Nestlé. Good food, Good life

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES

Annual Financial Report

Management Report

Responsibility Statement

Consolidated Financial Statements

December 31, 2019 and 2018

(With Independent Auditors' Report Thereon)

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES

Table of Contents

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES

December 31, 2019 and 2018

Management Report

Nestlé Holdings, Inc. ("NHI") (hereinafter, together with its subsidiaries, referred to as the "Company") incorporated in the State of Delaware, United States, is a wholly owned subsidiary of NIMCO US, Inc., which is an indirect wholly owned subsidiary of Nestlé S.A., incorporated in Switzerland, which is the holding company of the Nestlé group of companies (hereinafter, referred to as the "Nestlé Group"). NHI is the holding company for Nestlé S.A.'s principal operating subsidiaries in the United States, other than Nestlé Waters North America Inc., Terrafertil US LLC and Atrium Biotech USA, LLC. The Company engages primarily in the manufacture and sale of food products, pet care products, and beverage products. These businesses derive revenue across the United States.

Key Figures

	2019	2018	Change
	(Dollars in millions)		
Sales	$ 23,518.7	22,423.9	4.9%
Cost of goods sold	(12,871.1)	(12,380.5)	4.0%
as a percentage of sales	(54.7)%	(55.2)%	
Trading operating profit	1,848.5	2,156.0	(14.3)%
as a percentage of sales	7.9%	9.6%	
Net financial expenses	(253.7)	(212.4)	19.4%
Income tax expense	(413.2)	(669.4)	(38.3)%
Net income/(loss)	1,000.2	(406.5)	346.1%
as a percentage of sales	4.3%	(1.8)%	
Operating cash flows	2,286.8	2,016.6	13.4%
as a percentage of sales	9.7%	9.0%	
Capital expenditures	1,134.7	851.0	33.3%
as a percentage of sales	4.8%	3.8%	

Overview

The Company is actively involved in portfolio management, demonstrated by product launches and expansions, as well as acquisitions and divestitures in 2018, and as a result the Company delivered a 4.9% improvement in sales. The Company is committed to continued execution of cost reduction initiatives, improved operational efficiencies, and further investment in its brands.

Sales

For the years ended December 31, 2019 and 2018, consolidated sales totaled $23.5 and $22.4 billion, respectively. The main factors per segment are as follows:

- **Nestlé USA Brands** sales were $11.3 billion and $9.9 billion for the years ended December 31, 2019 and 2018, respectively. Sales growth was primarily driven by *Coffee-Mate,* and *Starbucks* branded products. Some prominent brands in this segment include *Coffee-Mate*, *Nescafé*, *Nesquik, Stouffer's, DiGiorno, Lean Cuisine, Hot Pockets, Nestlé Toll House, Dreyer's, Edy's*, and *Starbucks.*

- **Nestlé Purina PetCare** sales were $8.4 billion and $7.8 billion for the years ended December 31, 2019 and 2018, respectively. PetCare had strong sales development, particularly with *Pro Plan*, and *Purina One,* in the e-commerce channel and *Tidy Cats* litter had double-digit growth. Some notable brands in this segment include *Beneful, Alpo, Purina ONE, Dog Chow, Pro Plan, Beyond, Fancy Feast, Friskies, Cat Chow,* and *Tidy Cats*.

- **Nutrition** sales were $1.0 billion and $1.1 billion for the years ended December 31, 2019 and 2018, respectively. Sales growth in this segment is primarily driven by *Gerber's* baby food sales which are driven by innovations in the organic range and heathy snacking. A notable brand in this segment is *Gerber*.

- **Other** businesses sales were $2.8 billion and $3.6 billion for the years ended December 31, 2019 and 2018, respectively. Excluding the sale of Gerber Life Insurance in 2018, the Others segment sales are increasing, primarily attributable to *Nespresso* which maintained mid single-digit growth.

Profitability

Trading operating profit was $1.8 billion and $2.2 billion for the years ended December 31, 2019 and 2018, which equaled 7.9% and 9.6% of sales, respectively. The decrease, as a percentage of sales, was primarily due to higher royalties to affiliated companies and an increase in net other trading expenses.

Cost of goods sold was $12.9 billion and $12.4 billion for the years ended December 31, 2019 and 2018, which equaled 54.7% and 55.2% of sales, respectively. The increase, as a percentage of sales, was due to higher commodity costs and other variable expenses, partially offset by operational efficiency savings.

Distribution expenses were $2.2 billion and $2.1 billion for the years ended December 31, 2019 and 2018, which equaled 9.2% and 9.2% of sales, respectively.

Marketing, general and administrative expenses were $3.6 and $3.5 billion for the years ended December 31, 2019 and 2018, which equaled 15.4% and 15.5% respectively.

Net other trading expenses were $521.3 million and $225.5 million for the years ended December 31, 2019 and 2018, respectively. The increase was primarily due to impairment charges related to property, plant and onerous contracts related to the exit of Direct-Store-Delivery (DSD) network for Frozen Pizza and Ice Cream.

Net Profit Margin – Other Items of Interest

Net financial expenses increased by $41.3 million in 2019 primarily due to increases in net financing cost.

The Company's income tax expense decreased by $256.2 million in 2019, primarily as a result of a decrease to prior years' taxes and non-deductible amortization of goodwill and other intangible assets related to the 2018 disposal of Gerber Life Insurance. These decreases are offset by an increase in income from continuing operations before income taxes in 2019.

Cash Flow

Operating cash flow was $2.3 billion and $2.0 billion for the years ended December 31, 2019 and 2018, respectively.

Principal Risks and Uncertainties

Risk Management

At the Nestlé S.A. level, the Nestlé Group Enterprise Risk Management (ERM) framework is designed to assess and mitigate risks in order to minimize their potential impact on the Nestlé Group, including the Company.

A top-down assessment is performed at the Nestlé Group level once a year to create a robust understanding of the Group's mega-risks, to allocate ownership to drive specific actions around them and take any relevant steps to address them. A bottom-up assessment occurs in parallel resulting in the aggregation of individual assessments by all markets and globally managed businesses of the Nestlé Group. These different risk mappings allow the Company to make sound decisions on its future operations.

