DS Smith Full Year Results

Conference Call Transcript

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Speaker Key:

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MR Firstly, thank you very much, indeed, to everybody here for coming, sparing the time to come and hear about our full year results for the year to the end of April, but also about a proposed acquisition that we're asking shareholders to support. We're seeking their support, not only for a Class 1 transaction but also on a fundraising.

First of all, the results for the year to the end of April. The business model is working. It's working again. It has been a very volatile environment but you've seen the headline numbers. The results are in, absolutely as everybody has expected. Volumes are strong. They're improving in the second half.

Volumes up 3.2%, building momentum in the year, it's better than the first half, all regions in growth and we're absolutely delighted by the support and the growth we've had from our pan-European customers who really continue to consolidate their supply chains into DS Smith.

We are strengthening the business. We've made a number of acquisitions in the year and these, but also the other acquisitions we've made over the years, are really performing very well. We're very pleased with how they've integrated, how we've joined together and made a stronger business. And, of course, we've invested in line with our strategic priorities around the packaging, digital printing, improving the offering we can give our customers.

E-Commerce and Display: we had a super Capital Markets Day and we've really seen very, very good growth in these categories and in e-commerce that's gone even further. Some of the relationships we have with our customers have expanded out from their original base.

We've delivered against all our financial medium-term targets. What's really important is we enter 2017 with real momentum, momentum in the volumes but also momentum in terms of recovery of the raw material costs. We're feeling very confident about that.

Now, with that backdrop on the results, we've also announced today our proposed acquisition of an absolutely super business called Interstate Resources and I'll be talking a lot more about that, our first entry into the US fibre-based corrugated packaging market. Adrian.

AM Thank you, Miles, and good morning everyone. At last year's results presentation, we were voting on Brexit, a foregone conclusion, and we were worrying about what impact all the new European paper capacity would have on pricing and when DS Smith would make its next transformational acquisition.

Well, it's certainly been a very interesting 12 months for us. Miles will run you through the transaction in a moment but it falls upon me to take you through another great business performance in an extremely volatile 12 months. Once again, I'm able to report that we've delivered against all our targets and that there's good momentum in the business.

Not surprisingly, currency translation has had a large positive impact on our translated financial results for the year as a whole and, as usual, in order to explain what's been happening in the business, I'll be talking about the constant currency changes as I go through the presentation.

This has been another year of delivering consistently on all our targets. We've had a very good volume growth of 3.2% with a very encouraging second half to the year, particularly in the last quarter, giving momentum into the new year.

We're delivering in the upper half of our upgraded margin target and also at the top end of our returns. These figures take into account all acquisitions made. The margin also reflects the high paper costs in the last quarter which we're fully focused on recovering in the box market. Our balance sheet remains strong and with decent cash flow we are, before the new acquisition, below our target gearing level and EPS was up 7%.

Here are our financial headlines. Revenues up 6% and operating profit up 5%. I'll take you through bridges for these key line items in a moment. That growth is reflected in earnings per share, also up 7% on a constant currency basis and up 19% at actual exchange rates. Dividend per share is up 19% in line with reported EPS growth at actual exchange rates. Asset turnover is another key lever of return on capital and has remained constant year-on-year, whilst return on average capital employed reflects the full capital base of all acquisitions made. Margin, as I noted earlier, is broadly flat but does reflect higher paper prices towards the end of the year.

Let's now go through the impacts on revenue. Currency translations added £432 million to our reported revenue, which reflects a substantial tailwind, particularly in the first half. Taking a starting point of 4,498 million, the largest impact is from acquisitions contributing circa 3% growth. It's been another busy year with five modestly-sized acquisitions and we're delighted with the performance of these businesses and how well the integration has gone.

From there, you'll see that on underlying basis, revenue grew by 3%. Our 3.2% corrugated box volume delivered an uplift of £78 million which sales price/mix added £9 million, reflecting the pass through of paper which started going through in the latter part of the year. Other volumes relate to paper recycling and corrugated sheet.

Moving now onto the operating profit bridge. Our growth has been driven by both volume growth and acquisitions in roughly equal part. FX is a tailwind, as I've discussed, and regarding acquisitions, I'm pleased with the contribution made and we're seeing the expected synergies from the businesses acquired in the past two years.

