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Nestlé S.A.

In late May 2001, Peter Brabeck, Vice-Chairman and CEO of Nestlé S.A., sat at his desk in Vevey, Switzerland and took stock of the company he had led for the past four years. Through 130 years of selling food products around the world, Nestlé had developed a corporate culture that stressed maintaining its leadership role in providing consumers the staples for healthy, nutritious, pleasurable, and socially satisfying diets. The lifestyles of complex modern societies meant consumers more than ever expected food products that satisfied not only the wellness of their bodies, but their souls and pets as well.

When he took control in June 1997, Nestlé had been through a 16-year period of major change under his predecessor Helmut Maucher, who was widely credited with revitalizing a stagnant company. Maucher shed some underperforming brands, made numerous acquisitions, positioned the company for strategic growth in new product categories, and built a solid foundation overall for the company going forward. He carried out his program, moreover, while the food industry dealt with the impact of several major events: rapid consolidation; new technologies; increasing speeds in everything from manufacturing to transportation; changing dietary habits; and a seismic shift in global economic sentiments as countries around the world opened their borders to trade and business competition. Despite the company's improvement, some analysts in the mid-1990s felt Nestlé lacked organizational rationality and lagged behind competitors such as Unilever, Phillip Morris, and Danone in organic growth and brand profitability.

Brabeck wasted no time putting his own stamp on the company. With a renewed senior management team of his own choosing, he started the MH97 program for important efficiency gains on the production side, and he announced that future revenue growth would be derived two-thirds internally and one-third externally. The mix was a reversal of how Nestlé had grown during the Maucher years. Following through, he continued Maucher's strategy of selling mature and underperforming assets and noncore businesses and brands, such as Contadina, Sarotti, and Locatelli. At the same time, he made selective bolt-on acquisitions to consolidate Nestlé's position in core growth areas such as mineral water, pet food, and ice cream. Most importantly, he sold and closed factories, and restructured many basic functions—R&D, supply channels, marketing, the role of Food Service—to create greater efficiency and increase brand value.

By the end of 2000, the actions he had taken resulted in significant cost savings and higher brand profit margins. From 1998, Brabeck's first full year as CEO, through 2000, annual sales growth in

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CHF jumped from 2.4% to 9.1%, net profits rose from 5.9% to 7.1%, and real internal growth[1] (RIG) went from 3.3% to a record-setting 4.4%, which exceeded the company's annual trend target of 4%. Furthermore, Nestlé's market capitalization increased from CHF55 billion to CHF155 billion (it was CHF3 billion in 1981 when Maucher became CEO). The achievements were reached, moreover, in the face of a rolling series of severe economic crises in Asia, Russia and Central Europe, and Latin America.

Using a nautical metaphor, Brabeck commented about the general direction of the company:

> We agreed on a course to steer, and I first of all changed the crew. New people came on board the boat. Then I set the sails a little bit differently. I put the beam a little bit down, and I brought the fork a little bit stronger in. And we achieved, I would say, a cruising speed that was superior to the one we had before, but still staying on the same course, steering in the same direction.
>
> Now we are coming to the stage of preparing a change of course for the boat. It's a physical law that you cannot go faster than the construction of the boat allows you to go. If you want to accelerate even further, you have to change the dynamics, the structure of the boat, or you set a different course. I have come to the conclusion that we need an internal restructuring in the way we organize and run the company.

The company was designed, he said, for top growth of around 4% annually, and he wanted to push the figure into the 6% range. Building on the success of programs already in place, Brabeck turned his attention in 2001 to re-engineering the company itself. He had launched a massive project known as GLOBE—for "Global Business Excellence/Unlocking Nestlé's Potential"—which aimed to deliver greater flexibility and global manageability, but also cost savings and rationality by improving the application of modern technology to the company's far-flung business activities. His aim was to make the size of the company once again an asset instead of a burden. He also was pushing ahead with the strategic concept of positioning Nestlé as a provider of human "wellness" for people and pets alike.

Since he became the CEO, Brabeck said his primary mission was to ensure that Nestlé, with its roots in the mid-nineteenth century, was in a strong position for the fiercely competitive environment of the twenty-first century. "Food is fundamentally a demographics business," he said. Developing countries, where almost 80% of the world's population resided, were benefiting enormously from freer economies. Lower trade barriers would permit greater business opportunities in the future, and more and more people in developing regions were reaching income levels where Nestlé products would become a part of household budgets. Brabeck intended that Nestlé would be well-positioned to serve those consumers.

History

In 1867, Henri Nestlé (1814-1890), a pharmacist in Vevey, Switzerland developed a nutritious infant formula from powdered milk, wheat flour, and a little sugar, to which he applied a unique drying process that retained most of the mixture's nutrients. He created it for mothers unable to breast-feed, and it proved effective in curbing infant mortality due to malnutrition. Nestlé marketed the formula as Farine Lactée Nestlé (Nestlé Milk Cereal) and soon expanded sales into other

[1] Real Internal Growth=sales volume, less impact from acquisitions, divestitures, price changes, and foreign currency exchange rates.

European countries, thereby giving the company an international orientation very early. In German, Nestlé meant "little nest" and he adopted the symbol of a bird feeding babies in a nest as a trademark to give the company a clean, healthy, nurturing and caring image.

In 1905, the Nestlé Company merged with its chief rival, the Anglo-Swiss Condensed Milk Company founded by two American brothers, ending years of fierce competition between them in the market for condensed milk. By the early 1900s, Nestlé operated factories in the United States, England, Germany, and Spain. In 1907, it began manufacturing in Australia and soon established warehouses in Singapore, Hong Kong, and Bombay to supply the rapidly growing Asian markets with infant formula and condensed milk. In 1929, Nestlé began to expand its product portfolio when it merged with Swiss chocolate makers Peter Caillier Kohler. In 1938 it introduced Nescafé, the world's first soluble coffee. Nestlé developed it in response to requests from the Brazilian Coffee Institute for new products to help alleviate Brazil's chronic coffee surpluses. The company relied on the same technology to create Nestea in the early 1940s.

For several decades after World War II, Nestlé grew by leaps and bounds following a policy of diversifying within the food industry. Major acquisitions included: *Maggi* seasonings and soups (1947); *Crosse & Blackwell* preserves and canned goods (1960); *Findus* frozen foods (1962); *Vittel* mineral water (1969); *Libby* canned fruits and vegetables (1970); *Stouffer's* frozen foods (1973); *Carnation* (1985); *Buitoni-Perugina* pasta and Italian cuisine (1988); *Rowntree* chocolates and confectionery (1988); and *Perrier* mineral water (1992). Throughout the years, Nestlé constantly developed products of its own creation—*Nesquik* was introduced in 1948—and improved and adapted existing ones to suit changing consumer tastes. Since its origins, Nestlé built its reputation around innovation, quality products, and strong brands.

In 1974, Nestlé made its first foray beyond the food and beverage sector with a minority investment in the French cosmetics company L'Oréal, which marketed products worldwide. Nestlé made a second non-food venture in 1977 with the acquisition of Alcon Laboratories of Fort Worth, Texas, a manufacturer of pharmaceutical and ophthalmology products.

Nestlé in 2001

Nestlé was not only the world's largest food company, it was one of the most thoroughly international companies in the world. Less than 2% of its sales came from the domestic Swiss market. At the end of 2000, it operated 479 factories in 81 countries, employed approximately 225,000 people, and its products were sold in every country around the globe, even North Korea. It had over 8,000 mostly local product brands for an even wider choice of recipes and sales of CHF81[2] billion in 2000 (see **Exhibit 1**). Despite its size, Nestlé's management structure was relatively flat with only 12 functions reporting directly to the CEO (see **Exhibit 2**). In terms of worldwide market share, it was estimated that Nestlé had 1.4% of the food and beverage business and 2.6% of processed and branded products. The company was almost exclusively concentrated in food and beverages, with only 4% of its total sales coming from outside the sector.

The company's strength was its internationally recognized branded products. Six worldwide corporate (i.e., strategic) brands that cut across broad food categories and covered a variety of individual products contributed about 70% of total sales. The strategic brands included *Nestlé* (chocolate and confectionery, ice cream, dairy, breakfast cereals, infant and dietary foods), *Nescafé* (soluble coffee), *Buitoni* (culinary/frozen food), *Maggi* (culinary/frozen food), *Friskies* (pet food), and

[2] Exchange rate at the end of 2000: 1USD=1.61 CHF (Swiss francs).

Nestea (beverages) (see **Exhibit 3**). The Nestlé umbrella brand was the largest and most global, accounting for 40% of the company's total sales.

Nestlé was the market leader in many of the categories in which it competed. It was the global number one player in soluble coffee, dairy, mineral water, chocolate/confectionery, and infant nutrition, and strong number two in ice cream and pet food (see **Table A**). Geographically, Nestlé generated the bulk of its sales from mature markets, with Western Europe generating the highest share of turnover. In the United States, where it was perceived as a chocolate company, Nestlé became the second biggest food manufacturer with a broad based product portfolio in food. Nestlé was slightly better exposed to emerging markets than its chief competitors[3] (see **Table B**).

Table A Nestlé Market Position for Selected Categories

Category	World	Europe	North America	ROW
Soluble coffee	1	1	1	1
Bottled water	1	1	1	NM
Chocolate/malted drinks	1	1	1[a]	1
Condensed/evaporated milk	1	1	1	1
Powdered milk	1	NM	NM	1
Infant nutrition	1	1	4	1
Chocolate/confectionery	1	1	3	2
Frozen prepared dishes	1	2	1	NM
Dehydrated bouillons/seasonings	1[b]	1	NM	1
Ice cream	2	2	2	2
Chilled desserts	1	2	-	NM
Breakfast cereal	NM	2	NM	2
Pet food	2	2	2	2

Source: Nestlé

[a]Tied with Bestfoods

[b]Impulse segment

Table B Sales Breakdown by Region Compared with Peers, 1999

	Nestlé (%)	Unilever (%)	Danone (%)
Western Europe	38.0	45.0	71.7
North America	23.0	21.6	7.7
Other (Australia/New Zealand/ Japan/South Africa)	8.0	6.0	NA
Total developed markets	**69.0**	**72.6**	**79.4**
Latin America	16.0	12.0	7.5
Eastern Europe	3.0	2.0	4.3
Asia Pacific	7.0	9.0	8.8
Other (Africa/Middle East)	5.0	4.4	NA
Total developing markets	**31.0**	**27.4**	**20.6**
Total Sales	100.0	100.0	100.0

Source: Company data, UBS Warburg estimates

[3] Unilever also sold personal care and household products.

Taking Charge

Salesman to CEO

The 57-year-old Brabeck joined Nestlé in 1968 after studying economics in college in Vienna. He began his career peddling ice cream and frozen foods from a truck to local markets and cafes in his native Austria. In 1970 he was assigned to Chile, where he worked his way up the ladder to fill the roles of national sales manager and director of marketing. His assignment coincided with a period of national strife surrounding the coming to power and overthrow of the Marxist Allende government. Operating in a business climate charged with adversity and chaos, Brabeck said, was excellent management experience for a young executive.

