareholders – absolute win-win: win for the customer and a win for us in new business, etc.

Hector Forsythe

Okay, just a final question, then. Steve, could you just talk us through some of the cost base? In particular, I'm thinking about energy, as to how that's coming through in some visibility into next year, and your ability to keep passing that on. And so, as you're expecting at the moment, are you still putting up prices for your customers in terms of your supply?

Steve Dryden

Okay, in terms of energy, you'll probably see, as we look in the next year, we're looking probably at about another £5 million headwind there, where I'd have to say, as I looked most last month, that's started to ease off in terms of what we're seeing. But I think you'll find that for the whole sector, certainly in terms of papermakers across Europe, they're seeing year-on-year energy cost increases. And I think that's an interesting point about how far will paper prices fall, because I think there's cost pressures there from energy, and ultimately you have to believe there'll be cost pressure there on waste fibre in the medium-term because of the growth of markets outside of North America and Western Europe. But that's… energy is a headwind for us, and we're obviously trying to make sure our business is as energy-efficient as possible, hence some of the things we're doing and the investments we're making, undoubtedly focusing back onto one main site – paper's our largest user of energy – undoubtedly focusing on the main site and one very efficient site in the UK will actually help us in terms of our energy-efficiency position there.

In terms of cost increases, it's quite interesting; the… there's almost an atmosphere of, oh, well, prices are coming up, but, actually, if you look back from six months ago, and three months ago, prices are still… You know, energy costs, OCC prices, paper prices, you know, if you look back six months ago, they're still higher. And that's quite interesting. So we have a programme of going out with the customers on pricing. Now, that will obviously start to switch as the industries come off, and people, in terms of their contractual arrangements, you know, the lower industries start to come in. But, you know, up till last month, you know, we were still out there saying to customers, your contract ended six months ago, because don't forget that four months trying to get the three months is an average… you know, as people's contracts ended, you know, the price period came up for review, we were in discussions based on how the industries have moved, and, generally, they have been on a, until recently, on an upward progression. Now, as they start to come up… well, that's a different set of descriptions to have.

Don't forget, our whole push is not to try and be clever and beat the cycle on pricing; we're just setting out to… costs go up, we want to put our prices up; and if costs come up, we'll have to take down our

prices, but our key thing is that pass through. I'm not trying to guess the cycle; I'm trying to have that whole customer debate about value-add, not: am I trying to guess the cycle revenue, because people have found that incredibly hard to do successfully.

Hector Forsythe

Thank you.

Closing Comments

Miles Roberts

Okay, well, look, I'm conscious, it's just gone 11. Thank everybody for your time this morning and hearing our half-year. Our next announcement is our IMS, which will go, I think it's February…

Rachel Stevens

March.

Miles Roberts

…is it March, early March, sorry, early March, for an update on the next three months. But thank you very much for your time. Well, obviously, Steve and myself will be around afterwards for any other sort of residual questions. Thank you.