Input costs, as you all know, have been a considerable headwind, as we described at the half year, with a net negative effect of £36 million. In line with our business model and the same as prior years, we're actively recovering the higher paper prices in packaging. Volumes have been the largest driver of our profit growth with a continued good level of drop through. Margins have been stable at 9.3% despite the substantial headwind just discussed, with that level being in the upper half of our target range.

Of the corrugated packaging regions, the improvements have been particularly strong in Western Europe and in Central Europe & Italy. What those regions have in common is that both benefited from large acquisitions in the prior financial year, Duropack and Lantero, and what we're seeing is these businesses are now well-integrated and delivering the growth we expected. That's a real credit to our teams on the ground and our integration team, who continuously improve what is now a well-trodden integration path and this gives us great confidence as we embark on another significant acquisition.

DCH & Northern Europe have seen a more challenging environment, driven in a large part due to the relative balance in that region between packaging and paper. The UK has seen good growth in overall profitability, driven both by the acquisition in the region and growth from large customers.

Cash flow has been good once again. There's been a further significant benefit from working capital and you can see that in the working capital to sales ratio at the foot of the page of 0.9% is our average rate for the year. We use the average rate through the year as our KPI for obvious reasons, not least because this year end fell on a Sunday which obviously has an impact on reported inventory.

When I first presented to you, I reflected that this would be a real area of focus, and I've described every time since that this remains a constant focus, and I'm always asked if we can do more. When I gave my original comments, I said I was not content to be class-leading in packaging but wanted to be class-leading by comparison to world-class manufacturing companies and our major customers, not just packaging or paper companies.

So, where are we today, some four years on? I think we've definitely improved and we're now class-leading, in my opinion, in inventory compared to our immediate competitors and similarly strong in accounts payable and somewhere in the pack still for accounts receivable but not yet at the front. Therefore, when compared to our peers, our overall working capital ratio is good, driven by our inventory and creditors' management.

So, how have got there and do I believe there is more we can do? Firstly, it's important to note that acquisitions always give us an opportunity to improve, so we do have that advantage over less acquisitive businesses. This is particularly true in inventory and creditors' management. We've focused hard on inventory to get to this position and there's still more we can do, particularly around spare parts across our global business.

That said, we believe we're uniquely placed in how we manage our make, buy and sell decisions on paper in our packaging business. We've created a paper supply platform which continuously optimises our overall inventory position and we've managed, for example, to significantly reduce safety stock that gets held in packaging sites, thus, when we acquire a new business and integrate them, we're able to secure this benefit very quickly.

Turning to receivables, whilst it's true we're not the best performing amongst our immediate peers, we've still been very focused but the opportunities for improvement are much more limited. Clearly, we always have to balance between either offering discounts for early payment, trying to improve terms with customers that are themselves major multinationals and pretty good at their own working capital management or selling, without recourse, high-quality credit receivables and we seek to always maximise the economic opportunity, as you'd expect. In addition, we review each month, with every business, their level of receivables and past due balances and have, over the last few years, set up centres of excellence for credit management.

Turning to payables, this, like inventory management, is an area where we can clearly differential ourselves in our industry and we've again benefited from the global supply chain we've created, and apply the same disciplines our major customers apply on us, to our own suppliers. We've reduced significantly the number of suppliers we have and, as part of an overall supply chain management strategy, have materially improved our own payment terms. We get this benefit from our scale and our systems and processes and, again, when we acquire a business, this is an immediate and material working capital synergy which we can achieve relatively quickly.

So, back to the question can we do better? And, the simple answer is we must be able to. You only have to look at manufacturing companies in other sectors and our pan-European customers, which have significantly negative working capital positions, to see what is the art of the possible. However, four years on, I can report it is a slower journey than I expected and has required us to build our internal/external supply chain engines and then drive each month for continuous improvement but the results are improving and I'm confident they'll improve further.

Capex of £226 million has increased principally due to FX translation where we're investing in European assets and opportunities to strengthen the business, particularly in E-Commerce and Display. Our leverage is under our medium-term target of 1.8 times. Taking our starting point last year, we have the benefit of free cash flow, cash exceptions broadly tracked the income statement charge, reflecting integration of new acquisitions and certain restructuring projects. The acquisitions and disposal outflow is the cash cost, including assumed debt, of Creo, Deku-Pack, Gopaca, P&I and Parish Manufacturing.