Altogether he spent 17 years in Latin America, eventually serving as country manager in Ecuador and Venezuela. In 1987, he was summoned to corporate headquarters in Vevey, and over the next 10 years headed the culinary products division, then strategic business development with worldwide responsibility for half of the Nestlé product groups, marketing services, communications, and public affairs. Brabeck was fluent in German, French, Italian, Spanish, and English. In late 1995, a year and a half prior to Maucher's retirement from his executive function, Nestlé announced publicly that he would be the company's next CEO.

Four Pillar Strategy

In his inaugural address as CEO to a group of market heads in June 1997, Brabeck warned about the dangers of complacency and exhorted everyone to keep a "vigilant attitude and commitment to continuous improvement." He outlined what he called his "Blue Print for the Future," which centered on "four strategic pillars to achieve worldwide sustainable competitiveness." They were:

1. Low cost, highly efficient operations
2. Renovation and Innovation
3. Product availability: whenever—wherever—however
4. Consumer communication

He viewed the strategy as a very pragmatic approach to reaching his goal of 4% annual real internal growth. "If I just wanted to grow by acquisition," he said, "I can do this with a very good negotiator and a good banker." Real internal growth was "a much tougher way of growing, but was a healthier way." He felt greater internal efficiency was absolutely necessary to make Nestlé a lean, flexible organization capable of responding to the increasingly fast changing consumer demands of the globalized marketplace. The successful implementation of the four-pillar strategy produced RIG of 4.4% in 2000.

Efficient operations The continuous improvement program helped generate significant cost savings. The company sold and closed plants, improved manufacturing processes, and maximized assets by combining production facilities. Benchmarking of labor and material costs and the application of new technologies led to better utilization of resources and less raw materials, packaging, and labor. "We achieved operational efficiency savings in the order of CHF3.1 billion," Brabeck said, "and only in the production area, which is a substantial savings."

Renovation, innovation Brabeck restructured the company's research and development program, shifting from small, decentralized units to a few large, resource intensive centers organized by product groups. Among other things, it permitted much better feedback of information about product quality, etc. from different geographic regions. Basic scientific research was directed toward discovering new "proprietary, protectable, patentable" products. Emphasis was put on looking for ways to reinvigorate old brands, such as finding multiple uses for them. An established brand such as *Nesquik*, for example, which was sold traditionally as a powder, was developed into syrup form and also in ready-to-drink varieties.

Management took an aggressive stance to portfolio streamlining, disposing of underperforming businesses (U.S. roast and ground coffee), products (cheese, frozen potatoes), and brands (Findus frozen foods) (see **Exhibit 4**). The move sent a powerful signal to investors that Nestlé was becoming more proactive in dealing with low growth and nonstrategic parts of its portfolio. To judge the performance of Nestlé products, Brabeck instituted a 60-40 preference rating system. All units benchmarked their products both against direct competitors and similar products, which included private labels. The Nestlé quality benchmark system said that each Nestlé product had to be preferred by 60% of participants in blind testings. For a product that failed to achieve the 60% level, a decision could be made on measures to reinvigorate it.

Product availability In the modern environment, consumers increasingly were turning to non-traditional means of purchasing their products. Nestlé's main retail outlets had long been grocery stores and supermarkets. In order to make its products readily available to consumers, the company pursued new sales channels such as convenience stores, bodegas, kiosks, vending machines, etc. The purpose was to put Nestlé products into the hands of consumers whenever, wherever, however they wanted to experience them.

Nestlé's Food Service division became a more important channel and was bringing in solid growth marketing Nestlé products to restaurants, cafeterias, airline caterers, etc. It aggressively sought business opportunities with fast food chains such as McDonald's (e.g., with *Nescafé*). Brabeck saw Food Service as a major vehicle for growth in the future, and many executives in the company referred to the division as an unofficial food and beverage product category in the Nestlé organization.

Consumer communication With the explosion of cable television channels and personal computers in the 1990s, Nestlé explored new ways of communicating with consumers. The company made wider use of its birds nest logo—giving it greater prominence, expanding the number of products that carried it—as an assurance to consumers that they were getting all the things they expected from a Nestlé product—quality, nutrition, taste, safety. Novel methods of direct communications were created. In France, Nestlé marketing teams offered morning train commuters a free breakfast that featured Nestlé products—*Nescafé*, *Libby* juices, *Milk Maid* condensed milk, Nestlé cereals from its CPW joint partnership, *Herta* deli ham. The company was not just trying to raise interest in its products; it also was promoting the value of eating a healthy, nutritious morning meal.

Beginning in the mid-1990s, it launched direct marketing with Nestlé food clubs for various branded products, using databases to contact consumers of those products. A Buitoni Club, for instance, was made available for people who loved Italian cooking and wanted to learn more about it. In different markets there were Nestlé food club websites for products such as *Friskies*, *Nesquik*, *Nescafé*, and *Carnation*. In certain Nestlé businesses, consumer databases helped gain consumer insight for better products.

Although Nestlé did not engage directly in e-tailing except for its *Nespresso* Club, it did have e-marketing agreements with several companies, such as peapod, webvan, and homegrocer.com.

Research and Development

Product Technology Centers

The driving force behind the second strategic pillar, renovation and innovation, was research and development, which always had played an important role at Nestlé. Brabeck completely restructured the decentralized system that existed when he took over to bring it in line with his campaign to leverage Nestlé's strengths (see **Exhibit 5**). Rupert Gasser, whom Brabeck assigned to oversee research and development activities, said: "We eliminated a number of R&D units that were dealing with issues below a critical minimum of resources needed to do an efficient job, and we redeployed [resources] into established centers that had all the technical and scientific know-how needed to support the renovation and innovation process in a given business area."

The company formed eight sophisticated Product and Development Centers (PTCs), each one focused on a product category in Nestlé's business portfolio with the concentrated resources of 200-300 scientific and technical professionals. The PTCs often worked in tandem with specialized research and development centers and factories. Nestlé's R&D center in Marysville, Ohio, for instance, had long been important for coffee development and worked closely on specific parts of a project with the PTC for beverage products in Orbe, Switzerland. Similarly, the R&D center in Amiens, France, which specialized in pet treats, a very important product segment in Europe, worked in tandem with the PTC for pet food located in St. Joseph, Missouri. Gasser said: "The PTC is responsible for coordinating the annual working programs, maintaining alignment with the business strategy, and keeping contact with the markets and SBUs."

The PTCs also integrated their work into markets with adaptation centers. Smaller in size and with fewer resources, adaptation centers were regionally focused, drawing on the experience of PTCs but adapting products and technologies to fit regional and local requirements. Shelf-stable culinary products developed at the PTC in Kemptthal, Switzerland, for example, were modified in Singapore to satisfy consumer preferences in the Southeast Asian region. In addition to the adaptation centers in Singapore and Ivory Coast, another was scheduled to open soon in Israel. Furthermore, Gasser said, "For non-strategic businesses, such as cold sauces, we have provided two other groups. While a full-fledged PTC is not justified, we have dedicated smaller centers—one in Germany for sauces, another in the United States for frozen foods." As with all centers, the underlying scientific research to support the health, nutrition, quality, and social satisfaction of products was derived from work done at the Nestlé Research Center.

Nestlé Research Center for Basic Research

Nestlé's science center in Lausanne, Switzerland performed the fundamental advanced scientific research relating to its businesses. A large facility with a permanent staff of approximately 550 people, plus another 100-150 guest professors and graduate students, Lausanne, Gasser said, "was the heart at the center of the body. The science created there flowed to all the PTCs and adaptation centers." A related but much smaller facility in Tours, France of around 50 people carried out basic research in plant science.

With the creation of PTCs, Nestlé re-oriented its basic scientific research to focus on three areas—nutrition; food safety and product quality; and food science and advanced food technology. Toxicological and microbiological studies were undertaken to identify possible risks that could emerge in the future, and what they could mean in terms of food safety and product quality. All the analytical methodology was maintained on file in Lausanne for eventual utilization by regional laboratories and factories.

Research into food science and advanced food technology didn't focus on existing unit operations, but looked to the future. Gasser explained:

> Due to developments in genomics, we understand the role of proteins much better. As a consequence, we look for very novel kinds of technologies that maintain the properties of these proteins. No equipment builder today can anticipate this because they don't have the knowledge. But it is very important for us to create this know-how and bring it into the development process.

Nestlé Spirit

To mark the generational change in leadership with a sense of continuity, Maucher and Brabeck co-authored a document, "Nestlé Leadership and Management Principles" (see **Exhibit 6**), for distribution to all employees. The large number of acquisitions under Maucher had brought many new employees into the company, and both felt it necessary to issue a formal declaration of the company's values and guiding principles—commitment to quality, respect for all cultures and traditions, dedication to people and products, etc. It was not a mission statement, but a clear message to employees, Brabeck said, that "there would be change, more of it and in ever shorter periods, but that the leaders would remain committed to the values [that employees] knew and could identify with."

Nestlé's traditional method of decentralized operations gave country managers—called market heads—a large degree of autonomy in matters dealing directly with consumers. The company felt local management understood the cultural traits, tastes, and motivations of consumers, and could best translate that knowledge into products tailored to meet their needs, which in turn would lead to long-term consumer-product relationships. Thus, within company guidelines product recipes, pricing, marketing, and promotions were decided largely at the local level, while product strategy, strategic branding, investments, and research and development were centralized in the strategic business units (SBU) in Vevey. Brabeck particularly wanted proactive leaders and he let it be known that he "made an effort to look for non-conformists." He claimed that he would prefer promoting someone who had made a mistake once or twice and learned from it because they had acted, made a decision, taken a risk. "I am not looking," he said, "for career fetishists."

Brabeck described Nestlé's management style as "the pragmatic, non-doctrinaire approach of the Swiss," in which "certain core virtues" dominated—"respect for hard work, straightforwardness, and simplicity." The company's Swiss culture inculcated an ethos in its employees to work hard but quietly toward achieving results, and it encouraged a spirit of cooperation among employees, wanting them to share ideas, skills, knowledge, and experience for the common purpose of adding value to the company. Nestlé repeatedly stated that its primary objective was to serve the needs of consumers, and though it strove to provide value for investors, it was not a short-term oriented company. Frank Cella, Executive Vice-President for Strategic Business Units, explained how Nestlé addressed consumer needs:

> We don't go into a market like India or China and say there's one Indian taste or there's one Chinese taste. There are very definite regional tastes that we go in and study. We have people go into consumers' homes to understand how they prepare food—what seasonings they use, how they use them, what their traditions are, etc. That helps us to develop products. It's that

specific. . . . What we do is sell one consumer, one shopper at a time, frequently one dollar at a time. Knowing what the consumer needs, satisfying those needs, and doing it over and over again is what Nestlé is about.

Within financial and business circles, Nestlé was known as an earnest, steadfast company that disdained flash and flamboyance and yet stayed current or ahead of business trends. "Nestlé has always been reticent about the latest management fads," Brabeck said, "and we looked with some amusement at the theories . . . about the non-hierarchical company of the future." It was modest about communicating its accomplishments to outsiders. Brabeck liked to cite the adage that a chicken never clucked until it produced the egg as a way of explaining the company's reserved attitude. "We should never forget," he told the company's market heads, "that we are here to serve simple consumers with simple products. Therefore, we have to be simple and modest, no matter how big Nestlé is."