Risk assessments are the responsibility of business line management; this applies equally to a business or a function, and any mitigating actions identified in the assessments are the responsibility of the individual line management. If Nestlé S.A. intervention is required, responsibility for mitigating actions will generally be determined by the Nestlé Group Executive Board.

The results of the ERM are presented annually to the Nestlé Group Executive Board, half-yearly to the Audit Committee of Nestlé S.A., and reported annually to the Board of Directors of Nestlé S.A.

The factors identified below are considered the most relevant for the Company's business and performance.

Factors Affecting Results

Maintaining high levels of trust with consumers is essential for the Company's success. Any major event triggered by a serious food safety or other compliance issue could have a negative effect on the Company's reputation or brand image. The Company has policies, processes, controls and regular monitoring to ensure high-quality products and prevention of health risks arising from handling, preparation and storage throughout the value chain.

The success of the Company depends on its ability to anticipate consumer preferences and to offer high quality, competitive, relevant, and innovative products. The Company's Nutrition, Health and Wellness strategy aims to enhance people's lives at all stages through industry-leading research and development to drive innovation and the continuous improvement of the Company's portfolio.

Prolonged negative perceptions concerning health implications of processed food and beverages categories could lead to an increase in regulation of the industry and may also influence consumer preferences. The Company has long-term objectives in place to apply scientific and nutritional know-how to enhance nutrition, health and wellness, contributing to healthier eating, drinking and lifestyle habits, as well as improve accessibility of safe and affordable food.

Changing customer relationships and channel landscape may inhibit the Company's growth if the Company fails to maintain strong engagements or adapt to changing customer needs. The Company's strategy is to maintain and develop strong relationships with customers across the United States to help them win in their respective prioritized categories where the Company operates.

The Company is dependent on the sustainable supply of a number of raw and packaging materials. Issues relating to longer-term changes in weather patterns, water shortages, shifts in production patterns, economic and social inequality in supply chains, etc. could result in capacity constraints, as well as reputational damage. The Company has policies, processes, controls and regular monitoring in place which are intended to allow the Company to anticipate such events and adequately mitigate against them.

The Company manages risks related to climate change and water resources.

The Company is subject to environmental regulation regimes and has controls in place to comply with legislation concerning the protection of the environment, including the use of natural resources, release of air emissions and waste water, and the generation, storage, handling, transportation, treatment, and disposal of waste materials.

The Company is reliant on the procurement of materials, manufacturing and supply of finished goods for all product categories. A major event impacting input prices, or in one of the Company's key plants, at a key supplier, contract manufacturer, co packer, and/or warehouse facility could potentially lead to a supply disruption. Active price risk management on key commodities and business continuity plans are established and regularly maintained in order to mitigate against such events.

The investment choices of the Company evolve over time and may include investments in emerging technologies, new business models, and the creation of, or entry into, new categories. This may result in broader exposures for the Company, e.g. a more highly regulated environment for the healthcare segment, etc. The Company's investment choices are aligned with the Company's strategy and prioritized based on the potential to create value over the long-term.

The Company, as part of its strategy, undertakes business transformations such as large scale change management projects, mergers, and acquisitions. To ensure the realization of the anticipated benefits of these business transformations, they receive executive sponsorship with aligned targets as well as appropriate levels of resources to support successful execution of them.

The ability to attract and retain skilled, talented employees is critical to the success of the Company's strategy. The Company's initiatives and processes aim to sustain a high-performance culture, supported by a total awards approach and people development that emphasizes diversity, innovation and growth.

The Company is subject to health and safety regimes and has procedures in place to comply with legislation concerning the protection of the health and welfare of employees and contractors, as well as long-term initiatives to promote safe and healthy employee behaviors.

The Company depends on accurate, timely data along with increasing integration of digital solutions, services and models, both internal and external. Disruption impacting the reliability, security and privacy of the data, as well as the information technology infrastructure, is a threat to the Company's business. Contingency plans along with policies and controls are in place aiming to protect and ensure compliance on both infrastructure and data.

The Company's liquidity/liabilities (currency, interest rate, hedging, cost of capital, pension obligations/retirement benefits, banking/commercial credit, etc.) could be impacted by any major event in the financial markets. The Company, along with its parent company, Nestlé S.A., has the appropriate risk mitigation measures in place with strong governance to actively manage exposures and long-term asset and liability outlook.

Security, political instability, legal and regulatory, fiscal, macroeconomic, foreign trade, labor, and/or infrastructure risks could potentially impact the Company's ability to do business. Major events caused by natural hazards (such as flood, drought, infectious disease pandemics, etc.) could also impact the Company's ability to operate. Any of these events could lead to a supply disruption and impact the Company's financial results. Regular monitoring and ad hoc business continuity plans are established in order to mitigate against such events.

Outlook

The Company is well positioned with strong, high quality brands, which are valued by the customer but any adverse developments in the United States economy could impact consumer demand. In particular, there is a significant increase in economic uncertainty which is, for example, evidenced by more volatile asset prices and currency exchange rates, and rising unemployment claims. Due to the uncertainty of the outcome of the current events, the Company cannot reasonably estimate the impact these events will have on the Company's financial position, results of operations or cash flows in the future. There are opportunities to leverage the Company's competitive advantages, deliver on growth opportunities, and benefit from the drive for continuous improvement. The Company is committed to supporting the Nestlé Group in achieving its financial objectives including continued improvement in organic sales growth, underlying trading operating margin, underlying earnings per share in constant currency and capital efficiency.

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES

December 31, 2019 and 2018

Responsibility Statement

Kathleen Carl, Chief Accounting Officer, confirms that to the best of her knowledge:

(a) the financial statements, prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), give a true and fair view of the assets, liabilities, financial position and profit or loss of NHI, and the undertakings included in the consolidation taken as a whole; and

(b) the management report includes a fair review of the development and performance of the business and the position of NHI and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

March 31, 2020

KPMG LLP
Suite 900
8350 Broad Street
McLean, VA 22102

Independent Auditors' Report

The Board of Directors
Nestlé Holdings, Inc.:

Opinion

We have audited the accompanying consolidated financial statements of Nestlé Holdings, Inc. and its subsidiaries (the Company), which comprise the consolidated balance sheets as of December 31, 2019 and 2018, and the related consolidated statements of income, comprehensive income, changes in equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Nestlé Holdings, Inc. and its subsidiaries as of December 31, 2019 and 2018, and their consolidated financial performance and their consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IFRS).

