Half Year Results 2021/22

Thursday, 9th December 2021

Half Year Results 2021/22

Participants

Miles Roberts – CEO

Adrian Marsh – CFO

Miles Roberts: So good morning and welcome. Welcome to our presentation on the results for the six months to the end of October. I'm Miles Roberts, the Group's Chief Executive, and I'm joined by my colleague, Adrian Marsh, our Group Finance Director. The half year showed continuing good progress right across the company. As a solely fibre-based business – that's with no plastics – we continue to benefit from a very dynamic market, a market we positioned ourselves to benefit from. Different retail channels are developing quickly and continue to change, and there's a different relationship between consumers and packaging. And of course, COP26, it's intensified the debate and the demand for circular solutions, as well as carbon reduction. So all of this has positioned us not only to grow in the last six months, but for continued good growth.

With this background, we've seen our volumes grow strongly, up 9.4%. But we've also seen good pricing momentum which, when combined with our financial hedging and long term deep supply arrangements, has allowed us to mitigate the increasing operating costs. Consequently, our operating profit has risen by 26% and our earnings per share by 33%. And I'm very pleased to see how the US has continued to perform with operating profits up 64%, benefiting not only from excellent pricing momentum, but strong volume growth. And our cash flow's been strong, and it's brought our leverage to 1.9 times net debt to EBITDA, well inside our medium-term target.

And looking ahead to the second half, it has started well. We also have new investments coming on stream later in H2. And we expect to make a significant further improvement in profitability and progress towards our medium-term targets in the second half.

Adrian, would you take us through the detail of the financial results?

Adrian Marsh: Thank you, Miles, and good morning, everyone. By way of my normal reminder, I've described the performance of the business on a constant currency basis. Here are our financial highlights.

Revenue is up 22%, reflecting record box volume growth and higher prices across packaging, paper and recycling. Together, these more than offset significant cost increases, with operating profit up 26%, including a 64% increase in the US. Return on sales before exceptional or adjusting items increased 30 basis points. The extent that our increased input costs are matched almost pound for pound in our revenue line, then mathematically we have a small optical margin dilution, which is more than offset by our volume growth. Clearly, our margin becomes much more accretive as the rate of price recovery in the second half of the year and into our next financial year overtakes the rate of input cost inflation, driving a return to our target range.

Profit growth has flowed through to EPS and cash. And I'll talk more about our net debt and leverage reduction shortly.

Return on average capital employed has significantly improved, which, of course, does not have the same nuance as the margins and demonstrates more immediately our improvement in returns. With growing profits, and after a period of expected dilution following our significant acquisitions and the even more recent impact of COVID, then we can clearly demonstrate we're also on track to return shortly to our medium-term target, return on average capital employed.

Whilst it's not on this slide, I'm sure the sharper eyed of you will have spotted that exceptional or adjusting items are, as we've advised they would be, de minimis in the period. I'll now go through the main moving parts with the usual bridges.

Record box volume growth of 9.4% contributed ₤172 million to revenues. Other volumes is a mix of increased volumes of other packaging and recycling, offset by less external paper sales as we use more internally. The largest increase is clearly the sales price increase. Around ₤200 million of the ₤432 million is packaging pricing, representing double-digit average increases in box prices, with the balance made up of external paper and recyclate sales.

Turning to EBITDA, the contribution from volume growth has dropped through in the normal way, and that essentially is what's driven our profit growth. Other volumes is the same story as on the revenue side, with less external paper sales offsetting increased Other packaging volumes.

Sales price mix dropped straight through to profit, and it's pleasing that we've been successful in pushing through pricing to more than offset the very significant headwinds on the cost side, as well as managing the magnitude of those costs through our proactive procurement. All of which said, we still have the usual lag in our price recovery, which whilst positively impacting our second half, will be somewhat tempered by additional input cost inflation in the last three months of this half. Taking all this into account and where we are with box prices and index contracts still to trigger, we're confident of additional price recovery and margin improvement in the second half of this year.