Raw Material and Packaging Costs

In 2000, raw material costs amounted to approximately 24% (CHF19.7 billion) of total sales, and four products—coffee, cocoa, milk, and sugar—accounted for over 40% of that figure. By far the largest raw material expense, about 20% of the total spent, was for milk. It was a perishable, non-tradable commodity—i.e., not traded on any exchanges—that was used in many products. Nestlé's needs, however, were only a small part of global milk production. The company purchased much of its fresh milk supplies from local milk districts for delivery to nearby Nestlé processing plants. In most countries, milk was heavily influenced by government price and food safety policies.

Coffee, cocoa, and sugar were tradable commodities, and each accounted for 5%-7% of raw material costs. Nestlé's presence in the coffee and cocoa markets was relatively important. It purchased approximately 12% of global coffee production and 10%-11% of global cocoa output. Nestlé was committed to the long-term stability of the markets and followed a strictly non-speculative approach to purchasing. It used the New York and London commodity exchanges only for hedging and pricing purposes; it never took delivery from an exchange. The company pursued a policy of "noncrisis intervention" during periods of market turbulence, preferring to ride out the storm and avoid actions that would further fuel speculation.

There was no centralized purchasing function for raw materials at the company. In keeping with its policy of decentralized management, all hedging and purchasing was done locally. In coffee and cocoa producing countries where Nestlé had a manufacturing facility, the products were bought directly from local farmers or cooperatives. In developed markets where commodities were imported—Europe, North America, Japan, Australia—Nestlé purchased them from multinational trading companies. However, it did maintain a small team to provide expert advice in commodities' price forecasting to management and markets.

Nestlé believed in paying fair prices for inputs. Unlike most competitors, it had been very supportive of international commodity agreements with coffee and cocoa producing nations. It avoided vertical integration by encouraging long-term local agricultural development, providing advice and technical assistance, for instance, to local dairy farmers. Gordon Gillett, senior vice-president for purchasing, explained:

> Nestlé has always been supportive of any pragmatic way of assuring price stability. Price stability at a reasonable price assures the incentive for growers to deliver the quantity and quality we desire. It gives us assured supply and the confidence to build our strategy,

marketing campaign, and promotional activity knowing we are not going to face a doubling or halving of raw material prices.

Nevertheless, coffee, cocoa, and sugar prices had been very depressed in recent years (see **Exhibit 7**) and the company was somewhat alarmed by the trend. In mid-2001, coffee was trading at 40-year lows. "Just when consumption was increasing rapidly for Nestlé," Gillett said, "there was no incentive for growers." "Nestlé today spends more on paper and board than it does for green coffee," he continued. "It has turned the world upside down because Nestlé's focus always has been on raw materials."

Packaging costs amounted to about 10% of the company's total sales. Once a big user of tinplate and glass, Nestlé had been moving increasingly toward less expensive flexible packaging—soft, collapsible pouch-like cartons capable of standing upright on a shelf. Most of the water products were sold in PET containers instead of glass, which was not only cheaper but also saved on transportation costs because the containers weighed much less than glass. Even the traditional bag-in-a-box combination was being replaced more and more by flexible packaging. Nestlé did not produce packaging material in-house, but purchased it from local manufacturers.

Product Groups

Nestlé organized its brands and products into five business categories (see **Tables C** and **D**).

Table C Sales by Product Group

Category	% Volume Growth in 2000	% of Total Sales in 2000	Sales in Millions CHF 2000	1999	1998
Beverages	5.6	28.3%	23,044	20,859	19,879
Milk products, nutrition, and ice cream	3.2	27.0%	21,974	19,411	19,175
Prepared dishes, cooking aids, & pet care	4.0	25.3%	20,632	20,185	18,765
Chocolate, confectionery, and biscuits	1.7	13.5%	10,974	10,195	10,485
Pharmaceutical products	7.3	5.9%	4,798	4,010	3,443

Source: Nestlé

Table D Profit (in millions of CHF) and Operating Margins by Product Group

Category	% of Total Profits in 2000	-------------2000-------------		-------------1999-------------		-------------1998-------------	
Beverages	38.3%	4,318	18.7%	3,764	18.0%	3,253	16.4%
Milk products	23.3%	2,620	11.9%	2,168	11.2%	1,837	9.6%
Prepared dishes	17.3%	1,948	9.4%	1,850	9.2%	1,617	8.6%
Chocolate	10.3%	1,166	10.6%	882	8.7%	976	9.3%
Pharmaceuticals	10.8%	1,212	25.3%	1,077	26.9%	915	26.6%
Unallocated items		(2,078)	-2.4%	(1,827)	-2.4%	(1,517)	-2.1%
Trading profit		9,186	11.3%	7,914	10.6%	7,081	9.9%

Source: Nestlé

Beverages

Coffee Beverage products generated the highest sales and operating profits in the company. Approximately one-third (CHF7.4 billion) of total beverage revenue came from water and two-thirds (CHF15.6) from "the rest," mostly coffee. It was estimated that one in five cups of coffee consumed around the world was a Nestlé product. *Nescafé* was one of the most widely recognized branded products in the world and gave Nestlé a dominant position in the global soluble coffee business. It was the number one seller in markets such as Germany, Italy, Spain, France, U.K, Mexico, Brazil, Canada, Australia, Japan, the Philippines, and South Africa. According to some financial analysts, *Nescafé* in 1999 accounted for 10% of Nestlé's total food/beverage sales and 27.4% of its profits.

Nescafé was never very popular in the U.S. market, where *Maxwell House* (Phillip Morris) and *Folger's* (Proctor & Gamble) competed fiercely for the top position. Consequently, with the development of freeze dried coffee in the mid-1960s, Nestlé decided to create a new brand, *Taster's Choice,* specifically for the U.S. market.

Nescafé came in more than 100 strengths and flavors tailored to local tastes—*Nescafé Expresso*, *Nescafé Cappuccino*, etc. Consumption of instant coffee was most popular in Europe (see **Exhibit 8**). The company had launched a major marketing effort in Eastern Europe to make *Nescafé* a daily part of life in those countries. A key challenge was to attract younger European consumers to the brand, which it was trying to do with specially developed flavors—for instance, *Nescafé Nes* in France, a range of flavored coffees under *Nescafé for you* in the Netherlands, and *Nescafé Ice* in the United Kingdom.

The company was excited by consumer response in 2000 to a new technology-based quality, *Nescafé Gold Blend*, which it called "the best soluble coffee ever produced by Nestlé." The product was well received in the United Kingdom and Japan, two of Nestlé's biggest coffee markets, and was set for a wider launch. Nestlé promoted *Nespresso,* a coffee line extension, through shop-in-shops in major European department stores where consumers could purchase the coffee-making system and supplies. In 2000, it opened the first *Nespresso* boutique store in Paris.

Nestlé's roast and ground coffee business, concentrated mainly in the Untied States and once considered a core unit, experienced increasingly stiff competition and low margins in the 1990s. In 1999, Nestlé sold its U.S. roast and ground coffee holdings, which consisted of the *Hill's Brothers*, *MJB*, and *Chase and Sanborn* brands, and retained only a limited position with local brands elsewhere, mostly in Sweden, Greece, Spain, and Germany.

Nestlé's biggest global competitor in the coffee business was Phillip Morris. In soluble coffee, Nestlé commanded 59% of the market to Phillip Morris' 13% share, while in roast and ground coffee Phillip Morris had 15% of the global market to Nestlé's 3% share (see **Exhibit 9**).

Bottled water By acquiring a 30% stake in *Vittel* in 1969, Nestlé took its first step into the mineral water sector. In 1971, Nestlé established a foothold in the German market with the Blaue Quellen group. Although Nestlé had flirted with mineral water since 1969, it never thought the business promising enough to pursue until the early 1990s when it made a strategic decision to enter the segment in force. With the US$2.3 billion acquisition of *Perrier* in 1992, Nestlé became the global market leader in mineral water. By 2001, its mineral and spring water brands included *Vittel, Contrex, Perrier, San Pellegrino, Levissima, Vera, Panna, Fürst Bismarck*, and *Naleczowianka* in Europe, and *Arrowhead, Poland Springs, Zephyrhills, Deer Park*, and *Ozarka* in the United States. All brands were identified with a specific water source, and that link drove consumer sales.

The *Nestlé Pure Life* brand of purified bottled water was developed for emerging markets. It was successfully rolled out in Pakistan in 1998, Brazil in 1999, and other selected Asian and Latin American markets in 2000. Nestlé planned to expand the brand into all markets within a few years. In 2000, spring water under the *Nestlé Aquarel* brand was launched in five European countries. Neither product was linked to a specific source and therefore they were sold under the Nestlé umbrella brand with the possibility of multi-site sourcing and bottling.

Nestlé executives thought water in general was a dangerously ignored resource and that future global demand would outstrip supply. Bottled water had a promising future as more consumers turned to it as an alternative to sugar or alcohol based refreshments, recognized the importance of minerals for personal health, and in preference to the quality of local tap water. Nestlé perceived it as a product where the company's quality assurance and efficient logistics could add value for the consumer. With low per capita consumption outside Western Europe (see **Exhibit 10**), the company saw enormous growth potential and looked for further acquisition opportunities. "We are now selling more water than *Nesc*afé," Brabeck said. "It's one of our fastest growing businesses." Nestlé's biggest competitor in mineral water was Danone, though the success of bottled waters had attracted interest in the sector from other multinationals such as Coca-Cola and PepsiCo. Increased competitive pressure from new entrants could create higher marketing costs and lower profit margins.

Other Nestlé was a major global player in chocolate and malt-based drinks, led by its *Nesquik* and *Milo* brands, and it sold fruit juices through the *Libby* brand. Through a partnership with Coca-Cola (worldwide, excluding Japan), the company pursued opportunities in the ready to drink beverage segment (canned coffees and teas), which were particularly popular in Asia. It competed with a similar Unilever (Lipton)/PepsiCo venture in several markets.

Milk Products, Nutrition, and Ice Cream

The Nestlé name was universally associated with powdered and condensed milks and infant formula, the original company products. They were often the strategic foundation for Nestlé's entry and growth in developing markets. The majority of Nestlé's powdered milk sales came from emerging markets. Infant cereal sales had a significant position in such major markets as India and Brazil. Nestlé also sold baby foods in jars, primarily in Europe. Nestlé was the world leader in shelf-stable milk with brands that included *Nido*, *Nespray*, *La Lechera*, and *Carnation*, and it dominated the U.S. market for powdered creamers with the *CoffeeMate* brand.

Adult nutrition included weight control products (*Nestlé Sweet Success*), sports nutrition (*PowerBar*), and nutritionally balanced breakfast foods (*Carnation Breakfast Bars* and *Instant Breakfast* drinks). Nestlé also marketed a variety of chilled dairy products with a nutritional emphasis. In 1994, Nestlé launched the LC1 range of fermented dairy products (yogurts and drinks) in France, and since had expanded them to other European markets. The products contained a patented *acidophilus lactobacillus* developed by Nestlé's science research center in Lausanne.

In mid-2001, Nestlé was in the process of forming a 50/50 alliance with the cooperative representing all New Zealand dairy farmers to distribute shelf-stable and refrigerated milk foods and beverages under its existing brands. The goals of the alliance included: combined sales progression in existing and new markets; optimization of each others' assets and infrastructures; purchasing synergies and optimal use of research and development and product development resources.