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS) and in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in the United States of America, together with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants*, and we have fulfilled our other ethical responsibilities in accordance with these requirements, respectively. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key Audit Matter	**How the matter was addressed in our audit**
Revenue recognition (Sales)	
Revenue from the sale of goods is recognized at the moment when control has been transferred to the buyer; and is measured net of pricing allowances, other trade discounts, and price promotions to customers (collectively 'trade spend').	We tested the design, implementation, and operating effectiveness of certain controls over the IT environment in which ordering and billing and other relevant support systems reside, including change control procedures in place around systems that bill revenue streams.

Key Audit Matter	How the matter was addressed in our audit
The judgments required by management to estimate trade spend accruals are complex due to the diverse range of contractual agreements with the Company's customers. There is a risk that revenue may be misstated due to fraud resulting from the pressure management may feel to achieve performance targets. Revenue is also an important element of management incentive schemes.	For a sample of revenue transactions, we agreed the quantity of goods being delivered to the bill of lading and the related customer invoice(s). We also recalculated the total revenue amount per the customer invoices(s) using the quantity and unit price of the goods being delivered, and agreed the total revenue amount per the customer invoice(s) to cash receipts. We tested the design, implementation, and operating effectiveness of certain controls over the revenue cycle and the completeness and accuracy of the calculation of trade spend. We performed a retrospective review of management's prior year trade spend accrual, in order to evaluate the historical accuracy of management's estimate, and performed a predictive analytic over the current year trade spend accrual. We tested, on a sample basis, manual journal entries recorded to increase or decrease revenue with characteristics we consider as indicators of a heightened risk of fraud, to determine the appropriateness of the accounting entry with reference to the business rationale, journal entry support and corroborative evidence provided by the Company. Through this dual-purpose test, we also tested the design, implementation, and operating effectiveness of management's control over the recording of manual journal entries by obtaining evidence of appropriate approval, in accordance with management's policies. We considered the accuracy of the Company's description of the accounting policy related to revenue, and whether revenue is adequately disclosed throughout the consolidated financial statements.
Carrying value of goodwill and indefinite life intangible assets	
The Company has goodwill of $15,687 million (including $1,401 million within assets held for sale), and indefinite life intangible assets of $4,598 million as of December 31, 2019 which are required to be tested for impairment at least on an annual basis. The recoverability of these assets is dependent on achieving sufficient level of future net cash flows. The Company applies judgment in allocating these assets to individual cash generating units (CGUs) as well as in assessing the future performance and	We evaluated the accuracy of impairment tests applied to significant amounts of goodwill, the appropriateness of the assumptions used, and the methodology used by the Company to prepare its cash flow forecasts. We also tested the design and implementation of certain controls over these impairment tests. For a sample of CGUs, identified based on quantitative and qualitative factors, we assessed the historical accuracy of the forecasts by comparing the forecasts used in the prior year model to the actual performance in the current year. We compared the forecasts for

Key Audit Matter	How the matter was addressed in our audit
prospects of each CGU and determining the appropriate discount rates. There was no goodwill impairment charge recognized in the year ended December 31, 2019, based on the Company's assessment of the recoverability of each CGU's assets.	future years to the latest plans and forecasts approved by the Company. We challenged the key assumptions used to determine the recoverable amount of these assets, including forecasted cash flows, long term growth rates and the discount rate based on our understanding of the commercial prospects of the assets. In addition, we involved valuation specialists, who developed independent estimates for certain key assumptions, based on observable market data, and performed various sensitivity analyses in order for us to analyze the impact of changes in assumptions from prior periods and assess the consistency of application. We also considered the appropriateness of disclosures in relation to impairment sensitivities and disclosures.
Income taxes	
The Company is regularly subject to tax challenges and audits by tax authorities, in particular the United States Internal Revenue Service, on various matters including intragroup financing, pricing and royalty arrangements, different business models and other transaction-related matters. Where the amount of tax liabilities or assets is uncertain, the Company recognizes management's best estimate of the most likely outcome based on the facts known at the balance sheet date.	We evaluated, and tested the design and implementation of certain controls over management's judgment of tax risks, estimates of tax exposures and contingencies with involvement of our tax specialists. We used third party opinions, past and current experience with the tax authorities in the respective jurisdiction and our tax specialists' own expertise to test the appropriateness of significant assumptions made by the Company to conclude on a best estimate of the most likely outcome of each uncertain tax position. We assessed the Company's analysis in conjunction with the approach elected to account for income tax uncertainties resulting from intragroup financing, pricing and royalty arrangements, different business models and other transaction-related matters. We evaluated the appropriateness of the related presentation and disclosures of income taxes in the consolidated financial statements.

Other Information

Management is responsible for the other information included in the annual report. The other information comprises the information included in the management report, but does not include the consolidated financial statements and our auditors' report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with IFRS; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's consolidated financial reporting process.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with GAAS and ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with GAAS and ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, no such opinion is expressed.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditors' report is David B. Crainer.

KPMG LLP

McLean, Virginia
March 31, 2020

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES

Consolidated Balance Sheet

December 31, 2019 and 2018

(Dollars in thousands, except capital stock par value and shares)