On the cost side, the largest contributing factors are external paper purchasing, together with fibre or OCC, which together make up around ₤300 million. Energy, labour and distribution have also increased significantly. Clearly, energy has been a topic *du jour* in the recent weeks, and we've been extremely well protected by a three-year rolling hedging programme. That said, we've not been immune from year-on-year costs, particularly on the unhedged 10% of our exposure. Without this hedging, our results would have been severely impacted. Given our level of forward hedging, in particular next year, we don't expect our energy costs to be materially worse than flat year on year, with an opportunity to improve if prices fall.

Overall, Group margin has increased, albeit, as I noted before, there is still a short-term dilutive impact from the input cost versus price inflation dynamic, which unwinds itself as the rate of price pass-through exceeds the rate of input cost inflation. Despite this short-term effect, we remain both confident that margins will return to our target range. With more paper capacity being added in Central Europe, our short paper strategy will continue, we believe, to offer the most efficient return on capital employed profile for our business by allowing us to allocate more capital to our higher value-adding packaging opportunities.

Regionally, there are always variances, depending on the level of our own paper production, which gets exaggerated when paper prices are either rising or falling sharply. Eastern Europe is the area where we're shortest paper and until the usual lag in pass-through to packaging completes, the effect on return on sales is therefore greatest in that region in this period. The key is that once the rate of price recovery exceeds the rate of paper price inflation, we then see margins rising, which is our expectation for the second half of next year too. As previously discussed, it's particularly pleasing to see the expected and continued improvement in North America, consistent with what we set out 18 months ago. We've seen in this half a 64% increase in our US profits, despite a planned maintenance shut in our paper mill in Riceboro.

I'm also pleased to report continued good cash flow during the first half. After an exceptional working capital performance last year, I think we've done well to essentially keep it flat during a rising pricing environment. Albeit whilst receivables have risen in line with selling prices, we've also benefited from the risk management of our energy hedges, which has positively benefited our creditors. For the full year, I still expect a small working capital outflow.

We've also again reduced our invoice discounting to £385 million, in line with our guidance of below £400 million. Just to note on CAPEX, we spent £125 million in the first half. I'll give my technical guidance shortly, but the phasing is such that the first half was always going to be less than the second half, and we're still expecting the full year amount to be around £430 million.

Moving to the cash flow bridge, net debt reduced by £155 million to its lowest level since April 2017, driven principally by the free cash flow. As guided, adjusting items are reduced to a negligible number and the acquisitions and disposal line is net of the sale of De Hoop and a deferred element of the Interstate put and a couple of minority interest buyouts. For me, one of the highlights of the results is that net debt to EBITDA is back below 2x, driven by both an increasing EBITDA this half and also a reduction in net debt, and I expect it to continue to be below target for the full year, recognising that there are cash flow headwinds to come.

Finally, my technical guidance. We're on track to deliver in line with our guidance at the start of the year and further improve our financial KPIs. So with that in mind, there's basically no change to the guidance that we've previously given, subject to any small variations which foreign exchange translation may cause.

I'll now hand you back to Miles to take you through some of the operational highlights and some of the opportunities that we're really excited about.

Miles Roberts: Thank you Adrian for taking us through the detail of the financial results. I'd like to now to spend a bit of time just talking about why we're succeeding with our customers, to highlight some of the background behind that, what gives us the confidence for the future growth, the future opportunities for us.

But firstly, I'd just like to recap on some of the operational highlights from the first half. Turning to our people. Everybody who works in DS Smith, once again, we've seen a huge level of commitment and responsiveness throughout the whole company. Where there have inevitably been some local issues, these have been very short lived and covered through our scale and our flexibility, combined with all of our plants being fully operational throughout the whole period.

And looking at our supply chain, this has remained very secure. A group-wide procurement and sourcing function, combined with long-term deep relationships with many of our suppliers, particularly in critical areas such as starch, energy, chemicals and, of course, paper, has resulted in good security of supply and good levels of supplier service.

And with our customers, we stayed really close to them; listening to them, understanding their challenges and responding to them. And this has enabled us to maintain good levels of service. We've had good agility in meeting these changing needs, often supported by extensive use of new digital technology, helping us to really adapt quickly. And of course, all of this has supported good pricing momentum to recover our increasing costs.

