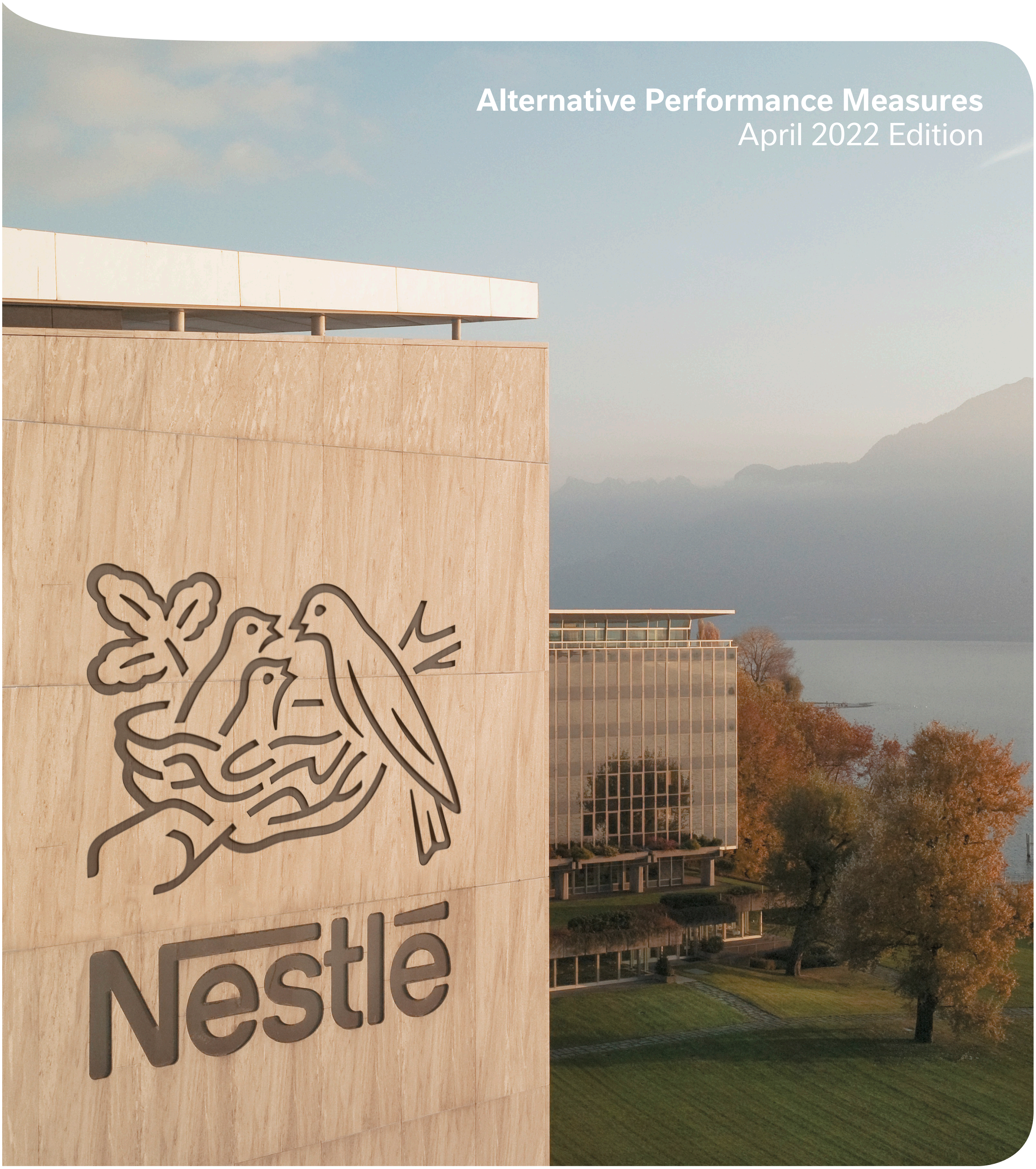
Nestlé

Good Food, Good Life

Alternative Performance Measures

April 2022 Edition



Definitions of Alternative Performance Measures

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

Foreword

The April 2022 Edition of the Alternative Performance Measures is an update to the February 2022 Edition. It includes changes to the Organic Growth, which are applicable from January 1, 2022.

Since the outbreak of the war in Ukraine in late February 2022, certain countries announced sanctions relating to Russia and Belarus. There has been an abrupt change in the geopolitical situation, with significant uncertainty of the duration of the conflict, changing scope of sanctions and retaliation actions including new laws. These new circumstances strongly limit the freedom of Nestlé Russia Region businesses to operate, and lead to a distortion and significant volatility in the level of activity.

As such, including Nestlé Russia Region businesses[1] in the Organic Growth (OG) no longer serves the purpose of providing a "like-for-like" comparison. The activity in 2022 will be in no way comparable to that in 2021, and will not serve as a basis for understanding the evolution of the underlying business dynamics. Consequently, the evolution of sales of Nestlé Russia Region businesses is excluded from OG since January 1, 2022, with a corresponding impact in the "effect of exchange rates" and "effect of acquisitions, divestitures and other changes in Group scope activity". OG for 2021 does not need to be restated because the distorting effect arose only in 2022.

