

# FINAL TRANSCRIPT

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## **BN.PA - Q3 2008 Groupe Danone Sales Conference Call**

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Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

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## PRESENTATION

**Operator**

Good day and welcome to the 2008 third quarter sales conference call. Today's conference is being recorded. At this time I would like to turn the conference over to Mr. Pierre-Andre Terisse. Please go ahead, sir.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Thanks very much. Good morning to all of you who are connected. I'm Pierre-Andre Terisse, Group Danone CFO. I'm here this morning with Robin Jansen, Head of the Investor Relations, and Laura Palmeiro, Deputy Investor Relations. Thanks very much again for being with us.

I'll start with an overview of our third quarter sales and refer to the presentation for this purpose. In a second's time then we will be ready to take your questions and answer them. Let me thus start with comments regarding the Group sales performance and we can move directly to page three.

Overall I would say that Q3 was a good quarter for us, with 8.3% growth, as you can see on the chart, which is in line with our 2008 guidance despite what we would qualify as a very volatile environment. We are now, at the end of September, with a 9.2% year to date sales organic growth and hence this puts us in a very good position to achieve our 8% to 10% target growth for the full year.

Four main topics about the quarter. The first one is about Dairy, which we will see as being rebounding in terms of volumes, as we expected. Second, Water, which has still been growing strongly in emerging countries, but where difficult market conditions, as we see it, have been confirmed in UK and in France. The Baby Nutrition division which has been performing, once again, very well, with solid volumes and double digit growth. And last, our Medical division, which is on the same historical trend.

If you move to page four you will see the breakdown of our sales evolution between historical, currency, and like-for-like effects. So obviously the integration of Numico brings an additional sales with a significant amount of EUR699m, which represents 23.9% of sales growth.

The remaining 7.3% are made of two things. Currency effect, which has improved compared to what it was during the first and second quarters, but remains negative with a minus 2.3%. And on the other hand, 8.3% sales growth like-for-like, made of 2.6% of volumes and 5.7% of value. The volume component has increased compared to what it was in the second quarter, while the value component has slightly decreased.

Moving to the divisions now and we can start with the Dairy. Dairy closed the quarter with an 8.2% sales growth, with a price mix of 8.4% and volume decrease of minus 0.2%, which is similar to what we delivered during the first quarter, and which is -- which represents an increase of 1.3 points versus what we delivered during the second quarter. This rebound in volume is very much the result from moving away from the timing we put the price increase earlier this year and at the end of 2007, and from an increased and refocused commercial activity as we have previously discussed.

The rebound extended to different geographies. You will remember that we mentioned during the second quarter that we have seen the rebound in four countries, which were Brazil, Italy, (inaudible) and Saudi Arabia. In these countries, of course, we have seen confirmation of the ramp up of volumes. We have added approximately 10 geographies to these four, which are Portugal, Belgium, Poland, Czech Republic, Baltics, Romania, Bulgaria, Greece, Algeria and [some others]. So all together we are moving in the right direction.

New geographies on the other hand continue performing well. Egypt, which is one of the countries which we entered recently has now taken over the leadership position in the country and has reached break even. Chile is progressing well as well.

A word on some countries which remain a bit more difficult than the ones which I've mentioned for different reasons. France remains negative in terms of volume evolution for this quarter at minus 9%. This is clearly a progress compared to what we have seen during the second quarter but it remains in negative territory. The good point as well for France is that the market share in this country is stabilizing.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

Spain remains slightly negative, very much in line with what we had delivered during the second quarter, clearly due to a difficult economic situation. And last, the US, is still facing very strong competition from Yoplait through promotion and the reaction is underway.

Another important factor, which we had already outlined during the second quarter, is the performance, the relative performance, of blockbusters compared to the average performance of the division. And blockbusters have basically continued to over-perform the portfolio in line with what we have seen in Q2, with a very strong Activia and an even stronger Danacol, which is really taking off, less strong Actimel, and an improvement on Danonino. So confirmation that's very important that the blockbusters keep playing their role and keep remaining, by far, growing faster than the rest of the range.

We will of course keep monitoring the gradual ramp up of volumes in the coming quarters, while the price effect will fade away again from next quarter.

Page six, a word on Waters. I believe the picture this quarter is becoming a bit clearer. The growth in emerging countries has remained strong, with the same trends as observed in the previous quarters and with performance in Indonesia, in Mexico, in Argentina, which remain very solid despite, as we already noted in Q2, a slightly more difficult environment in Mexico. These emerging countries represent, I recall you, 50% of the business.

The remaining 50% of all water business in Western Europe is mainly composed of four countries, being France, UK, Germany and Spain. We had, in the second quarter, clearly, adverse weather conditions, explaining the poor performance of those businesses. This has not been the case in Q3 since the weather has been quite comparable to what we had last year.

Therefore, the performance in Europe is mainly driven by two factors. Number one, Germany and Spain are still growing in line with expectations and they represent about 40% of Western Europe. On the other hand, negative market trends, which were observed already in the second quarter in the UK have now materialized in France, although as we anticipated to a different and lower extent. These trends as you know are mainly made of environmental concern and consumer arbitrage in favor of non-bottled water.

(technical difficulty) Sorry, the line was cut.

Of course, we don't anticipate for in the case of France to have the same impact as the one we have observed in UK and, to some extent, in the US, as this country is a more mature market in terms of mineral water.