Assets	**Note(s)**		**December 31, 2019**	**December 31, 2018**
Current assets:				
Cash and cash equivalents	11	$	322,711	368,045
Short-term investments			12,552	1,256,010
Trade and other receivables, net	3/11		17,370,403	16,606,655
Inventories, net	4		1,845,297	1,685,947
Derivative assets	5/11		1,223	26,464
Assets held for sale	13		2,112,278	—
Prepayments			43,500	41,131
Total current assets			**21,707,964**	**19,984,252**
Non-current assets:				
Property, plant and equipment, net	6		5,909,005	6,200,920
Employee benefits assets	7		402,647	340,631
Investments in associates	8		25,288	38,824
Deferred tax assets	9		799,328	580,866
Financial assets			1,583,687	1,266,893
Goodwill	10		14,286,338	15,652,386
Intangible assets, net	10		4,598,033	4,598,515
Total non-current assets			**27,604,326**	**28,679,035**
Total assets		**$**	**49,312,290**	**48,663,287**
Liabilities and Equity				
Current liabilities:				
Trade and other payables	11	$	2,724,071	3,101,547
Financial liabilities	11		7,122,540	6,064,089
Provisions	15		288,896	191,980
Derivative liabilities	5/11		308,701	292,990
Current income tax liabilities			682,773	475,423
Liabilities directly associated with assets held for sale			127,050	—
Accruals	14		1,793,583	1,608,194
Total current liabilities			**13,047,614**	**11,734,223**
Non-current liabilities:				
Financial liabilities	11		14,582,326	16,389,379
Employee benefits liabilities	7		1,722,272	1,675,234
Deferred tax liabilities	9		1,285,438	1,223,889
Provisions	15		62,991	79,245
Other accrued liabilities			17,920	6,398
Total non-current liabilities			**17,670,947**	**19,374,145**
Total liabilities			**30,718,561**	**31,108,368**
Equity:				
Capital stock, $100 par value. Authorized, issued, and outstanding, 1,000 shares			100	100
Additional paid-in capital			5,624,297	5,624,297
Other equity reserves			(967,093)	(1,002,750)
Accumulated earnings			13,936,425	12,933,272
Total equity			**18,593,729**	**17,554,919**
Total liabilities and equity		**$**	**49,312,290**	**48,663,287**

See accompanying notes to consolidated financial statements.

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES

Consolidated Income Statement
Years ended December 31, 2019 and 2018
(Dollars in thousands)

	Note		2019	2018
Sales	2	$	23,518,714	22,423,945
Cost of goods sold			(12,871,064)	(12,380,475)
Distribution expenses			(2,169,898)	(2,064,750)
Marketing, general and administrative expenses			(3,626,531)	(3,472,684)
Royalties to affiliated company			(2,481,418)	(2,124,487)
Other trading income	17		117,663	38,477
Other trading expense	17		(638,962)	(263,978)
Trading operating profit			**1,848,504**	**2,156,048**
Other operating income	17		186,271	909,565
Other operating expense	17		(354,094)	(2,586,765)
Operating profit			**1,680,681**	**478,848**
Financial income	16		546,050	441,376
Financial expense	16		(799,746)	(653,775)
Profit before taxes, associates, and joint ventures			**1,426,985**	**266,449**
Income tax expense	18		(413,227)	(669,419)
(Loss) from associates			(13,536)	(3,579)
Profit/(loss) for the year		**$**	**1,000,222**	**(406,549)**

See accompanying notes to consolidated financial statements.

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES

Consolidated Statement of Comprehensive Income

Years ended December 31, 2019 and 2018
(Dollars in thousands)

		2019	2018
Profit/(loss) for the year recognized in the income statement	**$**	**1,000,222**	**(406,549)**
Fair value changes and recycling on debt instruments, net of taxes		—	(40,988)
Fair value changes and recycling on cash flow hedges, net of taxes		(55,133)	29,866
Items that are or may be reclassified subsequently to the income statement		**(55,133)**	**(11,122)**
Remeasurement of defined benefit plans, net of taxes		92,753	76,929
Fair value changes on equity instruments, net of taxes		968	2,348
Items that will never be reclassified to the income statement		**93,721**	**79,277**
Other comprehensive income for the year		**38,588**	**68,155**
Total comprehensive income/(loss) for the year	**$**	**1,038,810**	**(338,394)**

See accompanying notes to consolidated financial statements.

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES
Consolidated Statement of Changes in Equity
Years ended December 31, 2019 and 2018
(Dollars in thousands)

		Capital stock	Additional paid-in capital	Other equity reserves	Accumulated earnings	Total
Equity as at January 1, 2018		**100**	**5,624,297**	**(1,070,905)**	**13,339,821**	**17,893,313**
Loss for the year		—	—	—	(406,549)	(406,549)
Other comprehensive income for the year		—	—	68,155	—	68,155
Total comprehensive income/(loss) for the year		—	—	68,155	(406,549)	(338,394)
Equity as at December 31, 2018	**$**	**100**	**5,624,297**	**(1,002,750)**	**12,933,272**	**17,554,919**
Equity as at January 1, 2019		**100**	**5,624,297**	**(1,002,750)**	**12,933,272**	**17,554,919**
Profit for the year		—	—	—	1,000,222	1,000,222
Other movements		—	—	(2,931)	2,931	—
Other comprehensive income for the year		—	—	38,588	—	38,588
Total comprehensive income for the year		—	—	35,657	1,003,153	1,038,810
Equity as at December 31, 2019	**$**	**100**	**5,624,297**	**(967,093)**	**13,936,425**	**18,593,729**

See accompanying notes to consolidated financial statements.

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES
Consolidated Statement of Cash Flows
Years ended December 31, 2019 and 2018
(Dollars in thousands)