Throughout H1, we've seen good volume growth. We've been taking market share; said previously, the growth at 9.4%. The FMCG sector has remained very strong and very robust. We have seen a partial recovery in the industrial sector. This is a relatively small part of our business, probably around 16%. It's suffered by some of our customers having some capacity constraints, but we expect that to come back. And with our large customers, we've continued to grow strongly. Over the last six months, they've, of course, been looking for assurance on the security of supply, which we can give them; strong governance; but also meeting their needs on innovation and meeting their sustainability objectives.

And in the US, we've been particularly strong, once again with our global accounts. Being perfectly honest, we could have grown even more strongly in the US if it wasn't for the labour market being so tight.

Volumes in H2 have started well. We have a healthy order book and a number of really exciting opportunities give us confidence in the outlook for the year. At DS Smith, we positioned ourselves at the centre of three structural growth drivers: digital enablement, a changing retail environment and the whole debate around sustainability and plastic replacement. And COP26 has further intensified the debate, raised awareness once again of the importance to all of us of the environmental impact of how we're living. And of course, it's on carbon, where we have a science-based target and a commitment to net zero by 2050. But it's also our work on the circular economy, about the closed loop, the reuse, the recycling and about plastic replacement at every opportunity. And this replacement is being supported by new legislation, which now has come in and will continue to come in across the EU and also in the UK.

I show here our performance across a whole range of ESG indices over a number of years. And you can clearly see constant, good, strong, steady progress. And with MCI, where we have an AA rating that is particularly relevant for shareholders and the providers of capital, when we talk to our customers, they remain very interested in the CDP score and they're delighted with our continuing progress there, just reaffirmed this week with a further improvement in our ranking.

And turning to some practical examples of sustainability in action. The first is around the circular economy, about the recyclability and the actual recycling of packaging. As Europe's largest fibre recycler with extensive recycling operations across Europe; with 100% recyclable products; and our approach to a fully closed loop where we collect waste product from our customers and convert it into packaging, we're seeing a number of customers awarding new long-term contracts on the basis of a closed loop.

I show here an example with Laithwaites, the wine supplier, where we pick up waste from them, we convert it into packaging within 14 days to bring it back to them. But very importantly, we've just secured a significant new contract with a very large customer, over many years, where our closed loop offering was instrumental to us securing that business.

And, of course, in plastic replacement. That new legislation, the new taxation on plastics, combined with consumer awareness, is seeing an acceleration in the conversion of plastic to fibre. In the whole of the last financial year, we replaced 54 million plastic products with fibre products; in the first six months of this year, we converted 118 million, and we expect this rate of change to increase over the coming years.

And we continue to invest behind this growth. We've seen strong, consistent demand coming to our business, the structural tailwinds and also our deeper conversations with our customers. As we continue to invest in new technology, new capacity, often it's much more efficient, carbon neutral, providing very attractive returns on capital of between 15 and 20%. And as an example of these, we have our two new packaging plants. Both will be online in H2. They're both 50% pre-sold, and our customers are very excited about these real state-of-the-art facilities. And, of course, we continue to evaluate further opportunities with our customers to support them over the medium term.

When we combine these deep customer relationships with the structural tailwinds our market offers and our supply chain and operational capabilities, we can see good volume growth going forward – increasing productivity and pricing momentum – and all of this underpins our confidence in achieving our medium-term targets.

As a summary we're pleased with the progress in H1; with rising volumes, our levels of customer service, the strength of our supply chain, how that's allowed us to manage our cost base and the pricing momentum combined with that strong cash flow. And looking ahead, we've had a good start to H2, both in volume and pricing momentum. So in H2, we do expect there to be a significant improvement in profitability and strong progress towards achieving all of our medium-term financial targets.

Thank you very much. Now, myself and Adrian are very happy to take any questions you may have.

Operator: Thank you. So if you would like to ask a question or make a contribution on today's call, please press star one on your telephone keypad. You will be advised when to ask you a question. We ask that you initially limit each contribution to one question wherever possible. So, as a reminder, if you would like to ask a question, please press star one on your telephone keypad.

So our first question comes from the line of Lars Kjellberg, you're now unmuted, please go ahead.