As I commented or we commented previously, the Group has started already, and will continue in the coming months, delivering an appropriate answer to this trend. This is going to be through advertising the benefits of mineral waters versus other forms of waters, and explaining all the initiatives which we have been taking and we will keep taking to mitigate our environmental impact and to protect the springs. We believe that the prospects of mineral water in Western Europe remain good, provided that we address these concerns in a proper manner.

Moving to Baby Nutrition, page seven, this division posted another very solid performance, which was made of volumes holding up well at 5.1%, in line with the 5.6% which we delivered in Q2, and from a lesser value effect. The performance has been driven mainly by infant milks and all regions contributed to it, from Western Europe to Eastern Europe and of course Asia despite a negative impact of the timing of Ramadan in Indonesia this quarter.

A word on Medical Nutrition, which has delivered a growth in Q3, very much in line with the historical background, just below 12%. The growth was, as you know, entirely driven by volumes, while a slightly negative price effect was observed, as usually I would say, reflecting a price pressure in two geographies and one category, which are [tube] in Germany and Netherlands. The targeted disease nutrition grew, as usual, faster than the average of the division and all regions contributed to the growth.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

A word about the regions, which again were very much in line with what we have observed in the second quarter. Europe grew close to 5% reflecting some rebound in Dairy volumes that are offset by a difficult Water performance in France and in the UK as mentioned. Asia grew to close to 14%, driven by Water, Baby Food and to a lesser extent by Dairy. And the rest of the world, which includes, I recall, America, the Middle East and Africa, grew 14.3% in line with the second quarter and driven by the performance of Waters in Mexico and Argentina, as well as the one of Dairy in South America.

A word about the debt, which is obviously an important topic this time. I would like to give you an update on a few elements and on the debt, which for us is a strong element of comfort in these times.

On the short-term debt first, I recall you that the bridge loan which we took for the acquisition of Numico has been fully repaid and that there is no outstanding amount at the end of June, neither at the present time for this loan. This was achieved by the sell up of a syndicated credit line in December last year, plus a number of bond issues during the first half. One of these bond issues, the last one, was indeed made at the end of the second quarter, during the month of July to be precise, amounting EUR500m at very attractive conditions, and allowed us to extend our debt maturity.

On the short-term side we remain with a total EUR1.9b of commercial paper, which we have been keeping rolling over in the past days and weeks on a regular basis and at satisfactory conditions. These commercial paper are obviously fully backed by an amount of more than EUR3b of credit lines with first category banks, plus by cash on hand and treasury stock on the balance sheet.

Looking forward and having a look at the long-term debt, our next significant maturity stands at the very end of 2010 for EUR2.3b. Only a few EUR100m of euro medium-term notes will be due by then. And I will just recall you as well that there is no financial covenant in either of syndicated loan or back ups for our loans, obviously. So, we spoke to you, page 11, the debt maturity profile, which I've largely commented and I'm not going to come back on that, but we're very comfortable with the debt profile we have at the moment.

I'll end up this presentation, page 12, by confirming our guidance for 2008. Coming first with the like-for-like growth of sales, which we confirm at 8% to 10% for the full year, with 9.2% performance year-to-date, which is a strong support, obviously. 40 to 50 basis point improvement of the operating margin and at least 15% of underlying EPS growth versus our pro forma of EPS for 2007.

That's the end of the presentation and we'll now be happy to take your questions. Just one thing before that, on the press release page two you have a title on the Waters paragraph where the value effect is mentioned at minus 3.1%, while obviously the number is minus 2% as it is explained in the presentation on the slide 17. So minus 2% instead of minus 3.1% and we apologize for this typo.

We'll now be ready to take your questions. Please go.

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## QUESTIONS AND ANSWERS

### Operator

Thank you Mr. Terisse. (Operator Instructions). We will take our first question from John Parker, from Deutsche Bank. Please go ahead sir.

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Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**John Parker** - *Deutsche Bank - Analyst*

Yes, good morning. Could I ask two questions? Firstly, in Dairy, you say the blockbusters continue to outperform the rest of the portfolio. Is that a function of the blockbusters being over-represented in the faster-growing markets or is it true of virtually all markets, including France, that the blockbusters are outperforming other products? It would be helpful just to have a little bit more detail there.

And secondly, I wonder if you can say anything about cuts in milk prices that I think you're putting through in France and elsewhere at the moment, and what sort of order of magnitude of milk price cuts that in terms of your costs you're going to be looking at in the fourth quarter and into 2009?

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Okay, thanks. On the milk prices, as you have seen, there has been the big decrease in the price of the skimmed milk powder, which is an important KPI for the evolution of the cost of milk, but which is not the majority of the milk we are buying. We are buying about 90% of our milk in a liquid form and locally.

We are, as you mentioned, going through some discussion times in France at the moment. I'm not going to comment on that except to say that what we are going through at the moment demonstrates that there is no one-to-one correlation neither in terms of timing nor in terms of price between the price of skimmed milk powder and the price of liquid milk.

And, again, on the discussions which are going on, I would not comment on that. We have to wait for the outcome of (technical difficulty).

On the blockbusters, the answer is very clearly everywhere, but it's not a function of mix. It's really that wherever we are, whether in Western Europe or in emerging countries or in America, our blockbusters grow faster. And the explanation for that is extremely clear to us. That's the fact that whenever we provide a specific, understood benefit to the consumer, it's just sticking to the product and ready to accept the price for that.