	Note	2019	2018
Cash flows from operating activities:			
Net income/(loss)		$ **1,000,222**	**(406,549)**
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation of property, plant, and equipment	6	674,548	696,282
(Gain) loss on sales of property, plant and equipment		(7,745)	18,682
Impairment of property, plant and equipment	6/17	199,932	69,753
Amortization of intangible assets	10	57,507	70,542
Impairment of goodwill	10/17	—	260,000
Impairment of intangibles	10	23,181	8,288
Loss on disposal of assets held for sale and other	19	4,966	1,368,804
Decrease in cash surrender value of Company-owned life insurance policies		—	5,964
Increase (decrease) in provisions	15	19,598	(19,717)
Deferred tax (benefit) expense	18	(40,721)	(314,221)
Taxes on other comprehensive income		(14,860)	(26,318)
Change in working capital (excluding effects from acquisitions and divestitures):			
Trade and other receivables, net		(659,297)	(185,474)
Inventories, net		(323,936)	(55,224)
Prepayments and other current assets		(35,322)	(963)
Trade and other payables and liabilities		1,305,808	631,254
Decrease in working capital		287,253	389,593
Share from investments in associates		13,536	3,579
Dividends from associates		—	111
Non-monetary movements on financial assets and liabilities		(26,432)	83,474
Movements of trading derivatives		(4,330)	—
Movements of operating derivatives		(79,720)	(62,709)
Other employee benefits, net		179,857	(128,950)
Total adjustments		**1,286,570**	**2,423,157**
Net cash provided by operating activities		**2,286,792**	**2,016,608**
Cash flows from investing activities:			
Capital expenditures		(1,134,723)	(851,043)
Proceeds from sale of property, plant and equipment		42,965	18,678
Acquisition of businesses		(20,205)	(5,551,456)
Proceeds from business divestitures		(53,212)	2,911,199
Expenditure on intangible assets		(80,206)	(174,238)
Investments (net of divestments) in associates and joint ventures	8	—	7,356
Inflows (Outflows) from treasury investments		35,753	(238,936)
Other investing activities		1,243,123	(1,201,409)
Net cash provided (used in) by investing activities		**33,495**	**(5,079,849)**
Cash flows from financing activities:			
Net borrowings of commercial paper		615,943	503,851
Net borrowings (repayment) of line of credit facilities		106,958	(14,957)
Bonds issued		—	8,514,746
Bonds repaid		(1,399,998)	(1,744,803)
Cash movement on derivatives hedging bond principal, net		—	(111,173)
Loans (from)/to affiliates issued, net		(1,016,597)	(1,116,465)
Loans to parent company issued, net		(405,327)	(2,500,915)
Other changes in financial liabilities		(266,600)	(144,901)
Net cash (used in) provided by financing activities		**(2,365,621)**	**3,385,383**
Net (decrease) increase in cash and cash equivalents		**(45,334)**	**322,142**
Cash and cash equivalents at beginning of the year		368,045	45,903
Cash and cash equivalents at end of the year		$ **322,711**	**368,045**
Supplemental information:			
Cash paid for:			
Interest		$ 86,194	181,762
Taxes		262,866	903,362

See accompanying notes to consolidated financial statements.

(1) Accounting Policies

Nestlé Holdings, Inc. ("NHI") (hereinafter, together with its subsidiaries, referred to as the "Company") is a wholly owned subsidiary of NIMCO US, Inc., which is an indirect wholly owned subsidiary of Nestlé S.A., incorporated in Switzerland, which is the holding company of the Nestlé group of companies (hereinafter, referred to as the Nestlé Group). NHI is the holding company for Nestlé S.A.'s principal operating subsidiaries in the United States, other than Nestlé Waters North America Inc., Terrafertil US LLC and Atrium Biotech USA, LLC. NHI was incorporated in the State of Delaware in 1983 under registration number 833330118. NHI is a corporation and has unlimited duration. The address of the registered office of NHI is 1209 Orange Street, Wilmington, Delaware 19801.

The Company engages primarily in the manufacture and sale of food products, pet care products, and beverage products. These businesses derive revenue across the United States.

The consolidated financial statements were authorized for issue by NHI's directors on March 31, 2020.

(a) Significant Accounting Policies

Basis of Preparation

The consolidated financial statements of the Company comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

The consolidated financial statements have been prepared on a historical cost basis, unless stated otherwise. All consolidated companies, and associates have a December 31 accounting year-end.

Accounting policies are included in the relevant notes to the consolidated financial statements. The accounting policies below are applied throughout the consolidated financial statements.

The preparation of the consolidated financial statements requires Company management to exercise judgment and to make estimates and assumptions that affect the application of policies, the reported amounts of revenues, expenses, assets, and liabilities; and disclosures. These estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results could differ from these estimates.

Those areas that involved a higher degree of judgment or uncertainty are explained further in the relevant notes, including classification and measurement of assets held for sale (Note 13), recognition and estimation of revenue (Note 2), identification of lease and lease term (Note 6), identification of cash generating units (CGUs) and estimation of recoverable amount for impairment tests (Note 10), assessment of useful lives of intangible assets as finite or indefinite (Note 10), measurement of employee benefit obligations (Note 7), recognition and measurement of provisions (Note 15) and estimation of current and deferred taxes (Notes 9/18).

Scope of Consolidation

The consolidated financial statements comprise the financial statements of NHI and its subsidiaries. All material intercompany profits, transactions, and balances have been eliminated. The subsidiary companies, which are wholly and directly owned by NHI and incorporated in the United States, are as follows:

Gerber Products Company
Nespresso USA, Inc.
Nestlé Capital Corporation
Nestlé HealthCare Nutrition, Inc.
Nestlé Insurance Holdings, Inc.
Nestlé Purina PetCare Company
Nestlé Regional Globe Office North America, Inc.
Nestlé USA, Inc.
TSC Holdings, Inc.

Newly acquired companies are consolidated from the effective date of control using the acquisition method.

Foreign Currency

For the Company, transactions in currencies other than the Company's functional currency (U.S. dollars) are recorded at the rate of exchange at the transaction date. Monetary assets and liabilities that are denominated in foreign currencies are remeasured at the year end rates. Any resulting exchange differences are taken to the consolidated income statement, except when deferred in other comprehensive income as qualifying cash flow hedges.

Expenses

Cost of goods sold is determined on the basis of the cost of production or of purchase, adjusted for the variation of inventories. All other expenses, including those for advertising and promotions, are recognized when the Company receives the risks and rewards of ownership of the goods or when it receives the services. Government grants that are not related to assets are credited to the consolidated income statement as a reduction of the related expense when they are received, if there is reasonable assurance that the terms of the grant will be met. Additional details of specific expenses are provided in the respective notes.

(b) Changes in Accounting Standards

A number of existing standards have been modified on miscellaneous points with effect from January 1, 2019. Such changes include Prepayment Features with Negative Compensation (Amendments to IFRS 9), Long-term Interests in Associates and Joint Ventures (Amendments to IAS 28), Annual Improvements to IFRSs 2015-2017 Cycle (Amendments to IFRS 3, IFRS 11, IAS 12, and IAS 23), and Plan Amendment, Curtailment or Settlement (Amendments to IAS 19).

None of these other amendments had a material effect on the Company's Financial Statements.