The Nestlé-General Mills joint venture, Cereal Partners Worldwide (CPW), for breakfast cereals outside North America was hugely successful. CPW operated in almost 80 countries selling such popular brands as *Cheerios* and *Wheaties*. Its consolidated market share in those countries was 21%, a strong number two position behind Kellogg.

The company had expanded its position in the global ice cream business in the 1990s through several acquisitions. About 70% of sales were from local brands and 40% were sold through channels other than mass-retail channels. It marketed a wide variety of novelties from carts, coolers, vending machines, etc. with blue swimming pool visual identity graphics for easy consumer recognition. Nestlé was the number two global player with 9% market share, behind Unilever's roughly 15% market share. It was continuing to make selective acquisitions. In mid-2001, Nestlé announced that it was purchasing the other half of its joint venture with Haagen Dazs USA and Schöller, a major European ice cream manufacturer.

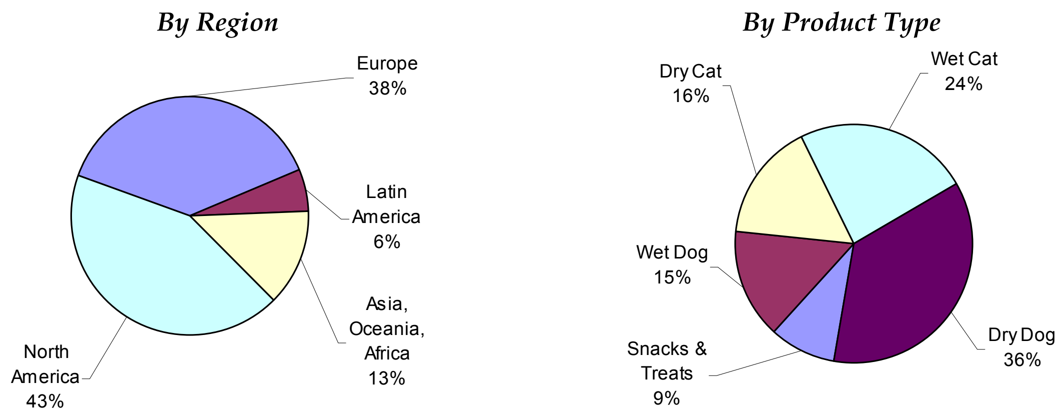
Prepared Dishes, Cooking Aids, and Pet Care

The division contained a variety of product lines, from frozen foods (*Stouffer's*), to soups, bouillon, and sauces (*Maggi*, *Crosse & Blackwell*), to pasta and sauces (*Buitoni*), to delicatessen products and cold meats (*Herta*), to pet food (*Friskies*, *Alpo*). A strong focus on local foods and cooking habits generated strong sales and profits, especially in cooking aids and prepared dishes, the group's priorities in the culinary sector. The division as a whole was benefiting from the global trend toward convenient food, which required little home preparation. Analysts applauded Nestlé's efforts to divest the group of under-performing and low margin brands, such as Findus (frozen foods), and to concentrate more and more on value-added products where it had better control over pricing and could boost margins. Nestlé was a leading player in all the segments it competed in, though in many instances it ran neck-in-neck with Bestfoods, which had been purchased in 2000 by Unilever.

Nestlé had stumbled into the pet food business in 1985 as a result of the Carnation acquisition, which brought with it the *Friskies* brand of cat food. Rather than dispose of the brand as initially planned, however, the company had decided by 1990 to make a new growth platform of pet foods, which enjoyed high profit margins and a worldwide trend toward increasing pet ownership. In early 2001, Nestlé announced the US$10.3 billion acquisition of U.S. pet food giant Ralston Purina. If the deal received the approval of all the various government regulatory agencies, Nestlé said it intended to replace Friskies with Ralston Purina as one of its six strategic brands.

Analysts were highly supportive of the purchase, viewing it as an excellent fit. Nestlé was predominant in wet pet food with a strong bias toward cats, and its largest market was Europe. Conversely, Ralston Purina was almost completely in the more popular dry pet food with a strong bias toward dogs, and its biggest markets were North and South America. In terms of sales channels, Nestlé was primarily sold in traditional grocery stores, while Ralston Purina had penetrated pet-specialty stores, a growing and important new outlet. Nestlé estimated the global dog and cat food market at US$25 billion in 1999, larger than sugar confectionery, bottled water, or ice cream. More than 80% of sales came from the high pet owning countries of Europe and North America (see **Table E**). The union with Purina would make Nestlé the leader in the North American pet food category and allow it to challenge number one player Mars for global leadership.

Table E Global Dog & Cat Food Market (1999)



Source: Nestlé

Chocolate, Confectionery, and Biscuits

Nestlé was the world's leading chocolate and confectionery company with approximately 12% global market share, followed by Mars with about 10% share. The company's principal international brands included *Nestlé*, *Crunch*, *KitKat* (except in the United States, where it was sold by Hershey), *Smarties*, *Lion*, *After Eight*, and *Polo*. They were complimented by strong local brands such as *Cailler*, *Milky Bar*, *Rossiya*, *Baby Ruth*, and *Butterfinger*. Nestlé's biggest selling brand was *KitKat*. Analysts had criticized the division for lackluster profit margins, but divestments and improved manufacturing efficiency had yielded more positive results by 2001.

The global market for chocolate and confectionery was highly fragmented, with the combined market share for the top five companies—Nestlé, Mars, Phillip Morris, Cadbury, Hershey, and Ferrero—estimated to be 41%. Fragmentation was greatest in developed countries, which accounted for 51% of consumption and where the top five had about 20% of the market. However, the same five manufacturers held roughly 55% market share in developing countries, where the largely youthful populations there were generating rapid increases in the consumption of sweets.

Nestlé was particularly keen on emerging markets, with their huge populations, and had spent several years' patiently building infrastructure and market position in those areas. It was also very well established in transition economies such as Russia. With rising disposable incomes, consumers in developing regions viewed of candy bars and similar treats as affordable luxuries.

Pharmaceutical Products

The small but highly profitable division, with margins consistently in excess of 20%, specialized in vision care through Alcon Laboratories and dermatology through Galderma, a 50-50 joint venture created in 1989 between Nestlé and L'Oreal. The division contributed about 4% of total sales and was the only non-food business to survive the company's divestment of non-food assets. Alcon, which had been strengthened by several acquisitions over the years, marketed therapeutic, surgical, and consumer products relating mostly to eye care. In 2000, Alcon undertook a significant expansion with the acquisition of Summit Autonomous, the market leader in refractive eye surgery. Galderma, with its own R&D center in France, sold products worldwide that treated skin ailments such as acne, psoriasis, rosacea, and nail fungus. In 2000, it launched a new subsidiary in Hong Kong.

Associated Companies

In 1974, in a 51%/49% arrangement with the family that founded L'Oreal, Nestlé became the minority partner in Gespaeral, the holding company that controlled 53.65% of Paris-based L'Oreal. Thus, Nestlé held 26.3% of the cosmetics giant. Nestlé had the right of first refusal of the Bettencourt shares. Many analysts considered the investment a crown jewel and underrated. L'Oreal marketed over 500 brands and more than 2,000 products worldwide in the personal care business—skin care, perfumes, hair care, sun protection, cosmetics, and professional products. It achieved double-digit growth in 2000 for the sixteenth consecutive year.

Well-Being

Recognizing the growing consumer awareness of the link between food and personal well-being, Brabeck created a new Division of Nutrition at Nestlé that reported directly to him. There were two significant demographic trends to be addressed from a nutritional perspective. On one hand, the population of developed markets such as Europe and North America was getting increasingly older and had special nutritional needs. Brabeck said surveys revealed "nobody is elderly anymore until one year before they die." Older consumers wanted to lead active lives and were concerned about the quality of life, and sought diets geared to their age and desires. On the other hand, the bulk of the world's population resided in developing countries and most of it was just entering adulthood. Those consumers wanted to look beautiful and feel good about themselves, and knew much of that satisfaction came from eating the right nutritional foods.

In addition to the Nutrition Division, Brabeck also had assembled committees of executives from different businesses and departments to discuss informally ways to promote well-being through such things as new product development. One committee handled a joint conceptual effort in the non-food area between pharmaceuticals (Alcon) and cosmetics (L'Oreal). Brabeck anticipated introducing more products along the lines of LC1 and new ways of communicating to fulfill the nutritional requirements and desires of both groups of consumers.

Challenge: Developing Markets

Emerging markets were progressively becoming the driving force for top-line growth and profits at Nestlé, a dividend of the company's long-term efforts to establish its presence in the developing world. Nestlé opened its first factory in a developing country in Brazil in 1921, and it built its business continuously there over the years despite periods of crises and hyperinflation. Nestlé's long-term involvement paid off for it became the number one food manufacturer in the Brazilian market, and several other Latin American markets as well, such as Mexico and Chile. Carlos E. Represas, head of Nestlé's Zone Americas, explained: "In spite of the fact that most of our development took place under public policy models of import substitution, early restructuring and flexibility have allowed Nestlé to maintain and even strengthen its number one position on the continent after the opening of its economies."

While business throughout Latin America continued to grow, the economic take-off of Asia began to make an impact. Michael Garrett, head of the company's Asia-Oceania-Africa Zone, cited three major developments since the mid-1990s that had fueled growth throughout the world—the Uruguay Round of GATT and regional trade agreements (EU, NAFTA, ASEAN, etc.) that drove trade in the agricultural sector; a significant decrease in transportation costs (in 2001 it was cheaper to ship a container of green coffee from South America to Japan than to transport it 60 km inland from the Japanese port to the Nestlé factory); and advances in information technology.

Nestlé studied the evolution of purchasing power and population growth around the globe to better understand market trends (see **Table F**). Developing nations, with 80% of the world's population, had high numbers of people shifting into the trigger point category, set at US$1,800 annually, when according to Nestlé they started to accelerate their purchases of industrial products and some manufactured food. Herbert Oberhänsli, Assistant Vice-President Economic and International Relations, said:

> Paying full attention to consumers at the lower end of the economic scale is something Nestlé does systematically. The idea is to pick up the consumer as soon as possible to establish the Nestlé brand with him. That would mean to go into a market that is not yet a rich country and start with some essentials like milk products or the *Maggi* range. . . . They want to have a very small unit of something they see as their future—a sachet of *Nescafé*, one *Maggi* cube, a small portion of condensed milk. We have seen so many people moving out of poverty in the last ten years and gain a decent income, and they don't forget Nestlé. That's been our experience.

In the early 1990s, Nestlé took advantage of the ASEAN Industrial Joint Venture (AIJV) trade agreement, a duty reduction scheme among ASEAN nations, to move away from its traditional method of sourcing and manufacturing and gain greater efficiency from economies of scale. The import substitution policies that most developing nations had long followed dictated that multinational companies build factories and manufacture products locally. With AIJV and its successor agreement, Nestlé was permitted to consolidate manufacturing in the region and import within ASEAN countries under low tariff rates. The ASEAN members consisted of six countries—Singapore, Malaysia, Thailand, Indonesia, Brunei, and the Philippines—with a combined population of about 450 million people.