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**John Parker** - *Deutsche Bank - Analyst*

Thank you.

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Thanks

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**Operator**

Our next question will come from Warren Ackerman from Dresdner Kleinwort. Please go ahead, sir.

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**Warren Ackerman** - *Dresdner Kleinwort - Analyst*

Good morning, it's Warren Ackerman here at Dresdner. I just wanted to go back to the guidance on Dairy. At the interim stage you said that volumes in dairy in H2 would be up. You didn't quantify what up would be, but clearly they're not up in Q3. And you went on to say that volumes in '09 in dairy would be up 4% to 6%. Are you still confident of both the H2 and the '09 volume picture in Dairy, given the Q3 performance? That's the first question.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

The second question similarly on Dairy. I know its early days but can you maybe give us some color on how the ecopacks are performing. You're clearly changing price points across some of the portfolio and what you're doing on promotions at the moment. Is it true that promotions were quite back end-loaded in the second quarter?

And then just finally on Dairy as well, when I look at the mix number for the quarter, the 8.4%, I'm trying to get a feel for how much of the 8.4% is due to mix versus how much is due to pricing. I'm trying to get a feel for when the pricing falls away, how much of that 8.4% is ongoing as the blockbusters become a bigger part of the portfolio. Thanks.

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Thank you. What we said clearly, we expected during the second quarter was a gradual ramp up of volumes with a greater -- an increasing number of geographies moving back to this ramp up profile, and with a positive trend from the volumes in Dairy. That's what we are seeing at the moment and minus 0.2% is indeed still a negative number, although extremely close to flat. That's an increase of 1.3 points compared to what we have seen in Q2 and that's basically in line with what we expected.

Another very reassuring sign to us is the list of countries, which I gave you earlier. That's not something which is happening all of a sudden in all countries but that's the phenomenon which is taking place progressively in different countries.

So I would say that we are very much on the path which we expected and confident in the fact that the volumes are going to move into positive territories in the coming quarter.

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**Warren Ackerman** - *Dresdner Kleinwort - Analyst*

But do you think 4% to 6% in '09? It seems to me that 4% to 6% in '09 is quite a big jump up from sort of flat in Q3 and down in H1.

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

That's for 2008, what I commented.

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**Warren Ackerman** - *Dresdner Kleinwort - Analyst*

Yes

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

2009 is a different discussion and we are, as you know, working on that and that's not really the proper time for us now to discuss about that. We'll come back to you at a later stage as you know. But from what we have seen during the third quarter, yes, that's very much in line with what we expected.

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**Warren Ackerman** - *Dresdner Kleinwort - Analyst*

So are you still happy with up in the second half, overall, as you said earlier?

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Yes.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Warren Ackerman** - *Dresdner Kleinwort - Analyst*

Okay.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Ecopack, it's indeed early days because we are progressively increasing the penetration, which is about one-third September, one-third October, one-third November. But the first two takeaways we get from that are, number one, that it's working for the time being in line with expectations. And number two that we have not seen, at this stage, any sign of cannibalization, which we thought could happen to a limited extent with the plain standard yoghurt, but which for the moment has not taken place. So it's moving along the lines we expected, but again it's a bit early to comment more than that I suspect.

About the mix, it's very much along the same lines as we have been having historically, i.e. above 1 point of mix, 1.5%. So no change on this respect and this is, as you say, driven by the fact that the blockbusters are growing faster than (inaudible).

**Warren Ackerman** - *Dresdner Kleinwort - Analyst*

Sorry, so 1.5% of the 8.4% is mix and the rest of its price. Is that correct?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Yes.

**Warren Ackerman** - *Dresdner Kleinwort - Analyst*

Okay. And just on the promotions, is it true that the promotions in Dairy were more back-end weighted in the Q2 -- sorry, in the Q3 results or were the promotions in Dairy quite even over the quarter?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

No, no that's absolutely true just for a simple reason, which is that July and August are vacation times in --

**Warren Ackerman** - *Dresdner Kleinwort - Analyst*

Sure. Okay, thank you, very helpful

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Thanks very much.

**Operator**

We will now take a question from David Hayes from Nomura. Please go ahead.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**David Harris** - *Nomura Securities - Analyst*

Good morning all, hi, two questions if I can. Just firstly on Asia, quite a different shape to the performance in the third quarter with volumes down to 6.6% from a 13%-plus level in the first half and pricing up to 7.2% having been down slightly in the second quarter. I just wondered whether you can talk about what the change in that shape is driven by, why volumes have dropped off so much and why price is making up for that?

And then, secondly, just in terms of the Dairy performance and the blockbuster brands, coming back to that question, in the second quarter you talked about Activia being obviously a big driver of that, up 26% in terms of value. Can you give us that number for the third quarter in terms of Activia, how much of the growth in the Dairy was driven by the Activia brand? Thanks very much.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Hi David, glad to hear you. One, so let's take on the second question, Activia performance in Q3 was almost exactly the same as the one we had in the second quarter. So no change on that, very much the same. Yes, that's basically the answer.

On Asia I believe that's the combination of -- I mean, as you know, in Asia we have mainly Water and Baby Food business. The Water business has kept increasing as has it done in the past, maybe at a slightly lower pace but really nothing which is a trend. And then the Baby, which has been impacted by Ramadan in Indonesia, as we said, and where the pricing -- I mean what we call the value of pricing is mainly a function of mix. As you know, in some countries of Asia we have observed in Baby Food, very significant up-trading, as opposed to down-trading, which is fuelling the value effect.