(Continued)

The Company early adopted IFRS 16- Leases and IFRIC 23- Uncertainty over Income Tax Treatments on January 1, 2018 with the impacts already disclosed in the 2018 Consolidated Financial Statements.

Changes in IFRS that may affect the Company after December 31, 2019

There are no standards that are not yet effective and that would be expected to have a material impact on the Company in the current or future reporting periods.

(2) Analyses by Segment

Segment Reporting

Operating segments reflect the Company's management structure and the way financial information is regularly reviewed by the chief operating decision maker (CODM). The CODM has been defined as a body comprising the members of the Nestlé Group Executive Board to whom the various operating segments report, since this is the level at which resources are allocated and results are assessed.

- The Company's management structure is aligned with the Nestlé Group management structure and is organized around products.
- The Nestlé USA Brands segment forms part of the Nestlé Group Zone Americas segment. It consists primarily of beverages, snacks, frozen prepared foods, pizza, ice cream, and other food products.
- The PetCare segment also forms part of the Nestlé Group Zone Americas segment and sells products for domestic pets.
- The Nutrition segment is part of the Nestlé Group Zone Americas segment and consists primarily of infant and baby food products.
- The Other businesses segment category comprises other operating segments that do not meet the criteria for separate reporting, such as Nestlé Professional (forming part of the Nestlé Professional Regionally Managed Business (RMB) within Zone Americas), which sells products for the food services industry, Nestlé Health Science which provides pioneering science-based nutritional solutions to deliver improved personalized health care for people with medical conditions, and the Nespresso business unit. Nespresso, Nestlé Health Science, and Gerber Life Insurance (in 2018) form part of the Nestlé Group Other businesses segment.

Segment results (Trading operating profit) represent the contribution of the different segments to central overheads and the trading operating profit of the Company. Specific corporate expenses are allocated to the corresponding segments. In addition to the Trading operating profit, Underlying Trading operating profit is shown on a voluntary basis because it is one of the key metrics used by the Company to monitor the Company on segment performance.

Depreciation and amortization include depreciation of property, plant and equipment (including right of use assets under leases) and amortization of intangible assets.

No segment assets and liabilities are regularly provided to the CODM to assess segment performance or to allocate resources and therefore segment assets and liabilities are not disclosed. However, the Company discloses the invested capital, goodwill and intangible assets by segment on a voluntary basis.

Invested capital comprises property, plant and equipment, trade receivables and some other receivables, assets held for sale, inventories, prepayments and accrued income as well as specific financial assets associated to the segments, less trade payables and some other payables, liabilities directly associated with assets held for sale, non-current other payables as well as accruals and deferred income.

Goodwill and intangible assets are not included in invested capital since the amounts recognized are not comparable between segments due to differences in the intensity of acquisition activity and changes in accounting standards, which were applicable at various points in time when the Company undertook significant acquisitions. Nevertheless, an allocation of goodwill and intangible assets by segment and the related impairment expenses are provided.

Invested capital and goodwill and intangible assets by segment represent the position at the end of the year.

Capital additions represent the total cost incurred to acquire property, plant and equipment (including right of use assets under leases), intangible assets and goodwill, including those arising from business combinations.

Unallocated items represent items whose allocation to a segment would be arbitrary. They comprise mainly corporate expenses and related assets.

Revenue

Sales represent amounts received and receivables from third parties for goods supplied to the customers and for services rendered. Sales are recognized when control of the goods has transferred to the customer, which is mainly upon arrival at the customer.

Revenue is measured as the amount of consideration which the Company expects to receive, based on the list price applicable to a given distribution channel after deduction of returns, sales taxes, pricing allowances, other trade discounts and couponing and price promotions to consumers. The level of discounts, allowances and promotional rebates is recognized as a deduction from revenue at the time that the related sales are recognized or when the rebate is offered to the customer (or consumer if applicable). They are estimated using judgments based on historical experience and the specific terms of the agreements with the customers. Payments made to customers for commercial services received are expensed. The Company has a range of credit terms that are typically short term, in line with market practice and without any financing component. Sales returns are generally not allowed, except in limited cases mainly in the Infant Nutrition business. Historical experience is used to estimate such returns at the time of sale. No asset is recognized for products to be recoverable from these returns, as they are not anticipated to be resold.

Trade assets (mainly coffee machines and freezers) may be sold or leased separately to customers. Arrangements where the Company transfers substantially all the risks and rewards incidental to ownership to the customer are treated as finance lease arrangements. Operating lease revenue for trade asset rentals is recognized on a straight-line basis over the lease term.

(Dollars in thousands)

Revenue and Results

2019	Brands [a]	PetCare	Nutrition [a]	Other [a]	Total
Sales	$ 11,255,438	8,354,259	1,044,747	2,864,270	23,518,714
Underlying Trading operating profit [b]	1,288,665	821,067	46,848	213,222	2,369,803
Trading operating profit [c]	799,147	835,489	29,625	180,864	1,845,124
Net other trading (expenses)/income [d]	(479,043)	7,325	(17,223)	(32,358)	(521,299)
Of which impairment of property, plant and equipment	*(187,337)*	*(8,478)*	*(5,222)*	*(22,076)*	*(223,113)*
Of which restructuring costs	*(145,679)*	*(364)*	*(4,856)*	*2,528*	*(148,371)*
Depreciation and amortization	(296,885)	(253,965)	(66,283)	(114,922)	(732,055)

2018	Brands [a]	PetCare	Nutrition [a]	Other [a]	Total
Sales	$ 9,948,534	7,849,879	1,072,792	3,552,740	22,423,945
Underlying Trading operating profit [b]	995,911	964,165	29,230	393,438	2,382,744
Trading operating profit/(loss) [c]	955,702	885,692	(40,325)	359,784	2,160,853
Net other trading expenses [d]	(40,232)	(78,238)	(69,555)	(33,866)	(221,891)
Of which impairment of property, plant and equipment	*(13,160)*	*(414)*	*(50,951)*	*(9,721)*	*(74,246)*
Of which restructuring costs	*(31,523)*	*(53,972)*	*(10,510)*	*(21,220)*	*(117,225)*
Depreciation and amortization	(319,572)	(247,058)	(60,690)	(139,504)	(766,824)

[a] Nestlé USA Brands primarily consists of beverage (including Nestlé Coffee Partners), beverage, prepared foods, ice cream, snacks, and other food products. Nutrition primarily consists of infant and baby food products. Other primarily consists of Nestlé Professional, Nespresso, and Nestlé Health Science, and in 2018 Gerber Life Insurance, which do not meet the criteria for separate disclosure. Inter-segment sales are not significant.