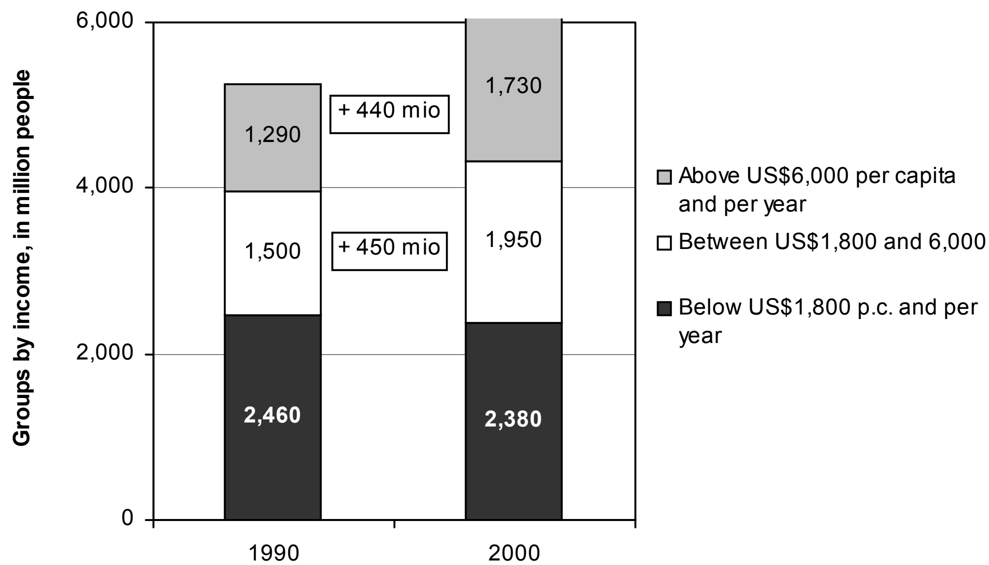
The AIJV was an early example of the type of regional trade pact that Nestlé felt would become more common in future years. Almost simultaneously, the company's Americas Zone (AMS) also moved forward with regionalization. Grouping several Latin American countries together, Nestlé increased inter-market supply and developed competence centers and shared service centers, decreasing the number of reporting points from 21 to 11.

Garrett said the "ability to manage complexity was facilitated by the application of information technology," and the AOA zone had pioneered in the use of IT throughout its operations. The zone implemented a business excellence program to measure the business practices and processes of all its units, and adapted the best ones for all markets. In the late 1990s, the zone began to separate tradable (coffee, infant formula) and non-tradable (chilled dairy) products, and centralize the sourcing and manufacturing of tradable products. "The issue we've really been addressing in the last 10 years," Garrett said, "is to move from producing everything locally to regional manufacturing centers capable of achieving economies of scale and increasing our competitiveness."

Nestlé had followed a traditional approach to manufacturing in China because of the country's immense population (1.2 billion) and geographic size. In 2001, Nestlé had 17 factories in Greater China, and between 1995 and 2001 its sales volume had grown from approximately CHF150 million to CHF 1.4 billion. Garrett felt the company was well positioned there and saw a very bright future in the market.

Table F People Benefiting from Globalization

Growing Number of People Worldwide with Sustainable Livelihood



Source: Nestlé

Brand value To bring rationale to the 8,000-plus products Nestlé sold globally, all products, with the exception of source-linked mineral waters, were grouped under one of the six corporate brands. The Nestlé brand generated 40% of total sales. The 60% of sales from brands not prominently identified with Nestlé (e.g., *Friskies*, *Buitoni*, *Maggi*, etc.) still carried the Nestlé bird's nest Seal of Guarantee so that consumers could clearly recognize the company behind those products.

Furthermore, Nestlé managed its brand portfolio by constantly benchmarking its products on a business-to-business basis against the industry standard EBITA for competing products. Nestlé executives credited Brabeck with really pushing the benchmarking of products and brands. The program assumed that Nestlé, as the largest food company in the world, should have products equal to the best EBITA in any category. If the Nestlé product fell short of the EBITA benchmark, reasons for the gap were examined and efforts undertaken to bring it up to world class standards. If achieving those standards was considered unobtainable, then management could make an alternative decision.

Good citizen Around the world, Nestlé always had worked hard to integrate its business with local cultures and be perceived as a local company. It was the company's best protection, Garrett said, against becoming the target of a backlash. He explained:

> We try hard in a modest, almost a humble way, to work with the governments and various stakeholders in the business to be seen to act as a very responsible corporate citizen. In

Indonesia, for example, when everyone else left the country during the recent crisis, our people remained. We are accepted as part of the local scene in developing nations, in a good way. . . . We work closely with farmers and use local raw materials wherever possible. Developing countries value this commitment very highly.

GLOBE

In mid-2000, Brabeck launched the GLOBE (Global Business Excellence) program to improve the performance and operational efficiency of the Nestlé Group, worldwide. It was the most ambitious business process-reengineering program that Nestlé had ever initiated. It was not simply an IS/IT project, but rather a business benefit driven program with three objectives: 1) harmonization of "best practice" business processes; 2) standardization of master data; and 3) standardization of the information system infrastructure. GLOBE would enable Nestlé to leverage its size as a strength, rather than a liability; unite and align the Group internally so that it could be more competitive externally; and exploit the power of e-technology. Three pilot markets—Switzerland, the Andean Region (Chile, Peru, and Bolivia), and Malaysia/Singapore—had been chosen to implement the full GLOBE solution in 2002. Globe would be implemented globally by 2005. One of the major advantages would be the ability to access information in multiple settings. "We are breaking down our businesses into small three-dimensional cells," Brabeck said. "You have geography, then sales channel, and then product category."

The program was designed to promote business excellence. By examining all aspects of business practices, the most efficient methods could be identified and adapted to different markets and products. It was a way for Nestlé to gain significant cost savings by leveraging its size, but it was strictly a support mechanism. "GLOBE is centralized, but not the decision-making," Brabeck said. "I think it will give us an enormous competitive advantage. It should help us to have size, complexity, and still be the most efficient. It would allow us to grow even faster." It was a key element of his restructuring plan to design Nestlé to grow 6% or more annually.

Looking Ahead

More and more, consumers were demanding that multinationals provide them with products that fit their complex lifestyles. They wanted food that was nutritious, safe, traceable, and good tasting, and they wanted it in different forms and delivered in convenient outlets. At the same time, they expected companies to conduct their business in a socially conscious manner, such as showing sensitivity to environmental concerns and supporting the economic development of countries where they operated. Going forward, Brabeck wondered what new responsibilities Nestlé would have to accept in addressing the social, political, and cultural priorities of consumers in different regions of the world.

Exhibit 1 Consolidated Income Statement for Year 2000

In millions of CHF	2000	1999
Sales to customers	81,422	74,660
Cost of goods sold	(38,121)	(35,912)
Distribution expenses	(5,884)	(5,268)
Marketing and administration expenses	(26,467)	(23,887)
Research and development costs	(1,038)	(893)
Restructuring costs	(312)	(402)
Amortization of goodwill	(414)	(384)
Trading profit	9,186	7,914
Net financing cost	(746)	(998)
Net nontrading items	(99)	(57)
Profit before taxes	8,341	6,859
Taxes	(2,761)	(2,314)
Net profit of consolidated companies	5,580	4,545
Share of profit attributable to minority interests	(212)	(160)
Share of results of associated companies	395	339
Net profit for the year	5,763	4,724
As percentages of sales		
Trading profit	11.3%	10.6%
Net profit for the year	7.1%	6.3%
Earnings per share (in CHF)		
Basic earnings per share	149.1	122.1
Fully diluted earnings per share	147.8	120.7

Source: Company document

Exhibit 1 (continued) Consolidated Balance Sheet for Year 2000 (before appropriations)

In millions of CHF	2000		1999	
ASSETS				
Current Assets:				
Liquid assets				
Cash and cash equivalents	5,451		3,322	
Other liquid assets	4,680		3,348	
		10,131		6,670
Trade and other receivables		12,685		12,443
Inventories		7,168		7,383
Prepayments and accrued income		763		673
Total Current Assets		30,747		27,169
Fixed Assets:				
Tangible fixed assets				
Gross value	43,519		44,014	
Accumulated depreciation	(24,894)		(24,796)	
		18,625		19,218
Financial Assets:				
Investments in associated companies	2,173		1,828	
Deferred tax assets	2,569		2,293	
Other financial assets	2,692		2,431	
		7,434		6,552
Goodwill		7,902		5,258
Intangible assets		816		742
Total Fixed Assets		34,777		31,770
Total Assets		65,524		58,939

Exhibit 1 Consolidated Balance Sheet for Year 2000 (continued)

In millions of CHF	2000		1999	
Liabilities and Equity				
Current liabilities:				
Trade and other payables		10,001		9,635
Financial liabilities		8,376		7,967
Tax payable		1,035		985
Accruals and deferred income		3,762		3,595
Total current liabilities		23,174		22,182
Medium and long-term liabilities:				
Financial liabilities		4,768		4,905
Employee benefit liabilities		2,860		2,822
Deferred tax liabilities		1,550		1,327
Tax payable		53		72
Other payables		402		264
Provisions		2,204		2,289
Total medium and long-term liabilities		11,837		11,679
Total Liabilities		35,011		33,861
Minority interests		609		625
Equity:				
Share capital		404		404
Share premium and reserves				
Share premium	5,926		5,926	
Reserve for Treasury shares	2,232		2,873	
Translation reserve	571		839	
Retained earnings	23,388		17,439	
		32,117		27,077
		32,521		27,481
Less:				
Treasury shares		(2,617)		(3,028)
Total equity before appropriation		29,904		24,453
Total Liabilities and Equity		65,524		58,939

Source: Company document

Exhibit 1 (continued) Consolidated Cash Flow Statement for Year 2000

In millions of CHF	2000		1999	
Operating activities:				
Net profit of consolidated companies	5,580		4,545	
Depreciation of tangible fixed assets	2,737		2,597	
Impairment of tangible fixed assets	223		373	
Amortization of goodwill	414		384	
Depreciation of intangible assets	179		92	
Impairment of goodwill	230		212	
Increase/(decrease) in provisions and deferred taxes	(4)		101	
Decrease/(increase) in working capital	(368)		235	
Other movements	(140)		(352)	
Operating cash flow[a]		8,851		8,187
Investing activities:				
Expenditure on tangible fixed assets	(3,305)		(2,806)	
Expenditure on intangible assets	(188)		(139)	
Sale of tangible fixed assets	355		363	
Acquisitions	(2,846)		(440)	
Disposals	780		253	
Income from associated companies	107		86	
Other movements	39		(76)	
Cash flow from investing activities		(5,058)		(2,759)
Financing activities				
Dividend for the previous year	(1,657)		(1,469)	
Purchase of Treasury shares (net)	1,072		(2,311)	
Premium on warrants issued	81		--	
Movements with minority interests	(221)		(190)	
Bonds issued	1,016		328	
Bonds repaid	(1,143)		(400)	
Increase/(decrease) in other medium/long-term financial liabilities	(155)		500	
Increase/(decrease) in short-term financial liabilities	921		(3,488)	
Decrease/(increase) in marketable securities and other liquid assets	(2,788)		(355)	
Decrease/(increase) in short-term investments	1,452		12	
Cash flow from financing activities		(1,422)		(7,373)
Translation differences on flows		(175)		49
Increase/(decrease) in cash and cash equivalents		2,196		(1,896)
Cash and cash equivalents at beginning of year	3,322		4,984	
Effects of exchange rate changes on opening balance	(67)		234	
Cash and cash equivalents retranslated at beginning of year		3,255		5,218
Cash and cash equivalents at end of year		5,451		3,322

Source: Company document

[a]Taxes paid amount to CHF 2,714 million (1999: CHF 2,304 million). Interest received/paid does not differ materially from interest shown under note 2, "Net financing cost."