Dividends are clearly a very important component of our return to shareholders. We paid £121 million out for dividends in the years, with 19% growth for this year's total dividend. We seek to match the cash flow of our debt to liabilities with the cash generation of our business by currency. This, as you would expect, means that we have approximately three-quarters of our debt denominated in euros. The difference in the FX rate at the year-end versus the prior year-end has increased our translated net debt due to the relative weakening of sterling between those dates. The current matching of our cash flows means that there is no material impact on our leverage ratio.

Here's the usual guidance slide. I'm not going to take you through each line. You can read the figures. The majority of these are similar to last year, updated with FX and, clearly, we'll take specific questions, either at the end or through the usual process, through Investor Relations. We include this chart every year for a pretty good reason, it tells the story of how we've delivered excellent returns to our shareholders.

Over the last seven years, we've consistently grown EPS and dividend, with a compound annual growth rate of 28% and 25%, respectively. On that note, I'd like to hand back to Miles, who is going to take you through the very exciting announcement we made this morning.

MR Thank you, Adrian. Thank you. Very quickly, building our business organically and then we'll talk about acquisitions. What I really want to say here, we've talked about e-commerce before and the pace of change and demand from our customers is only increasing.

How do we add value? Void space reduction, supply chain optimisation, establishing a true industry standard for this new market is working very well. A number of our relationships with our key customers have gone from regional to national to, now, increasingly towards a pan-European supply.

The display success – you've probably seen a number of the displays outside in the foyer – again, delighted with the growth here, we're up 17% year-on-year organically; strong support from customers, again, consolidating their supply chains behind our offering.

It's been rewarded with a further recognition from many of our customers, there's Nestlé, Mars, etc. We're delighted with the reception about how we're providing the leadership to the packaging industry that our customers want and expect from us. This has all led to the 3.2% like-for-like improvement in volumes in the last year and, as I said, the second half was stronger than the first half and we have started this new year and we're busy.

Building through acquisitions. As you know, this has been a key feature for us, acquisitions in '15/'16 and into '16/'17, whether it's Duropack, Lantero, all entering new regions in Europe for us. How do we understand these businesses, understand the customers, understand the culture? How do we build a stronger business together? And, we're very pleased with the response that we've had, the results that they've generated, and also the further growth potential they can give us.

We have a very experienced integration team that work alongside the M&A throughout the process and, let's not forget, Europe remains a highly-fragmented market and there are some very exciting opportunities for us to work on.

So, let's just come on to Interstate. As I said, it's a very nice business with a tremendous heritage and ownership and we believe, by joining with Interstate Resources, we will create a higher-quality, higher-margin group with even more growth potential.

What are the transaction highlights? We are seeking to buy 80% of the equity of this US family-owned business based on the East Coast that's focused solely in corrugated packaging and the associated paper. We've undertaken considerable research into the US over a number years. Everybody knows about this. We've visited many companies, many customers. We reviewed our needs against the various options that we felt could be available.

And, then, we approached Interstate. We went to see them, to talk to them about their business and who we were. It's about a relationship. It's not about, with respect to the investment bankers, it's not about an information memorandum and having some advisers. There weren't advisers. We worked as two companies seeing how can we create value, not only for our shareholders, but for our customers and employees, as well.

So, we had exclusive bilateral negotiations from the start, extensive access to information, staff and facilities. So, we're confident about what we're buying and who we're buying from. The acquisition is expected to be immediately EPS accretive, return on sales and margin accretive, and in the first full year of ownership, which is to '19, we expect it to achieve a return ahead of the group's cost of capital.

We have not included any revenue synergies that could come from our customers, the larger FMCG businesses. And, I think as a response to this, the owner wanted to retain 20%. I'll be absolutely honest, we would have been very happy to buy everything but they want to retain 20%. They want to be part of that going forwards and they can retain that for up to five years.

They also have asked us to subscribe for $300 million worth of equity in the DS Smith Group as another sign of confidence of how they see the opportunity here. But, we're asking our shareholders for their support, firstly, on a Class 1 transaction. It's Class 1 because of the indeterminant final value of the 20% stub equity and we're also asking shareholders to support a fundraising through a cash placement of £280 million. But, I'm delighted to say the response we've had to date has been everything that we hoped that it would be.