Lars Kjellberg: Thank you and good morning. Just a couple of questions. One that stands out, there's been talks about energy surcharges in containerboard in particular. So just wanted to hear your thoughts, how you deal with that in the downstream corrugated activity, if you can pass such on or if you're even exposed to it.

The other one I just wanted to touch base with you on is sustainable packaging. You called out the – I think you said, 118 products being replaced this year versus 54 last year. Can you give us any sense of what that means in new business for yourself? Thank you.

Miles Roberts: Thank you, Lars. We have seen some, or we've read about some announcements from some suppliers who have put on energy surcharges. We haven't actually really experienced that ourselves from our supply chain. As said, we work with a whole number of paper suppliers. They tend to be quite long and deep relationships. So we haven't actually seen that, but we understand that some people have done that elsewhere. Certainly from ourselves, we haven't done that. As I said, we've got extensive hedging in place. And I think it's not just the hedging, it's the other solutions we used with more biomass and different types of energy solution that helped us mitigate that.

But nevertheless, for a variety of reasons, the price of paper has risen very strongly. You can see in our results, we have actually fully mitigated all the increasing costs that we've faced with the price increases, and we absolutely expect that to continue in the second half. We've seen obviously November and that's reinforced our confidence in that.

I think in terms of plastics, the wide environmental debate, we've actually looked at all of the renegotiations we've had with many of our customers. And just monitoring the importance of the environmental issues, where they place them – the ability to replace plastics is one of them. And you'd go back a few years – we've monitored for quite a long time. If you go back a few years, it was just one of the issues, but now it's right up there. Often it's the first thing that they want to talk about, they want to discuss, about that long-term innovation: how can we take plastic out? What are the opportunities there? How can we improve our environmental footprint? As you know, we have our design metrics, which we use with all our customers, that really show them the environmental impact of their product and how we're performing there. I think that's really taken now as an industry standard.

So it's becoming much more important. We put the plastic there because they've been – the example plastic plays in the 118 million. We've been monitoring over the last couple of years. And it's probably over that period, maybe getting about – it's probably less than 1% in terms of our revenue. But I think in terms of what we feel quite excited about, is it's just part of that overall debate, but the rate of increase; 54 million units last year, 118 million in the first six months. And we know the effect of the legislation that's coming on. We know there's taxation on plastics. As said, we don't produce plastic products, so we don't have any conflicts in our business on this. We can see what our customers are saying to us and we expect that rate of increase to continue to grow. And let's see where it gets to, but it's just another one of those tailwinds that are there. But thank you for your question.

Operator: So our next question comes from the line of Cole Hathorn from Jefferies. You're now and muted. Please go ahead.

Cole Hathorn: Morning Miles, morning Adrian. Thanks for taking my question. Just got two. The first is on demand trends. I mean, you've talked about the second half starting well. Can I just start thinking about how this progresses? I mean, you do have tougher comps. Are you looking at that demand trends, yes, you'll have tougher comps so your volume growth will obviously slow but demand is staying at a high level and you're talking a little bit about industrial recovery. So I'm just wanting to understand how you think about that volume progression through the year and into next year.

And then secondly, on the North America division, you talked about good recovery there, and there is recovery, but export prices in the US have been really strong. Will that benefit be seen in the second half results for your business, for your export prices, that really starts to be realised and you see that recovery in that North America division? How should we see the second half phasing of the North America division? Thank you.

Miles Roberts: I think Cole re the demand, you're absolutely right, we have a much stronger, tougher comparative in the second half of last year, about 8.4% during the second half of last year, 3.5% over the full year. But nevertheless the demand remains strong. We remain very busy. We've obviously got the lead up to Christmas at the moment and e-commerce continues to move ahead very well. The outlook, when we look over the second half, we've got a number of new contracts, the whole environmental debate continues, so we actually see the absolute level of demand – our forward order book is strong. It's strong, it's very encouraging. We have these two new sites coming on and we're obviously looking forward to them coming on. They're 50% presold, they're all on track. And I think the rest of their capacity could be taken probably a bit earlier than we originally planned. It does look good and that looks set to continue to next year.

Now, obviously, the whole economy is uncertain, and what's going to happen and all of these things, so we can't give exact numbers, but it does feel – continues to be strong.