[b] Trading operating profit before Net other trading (expenses)/income.

[c] The Company determines Trading operating profit by allocating corporate expenses to its operating segments based on activity-based- cost drivers.

[d] Included in Trading operating profit.

(Dollars in thousands)

Invested Capital and Other Information

2019	**Brands** [(a)]	**PetCare**	**Nutrition** [(a)]	**Other** [(a)]	**Total**
Invested capital	$ 3,717,833	2,871,089	469,954	590,701	7,649,577
Goodwill and intangible assets	8,881,047	8,741,982	773,604	487,738	18,884,371
Impairment of goodwill	-	-	-	-	-
Capital additions	537,877	556,240	67,102	88,243	1,249,462

2018	**Brands** [(a)]	**PetCare**	**Nutrition** [(a)]	**Other** [(a)]	**Total**
Invested capital	$ 1,831,255	2,154,607	539,050	728,711	5,253,623
Goodwill and intangible assets	10,217,322	8,742,579	784,685	506,315	20,250,901
Impairment of goodwill	-	-	*(260,000)*	-	(260,000)
Capital additions	5,778,987	465,339	52,092	277,501	6,573,919

[(a)] Nestlé USA Brands primarily consists of beverage (including Nestlé Coffee Partners) beverage, prepared foods, ice cream, snacks, and other food products. Nutrition primarily consists of infant and baby food products. Other primarily consists of Nestlé Professional, Nespresso, and Nestlé Health Science, and in 2018 Gerber Life Insurance, which do not meet the criteria for separate disclosure.

Reconciliation of total segment Underlying Trading operating profit to profit before taxes:

	2019	**2018**
Trading operating profit	$ 1,845,124	2,160,853
Unallocated items	3,380	(4,805)
Total trading operating profit	**1,848,504**	**2,156,048**
Net other operating expenses	(167,823)	(1,677,200)
Operating profit	**1,680,681**	**478,848**
Net financial expenses	(253,696)	(212,399)
Profit before taxes, associates and joint ventures	**$ 1,426,985**	**266,449**

(Dollars in thousands)

Reconciliation from invested capital to total assets:

		2019	2018
Invested capital	$	7,649,577	5,253,623
Liabilities included in invested capital		4,658,973	4,807,237
Subtotal		**12,308,550**	**10,060,860**
Intangible assets and goodwill		18,884,371	20,250,901
Other assets		18,119,369	18,351,526
Total assets	**$**	**49,312,290**	**48,663,287**

Customers

The Company has one customer, with sales in all segments of the business, amounting to 17% and 25% of the Company’s sales for the years ended December 31, 2019 and 2018, respectively.

(3) Trade and Other Receivables, net

Recognition and measurement

Trade and other receivables are recognized initially at their transaction price and subsequently measured at amortized cost.

Expected credit losses

The Company applies the IFRS 9 simplified approach to measuring expected credit losses (ECLs) for trade receivables at an amount equal to lifetime ECLs. The ECLs on trade receivables are calculated based on actual credit loss experience over the preceding three to five years on the total balance of non-credit impaired trade receivables. The Company's credit loss experience has shown that the aging of receivable balances is primarily due to negotiations about variable consideration.

The Company considers a trade receivable to be credit impaired when one or more detrimental events have occurred such as:

- significant financial difficulty of the customer; or

- it is becoming probable that the customer will enter bankruptcy or other financial reorganization.

Impairment losses related to trade and other receivables are not presented separately in the consolidated income statement but are reported under the heading Marketing, general, and administration expenses.

(Dollars in thousands)

	2019			2018		
	Gross carrying amount	Expected credit loss allowance	Total	Gross carrying amount	Expected credit loss allowance	Total
Trade and other receivables (not credit impaired)	$ 17,374,438	(4,297)	17,370,141	16,610,138	(4,085)	16,606,053
Credit impaired trade and other receivables	528	(266)	262	820	(218)	602
	$ 17,374,966	**(4,563)**	**17,370,403**	**16,610,958**	**(4,303)**	**16,606,655**

The Company's three largest trade customers represent 34% (2018: 32%) of trade and other receivables, excluding amounts due from Nestlé S.A. controlled companies and associated companies.

Based on the historic trends and the expected performance of the customers, the Company believes that the above expected credit loss allowance sufficiently covers for the risk of default.

	2019	2018
By type:		
Trade, less allowances of $4,563 and $4,303, respectively	$ 1,805,366	1,751,737
Due from Nestlé S.A. controlled companies [1]	15,456,294	14,773,639
Due from associated companies	910	3,241
Other	107,833	78,038
Trade and other receivables, net	**$ 17,370,403**	**16,606,655**

[1] Management expects to realize these assets within twelve months after the reporting period.

(4) Inventories, net

Raw materials are valued at the lower of purchase cost calculated using the FIFO (first-in, first-out) method and net realizable value. Work in progress, sundry supplies and finished goods are valued at the lower of their weighted average cost and net realizable value. The cost of inventories includes the gains/losses on cash flow hedges for the purchase of raw materials and finished goods.

	2019	2018
Raw materials and work in progress	$ 593,299	530,233
Finished goods	1,286,494	1,186,320
Allowance for write-down to net realizable value	(34,496)	(30,606)
Inventories, net	**$ 1,845,297**	**1,685,947**

(5) Derivative Assets and Liabilities and Hedge Accounting

Derivative Financial Instruments

The Company's derivatives mainly consist of currency forwards and swaps; commodity futures and options, and interest rate forwards and swaps. Derivatives are mainly used to manage exposures to foreign exchange, interest rate, and commodity price risk as described in the Market Risk section in Financial Risks (Note 12).

Derivatives are initially recognized at fair value. They are subsequently remeasured at fair value on a regular basis and at each reporting date at a minimum, with all their gains and losses, realized and unrealized, recognized in the consolidated income statement unless they are in a qualifying hedging relationship.