So, why the US? What is it about this market that attracts us? No matter what the returns are, what are we looking to buy into? Does it make sense? Well, I've put on this slide here, slide 24, the fundamentals of the North American market. Well, it's a big market. We all know that. The US is a big company. It's got big retailers, big middle-class, big brands, big packaging industry and we like that.

It's grown consistently over a number of years, sometimes in line with the US economy but we feel that the packaging has an opportunity to grow ahead of the economy going forwards because of the increasing relevance of packaging to our customers.

As we know, the GDP outlook for the US is strong and has remained so and, very importantly, the market is quite consolidated. About 70% is operated by four very good competitors, they're large, they're very experienced, and that concentration has driven margins; it's a higher margin business than Europe and the price stability is also far greater than in Europe. But, 30% of a very large market still remains outside of the top four.

So, how can we think that we can make money in this market? Well, we think there is an opportunity for packaging to develop further and we would like to be part of that. We can see the market, in many of the categories they're working on, is behind where Europe is but there's a strong appetite from our customers to see the development in packaging.

I put some examples here which many of you will be familiar with because we've led this market in Europe over the last seven years. We are the ones talking about the opportunity for retail ready packaging. Look at the penetration we've got in the UK where we started, 50% of products in the retails and now in retail-ready, compared to 15% in the US.

But, in the US labour costs instore are increasing. It's now common to pay over $10 an hour, so it's expensive operating stores and, guess what, footfall is falling because people are going to the internet. So, they need a more efficient solution in store, it's called shelf ready packaging and we have the technology and we have the experience to come behind that.

You look at performance packaging. Again, in DS Smith, we've led that market. How do we provide our customers with the solutions they need using less fibre? Using less? Being a more efficient box? Selling on the performance, not the specification of the box. We started in the UK.

Look on that graph how we've driven down the average grammage and we share that benefit with our customers. We can see the US is still a lot heavier. You can park a truck on a lot of their boxes. They're great boxes but we think there's an opportunity here to work with our customers and share in that benefit.

E-commerce is growing strongly. Fantastic customers there, a fantastic business and it's growing and you know what our unparalleled position in e-commerce is in Europe. We're committed to how we can support the whole industry in raising the value creation with our customers.

Global customer opportunity: These are the people who have had consistent growth, well above the group average. 17 of our largest 20 customers work in the US and, of course, we've been talking to them. What are their needs? How do they see it? And, that's given us the confidence.

So, that's the market and here is Interstate. As I said, it's a nice business. Good ownership, good values, good people. It's based on the East Coast. What's important, it's not just national coverage, it's more about state concentrations and it has a very good proximity to Europe, which helps to drive our supply chain efficiencies. It has 12 corrugated sites. It's mainly focused in the food and drink sectors, very stable and growing categories.

It has two paper mills. It's very important for us, our security of supply in the US. It has a kraft mill. The US market is dominated by kraft and we think that the position of this mill, down in the Southeast, is in the most attractive wood basket of anywhere in the world. The trees grow very quickly. Energy costs are very competitive and the infrastructure is excellent. It's on the East Coast so, again, we can build supply chain synergies with Europe.

The assets are well-maintained but it is a smaller company than DS Smith and in working with the people there we can see how, together, we can build a stronger business in Interstate. We've had extensive access to the management. We know who these people are. We like the people and they're excited about it.

We've agreed a management structure and key processes and we're in the stage, at the moment, of going through and populating that and talking to and assessing people. Again, I think that's why the family wanted to retain 20% in the business.

So, what about the money? It all sounds great but how much do we make? Principal measures, return on capital, return on capital employed; and we're confident of the returns. We're confident we can achieve cost of capital returns in the first full year of ownership, immediately EPS accretive and ROS accretive, as well. And, we're maintaining a strong balancing sheet, not leveraging ourselves up so that we can't afford to carry on developing and growing this business. Strong balance sheet but our valuation is based on the synergised returns.