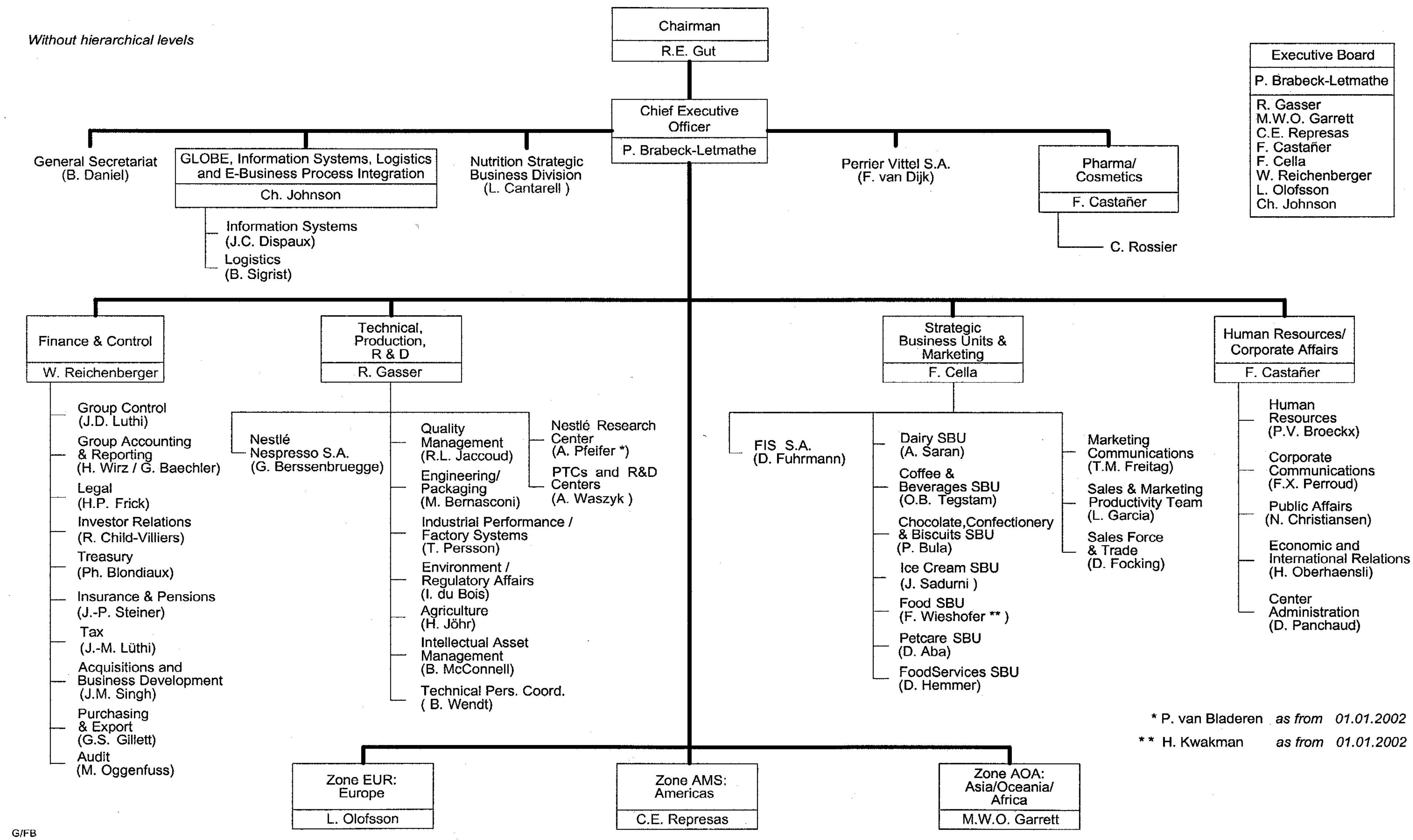
Exhibit 1 (continued) Financial Information—Ten-year Review

In millions of CHF (except for per-share data)	2000	1999[a]	1998	1997[b]	1996[c]	1995	1994[d]	1993	1992	1991
Results										
Consolidated sales	81,422	74,660	71,747	69,998	60,490	56,484	56,894	57,486	54,500	50,486
Trading profit	9,186	7,914	7,081	7,057	6,053	5,658	5,628	5,591	5,384	4,783
as % of sales	11.3%	10.6%	9.9%	10.1%	10.0%	10.0%	9.9%	9.7%	9.9%	9.5%
Taxes	2,761	2,314	2,000	1,842	1,552	1,561	1,647	1,669	1,745	1,605
Consolidated net profit	5,763	4,724	4,205	4,182	3,592	3,078	3,250	2,887	2,698	2,470
as % of sales	7.1%	6.3%	5.9%	6.0%	5.9%	5.4%	5.7%	5.0%	5.0%	4.9%
as % of average equity	21.2%	20.0%	19.5%	21.9%	22.9%	23.3%	19.9%	19.5%	18.4%	17.2%
Total amount of dividend	2,172[e]	1,694	1,469	1,376	1,180	1,043	1,040	972	870	793
Depreciation of tangible fixed assets	2,737	2,597	2,609	2,677	2,305	2,103	2,321	2,283	2,038	1,863
as % of sales	3.4%	3.5%	3.6%	3.8%	3.8%	3.7%	4.1%	4.0%	3.7%	3.7%
Amortization of goodwill	414	384	301	140	102	42	--	--	--	--
Balance sheet										
Current assets	30,747	27,169	26,467	25,671	23,070	20,927	21,420	20,982	20,670	19,195
of which liquid assets	*10,131*	*6,670*	*7,963*	*8,102*	*5,860*	*5,124*	*5,132*	*5,084*	*4,688*	*4,888*
Fixed assets	34,777	31,770	30,236	25,910	23,605	19,189	23,807	24,178	23,803	19,795
Total assets	65,524	58,939	56,703	51,581	46,675	40,116	45,227	45,160	44,473	38,990
Current liabilities	23,174	22,182	22,567	20,985	19,859	17,410	17,297	18,166	20,019	14,889
Medium and long-term liabilities and minority interests	12,446	12,304	11,321	9,990	9,239	8,862	10,986	11,334	10,524	8,731
Equity	29,904	24,453	22,815	20,606	17,577	13,844	16,944	15,660	13,930	15,370
Expenditure on tangible fixed assets	3,305	2,806	3,061	3,261	3,054	3,056	3,029	3,093	3,191	2,815
as % of sales	4.1%	3.8%	4.3%	4.7%	5.0%	5.4%	5.3%	5.4%	5.9%	5.6%
Data per share										
Weighted average number of shares outstanding	38,652,783	38,677,213	39,293,665	39,331,126	39,363,637	39,220,756	38,838,376	37,759,826	36,938,374	36,800,050
Consolidated net profit[f]	149.1	122.1	107.0	106.3	91.3	78.5	83.7	76.5	72.2	66.4
Equity[f]	774	632	581	524	557	459	436	415	373	413
Dividend[f]	55.0[g]	43.0	38.0	35.0	30.0	26.5	26.5	25.0	23.2	21.3
Payout ratio	36.9%[g]	35.2%	35.5%	32.9%	32.9%	33.8%	31.7%	32.7%	32.2%	32.0%
Stock exchange prices (high/low)[f]	3,893/2,540	3,107/2,508	3,498/2,122	2,192/1,421	1,487/1,250	1,298/1,090	1,437/1,063	1,294/1,015	1,162/857	876/651
Yield[h]	1.4/2.2[g]	1.4/1.7	1.1/1.8	1.6/2.5	2.0/2.4	2.0/2.4	1.8/2.5	1.9/2.5	2.0/2.7	2.4/3.3
Number of personnel	224,541	230,929	231,881	225,808	221,144	220,172	212,687	209,755	218,005	201,139

Source: Company document

(a) Figures prior to 2000 have not been restated following the first application of IAS 37 "Provisions, Contingent Liabilities and Contingent Assets." (b) Figures prior to 1998 have not been restated following the first application of IAS 19 (revised 1998), "Employee Benefits."(c) Figures prior to 1997 have not been restated following the first application of IAS 12 (revised 1996), "Income Tax." (d) Figures prior to 1995 have not been restated to reflect the change from net replacement values of tangible fixed assets to historical cost accounting. (e) As proposed by the Board of Directors of Nestlé S.A. This amount includes dividends payable in respect of shares with right to dividend at the balance sheet date (CHF 2,317 million) as well was those potentially payable on the shares covering options and shares held for trading purposes (CHF 35 million). (f) Figures prior to 1993 adjusted in order to make comparable the data per share, following a rights issue in June 1993. (g) As proposed by the Board of Directors of Nestlé S.A. (h) Calculated on the basis of the dividend for the year concerned, but which is paid out in the following year.

Exhibit 2 Nestlé Organization Chart, 2001



Source: Company document

Exhibit 3 The Six Worldwide Corporate Brands

Source: Nestlé

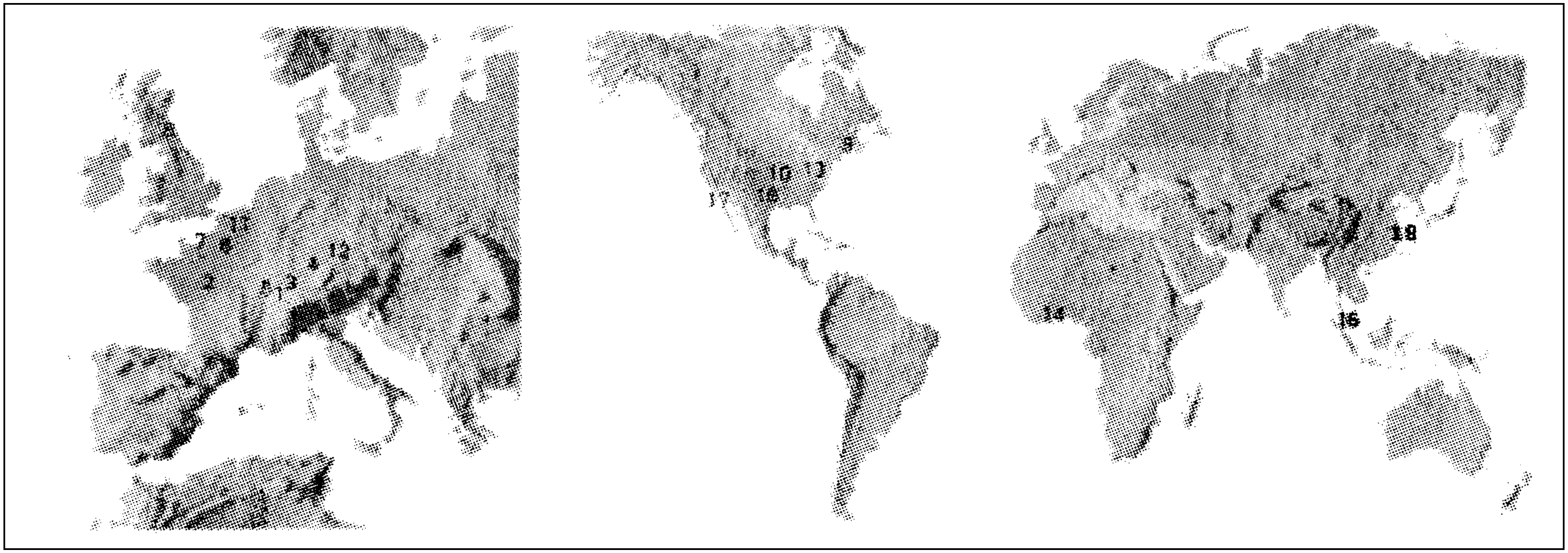
Exhibit 4 Main Acquisitions and Divestments (1997-2001)