**David Harris** - *Nomura Securities - Analyst*

Okay.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

By the combination of these two

**David Harris** - *Nomura Securities - Analyst*

Okay so there are no underlying trends particularly, from a quarter-on-quarter specific market perspective, just those issues?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

No, no, we have said in Q2 that the two most important countries for us in Asia being Indonesia and China. We're holding up very well and we confirm that.

**David Harris** - *Nomura Securities - Analyst*

Okay. Great, thank you.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Thanks

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Operator**

We will now move to Francois Digard from Natixis Securities. Please go ahead.

**Francois Digard** - *Natixis Securities - Analyst*

Good morning, the first question regards the volumes in Dairy. Could you share with us maybe some updates on how the volumes have evolved along the quarter, July, August, September and, if it's possible, the sustainability of rebounds in October.

Maybe also, a point on France. Volumes were down 9%, you mentioned that your market share was stabilizing. Do you imply that the market was down as well at minus 9% and how do you think it is evolving now?

And if you could, as well, some -- give us some more highlights on Spain. Are you seeing there more volumes decline? Do you think it is more about downsizing or down-trading and could you elaborate a bit more on Spain? Thank you.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Thanks Francois. One word about France then, yes, I have said that we are at minus 9% in volume and the market share has stabilized. When I say stabilized it means that it's not dropped in the same manner. So, yes, the evolution of the market is maybe not at minus 9% but quite close to that, negative mid-single digit.

On Spain, I mean, again, the performance of the quarter is very much, very similar to the one we have seen in the first two quarters, with a slight erosion compared to those, but with no specific reason or specific sign for that. I think it's a bit early to comment on Spain. We don't see any real change of trend for this country. The performance is just a bit below but we believe at this stage for punctual or temporary factors.

The first question was what?

**Francois Digard** - *Natixis Securities - Analyst*

About the feeling, actually, of volume rebounds in the course of Q3 and how do you see that's sustainable in the first weeks of October?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

It's really early days to talk about October. I mean the phasing during the first -- the June -- sorry, July, August and September months was quite regular, obviously impacted by differences in the number of days, but the volumes per day were -- have been increasing in an even manner, I would say, or rebounding in an even manner across the quarter. And again as for October, I think it's pretty early days to comment.

We do expect, as I commented already, volume growth Dairy to move up into positive territories for the fourth quarter. In terms of sales, it's clear that Q4 will have 1 point of difference compared to Q3, which is the base of comparison, no? As you can see on the page number five of the presentation, the fourth quarter of 2007 showed an increase of 13.9% compared to 11% or 12% in Q2 and Q3. And therefore we have a difference of 3 points on the base of comparison so that's clearly going to be important when looking at Q4. But again in terms of volumes, we look at moving into positive territory.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Francois Digard** - *Natixis Securities - Analyst*

Thank you.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Thanks

**Operator**

We will now take a question from Julian Hardwick from RBS. Please go ahead.

**Julian Hardwick** - *RBS - Analyst*

Good morning. You commented in your press release that the melamine issue in China did not negatively impact your Infant business in Q3. I just wondered, did it have any positive benefit to you and if so, can you quantify that?

And as you look ahead to the fourth quarter, given what's happened to the local players in China, is this an issue, which you would expect to have a positive impact on your Infant performance in Q4?

And secondly, I just wondered if you could give us the volume trends for water in both the UK and France in Q3?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Yes, on the melamine, I mean that's been basically a very bad thing for China as a whole. And it is true that given the fact that we've had no contamination whatsoever on one hand and that a large part of the market has had contamination of their product, then we have directly benefited from that somehow because we've seen the demand increasing at our side. That's not something which has had a significant impact on the third quarter because obviously this had started in September and we have only a few days, which have been impacted. But, yes, there is a positive impact, which is a kind of side effect for us.

At the same time, the most important for us is to help the Chinese government and the industry to recover because while we are clearly a leader in this category in this country, we just need to have a category which is holding up well. So no real positive effect but we really take that as an opportunity to rebuild the category and make it better.

As for the Baby Food in Q4, yes, obviously, there will be some impact. In fact there are two reasons why we expect Q4 to be better than Q3 for the Baby Food. One is the one we've just discussed and the other one is obviously the base of comparison of last year since, as you remember, we did make adjustment on the level of the inventory during the fourth quarter of last year.

Your last question was about the volume trends in France and in the UK. We've already mentioned in the UK that we are talking of negative double digit market evolutions, or I confirmed that. And I said during the presentation that France is different and is impacted to a lower extent. Since we are talking of mature markets and then the negative market trends is more in the negative mid-single compared to a negative double-digit in the UK.

**Julian Hardwick** - *RBS - Analyst*

And is your performance in line with both those market performances?

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

It's a bit worse actually. In both markets one of our brands, which is Volvic, is losing market share to the overall competition.

**Julian Hardwick** - *RBS - Analyst*

Okay, thank you.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Thank you.

**Operator**

We will now move to Marco Gulpers from ING. Please go ahead.

**Marco Gulpers** - *ING - Analyst*

Yes, good morning. This is Marco Gulpers from ING. Maybe a follow up question on the Water division. You mentioned that you are targeting the environmental issue. Could you elaborate a bit more on that, and would you also, in this light, consider bioplastic's moving forward?

