

DIRECTORS' REPORT

TO THE SHAREHOLDERS

The Directors of the Company are pleased to present the Annual Report along with the audited financial statements for the year ended December 31, 2018.

FINANCIAL PERFORMANCE

During 2018, Pakistan's economy showed mixed performance. Persistent increase in imports overshadowed a recovery in exports which further increased the trade deficit. This led to increased pressure on foreign exchange reserves which resulted in the depreciation of the Rupee. The pass-through of significant Rupee depreciation coupled with higher international commodity prices started to reflect in higher year-on-year inflation.

The Company recorded a revenue growth of 2.0% for the year despite increasingly difficult economic conditions and competitive pressures. However, the operating profit was impacted by higher input and energy costs due to Rupee devaluation and global increase in the prices of commodities.

Nestlé Pakistan continues to be committed to enhancing its product base through innovation and renovation which remains an integral part of the Company's vision to positively enhance the quality of life of our consumers. The major new product launches during 2018 included: NESTLÉ FRUITA VITALS PET, NESTLÉ MILKPAK 500ml, NESTLÉ NAN 1 with Human Milk Oligosaccharides (HMO), NESTLÉ CERELAC Savory Spinach & Pumpkin, NESTLÉ NAN Hypo Allergenic (HA).

PKR Million	2018	2017	Change
Sales	124,615	122,215	+2.0%
Gross Profit margin	33.2%	36.6%	-340 bps
Operating Profit margin	16.0%	19.3%	-330 bps
Net Profit after tax	11,545	14,642	-21.2%
Net Profit after tax (%)	9.3%	12.0%	-270 bps
Earnings per share	254.57	322.86	-21.2%

KEY FINANCIAL INDICATORS

- Sales grew by PKR 2.4 billion, a growth of 2.0% largely driven by pricing.
- We delivered a Gross Margin of 33.2% (-340 bps). The major factors behind the decline was due to significant Rupee devaluation and increased commodity prices, which could not be fully compensated with pricing and cost saving initiatives.
- Net Profit after tax reported was 9.3% (-270 bps). The drop mainly resulted from reduction in gross profit.

DIVIDENDS

In view of the financial performance of the Company, the Board of Directors has recommended to pay final cash dividend of PKR 63 per share, in addition to the interim cash dividend already paid of PKR185 per share, which brings the total dividend for the year to PKR 248 per share for 2018 compared to 320 per share in 2017.

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INVESTMENT PROJECTS

With a market driven approach and commitment to satisfy the needs of our consumers, in 2018 Nestlé Pakistan made investments of PKR 4.5 billion including expansion and development projects. Highlights are here under:

Project Description	PKR Million
Sheikhupura Factory - Extension and operational reliability	2,396
Kabirwala Factory - Extension and operational reliability	872
Water Plants - Extension and operational reliability	473
Extension of distribution and sales facilities	435
Milk collection infrastructure development	72
Others	285

Investments of approximately PKR 4.1 billion are planned for 2019, primarily in respect of operational reliability and capacity increase in order to meet consumer demands.

CORPORATE & FINANCIAL REPORTING FRAMEWORK

Nestlé Pakistan is committed to maintain high standards of corporate governance without any exception. The Directors are pleased to state that the Company is compliant with the provisions of the Code of Corporate Governance as required by SECP and formed as part of Pakistan Stock Exchange listing regulations. Statement of Compliance with Code of Corporate Governance is as under:

The Directors confirm that:

- The financial statements prepared by the Management of the Company presents fairly its state of affairs, the results of its operations, cash flow and changes in equity;
- Proper books of accounts of the Company have been maintained;
- Appropriate accounting policies have been consistently applied in preparation of financial statements and accounting estimates are based on reasonable and prudent judgment;

- International Financial Reporting Standards, as applicable in Pakistan and the requirements of Companies Act, 2017 have been followed in preparation of the financial statements; and any departure thereof has been adequately disclosed and explained;
- The system of internal control is sound in design and has been effectively implemented and monitored;
- There are no significant doubts upon the Company's ability to continue as a going concern;
- There has been no material departure from the best practices of corporate governance, as detailed in the listing regulations;
- The value of investments of employees funds are as follows (PKR millions):