You're absolutely right, in North America, export prices have been strong. The amount that we export has reduced quite significantly – since we opened up the new Lebanon facility. That continues to grow and develop very nicely, it is doing very well. And we're much less exposed to those export prices. But nevertheless, domestic pricing in the US has also been strong. The price recovery has been very good, but we will see more of the effect of this – I think as Adrian spoke about, we'll see more of the effect of this in the second half. So the outlook for North America in the second half is we're going to see further ongoing improvements in that business. Also, the first half, as Adrian said, we did have a shut in a big paper mill there, which won't happen in the second half, so we should see further good progress there. Volume, pricing and we won't have this paper mill shut. (It was a planned maintenance shut).

But thank you Cole, thank you.

Operator: So our next question comes from the line of Sam Bland from JP Morgan. Sam, you are now unmuted. Please go ahead.

Sam Bland: Thanks and good morning. I've got two questions, if I can, please. The first one is, can you talk about what proportion of volume is on indexed or contracted prices and hasn't yet really seen an increase yet following the recent rise in paper prices?

And the second question is, I guess, you're now below your leverage target and will probably move further below as profitability rises going forwards. What are the options? Does it keep on delivering a bit further for now? Or are there other things you can do with the cash, basically? Thank you.

Miles Roberts: No, absolutely. Thank you, Sam. I'll take the first and Adrian can talk to you about the leverage. You're absolutely right, we've got the index deals. These are working on averages, it could be the last three months. They do tend to take a little bit – and therefore a little bit longer to come through than our freely negotiated. At the moment we are running at between 45 and 50% of our contracts on indexed deals and 50 to 55% are on freely negotiated.

There are key index points. The next one is going – they happen all the time, but you get some big events – will be on the 1st January. And you're absolutely right, we certainly do expect to see a further very good automatic recovery of the paper price increases that really have come through over October, November and December, and are quite considerable. So, they will come through that as they have been doing in the first half.

But Adrian, on the leverage?

Adrian Marsh: Yes, Sam, on leverage, you're right, we're pleased it's now below our target level. And as you rightly say, mathematically, if you look forward, one easily expects to see further improvement, but it is just at our – below our target now. We're very encouraged with the free cash flow, but we're making two very, very big capital projects that come online, as Miles described, in the second half. The Polish greenfield and the Italian greenfield are two huge state-of-the-art facilities, chasing the organic growth there, very, very well, very good returns. And we continue to look at opportunities going forward, as you would expect. I mean, clearly, we've got a limited number of choices. We can invest behind growth capital to deliver ahead of our target return on capital, we can continue to deleverage or we can return capital. They're effectively the options and as you would expect, Miles and myself and the board are evaluating that very carefully. And likewise, we're having ongoing discussions with shareholders about what the expectations are. But good organic opportunities to give us a significant returns and clearly we're looking at those too.

Operator: So our next question comes from the line of Brian Morgan at Morgan Stanley. You're now unmuted. Please go ahead.

Brian Morgan: Hi, good morning, guys, thanks very much for the call. The sense that we get this year is that containerboard markets are very, very tight at the moment, and I just wanted to get a sense of your net short paper position. Are you struggling in any particular grade to get paper at the moment? Are there grades where you're quite short, or potential regions where you are short on paper at the moment?

Miles Roberts: No, look, as said, we do have a short paper position and that's really looking at all that capacity, that independent paper capacity in Germany that keeps on coming online. In fact, there's some more capacity just opening now. And rather than us investing in and around that region, we prefer to buy the paper. We don't think the returns on those assets are attractive for our shareholders. But we don't do this light-heartedly. We enter into long term supply agreements with many of those large independent paper producers. And quite a bit of the new capacity that's coming online, and has been announced will come online, we entered into arrangements with those suppliers over the last one, two, three years to take the paper that they're producing. So by and large, we haven't had any paper supply issues.

What's been more of an issue has been on the logistics side. But the paper that we need – just making sure that we can move it around and, inevitably, there have been some logistics issues around, they're very short term. We've got our own in-house fleet of vehicles. We've been able to utilise those, making sure that we're able to keep our level of service high to our customers. So no real issues – not particularly. Thank you.