Second question is on the Dairy division. You didn't mention Eastern Europe. Could you still confirm how Eastern Europe is progressing? Thank you.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Okay, thanks. Water environmental issue, we've been really taking a lot of action for the past 10/15 years at our side. Not because we've been -- not only because we've been a precursor on the environmental side but for cost reasons on one hand and to protect the spring from the other because we know that it's a very important asset.

For instance, we have organized a perimeter of 20 square kilometers around the spring to protect it, and we take care of that. For instance as well 70% of the transportation we use in France is done by train and there are many examples like that. For instance again we have decreased the weight of the bottle over the years very significantly. So that's what we have done and clearly we've not been very vocal about that. We need to be.

We have other projects, which include, as you say, recycled PET. We have already in France 25% of recycled PET in all of our bottles, which is not something which is known, but again we will make sure that consumers understand that. We are already planning to increase this percentage. We have plans to move to other forms of bottles so we are very active on that.

And in the coming months we could even announce more important measures. And we could target, in fact, for our Water division in -- or for some of our brands, say Evian or Volvic for instance, we could perfectly target to become carbon neutral to have neutrality in terms of footprint very quickly. So a bit early days to be fully precise on that, because communication will be coming, but we will have more details for you very, very soon and we are moving along the lines I mentioned.

Eastern Europe, no specific comment except to say that we had mentioned during the second quarter some softness observed in Russia in particular. What we have seen here in Q3 has been very reassuring. And to us this softness, which we saw a little bit

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

during Q2, is not fully confirmed. In addition to that we keep gaining market share and being ahead of competition in Dairy in Russia, so no specific concern about these countries.

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**Marco Gulpers** - ING - Analyst

Excellent. Thank you.

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**Operator**

Chris Wickham from MainFirst will ask the next questions, please go ahead.

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**Chris Wickham** - MainFirst Bank - Analyst

Thank you. On page two you do give us some details on the performance of the blockbuster, the brands, and you again are talking about the double digit growth. But I was wondering perhaps if you could give us a bit more clarity on price mix within the blockbusters, and then price mix within the more basic categories in Q3 relative to where you were in the first half of the year.

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**Pierre-Andre Terisse** - Groupe Danone - CFO

It's really the same composition, i.e. the price mix -- I mean the breakdown between price mix and volumes which you see overall on Dairy is very much the same for the blockbusters, which means that the blockbusters are outperforming the average of the portfolio in sales terms, but also very clearly in volume terms.

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**Chris Wickham** - MainFirst Bank - Analyst

Right. So between the first half and Q3 there is no real change in how they are performing?

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**Pierre-Andre Terisse** - Groupe Danone - CFO

No.

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**Chris Wickham** - MainFirst Bank - Analyst

And then the second point is I was wondering if you could tell us whether there is any difference at the moment. We saw a bit of divergence in Q2 between Actimel and Activia when -- how they performed relative to each other in Q3.

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**Pierre-Andre Terisse** - Groupe Danone - CFO

Yes, we've basically said in Q2 that Activia and Danacol are performing extremely well. And we said at the same time that Actimel, Vitalinea and Danonino were not performing as well and that we had some issues, different issues, to fix on these various products.

One of the products on which we have progressed during Q3 is Danonino, which has improved compared to what we have seen in Q2. Actimel is not the case yet. We have in the case of Actimel a question of renovation to address. We are working on that. We will come with that in the coming months, but we are not there yet.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Chris Wickham** - *MainFirst Bank - Analyst*

Okay. Thank you.

**Operator**

We will now take a question from Pablo Zuanic from JP Morgan, please go ahead.

**Pablo Zuanic** - *JP Morgan - Analyst*

Good morning everyone. I am still struggling with this issue of how are volumes in dairy going to get back to this 5%, 6% long term guidance in 2009. So really my question is when you look at the performance in 2008, in terms of volumes, would you attribute that mainly to price inflation or to something that the Company did wrong?

And the reason that's relevant is because when I think of 2009 I am trying to ask myself what's going to change. You are implying that the cost deflation benefits are not necessarily there, so retail prices may not come down. So what is the Company going to do next year that's going to be different that will improve the volume performance? I could argue that with the weaker consumer, and a strategy predicated on these functional brands, which by definition mean trade-up, it's difficult to see how volumes get back to 5% to 6%. So if you could just give us more color in terms of what's changing next year that would make us think that volumes should improve?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

I am very sorry I will have to disappoint you on that, because as I said this call is naturally for the discussion about 2009 since we are working on that. And I will plan to come back to you in the coming weeks and months to give you more clear about 2009. So I am not going to answer your question directly.

Maybe two words about some of the rest of your question, the first about the reason why the volumes have not been progressing as they have in the past years this year. There are two reasons in my view. The main one, which we see gradually phasing out, is the price increase which we have taken, which were very substantial, about 10% altogether in average across the portfolio. And which obviously have an impact, but that's true for every consumer industry, on the volume as you move to increase the pricing. And this impact is usually phasing away -- fading away sorry, that's what we start seeing during this quarter.

The other reason is obviously some economic conditions in a selective number of markets. We clearly flagged out France during the second quarter and we said that France was impacted by consumer confidence. And we said that this would remain for a while with minus 9% in Q3. It's very clear that this has not been so. We flagged as well Mexico where we have seen during the second quarter some negative signals from the economy on the effect on the consumptions, and we keep seeing that.

So the main reason, which is really the increase of price and the effect it has on volumes. A second impact, which is coming from the economies in certain countries.