	Audited 2018	Audited 2017
Provident Fund	3,466	3,542
Gratuity Fund	1,706	1,708
Pension Fund	2,922	2,729

Statements regarding the following are annexed or disclosed in the notes to the accounts:

- Key financial data for the last six years
- Pattern of Shareholding
- Trading in shares of the Company by its Directors, CEO, CFO and Company Secretary
- Number of Board meetings held during the year and attendance by each Director

REMUNERATION POLICY OF NON-EXECUTIVE DIRECTORS

The fee of the Non-Executive and Independent Directors for attending the Board and Committee meetings of the Company is determined by the Board from time to time.

EXTERNAL AUDITORS

Messrs KPMG Taseer Hadi & Company, Chartered Accountants have completed their assignment for the year 2018 and retire at the conclusion of the 41st Annual General Meeting. Being eligible, they have offered themselves for

re-appointment and pursuant to recommendation of Board Audit Committee, Board of Directors has endorsed and recommended same for Shareholders' approval.

HOLDING COMPANY

Nestlé S.A., a Company incorporated in Switzerland (the holding Company), holds 26,778,229 ordinary shares representing 59% equity interest in the Company. The principal activity of the Company is manufacturing, processing and sale of food products including imported products.

HUMAN RESOURCES MANAGEMENT & EMPLOYEES' RELATIONS

In 2018, we continued to spread positive energy across organization by transforming our people processes in order to provide better services to our employees and sustain an edge over competition. Transformation of the end-to-end HR process through technology and process redesigning brings in transparency and efficiency, thus helping with our service orientation. Key focus areas for 2018 included Leadership development, capability building, utilization of online learning



20 universities were approached for Campus Drives and Job Fairs



716 internships were offered



23 apprentices were taken onboard



31 apprentices were inducted under our program Kero Aitemaad - Women Empowerment Platform

platforms and employee relations management for building high performance teams to achieve organizational goals while diversity and commitment to compliance continued to remain at the heart of our agenda.

Few of the highlights are:

Our focus has been on Employee Relations through continuous and consistent employee engagement sessions, with the purpose of strengthening our relationship with the employees. These activities included Sports Galas, Connect Sessions, connecting with families of our employees and employee recognition program. Additional focus was given on improving the quality of employee services and promoting diversity and inclusion.

Considering the importance of industrial peace for long-term success of business, representatives of blue collar staff (Union) were on boarded at every step so they can also actively participate in spreading positive energy amongst the employees and can work side by side of the management staff. As a result of better negotiation and relationship with the Union, we were able to sign the Charter for next two years in a peaceful manner. As part of our Compliance journey, CARE Audit assessments were conducted by Auditors at Regional offices and Head office.

Along with this active community engagement, we also continued to ensure strong relationship with the surrounding communities across factories. In addition, performance appraisal and development process has been effectively sustained for non-management staff.

To support the diversity journey of the organization, facilities improvement projects and special drives are underway for differently-abled people.

Special focus was given to employee careers whereby career coaching clinics were conducted, helping them foresee their future within the Company. In this context:

- 355 Three Party Development discussion sessions were conducted across the organization
- 5 Career Clinics were arranged across sites where over 120 employees were coached on career growth

To maximize the impact of our people, our key Organizational Development (OD) Booklet courses like Nestlé Leadership Development Experience, Business Acumen Development and People Manager Toolkit continued to develop and enhance business and people skills of participants. These programs are designed for capability building of first line managers by deploying tools and concepts in various situations enabling a positive impact on business leading up to total Management Training hours of 71,459. The drive on fostering the e-learning culture helped us close the year with 9209 e-learning done.

Nestlé Pakistan ensured 100% payroll accuracy and timely disbursement of employees' monthly salary.