Our outlook for 2017 and beyond, and the results of 2017 in the year-to-date, are materially ahead of 2016 and, in addition to that, an acquisition has been made post-2016 that's contributed $6 million of EDITDA. On top of that, we have synergy creation, $25 million of cost synergies by year three and $95 million of working capital. The supply chain, creditor terms, stock holding, this is where we see opportunities; bring them to DS Smith standards, but as Adrian said, we're nowhere near the best of manufacturing. There's still a long way to go. We've got to learn and develop and improve the cash flow from our working capital.

Slide 28, those synergies, where do they come from? On the cost side, we've got procurement and operations. There are some associated costs there with achieving it but a lot of that is on capex. It's not going through the P&L, it's getting the assets to the condition that we believe our customers would want as we enter some new markets and IT and integrating the business.

I've talked about the working capital. Revenue growth opportunities from our customers are not included in the analysis. We've agreed the management structure and, on the integration, we have an absolutely super team here who've worked alongside all of our transactions. The person who heads this up was part of the SCA integration, the Duropack integration, and we feel we have strong process, strong people, strong approach.

But, it's about the customer at the end of the day. Can we win with our customers? There are some very good US competitors there. They've been there a long time, they know their business, so what gives us the confidence? Because we've spoken to our customers. I think we understand their future needs, and in those discussions, while we've never mentioned Interstate, we've obviously received some very encouraging, very strong feedback from a number of them in the meetings.

We said, well, would you put that in an announcement. Couldn't hold them back. This is the one from… Two super, super customers. And, here's Mondelez. You know, we're their sole supplier. They don't want to work with anybody else in Europe; not interested. It's been long-term. I know they're delighted with what we've provided and we're delighted to have them as a customer. And, as they say here, we're their sole supplier and they're excited about our entry into this market.

And, similarly with Nestlé, what a super, super company; long-term relationships and, again, they look forward to working with us on a more strategic basis across a wider geography. There's nobody else that can do this. There's nobody else.

How are we strengthening our business model? And, here is how we strengthen it. We're strengthening it with our customers and we're strengthening it with our supply chain, as well. So, we feel that that margin uplift we should get from this is because of a stronger business. In terms of the transaction overview, it is two-stage, we do have an option after five years to take full ownership. That 20% is subject to an annual put by the vendor if they want to do that. And, then, we do have an option at the end of the five years. Let's see where we get to, but we do have that option, ourselves, to acquire everything.

It is subject to shareholder approval and competition clearance. We don't believe that we have any barriers there because our business in the US at the moment is solely around plastic packaging, a different category. And, by the way, that's gone extremely well over the last few years. So, if everything happens we expect it should be closing at the end of September, subject to that clearance. The acquisition financing, we've got the initial consideration. We do have the placings that I've spoken about, the new debt facilities, as well, have been arranged. I think we'd be looking to take those out in to the capital markets in due course.

The leverage is held at a sensible level. It does allow for the put to be exercised and not to overleverage our balance sheet, allowing us to continue to invest and grow but the group is very cash generative. You know about our commitment to leverage, you know about our 2x leverage, and we'll be driving the debt down to that level and also a commitment to maintaining an investment-grade rating.

So, in summary, we're pleased with last year; volatile background, delivered all our numbers but we won with the customer and we've won in some key long-term categories, E-Commerce and Display. We've hit our medium-term targets but we enter the New Year with some momentum in there and, on the back of that, we're absolutely delighted to make our first entry into the US market and thank you very much everybody for listening to our presentation but we're very happy to take questions that anybody may have.

BD Thank you. It's Barry Dixon from Davy and congratulations on the deal. A couple of questions, if I could. First, in terms of the European business, obviously a strong performance in volumes. Miles, maybe you could just give us some sense as to the volumes since the end of April, perhaps by region around Europe relative to 3.2% and the full year. And, also, we've seen fairly substantial price increases on paper, both kraft liner and recycled, and maybe how your efforts at recovering that in corrugated prices are going. You might give us some sense as to where corrugated prices are year to day in percentage terms.

Secondly, just on the deal, if you could perhaps give us some sense as to… So, '15 seems to have been a very good year for Interstate and then '16 was poor. Maybe you might give us some sense as to why '16 was poor and then what's causing the performance in '17 to be so materially better than '16. Were there a couple of one-offs in that? Perhaps, you might give us some sense on that.