And then looking at 2008, which is really the only thing we can comment now, again the minus 0.2% for us is a rebound, which is in line with what we expected.

**Pablo Zuanic** - *JP Morgan - Analyst*

Thank you. Can I just have a quick follow up if I may on the Water business? When we think of Argentina, Mexico and Indonesia being half of your Water sales and clearly having a strong franchise there, I am just trying to think in terms of what is happening

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

with your competition there from Coke and Pepsi. They obviously have more scale in water. Granted its purified water, but it's also a lower price point.

So longer term I am wondering whether you are gaining distribution and taking share away from Aqua Indonesia or Bonafont in Mexico. How sustainable is your presence in those three countries, particularly when they have more scale in emerging markets when we think of all the countries together.

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

I think it's fair to say that they have a wider, at least for some markets, they have a wider distribution. I think it's equally fair to say that we have a knowledge in taking care of the springs, getting the water, selling mineral water, which they don't have, and we've demonstrated that over time.

These markets for us are really a no-brainer. These markets are growing, they are growing fast, they are growing very regularly, they are growing with volume and, therefore, there is no question mark on these markets for us.

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**Pablo Zuanic** - *JP Morgan - Analyst*

Thank you.

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**Operator**

We will now more to Cedric Lecasble from Kepler please go ahead.

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**Cedric Lecasble** - *Landsbanki Kepler - Analyst*

Yes, good morning, Cedric Lecasble actually from Kepler. I would have two questions, the first one on the situation in the tough markets for Dairy in Europe.

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Sorry, which market?

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**Cedric Lecasble** - *Landsbanki Kepler - Analyst*

France, Spain, the tough ones in Western Europe, can you --

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Right.

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**Cedric Lecasble** - *Landsbanki Kepler - Analyst*

Could you maybe comment on the evolution of the price differential between private labels and your products on the low end of the range, which seems to be where the problem is, as you explained?

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

How far do you think -- what is your action plan? It would be to reduce further in '09, this kind of price differential, to move again consumers towards your brands for the plain, the fruit yogurt in these countries. What did work in terms of consumer response to promotions and what didn't work yet? Maybe you could help us a little bit understanding what is going on.

And the second question is on North America. You said Yoplait was more competitive, putting pressure. Could you be a little more specific there and maybe explain us how this -- to what extent it impacted your Q3 performance in, mainly in volume? Thank you.

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Yes. France and Spain first, and maybe before starting with France and Spain just a word about Italy, which is a European market with very similar conditions to other markets like France and Spain, and Italy is just growing extraordinarily well. So just to outline that, we really have specific situation country by country with a few common points, which are basically the price increase, but that's mainly it.

On France we said indeed during Q2 that we had seen higher than in the past erosion in market share against private label and from our core range. We have said that we would bring two answers. Number one a level of promotion which would be back to normal because we had been extremely low on promotion during the first half. And number two the Ecopack which aims at providing to the consumer an alternative offer at a competitive price and Danone quality. Ecopack for the moment is doing well, although as I said it's a bit early to comment on that.

I think the higher promotions compared to the first half are the main explanation for the market -- sorry, for the performance evolution we have seen in France, i.e. moving from minus 15% in Q2 to minus 9% in Q1. So, again, very much what we expected as the reaction to the answers we are putting on the table and we will just continue and monitor that.

On the US -- sorry on Spain to complete, Spain has not really seen this shift to private label. It's more a matter of overall softness of the market. We continue maintaining our share. And the reason for that is that this market is very different from France because we have a very strong leadership, market share twice as big as the one we have in France and there are only basically two players in Spain, which are ourselves and a private label. So the market is reacting differently and the solutions are probably different to some extent to bring. We don't have anywhere in Spain the same program as we have in France of facing a very aggressive private label and losing market share to that.

In North America, yes, of course our competitor has been very aggressive. He has been basically shifting faster than we have from medium spending to promotion. That's something which we had already observed in the second quarter. The answer for us is to do the same and to become a bit more aggressive in promotion, and above all to shift from under-spending to promotion because we are basically entering into a different stage of the economy.

One important point about the US is again the same, i.e. that where we are having a problem is on the core range and not on blockbusters, which on the other hand Danone Active and Activia, continue to perform very well and to grow very fast.

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**Cedric Lecasble** - *Landsbanki Kepler - Analyst*

You would confirm that in France the promotional intensity in Q4 will play on three months instead of one, one and half and will be higher in Q4 than it was in Q3?

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

That's correct.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Cedric Lecasble** - *Landsbanki Kepler - Analyst*

Okay, thanks a lot.

**Operator**

We will now take a question from Michael Steib from Morgan Stanley, please go ahead.

**Michael Steib** - *Morgan Stanley - Analyst*

Good morning. Are you considering rolling out initiatives like the Ecopack or the different size packs that you've launched in the third quarter in France also in other markets in order to support your volume growth going forward?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Again its very early days to say that because we first need to see the results of this initiative in France before fully taking the decision. We could, however, selectively use that in some markets where we face competition from the private label or some shift from our core range, from the consumer from our core range to private label.

That's the case of France. That's the case in the US, not to private label but to Yoplait. So that's something we could envisage in the US. And that's something maybe we could envisage in Spain, even though it's a bit early to say.

There is no overall plan to roll-over Ecopack and to make it a blockbuster. It's a tactical instrument, which remains tactical for the time being.