Operator: Our next question comes from the line of David O'Brien at Goodbody. You're now unmuted, please go ahead.

David O'Brien: Hey, good morning, guys. Thanks for taking my questions. Two on sustainability, if I could. I guess you mentioned, Miles, in the commentary that sustainability is up the criteria list when discussing contracts with customers. I suppose firstly, is that allowing you to achieve, or do you think it will allow you to achieve a price premium in the near term, which is something, over the years, that the industry has struggled to really achieve? And I guess, you also touched on one of the contracts being very long term. Maybe you could comment on what is happening to duration of contracts as we evolve to look at more value-add offering to customers.

And then secondly, how do we think about the carbon, or how do you think about the carbon intensity of your business? And particularly when we think about recycling containerboards, do you have a carbon intensity per tonne average through the system at the moment and target for where you want to get in five or 10 years? And what are the key levers to get you there?

Miles Roberts: Two very important questions. On the sustainability, if you look in the graph that we put up about the price on the EBITDA bridge and you can see the raw material cost increase, and a slightly over-recovery through called price and mix. We're able to pass on our increasing prices. And if we actually look at the profitability in terms of the cents per square meter, the more sustainable products where there's more engineering in them, then it's certainly better. I think it's up to us to keep on reinforcing and explaining about the embedded value. And ultimately, it's about our customer making that case to the consumer. And where we see customers who are able to make that connection with the consumer about the full environmental credentials of their product, then there is clearly a premium there.

But this needs to be explained, there needs to be more marketing of this and where it works, it works well. But there's clearly more work to and I do think it will become a little bit more polarised over the coming years. We are claiming these credentials and various consumer groups will pay that premium. And I think there will be some others, but it's moving in the right direction. Certainly in the short term, I was very pleased with the price recovery and the stickiness of customers where we have those solutions and therefore our ability to price fairly. That's worked well.

You're absolutely right on the carbon intensity. We've got a science-based target. We have to reduce our carbon per tonne by 2050 by well over 90%. That's the criteria. We have made huge progress over the last 10, 15 years but we do have an interim target in 2030 where we need to reduce the carbon intensity per tonne by well over 40%. And we're absolutely on track to do that. Much of the way we're solving that problem actually ties in with some replacement of various power solutions and heat and energy solutions that we currently have. They're tied into the existing replacement programme, but obviously those new facilities have to be far more efficient and they also have to use some new technology. There's more about waste to energy. There's more about biomass. There's more about biogas. We're using known technology, again, with good supply chains for the energy source. And I think we are going to get to 2030 with those targets. We're actually discussing another date again in detail. We're on track to achieve them at a fair cost; we're not going to see some sort of explosion in capital expenditure here, simply as so much is tied into normal replacement anyway, and often we get government grants and support to do that.

So what we have to do, we've got a very good plan for it. But thank you for your question.

Operator: Our next question comes from the line of Justin Jordan at BNP Paribas Exane. You're now unmuted. Please go ahead.

Justin Jordan: Thank you. Good morning, everyone. Gentlemen, I've got a question regarding the estimates for paper strategy. In recent days, I've spoken with several of your leading shareholders, many of whom are delighted to be on the call with you today. Gentlemen, I'll be diplomatic in saying your shareholders feel somewhat confused. Your shareholders were sold the vision that DS Smith's short paper strategy would deliver both firstly, superior returns and secondly, less volatile returns than your more vertically integrated peers, such as Smurfit Kappa, Mondi in Europe or International Paper and WestRock in the US. Sadly, the factual reality is very different to that. Firstly, this morning, you're reporting sequentially declining EBIT margins, which were 8.8% in the six months to April 2021, and declined to 8.2% in the six months to December 2021. A period where you're more vertically integrated peers like Smurfit Kappa and Mondi have both reported sequentially improving margins because they've got less cost inflation. They're vertically integrated. You're not. You’re short paper.

Now, sadly, this is not a one-off event over the last six months. The factual reality is that each of the last five years, DS Smith's EBIT margins, return of capital employed have been consistently lower and consistently more volatile than your vertically integrated peers. So my question is, can you please explain to your shareholders, particularly those on the call with us today, why does the DS Smith board persist with this short paper strategy, which is condemning your shareholders to endure firstly, lower returns and more importantly, more volatile returns than your vertically integrated sector peers such as Smurfit Kappa and Mondi?