Company	Business	Country	Deal	Stake (%)	Sales (CHF mio)
2001 (until October 2001)					
Ralston Purina[a]	Pet food	United States	Acquisition	100%	4,930
Schöller[a]	Ice cream and frozen food	Germany	Acquisition	100%	N/A
Black Mountain	Mineral water	United States	Acquisition	100%	60
Dar Natury	Mineral water	Poland	Acquisition	50%	N/A
Dreyers	Ice cream	United States	Incr. in participation	from 21% to 24%	N/A
Fonterra	Dairy	Americas	Joint venture	N/A	N/A
Haoji Food	Bouillons	China	Acquisition	60%	N/A
Mineralbrunnen	Mineral water	Germany	Disposal	42%	N/A
2000					
Powerbar	Performance nutrition	United States	Acquisition	100%	220
UCC	Vending for beverages	Japan	Acquisition	100%	616
Cargill s.a.c.i.	Pet food	Argentina	Acquisition	100%	72
Summit Autonomous	Eye care	United States	Acquisition	100%	150
Joe	Confectionery	Romania	Acquisition	100%	N/A
Nestlé Mackintosh	Confectionery	Japan	Incr. in participation	from 66% to 100%	200
Consomate/Rosa Blanca	Bouillons	Mexico	Acquisition	100%	N/A
Wyeth-Ayerst	Infant formula	Canada	Acquisition	100%	N/A
Kekkuti	Mineral water	Hungary	Acquisition	90%	N/A
Aberfoyle	Mineral water	Canada	Acquisition	100%	135
Valvita & Schoonspruit	Mineral water	South Africa	Acquisition	100%	N/A
Fresh Water	Mineral water	Argentina	Acquisition	100%	N/A
Findus brand and related assets	Frozen food	Europe	Disposal	N/A	900
Frozen potatoes business	Frozen potatoes	United States	Disposal	100%	N/A
Vismara	Processed meat	Italy	Disposal	100%	N/A
1999					
La Cocinera	Frozen food	Spain	Acquisition	100%	N/A
Svitoch	Confectionery	Ukraine	Acquisition	75%	N/A
Totole	Bouillons	China	Acquisition	80%	N/A
La Universal	Biscuit	Ecuador	Acquisition	100%	N/A
Haagen-Dazs	Ice cream	United States	Joint venture	50%	N/A
Quilmes	Mineral water	Argentina	Joint venture	N/A	N/A
Hills Bros, MJB, Chase & Sanborn	Roast and ground coffee	United States	Disposal	100%	N/A
Laura Secord	Chocolate retail	Canada	Disposal	100%	N/A
Cocoa processing	Cocoa processing plants	Malaysia & Italy	Disposal	100%	N/A
Alder/Bavaria	Cheese	Argentina	Disposal	100%	N/A
1998					
San Pellegrino	Mineral water	Italy	Incr. in participation	from 50% to 100%	N/A
Borden/Klim	Milk powder	Regional	Acquisition	100%	N/A
Spillers	Pet food	United Kingdom	Acquisition	100%	N/A
Nestlé Philippines	Nestlé products	Philippines	Incr. in participation	from 55% to 100%	N/A
Libby's	Canned meats	United States	Disposal	100%	N/A
1997					
Ault and Dairy World	Ice cream	Canada	Acquisition	100%	N/A
Shanghai Fuller	Ice cream and milk	China	Acquisition	100%	N/A
D'Onofrio	Ice cream and confectionery	Peru	Acquisition	81%	N/A
Basotherm	Eye care and dermatology	Germany	Acquisition	100%	N/A
Cremo	Ice cream and dairy	Venezuela	Acquisition	100%	N/A
Dairy Farm	Ice cream and dairy	China	Incr. in participation	from 51% to 100%	N/A
Contadina	Canned tomato	United States	Disposal	100%	N/A

Source: Company document

[a]Closing yet subject to customary regulatory consents

Exhibit 5 R&D Centers



Nestlé research in the food sector

1. Lausanne (CH)
2. Tours (F)

Product technology centers

3. Konolfingen (CH)
4. Kemptthal (CH)
5. Orbe (CH)
6. Beauvais (F)
7. Lisieux (F)
8. York (UK)
9. New Milford (USA)
10. Saint-Joseph (USA)

Research and development centers

11. Amiens (F)
12. Weiding (D) http://zams.nesusa.com/us/rd/marysville
13. Marysville (USA) Solon
18. Shanghai

Adaptation centers

14. Abidjan (IC)
15. Singapore

Research and development at Alcon

16. Fort Worth (USA)
17. Irvine (USA)

Source: Nestlé

Exhibit 6 Maucher and Brabeck Co-authored Document, June 1997

The Basic Nestlé Management and Leadership Principles

This document is a straightforward and pragmatic approach to put on paper some thoughts on management and leadership principles which should be applied in all regions and countries where Nestlé is active. It is definitely not a "mission statement".

Nestlé, over its long historical development from a small village operation to the world's leading food company, has demonstrated an enviable capability to adjust continuously to an ever-changing external environment, without losing its fundamental beliefs and core values, so important for long-term success. During the recent past, not only has Nestlé maintained this capacity but some of the traditional values have been revalidated and further strengthened.

Today—and even more so tomorrow—change will have an increasing influence on how we run our business. A complex and decentralised organisation like Nestlé will have to maintain a high degree of flexibility and speed in adjusting to these new realities to increase its global competitiveness without losing the coherence with our more longer term values and principles expressed in the document.

With an increasing number of people joining our company and working throughout the globe, we consider it very important that this document is fully understood and applied by Nestlé management people at all levels within our organisation. It replaces also our previously introduced Management Commitment/Employee Involvement concept.

Finally, we draw your special attention to the last paragraph of these principles which says: "Apart from professional skills and experience, the capacity and willingness to apply these principles are the main criteria for promotion—and not a person's passport, ethnic or national origin!"

H. Maucher *P. Brabeck*

1. General Principles

- Nestlé is more people and product oriented than systems oriented. Systems are necessary and useful but should never be an end in themselves.
- Nestlé is committed to create value for its shareholders. However, Nestlé does not favour short-term profit and shareholder value maximisation at the expense of long-term successful business development. But Nestlé remains conscious of the need to generate a reasonable profit each year.
- Nestlé is as decentralised as possible, within the limits imposed by basic policy and strategy decisions, as well as the group-wide need for co-ordination and management development.
- Nestlé is committed to the concept of continuous improvement of its activities, thus avoiding more dramatic one-time changes as much as possible.

2. Organisational Principles

Nestlé is in favour of:

- flat organisations with few levels of management and broad spans of control, including project teams and task forces. Networking and horizontal communication are encouraged without blurring the authority of the managers in the decision-making process. These principles aim to make the organisational structure and working methods more flexible and efficient, without undermining the basic hierarchy (the underlying concept being: as much hierarchy as necessary, as little as possible);

– clear levels of responsibility in the management structure while avoiding too many hierarchical levels and limiting staff work to those tasks necessary for the support of line management;

– well defined line and function responsibilities and their inter-linked character. Nestlé gives line responsibility the edge over functions in order to assure operational speed and responsibility. However, if functional departments (which are equally important) are overruled and feel strongly about a line decision, both parties should discuss the question or refer it to the next higher level for resolution;

– having at every level of the organisation a team with a leader and not a team as a leader (teamwork with responsible leadership).

3. The Nestlé Value Added Leadership Concept

Members of the Nestlé Management at all levels are more concerned with continuously adding value to the company than exercising formal authority. They delegate all that can be delegated without abdicating their proper responsibility.

4. Qualities and Characteristics of a Nestlé Manager

The higher the level of the position and the responsibility of a Nestlé Manager, the more he/she should be selected on the basis of the following criteria (in addition to professional education, skills and practical experience):

- courage, solid nerves and composure; capacity to handle stress
- ability to learn, open-mindedness and perceptiveness
- ability to communicate, to motivate and to develop people
- ability to create a climate of innovation
- thinking in context
- credibility: in other words "practise what you preach"
- willingness to accept change and ability to manage change
- international experience and understanding of other cultures.

In addition: broad interests, a good general education, responsible attitude and behaviour and sound health.

5. The Nestlé Concept of People Involvement

Involvement of Nestlé people at all levels starts with appropriate information and communication about the overall activities of the company and the specific aspects of their work.

Any changes and possible improvements should be discussed and explained. People should be invited to contribute their ideas to the process. This will motivate the Nestlé staff, create more job satisfaction, contribute to personal growth and, at the same time, improve the results of the Company.

Nestlé gives great importance to training and development of people but is also conscious of the fact that the selection of the right people is crucial and will substantially increase the effect and the results of the training efforts.

6. Basics of the Nestlé Culture

HIGH COMMITMENT TO QUALITY PRODUCTS AND BRANDS

Henri Nestlé was a German entrepreneur and a pharmacist, living in Vevey, Switzerland. Worried by the high level of infant mortality at that time and relying on scientific research, he created a revolutionary product "Farine Lactee Nestlé" ("Nestlé Milk Cereal") which has helped to save the lives of many children the world over. Since then, product quality, innovative capacity and strong brands have been a priority for Nestlé. From the very beginning, Henri Nestlé adopted his personal coat of arms, the nest, as a strong identity for the Company ("Nestlé" in Germany means "little nest").

Respect of other cultures and traditions

From its inception, Nestlé developed its business internationally. This was due in part to the entrepreneurial spirit of Henri Nestlé but also the fact that Switzerland was too small a market to achieve the necessary economies of scale. Also Nestlé was always aware of the fact that food products have to be closely linked to local eating and social habits.

That is why Nestlé from the very start always showed respect for the cultures and traditions of all countries where the Company sells its products. Nestlé makes an effort to integrate itself as much as possible into the cultures and traditions of the different countries where it operates. Nestlé, therefore, accepts cultural and social diversity and does not discriminate on ethnic, religious or any other basis.

Furthermore, Nestlé believes that its activities can only be of long-term benefit to the company if these are, at the same time, beneficial for the country in question. In short, one can say: global thinking and strategies but local action and commitment.