CREATING SHARED VALUE (CSV) AND COMMUNITY WORK

Nestlé Pakistan, believes in Creating Shared Value (CSV) for the communities in which it works and lives. Our global focus areas are firmly embedded in our purpose. Individuals and families, our communities and the planet as a whole are interconnected, and our efforts in each of these areas are supported through our 42 specific commitments. These commitments will, in turn, enable us to meet our ambitions for 2030 in line with the timescale of the Sustainable Development Goals (SDGs).

In 2018, the company continued the "Seeing is Believing" initiative to showcase our Dairy Value chain from Grass to Glass to create advocates among our stakeholders and to make them aware of the quality and safety standards that we adhere. We also extended the initiative to our Caring for Water sites.

The key CSV initiatives completed during 2018 are:

- Nutrition awareness extended to another 40,000 school children in the rural, suburban and urban areas under Nestlé Healthy Kids Program extending the overall outreach to more than 1,80,000 kids across the country.
- Nestlé Healthy Women, a nutrition awareness program to motivate young women of age 17-24 years to adopt a healthy lifestyle by educating them about their nutritional needs and its future impact;
- Continued product support through Nutrition Support Program for the underprivileged institutions.
- Continued support, training and advisory services to dairy farmers under our Farmer Support Program;
- Continued support for programs involving dairy farmers and rural women for skill enhancement related to dairy;
- Continuation of Chaunsa Project in partnership with Agriculture Department Punjab for implementation of best farm practices in the Chaunsa mango sector;
- Development of Driver Training Facility at the National Highways & Motorway Police Training Institute, Karachi;
- Clean Drinking Water facilities in our operational areas providing clean drinking water to more than 60,000 people on a daily basis;
- Alliance for Water Stewardship Certification of Sheikhpura and Islamabad factory in collaboration with WWF;
- Water Resource Management Project in partnership with Agriculture Department Punjab;
- Endeavoring to achieve the least possible environmental impact throughout its operational stages by complying with environmental laws and regulations;
- Partner with University Veterinary and Animal Sciences, Lahore (UVAS) aiming at producing the use of drip irrigation among farmers.

- At Nestlé, we believe that if we are to continue to grow sustainably, we must ensure that we use the planet's resources wisely. We are working towards the day when through efficiencies and new technologies, we can reduce our environmental impact to zero. This will take time, but we firmly believe it is achievable. Nestlé Pakistan is taking steps and introducing various initiatives in its manufacturing units and beyond, to exhibit this Respect for the Future. Some key highlights include, Eco-efficient use of resources, Waste Water Treatment Plants (WWTP), Tree plantation campaigns and Energy consumption per ton of product reduced by 19% versus 2010.

PRINCIPAL RISK & UNCERTAINTY

- Increase in input cost due to rising inflation and likely further devaluation of the currency.
- Macroeconomic uncertainties leading to lower GDP and economic activities which might affect consumer demand.

FUTURE OUTLOOK

We continue to have a positive outlook on the long term growth potential of the business, however we do foresee certain headwinds in the short term in the form of Rupee depreciation, higher inflation and input costs which might have an impact on the future results. The management remains fully committed towards managing these challenges and delivering sustainable profitable growth capitalizing on our strong brands, I&R capabilities and operational excellence with Nestlé continuous Excellence mindset.

ACKNOWLEDGEMENTS

We take this opportunity to thank our valued consumers who have trust in our products and continue to provide sustained support in ensuring the progress of the Company. Our people are our greatest strength. We are driven by a compelling Purpose – enhancing quality of life and contributing to a healthier future. We are guided by strong values rooted in Respect. Our purpose and our values are the reasons why we all work for Nestlé's success. They are fundamental to everything we do, particularly in times of significant change inside and outside our Company.

Nestlé Pakistan, whilst bringing international expertise and standards into its products, processes and manufacturing sites, remains a "Har Dam Pakistani" Company and is very proud of its achievements in Pakistan.

**FOR AND ON BEHALF OF THE
BOARD OF DIRECTORS**



Freda Yahan Duplan

Chief Executive Officer



SYED YAWAR ALI

Chairman

Dated: February 26, 2019