Adrian Marsh: Justin, thanks for the question. So the first thing I would say is that's not the feedback we get, but fine. I mean, if you've got it, good. The reality is we set out, we've been very clear our primary target is return on capital employed. We've made a couple of very significant acquisitions, which, ahead of those acquisitions or at that point we announced them, we described the dilutive effect on return on capital employed. We're now seeing those returning to our targets.

With respect to margins, that's exactly what I set out in our presentation. Our margins will mathematically be dilutive as we recover costs. And then, as our rate of price recovery exceeds that level inflation, they become accretive back to our target again. So there's no issue there.

In terms of short or long paper, we've described before, it's about the amount of capital employed that we want to have in paper manufacturing. If we buy in or if we make it, we're no different to a comparable competitor that's fully integrated because you will still have the input cost of OCC and energy, unless, of course, there's super benefits to be made out of recycled paper at the moment. What we've seen is actually the opposite of that, the added value on recycled paper being compressed. Obviously, that's different on kraftliner.

The other point I'd say is I don't see a comparative. I mean, one of the companies you described is a long paper company. So of course, when paper prices are rising, they'll make a better margin. Likewise, they'll make a much reduced margin when it's falling. The other one you described has a number of similarities. It also has a significant plastics business. They don't split it out, we don't see what those different moving parts are. So all I can describe is our business, our strategy. We've been very clear about it. We believe it's the right one. We want to deploy capital where it's adding the most value and we're going to get the best return out of it. Historically, that's been through some significant acquisitions, which have had goodwill attached. If you strip the goodwill out, you obviously – you can work out different results too. So we're quite comfortable with that. We've confirmed our medium-term targets. We can see the bridges to those, but I appreciate the question. Thanks.

Operator: So our next question comes from the line of Harry Philips from Peel Hunt. You're now unmuted. Please go ahead.

Harry Philips: Yeah. Good morning, everyone. Just a quick question on your top line growth target. Just flicking back through history, you've had GDP plus 1% for a decade now. And Miles, you alluded to the plastics getting towards one percent in terms of substitution. E-commerce obviously is accelerating. So I just wonder, at what point do you think that target is too conservative and you might think about nudging that up a little bit?

Miles Roberts: Harry, it is a question and a challenge that we have been giving a lot of thought to. There's clearly been a disconnect between our business and GDP. Look at last year, our volumes grew 3.5% at a time when the GDP across our markets was heavily negative. Sitting here today, we continue to see good, strong growth, and our challenge is more about, is it more of an absolute level? It's quite clear in the medium term, with those drivers that we've spoken about, we should expect growth to be higher than it has been in the past. And we can see that in our customers, we can see the way they're talking, we can see how they've taken share, we can see us taking share within our existing customers. We can see the length and the duration of the contracts that we are with them. So we feel quite positive.

The thing that holds us back a little bit is it's just an uncertain environment. But what we can see is good growth going forward. Maybe it's at a more absolute level. Maybe we are decoupling a bit from GDP as we get so much more on the FMCG and those tailwinds that we've spoken about. But we do actively look at it, and when we're ready, we'll come back and we'll look at that target again. But it's certainly something that we look at going forward. Yeah, yeah, yeah. It'll come back in the medium-term target.

Operator: So our final question comes from the line of Cole Hathorn from Jefferies. You're now unmuted, please go ahead. Hi, Cole, are you unmuted locally?

Miles, it seems that we've lost Cole, so I'll just turn it back to you for any closing remarks.

Miles Roberts: Thank you, everybody for your time listening to us this morning. We're very grateful for that, but just as a summary, we're pleased with the volume growth. We're pleased with the pricing momentum. North America is coming strongly. The balance sheet is in good condition and just looking into the second half, as I said, we expect to see a significant improvement in profitability and a significant move back towards our medium-term targets. Thank you again.

Operator: Thank you for joining today's call. You may now disconnect your lines. Hosts, please stay on the line and await further instruction.