And, then the 25 million of synergies, procurement and operational. Maybe, you might also give us a little bit more colour on that in particular, I suppose in the sense that you don't have a business there already so it's hard to sort of try and get our heads around where the synergies come from in that context, so thank you for that.

MR All questions that are very active. If I just start on the European business and we'll come on with the deal. So, in Europe you see the first half we had 2.9 like-for-like growth, full year, 3.2. You can do the maths. You can see the second half for us was strong and it was building during the second half and that build has continued into May and June. So, we're busy but these are two months. Who knows where it's going to lead to but we're busy. We're seeing more consolidation of our big customers behind our offerings so things are turning even more to a pan-European business.

I think it's true to say we're seeing some regions have been strong and are actually building momentum in their economies. Places like Iberia has been very strong for us. We've seen France improving. Germany has always been reasonably strong; it's still there. Eastern Europe is good. UK, we're growing very well but I think that's more about our focus in particular categories. As we all know, the economy is looking not quite as robust as it was a couple of years ago but, for us, we maintain being very busy because of our sector focus. So, all regions were in growth last year and all regions are in growth again in the start to this year and it's strong.

You're absolutely right, Barry, about pricing. Adrian's put up the graph. You can see the raw material cost, which is paper for us predominantly, really come in in the final quarter. We saw some very steep increases and it's about recovering that. As you know, we have a very well-worn path there. Most of it is agreed with our customers. We have a mechanism about pass-throughs. We've always passed the cost reductions back when raw material costs go down and we like to have that returned to us when raw material costs go up. I wouldn't say it was quite mechanical but it's a well-worn path and our margin and our cost recovery to date is absolutely where we expected it to be.

Such is the size of the increase. It's not about 1%. These are quite sizeable increases and they need to be recovered and therefore we're absolutely where we expected to be. Our performance based packaging also allows us to mitigate that with our customers and, again, that's another margin enhancing activity for us. How do you mitigate the increase by changing people onto the performance of the packaging rather than specification? We gain in that as a second process, so we're quite comfortable with it.

In terms of the deal, itself, '16 was a poor year for the business. We have examined that in detail. It is a Class 1 transaction and therefore we have to report them. We can only report all the audited numbers but we're very satisfied with where 2017 is and the reasons of why the profit has dipped in 2016. 2017 is materially ahead of '16 and there's the acquisition and we're confident about making the financial returns that we have published. It's difficult for me to say any more considering it's a Class 1 transaction, in terms of 2016 but we have examined this in a lot of detail. We know where we are on that. Adrian, synergies?

AM Yes, synergies. As you say, Barry, it's not a contiguous acquisition for us, so you don't have the usual restructuring and reworking of the asset footprint, however what we do have is our procurement platform that it comes into which accounts for a bit of it. But, most of our synergies are around operational performance and how we are going to be operating the assets.

We talked a little bit earlier about how we operate as a business between paper and packaging, the whole make, buy, sell, the paper sourcing platform and how we're optimising what goes through the conversion facilities. This will be part of that. We'll look at, clearly, performance packaging and the opportunities around that. We have a degree of experience within our own mill utilisation from recycling. We'll be working with that. We clearly have opportunities around our own fibre utilisation and our recycling business.

We'll be working around that. And, because it is a Class 1 transaction we have had all of our synergies validated and, indeed, I wouldn't say haircut, but certainly put in place as a number that a third party can stand behind; has been validated. So, I'm very comfortable with those.

What we haven't included is any synergies of revenue. We haven't taken into account that if we grow the customer base with customers that we have, we can utilise the surplus capacity that's previously gone to export. That's not included at all, so clearly there's an opportunity that we're going to be focusing on but, in terms of the cost synergies, I think we have a pretty good road map to achieve those and on working capital, hopefully… I know I went on a little bit but it's to try and give some colour about why we're comfortable about $95 million of synergies there.

MR Very good. Other questions? Alex?

AM Thanks very much. Alex Mees from JP Morgan. A couple of questions, just on the deal. Firstly, I wonder if you could quantify or give some sense of the capacity utilisation of their packaging operations. Is there room to grow? And, as that happens, is it likely that the long paper position that the company is currently in might start to slim down?