Main elements of the Nestlé culture to be respected everywhere

Apart from the international attitude and respect for diversity, Nestlé is committed to a number of basic cultural values. These values, which come partly from its Swiss roots, have also been developed during its long history and have proved useful and appropriate for its type of business. They can be summarised as follows:

- a more pragmatic than dogmatic approach to business
- being realistic and basing decisions on facts rather than dreams or illusions
- commitment to a strong work ethic, integrity, honesty and quality
- relations based on trust, expecting mutual integrity and rejecting intrigues
- a personalised direct way of dealing with each other, thus trying to reduce bureaucratic procedures to a minimum
- Nestlé people do not show off but are conscious of their worth and take pride in the positive image of the Company. Basically they are modest but not without style and sense of quality
- Nestlé people are open to dynamic and future oriented trends in technology, changes in consumer habits, business ideas and opportunities, but they maintain respect for basic human values, attitudes and behaviour. Nestlé is sceptical of short-term fads and self-appointed gurus.

Nestlé—a human company

Nestlé is convinced that its people are the most valuable asset of the Company. This is reflected in its attitude and in its sense of responsibility towards its people. Nestlé is not a faceless company marketing to faceless consumers. It is a human company providing a response to individual human needs the world over.

7. Management Commitment

Members of Nestlé Management at all levels are strongly committed to the Company, its development, its culture and the leadership concept as described above.

Apart from professional skills and experience, the capacity and willingness to apply these principles are the main criteria for promotion—and not a person's passport, ethnic or national origin!

Source: *The Basic Nestlé Management and Leadership Principles*, © 1997 Nestlé S.A., Vevey, Switzerland.

Exhibit 7a Coffee, Brazilian (NY) Spot Price (US$/lb)

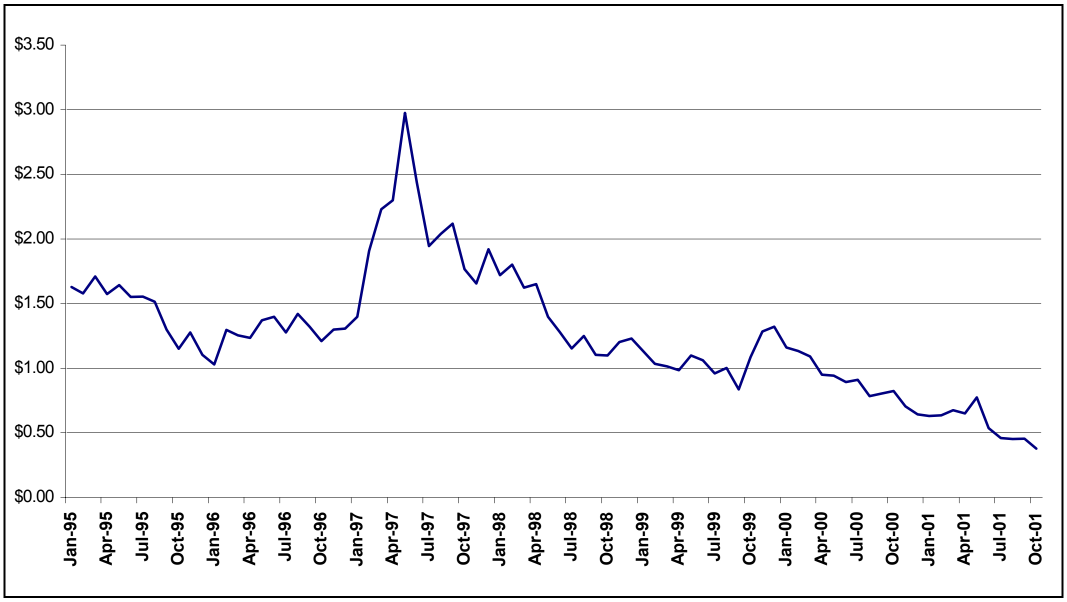
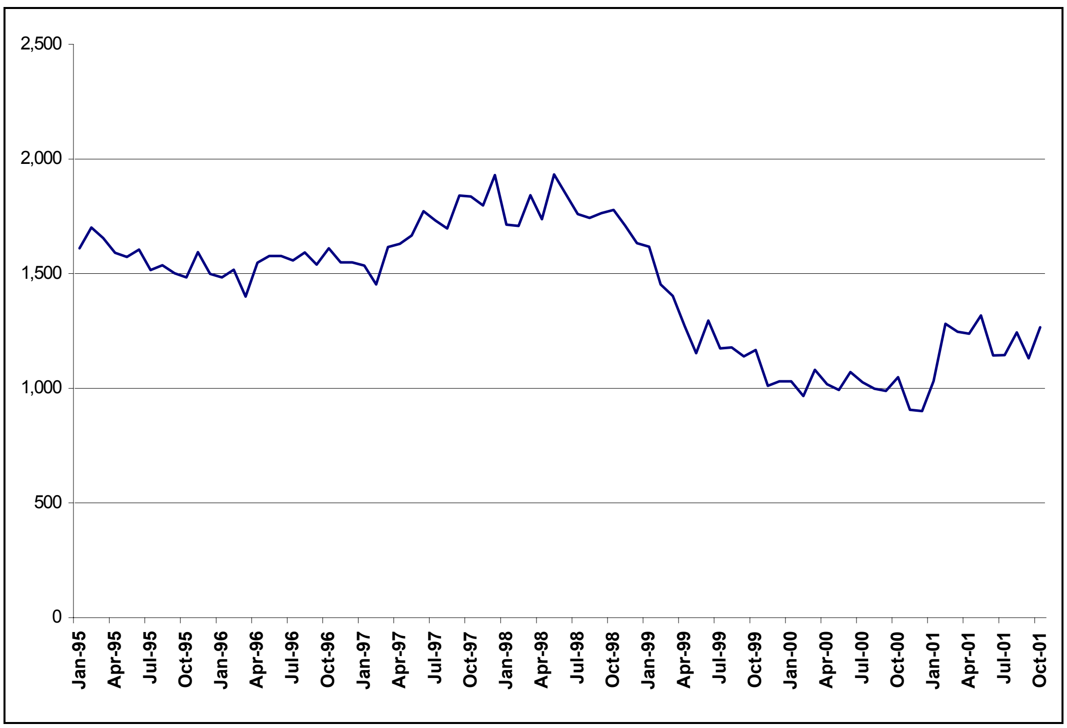
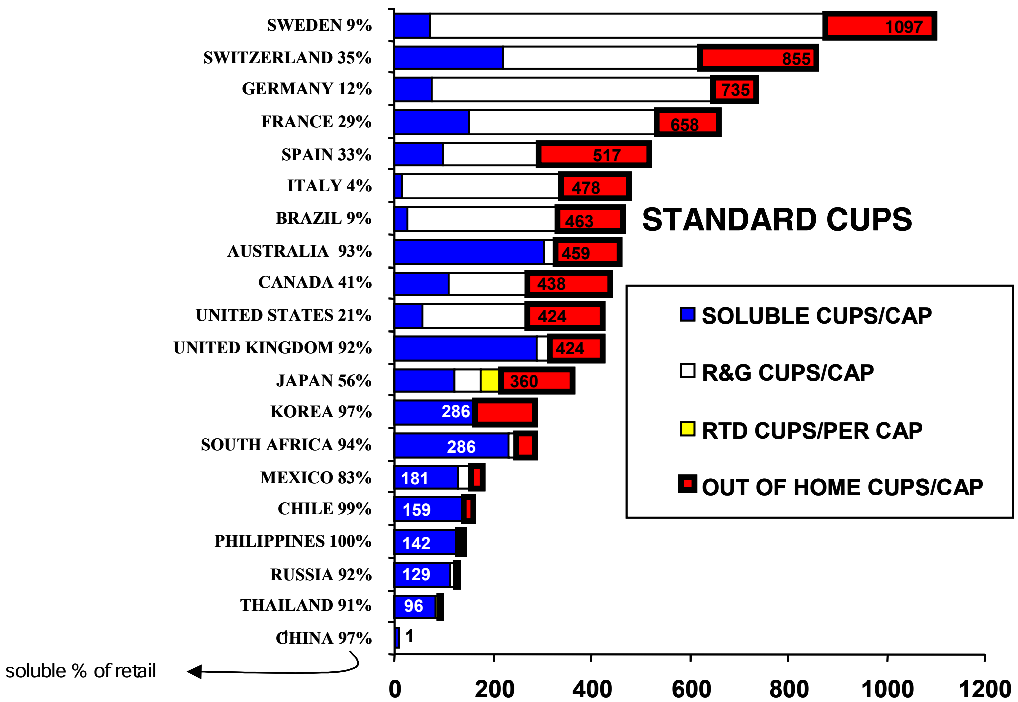


Exhibit 7b Cocoa, Ivory Coast Spot Price (US$/ton)



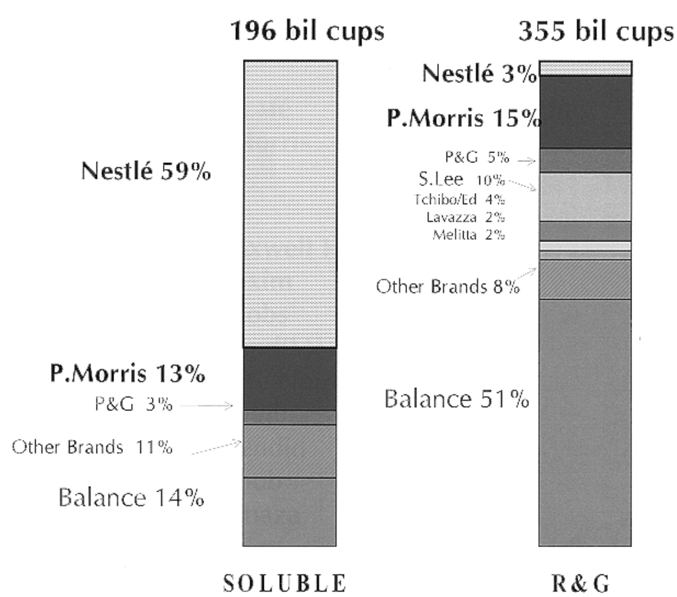
Source: *Datastream*

Exhibit 8 Coffee Consumption per Capita, 2000



Source: Nestlé

Exhibit 9 World Shares of Home Coffee Market (2000)



Source: Nestlé

Exhibit 10 Global Bottled Water Consumption, 1998 (per capita)

	GDP Purchasing Power Parity	Consumption (in liters)
Argentina	10,200	111
Australia	20,130	26
Austria	22,740	79
Belgium	23,480	116
Brazil	6,160	13
Canada	24,050	22
China	3,220	2
Czech Republic	10,510	53
Denmark	23,830	17
Egypt	3,130	2.3
Finland	20,270	10
France	22,320	120
Germany	20,810	98
Greece	13,010	39
Hungary	7,200	25
India	1,700	0.2
Indonesia	2,790	9
Italy	20,200	173
Japan	23,180	6
Jordan	3,230	5
Korea	12,270	26
Lebanon	6,150	42
Malaysia	6,990	2.3
Mexico	8,190	73
Morocco	3,120	5
Netherlands	21,620	15
Nigeria	820	11
Norway	24,290	14
Pakistan	1,560	0.2
Philippines	3,540	7
Poland	6,740	29
Portugal	14,380	64
Romania	3,970	23
Russia	3,950	12
Saudi Arabia	10,120	49
Singapore	28,620	12
South Africa	6,990	1.3
Spain	16,060	84
Sweden	19,480	14
Switzerland	26,620	88
Taiwan	19,870	28
Thailand	5,840	57
Tunisia	5,160	19
Turkey	6,350	14
UK	20,640	12
USA	29,340	52
Vietnam	1,690	1.3

Source: Company document