**Michael Steib** - *Morgan Stanley - Analyst*

Okay, thanks.

**Operator**

We will now move to Xavier Croquez from Exane, please go ahead.

**Xavier Croquez** - *Exane BNP Paribas - Analyst*

Yes good morning. Xavier Croquez at Exane. Two points that I am not sure I got right because the line was bad. The 8.4% of value factor in dairy you gave the split to Warren, mix and price, and I missed it. Can you please give it to me?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

I said approximately 1.5% was mix.

**Xavier Croquez** - *Exane BNP Paribas - Analyst*

Okay, thank you. You have the same growth in Q3 than in Q1 volume wise in dairy of minus 0.2%. You gave us the minus 9% for France. I can't remember the figure for France in Q1. What was volume doing at that time is my first little question?

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

And the broader question is, independently of businesses, if we look at emerging markets my quick calculation suggests that you have been growing there north of 12%. Could you validate that figure roughly or give us the right figure?

And if we go through an overview you mention here and there that Russia was no longer a reason for concern unlike Q2, that Mexico remains a bit of a concern. Could we get a quick review of the big emerging markets please? Thanks.

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Yes, if you don't mind on the precise figures we will get back to you. Top of my mind what you say about emerging is correct, but we will get back to you with more precise figures and details on that.

On the emerging markets again the situation -- lets put it this way, we've flagged two markets in which we had seen softness during Q2. One of them is confirmed is Mexico. One of them is not confirmed and that's Russia.

We said as well that Argentina was still holding well despite the chaotic condition of the country and the social unrest. This is still the case.

We said Brazil was doing extremely well. This is still the case.

We said China and Indonesia were doing well. This is still the case.

And I think that's very much it. So one confirmation and one, I would say, information concerning the two countries I've mentioned, Mexico and Russia. And for the rest we are really on the same trends as the one seen before.

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**Xavier Croquez** - *Exane BNP Paribas - Analyst*

Okay, thank you. And it's a precise figure, but Q1 volume in France in Dairy?

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Robin will get back to you.

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**Xavier Croquez** - *Exane BNP Paribas - Analyst*

Okay, thanks.

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

I am sorry.

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**Operator**

We will now move to Mario Montagnani from Cheuvreux. Please go ahead.

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**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Good morning.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Mario Montagnani** - *Cheuvreux - Analyst*

Good morning. Just a quick question on emerging markets, so Asia and the rest of the World. My question is about the phasing, if you experienced any kind of slowdown over the quarter and if you can quantify that by months. That would be the first question.

And the second I have is on commodity costs. I think you mentioned basically you are experiencing an easing pressure in terms of commodity costs especially from dairy or milk. Can you just quantify and elaborate a bit on promotional spending, how we went through the quarter, July, August, September for Danone in Dairy especially?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

I'm not sure I fully understand your second question. I believe it's about the phasing of promotional?

**Mario Montagnani** - *Cheuvreux - Analyst*

Absolutely.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Okay, it's very simple. As we said, in many markets we've been higher on promotions during the month of September because July and August are vacation time and therefore it's not the same consumption pattern. So clearly it's been weighted towards the month of September more than July and August.

On the emerging markets, no comment other than what I said before, i.e. that the progression of volume has been evenly distributed across the quarter with ups and downs obviously market by market, but overall evenly distributed.

**Mario Montagnani** - *Cheuvreux - Analyst*

Okay, just to come back on the first question. You mentioned basically September was the month where your spend basically, you went back to promotional spending. Was that a normalized level or something still below probably your average spending?

And the question related to that is you commented about a phasing of organic growth for that division in July, August, September. I think you were pointing out that there was a big difference in terms of volume growth, July, August, September, but can you -- did you see any impact from this [recent] promotional activities in September, in the month of September in terms of volumes? Thank you.

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

I'm not really going -- I'm not going to enter into more details than that. Sorry for that. But really the progression, the key things to keep in mind is that the progression has been really consistent across the quarter so there has not been any sudden change of trend across the quarter. And on the promotions, I said indeed that September is, very logically then, higher on promotion than July and August because of vacation.

**Mario Montagnani** - *Cheuvreux - Analyst*

Okay. Many thanks.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Thanks.

**Operator**

We'll take another question from [Nick Sochovsky] from Merrill Lynch. Please go ahead.

**Nick Sochovsky** - *Merrill Lynch - Analyst*

Yes hi. Just to change tack slightly, can you just tell us what the organic growth rate was for the Infant Nutrition business in Western Europe and then just split out volume and price, and also what the developing market growth rate was for Infant Nutrition?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

We're not giving a precise breakdown of that. What I can say is that obviously, number one, there's been growth across all regions. Number two, within Europe, UK has really been delivering a very good performance during this third quarter, but, again, among Europe, which overall has delivered growth. And number three, obviously, but that's something which we have --

**Nick Sochovsky** - *Merrill Lynch - Analyst*

That growth mid-single-digit?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Something which we have observed for the past quarters is that Eastern Europe and Asia has performed even better than Europe.

**Nick Sochovsky** - *Merrill Lynch - Analyst*

I.e. is Europe mid-single-digit? Is it around 5%?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

I'm sorry. I said we don't comment on that, Nick.

**Operator**

We will now take a question from Joseline Gaudino from Societe Generale. Please go ahead.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Joseline Gaudino** - *Societe Generale - Analyst*

Good morning. I want to come back to the situation of the blockbuster. You mentioned in your press release that in terms of volume they have done substantially better than the divisional average. Could you give us more detail? And for example, could you give us the split, a geographical split in volume for the blockbuster and especially for example for Activia?