Secondly, just on the mix between kraft and recycled CCM, do you see that mix shifting, evolving towards your European mix in time or is this something structural that you intend to retain? I'll leave it there.

MR The business is long paper. It produces more paper than its packaging requires. It therefore means that it does sell business on the export markets and they can be very volatile in the pricing and that has happened over the past couple of years and it's one of the reasons for some of the volatility. So, the question is how can we switch that long paper into US supply and that's where our organic growth on the revenue… There are some potential bolt-on acquisition opportunities, nothing large, but how do we start to balance that business so it's much more integrated?

There is some supply opportunity from elsewhere so our main objective is how do we build the packaging side because the financial returns from that are really very attractive as well as obviously meeting our customers' expectations. Could be talking about a 200,000-tonne switch into the US.

When we come to the mix of business, I think it's around the light-weighting. It's absolutely true that testliner, recycled paper, can offer some very cost-attractive solutions compared to kraft, so I think it's more a question about the light weight in the market over the medium-term and I think there are some opportunities there for CCM.

We've got a very enviable basis and experience in Europe. Let's just see how this evolves but we can certainly see some really value-adding opportunities to start to change the types of paper. If we can focus the American customer on to the performance of the packaging, then we've got an absolutely super opportunity of making the same success as previously. More questions?

JJ Hi. Justin Jordan from Jefferies. Just a few on the deal, obviously, firstly. Just on page 23, you talk about $300 million of consideration to the vendor in equity. Just so we're clear, is that presumably being done at the placing price and what sort of lock-ins has the vendor got on that consideration of shares that they're getting.

AM It's based on the three-day average price before issue, so it will be a fixed number of shares which will be calculated today and the lock-in is half for six months, half for 12 months.

JJ Thank you. And, just on page 28, the $55-60 million of one-off costs within the first three years, could you just give us some colour as to what exactly you're doing to the business and I'm assuming that's over and above its existing maintenance capex, whatever.

AM Yes. It's a split, as Miles said, between capital and operating cost, substantially capital. You have the obvious starting points which we put into every acquisition we make around health and safety in terms of getting the plant in a format that's consistent with how we operate globally and our standards.

There is work around looking at ensuring that the way the plants operate and manufacture, again, is consistent and can operate within our own performance packaging type of operations and, then, there's capital around certainly impact and how present to the customer. So, there's a reasonable investment as you can see, predominantly capital, to get the business closer to a DS Smith look and feel to start with and then we look at what's required going forward as we grow the business. So, I don't know if that helps you, Justin.

JJ That's great. Sorry, just one final thing on the deal. Obviously, historically, you talked about an enviable bias to FMCG in your European operations. Can you just give us some sense, on the same like-for-like basis, what the FMCG percentage of this business is currently before you obviously change it or improve it?

MR Well, the business is predominantly food and drink. There are some well-known companies in there around confectionary, etc, but it's predominantly there. There's little industrial and manufacturing customer base and we like that because of its consistency of demand. It's a strong platform. There's no great concentration with customers, so good local positions that we can really start to build on. There's very little overlap with our customer base which is obviously an opportunity for us.

JJ Sorry, just one final thing just on core DS Smith, as it were. Adrian, you talked about having sold some high-quality receivables without recourse at the end of the year. Can you just quantify how much of that was at the end of April?

AM I didn't say at the end of the year, Justin.

JJ Sorry.

AM I said, through the year, we consciously make a decision about whether you take cash discounts or whether you sell receivables, whether you change your credit terms, so this goes on every year, so it's not a year-end action.

JJ Sorry, could you just quantify how much please?

AM No. No more than I wouldn't quantify how much I'm giving cash discounts for, neither would you expect me to, but it's not a material figure and it's something we do in the same way as we give discounts; we extend terms, we get reduced terms. It's just a normal business activity.

JJ Okay. Thank you.

HF Hello. Good morning. Hector Forsythe from Stifel. A couple of questions for you, please. Very first question is, can you tell us what your WACC is? You refer to it several times.

AM 9% pre-tax, Hector.

HF Thank you very much. In terms of on the deal, can you say a little bit about management structure? You've said that you've planned that through but can you give us some indications of who those people are and who is staying, etc?