Organic Growth (OG)

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

In order to limit the distorting effect of hyperinflation, pricing in excess of around 2% per month (the level at which hyperinflation generally occurs) are excluded from OG calculations in hyperinflationary economies, with a corresponding adjustment in changes in exchange rates.

1 Nestlé Russia Region businesses: Russian Federation, Belarus, and countries managed by and highly dependent on Nestlé Russia (Kazakhstan, Uzbekistan, Georgia, Armenia, Azerbaijan, Turkmenistan, Tajikistan, Kirghizstan, and Mongolia, with total sales of less than CHF 0.2 billion in 2021).

Venezuela and, since January 1, 2022, Nestlé Russia Region businesses, are excluded from OG to remove the distorting effect on the like-for-like comparison due to limited freedom to operate in these extreme business environments. Corresponding impacts are recorded in the "effect of exchange rates" and "effect of acquisitions, divestitures and other changes in Group scope activity".

The increases or decreases in sales of an acquired business compared to its historical baseline are included in OG immediately following the business combination, unless a reliable baseline for the 12 months prior to acquisition cannot be established, in which case all sales during the first 12 months of the acquisition are excluded from OG.

Sales of a divested business are removed from comparatives for the 12 months prior to the divestiture. Sales made under supply agreements related to the divested business are included in acquisitions and divestitures during a transitory period.

The pricing impact of changes in the way that a business is transacted in an entire country (e.g. establishing a local operating company instead of exporting to a distributor, or vice versa) are included in acquisitions and divestitures, respectively.

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

Real Internal Growth (RIG)

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

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

As RIG is a component of OG, it excludes the impact of changes in exchange rates and of acquisitions and divestitures (as described in the previous section).

Pricing

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

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

Evolution of Sales

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

Total Group

	2021	2020
Sales (in millions of CHF)	87 088	84 343
Evolution vs prior year (in %)	+3.3%	–8.9%

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

Total Group
In %

	2021 vs 2020	2020 vs 2019
Real Internal Growth	+5.5%	+3.2%
Pricing	+2.0%	+0.4%
Organic Growth	**+7.5%**	**+3.6%**
Effect of exchange rates	–1.3%	–7.9%
Effect of acquisitions, divestitures and other changes in Group scope activity	–2.9%	–4.6%
Evolution of sales	**+3.3%**	**–8.9%**

Underlying Trading Operating Profit Margin

Underlying Trading operating profit margin is when Underlying Trading operating profit is calculated as a percentage of sales. Underlying Trading operating profit is Trading operating profit before the impact of Other trading expenses and Other trading income (mainly restructuring costs, impairment of property, plant and equipment, and litigations and onerous contracts). See note 4 of the Consolidated Financial Statements of the Nestlé Group 2021 (www.nestle.com/sites/default/files/2022-02/2021-financial-statements-en.pdf) for more details of Other trading expenses and Other trading income.

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

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

Total Group

In millions of CHF except for Underlying Trading operating profit margin

	2021	2020
Trading operating profit	**12 159**	**14 233**
Add:		
Other trading income	(171)	(238)
Other trading expenses	3 131	908
Underlying Trading operating profit	**15 119**	**14 903**
Sales	**87 088**	**84 343**
Underlying Trading operating profit margin	**17.4%**	**17.7%**

Trading Operating Profit Margin

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

Underlying Trading Operating and Trading Operating Profit Margins in Constant Currency

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

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

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

Total Group

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

	2021	2020
Sales	**87 088**	**84 343**
Retranslation at prior year rates	859	6 664
Sales in constant currency	**87 947**	**91 007**
Underlying Trading operating profit	**15 119**	**14 903**
Retranslation at prior year rates	154	1 278
Underlying Trading operating profit in constant currency	**15 273**	**16 181**
Underlying Trading operating profit margin (as reported)	**17.4%**	**17.7%**
Reported evolution (in basis points)	–30 bps	+10 bps
Underlying Trading operating profit margin in constant currency	**17.4%**	**17.8%**
Evolution in basis points compared to prior year as reported Underlying Trading operating profit margin	–30 bps	+20 bps
Trading operating profit	**12 159**	**14 233**
Retranslation at prior year rates	143	1 214
Trading operating profit in constant currency	**12 302**	**15 447**
Trading operating profit margin (as reported)	**14.0%**	**16.9%**
Reported evolution (in basis points)	–290 bps	+210 bps
Trading operating profit margin in constant currency	**14.0%**	**17.0%**
Evolution in basis points compared to prior year as reported Trading operating profit margin	–290 bps	+220 bps

Underlying Earnings Per Share (EPS)