I'm a little bit lost in all -- because you mentioned that blockbuster has done -- the pattern is virtually the same as in Q3 for the whole division, but in the press release it is substantially better in volume terms, so could you give us more detail?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

Yes, it was not very clear when I that. What I meant by that is that the excess of performance of blockbuster compared to the overall division has been substantial, number one. Number two has been the same, so the excess of performance has been the same across all regions. So in all regions the blockbusters are doing better than the average of the range.

**Joseline Gaudino** - *Societe Generale - Analyst*

And could you give us for example the detail in North America, France, Europe? The whole European countries and Latin America for example?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

We don't provide that. As I said in the case of North America, I commented that the blockbusters are really growing, keep growing fast and the problem is in core range. So the differential is probably even bigger in this specific case, but we don't give, we don't give a breakdown of this split, Joseline.

**Joseline Gaudino** - *Societe Generale - Analyst*

Okay. And so I'll come back on the situation of France and you mentioned that for Q2 France was minus 15%, for Q3 it was minus 9%. Could we have the situation in September, just September?

**Pierre-Andre Terisse** - *Groupe Danone - CFO*

No, no, we're not going to answer by month. What I can say is really recall what we said in Q2 and as appeared to be true in Q3, i.e. in the performance of Q2 there were a number of reasons, some of them which we think are going to remain for the second semesters, so Q3 and Q4. And these reasons are basically consumer confidence on the one hand plus all the implementation of new law and discussion with the retailers which are implied by this new law. And as you know the LME, the new law in France is not yet fully implemented.

And we said as well that there were some reasons which we thought would fade away during the second semester and one of them was clearly the fact that we have been low on promotions. And to us the comparison between Q2 and Q3 reflects exactly what I said about that.

Which means that we do not expect still France to come back into a normalized level during the fourth quarter because the two issues I mentioned, i.e. consumer confidence and above that the negotiation of -- the implementation of the new law, will remain for a while.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

**Joseline Gaudino** - Societe Generale - Analyst

I have a last question on Ecopack. It seems to me that it's slow to implement and has the product been accepted by all retailers or --

**Pierre-Andre Terisse** - Groupe Danone - CFO

It's been accepted by most retailers. There are a few missing but not major ones for that kind of product and basically we are happy with what we have achieved.

I would just correct a bit about what you say about the slow implementation because we've really been working hard and we are now already in between one third and 50% of the retail. Increasing the penetration gradually, but that's I would say a normal if not quicker implementation than for other normal products.

**Robin Jansen** - Groupe Danone - Director, IR

Maybe just add to that Joseline. As I say, we're on track based to what we planned, so we've selectively chosen the retailers where we want to start and from the beginning there was no intention to make it a big bang and try to be in every retailer at the same time. So according to our plans, we're at least on track.

**Joseline Gaudino** - Societe Generale - Analyst

Okay, thanks.

**Robin Jansen** - Groupe Danone - Director, IR

We take one last question.

**Operator**

Thank you. Our last question will come from Jeff Stent from Citi. Please go ahead.

**Jeff Stent** - Citigroup - Analyst

Good morning gentlemen. Two if I may. The first one is for a retailer what's the benefit of Ecopack? Is it a better cash margin than the average private label offering?

And secondly, looking at benzene and ethylene prices about 40% below recent contracts, I'm just wondering if you're able to give us any color on how much forward buying you've done on the plastics front. Thanks.

**Pierre-Andre Terisse** - Groupe Danone - CFO

On the benefit of Ecopack for the retailer, that's one of the elements, not the only one obviously, but one of the elements which we think is going to provide some more dynamics to the category. So that's something which as such basically is in the interests of ourselves of course but the whole category. And again that's one of the elements, but if it's successful that's going to be driving up sales and driving up sales for us and for the retailers.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

On the cost, as you know we are not buying directly oil. We are buying plastics which are being manufactured by people with oil. So there is an (inaudible) in the chain which basically means that there are a couple of months, three months of implicit forward buying in that.

In addition to it, the impact of the evolution of oil is not translated to us one to one. It's not been the case during the first half where we have been able to get better prices than what they should -- than what they would have been sorry, if we had been impacted directly by the increase, and it's going to be the case going forward, i.e. that we use that collaborating with the supplier and making sure we are -- we don't get the same volatility as you can observe on the stockmarket.

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**Jeff Stent** - Citigroup - Analyst

Thank you. And just to clarify your response to the first question so the cash margin is better for retailers on Ecopack than it is on their private label offerings, is that correct?

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**Pierre-Andre Terisse** - Groupe Danone - CFO

I've not said that and I'm not going to comment publicly on our level of margins for obvious reasons.

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**Jeff Stent** - Citigroup - Analyst

Okay, thank you.

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**Pierre-Andre Terisse** - Groupe Danone - CFO

Thanks.

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**Robin Jansen** - Groupe Danone - Director, IR

Alright. Well thanks very much to all of you. Very happy to have had this call and I'm sure we'll have other opportunities to interact in the coming days. Thanks very much.

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**Operator**

This will conclude today's conference call. Thank you for your participation. Ladies and Gentlemen you may now disconnect your lines.

Oct. 22. 2008 / 3:00AM, BN.PA - Q3 2008 Groupe Danone Sales Conference Call

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