MR Absolutely. We'll talk to individuals first about their position but in terms of the management structure, it's something that is extremely important, so on day one, when the acquisition completes, a management structure is in place, fully populated, everybody knows what his or her roles are, where they're reporting, duties and objectives. That will be in place on the first day of completion.

We have to be careful about gun-jumping because of the anti-trust, so we can't change anything prior to that but the management structure that will be in place in the US, it mirrors what we have in Europe. So, you've got paper, you have packaging, you have the group functions, and we've spent a lot of time and a lot of money building our group-wide platforms. It's what's allowed us to make these acquisitions.

When we buy a business, we don't just change the name and walk away. We're talking about a full integration on procurement, with customers, with operations, with the supply chain, with IT, with finance, with HR, so we have the group-wide functions we'll stretch across to the US. You'll have a US management and there'll be a head of paper, a head of packaging and you'll have this supply platform that we've spoken about, about how we optimise the relationship between paper and packaging and that fulcrum has created so much value from the SCA acquisition.

Let's not forget, we bought that business in SCA on the projection of €150 million of profit – previous year it made €30m – because we were confident in how we could run it. It was the same with Duropack. How can we create value in these businesses by deploying the group technology and expertise that we spent so long in developing? And, so the management structure will mirror what we have in Europe. The head of the US will report directly to myself and my reports in Europe have been slimmed down to allow me the time to spend with that US team.

There's a full integration team, as well. People will be based over there but that's no different to what we've done in Duropack, with SCA or into Iberia. And, that's all been discussed and is being agreed with the people in Interstate. We've discussed it with the previous owners. We're discussing it with the management team now and we're going through the assessment of people and just understanding more about the individuals there. We can't gun-jump but we're well advanced on this.

HF Okay, thank you. Previously, you've obviously articulated a view that you'd like to reduce your paper capacity within Europe. Has this deal modified any of that thinking?

MR No, not in the slightest. The US is a different market. It's far more consolidated, whereas in Europe we have a lot of independent paper capacity. So, the price of paper, we're able to source paper, there's no difficulty with us. We're a huge buyer. We source globally. This paper capacity hasn't changed anything on Europe but in the US, with the consolidation, we just felt that it was right for us to have more in-house supply as a first entry into that market, so we can concentrate on developing the business rather than are we going to get supplies. It gives us the security of supply in that market.

HF Okay, thank you.

HP Good morning. It's Harry Philips, Peel Hunt. Two questions, please. First of all, will you do anything with that debt in terms of re-financing or whatever and the, secondly, is Interstate the entry point for e-commerce and DS Smith, in that context, into North America or can it be?

AM Okay. I'll do the first. You can do the second, then. In terms of refinancing the debt, yes, the current debt situation involves secured debt in the business, as you'd expect with a small company. So, we have to remove the security and refinance it but that's the assumption behind our 400 million bridge and we will take that out through a debt capital markets issue, realistically as soon as we practically can, which won't be within the next two weeks but I'd expect within the next six.

MR This business is very good entry point to us. We have to make the right returns and we can see how we do that. That's why we wanted the East Coast, etc. What we haven't included is any real growth opportunities with various sectors that we favour and that's what we have to work out.

As you can imagine, we do have a number of plans. I think we want to come back to shareholders and say, look, we bought this business. It's your money. You've trusted us with your money. These are the returns we're making from it. Have we made those synergies? Are we creating the returns that we've committed to?

How do we then start to build out and start to close that paper-long position and, then, what about these customers? There's some super, very good existing suppliers but how can we put more innovation and lift that market; that's the bit we want to come back and say this is how it's looking. What's the traction we're getting with this?

And, if those three things happen, then you can start to see the returns, you start getting a bit of sizzle on the returns. It starts looking very attractive and then it's a question of how do we build out but let's get this right first. Let's get our customers, let's create these synergies, let's close that paper, let's build out a bit and then we'll be coming back and talking about it in more detail. It's a huge market, a lot of opportunity there, the first thing is let's get it right.

Right. Okay. Well, look, we've been running for 55 minutes. We always like to be on time. So, just to say thank you very much everybody for your time today. We really do appreciate you coming and listening to us. We're pleased with last year's results. There's good momentum into the current year. We're absolutely delighted to make this first move into the US and we'll be coming back to tell you more about it in the near future. Thank you very much.