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

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

Underlying Earnings Per Share (EPS) in Constant Currency

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

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

Total Group

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

	2021	2020
Net profit attributable to shareholders of the parent	**16 905**	**12 232**
Add:		
Restructuring costs	311	220
Impairment of property, plant and equipment, goodwill and intangible assets	2 614	711
Net result of disposal of businesses	(235)	(1 678)
Other adjustments in net other income/(expenses)	750	854
Adjustment for income from associates and joint ventures	(7 270)	(577)
Tax effect on above items and adjustment of one-off tax items	(684)	400
Adjustment in non-controlling interests	(57)	(179)
Underlying net profit	**12 334**	**11 983**
Retranslation at prior year rates	87	1 007
Underlying net profit in constant currency	**12 421**	**12 990**
Weighted average number of shares outstanding (in millions of shares)	2 788	2 845
Underlying EPS (as reported)	**4.42**	**4.21**
Underlying EPS in constant currency	**4.46**	**4.57**
Evolution in % compared to prior year as reported Underlying EPS (unrounded)	+5.8%	+3.5%

Net Financial Debt

Net financial debt represents the net level of financial debt contracted by the Group with external parties (e.g. bonds, commercial papers) after considering cash and investments readily convertible into cash. It is composed of the current and non-current financial debt, derivatives hedging financial debt and liquid assets less cash and cash equivalent and short-term investments. See Note 16.5 of the Consolidated Financial Statements of the Nestlé Group 2021 (www.nestle.com/sites/default/files/2022-02/2021-financial-statements-en.pdf) for the composition of Net financial debt and a reconciliation of the year-on-year Net financial debt evolution.

See Note 12.2e of the Consolidated Financial Statements of the Nestlé Group 2021 (www.nestle.com/sites/default/files/2022-02/2021-financial-statements-en.pdf) for more details on the monitoring of the Net financial debt.

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

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

Total Group

In millions of CHF

	2021	2020
Trading operating profit	**12 159**	**14 233**
Add:		
Net other trading income/(expenses)	2 960	670
Depreciation and amortization	3 440	3 465
Adjusted EBITDA	**18 559**	**18 368**

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

Free Cash Flow

Free cash flow represents the cash generating capability of the Group to pay dividends, repay providers of capital, or carry out acquisitions, if any. It equals Operating cash flow less capital expenditure, expenditure on intangible assets and other investing activities. See Note 16.5 of the Consolidated Financial Statements of the Nestlé Group 2021 (www.nestle.com/sites/default/files/2022-02/2021-financial-statements-en.pdf) for a reconciliation of Operating cash flow to Free cash flow.

Working Capital

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

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

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

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

Total Group

In millions of CHF

	5–quarters average 2021	5–quarters average 2020
Trade receivables	8 457	8 694
Inventories	11 420	10 091
Trade payables	(14 347)	(13 413)
Average Trade Working capital	**5 530**	**5 372**
Other receivables	2 691	2 475
Other payables	(3 961)	(4 081)
Other elements of Working capital [a]	(4 196)	(3 750)
Average of other elements of Working capital	**(5 466)**	**(5 356)**
Average of Working capital	**64**	**16**
Sales	**87 088**	**84 343**
Average Working capital as a % of Sales	**0.1%**	**0.0%**

(a) Mainly composed of prepayments (assets) and accruals (liabilities).

Return on Invested Capital (ROIC)

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

The numerator is Trading operating profit before Litigations and miscellaneous trading income/(expenses), net of tax. This figure is divided by average Invested capital during the year. Invested capital is a measure of the operational assets used to generate the results of the business, excluding financing, tax and cash-management activities. Further details of the definition of Invested capital can be found on Note 3 of the Consolidated Financial Statements of the Nestlé Group 2021 (www.nestle.com/sites/default/files/2022-02/2021-financial-statements-en.pdf).

Return on Invested Capital before Goodwill and Intangible Assets

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

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

The calculation of Return on invested capital is shown below:

Total Group

In millions of CHF

	2021		2020	
	Before GW & IA	After GW & IA	Before GW & IA	After GW & IA
Trading operating profit	**12 159**	**12 159**	**14 233**	**14 233**
Add:				
Net other trading income/(expenses)	2 960	2 960	670	670
Underlying Trading operating profit	**15 119**	**15 119**	**14 903**	**14 903**
Less:				
Impairment of property, plant and equipment	(344)	(344)	(302)	(302)
Restructuring costs	(311)	(311)	(220)	(220)
Impairment of intangible assets (excluding goodwill and non-commercialized intangible assets)		(1 749)		(1)
Impairment of goodwill and non-commercialized intangible assets		(521)		(408)
Trading operating profit before litigations and miscellaneous trading income/(expenses)	**14 464**	**12 194**	**14 381**	**13 972**
Tax rate [(a)]	(2 994)	(2 524)	(3 034)	(2 948)
Trading operating profit before litigations and miscellaneous trading income/(expenses), net of tax	**11 470**	**9 670**	**11 347**	**11 024**
Average Invested capital (Note 3.2)	27 484	27 484	27 585	27 585
Average goodwill and intangible assets (Note 3.2)		51 966		47 163
Average Invested capital, goodwill and intangible assets		79 450		74 748
ROIC	**41.7%**	**12.2%**	**41.1%**	**14.7%**

(a) Based on the Group Underlying Tax Rate (UTR) of 20.7% (2020: 21.1%).

Notes