Hedge Accounting

The Company designates and documents the use of certain derivatives and other financial assets or financial liabilities as hedging instruments against changes in fair values of recognized assets and liabilities (fair value hedges) and highly probable forecast transactions (cash flow hedges). The effectiveness of such hedges is assessed at inception and verified at regular intervals and at least on a quarterly basis to ensure that an economic relationship exists between the hedged item and hedging instrument.

The Company excludes from the designation of the hedging relationship the hedging cost element. Subsequently, this cost element impacts the consolidated income statement at the same time as the underlying hedged item.

For the designation of hedging relationships on commodities, the Company applies the component hedging model when the hedged item is separately identifiable and measurable in the contract to purchase the materials.

Fair Value Hedges

The Company uses fair value hedges to mitigate foreign currency and interest rate risks of its recognized assets and liabilities, being mostly financial debt.

Changes in fair values of hedging instruments designated as fair value hedges and the adjustments for the risks being hedged in the carrying amounts of the underlying transactions are recognized in the consolidated income statement.

Cash Flow Hedges

The Company uses cash flow hedges to mitigate a particular risk associated with a recognized asset or liability or highly probable forecast transactions, such as purchases of raw materials, finished goods and equipment, as well as the variability of expected interest payments and receipts.

The effective part of the changes in fair value of hedging instruments is recognized in other comprehensive income or loss, while any ineffective part is recognized immediately in the consolidated income statement. Ineffectiveness for hedges of foreign currency and commodity price risk may result from changes in the timing of the forecast transactions than was originally foreseen. When the hedged item results in the recognition of a non-financial asset or liability, the gains or losses previously recognized in other comprehensive income are included in the measurement of the cost of the asset or the liability. Otherwise, the gains or losses previously recognized in other comprehensive income are recognized in the consolidated income statement at the same time as the hedge transaction.

(Dollars in thousands)

Undesignated Derivatives

Derivatives which are not designated in a hedging relationship are classified as undesignated derivatives. They are acquired in the frame of approved risk management policies.

Derivatives by Hedged Risks

		2019		
		Fair value assets	**Fair value liabilities**	**Contractual or notional amounts**
Fair value hedges:				
Foreign currency and interest rate risk on net financial debt	$	—	138,262	542,649
Cash flow hedges:				
Currency risk on future purchases or sales		507	16	1,446,393
Foreign currency and interest rate risk on net financial debt		—	162,883	3,756,739
Commodity price risk on future purchases		197	7,542	184,070
Undesignated derivatives		519	(2)	
Total derivatives		**1,223**	**308,701**	**5,929,851**
Conditional offsets (*)				
Derivative assets and liabilities		(15)	(15)	
Balance after conditional offsets	**$**	**1,208**	**308,686**	

(*) Represent amounts that would be offset in case of default, insolvency or bankruptcy of counterparties.

(Dollars in thousands)

		2018		
		Fair value assets	**Fair value liabilities**	**Contractual or notional amounts**
Fair value hedges:				
Foreign currency and interest rate risk on net financial debt	$	—	134,831	542,648
Cash flow hedges:				
Currency risk on future purchases or sales		633	2,357	82,114
Foreign currency and interest rate risk on net financial debt		16,764	133,635	4,228,399
Commodity price risk on future purchases		9,067	21,661	483,681
Undesignated derivatives		—	506	
Total derivatives		**26,464**	**292,990**	**5,336,842**
Conditional offsets (*)				
Derivative assets and liabilities		(5,163)	(5,163)	
Balance after conditional offsets	**$**	**21,301**	**287,827**	

(*) Represent amounts that would be offset in case of default, insolvency or bankruptcy of counterparties.

Impact on the consolidated income statement for fair value hedges:

		2019	2018
Hedged items	$	5,789	47,208
Hedging instruments		(4,373)	(45,898)
Net gain/(loss)	**$**	**1,416**	**1,310**

The ineffective portion of gains/(losses) of cash flow hedges recorded during the years ended December 31, 2019 and 2018 in net financial expenses in the consolidated income statement was $82 and $1,929, respectively.

(Dollars in thousands)

(6) Property, Plant and Equipment, net

Property, plant and equipment comprises owned and leased assets.

		2019	2018
Property, plant and equipment - owned	$	5,316,045	5,452,320
Right-of-use assets - leased		592,960	748,600
		5,909,005	6,200,920

Owned Assets

Owned property, plant and equipment are shown in the consolidated balance sheet at their historical cost.

Depreciation is assessed on components that have homogenous useful lives by using the straight-line method so as to depreciate the initial cost down to the residual value over the estimated useful lives. The residual values are up to 30% on corporate offices and nil for all other asset types.

The useful lives are as follows:

Buildings and land improvements	15 – 40 years
Plant and machinery	10 – 25 years
Tools, furniture, and sundry	5 years
Vehicles	5 – 10 years
Information technology equipment	3 years

Useful lives, components, and residual amounts are reviewed annually. Such a review takes into consideration the nature of the assets, their intended use including but not limited to the closure of facilities and the evolution of the technology and competitive pressures that may lead to their obsolescence.

Depreciation of property, plant and equipment is allocated to the appropriate headings of expenses by function in the consolidated income statement.

Borrowing costs incurred during the course of construction are capitalized if the assets under construction are significant and if their construction requires a substantial period to complete (typically more than one year). The capitalization rate is determined on the basis of the short-term borrowing rate for the period of construction. Government grants are recognized as deferred income, which is released to the consolidated income statement over the useful life of the related assets.

(Dollars in thousands)

	Land and buildings	Plant and machinery	Tools, furniture, and sundry	Vehicles	Information technology equipment	Total
Net carrying amount						
At January 1, 2019	$ **2,638,573**	**2,432,134**	**247,269**	**17,593**	**116,751**	**5,452,320**
Capital expenditure [a]	516,501	324,728	57,511	15,494	41,809	956,043
Acquisitions through business combinations	—	—	—	—	—	—
Depreciation	(89,225)	(311,253)	(76,471)	(23,356)	(48,973)	(549,278)
Impairment of assets (note 17)	(47,911)	(8,074)	(4,116)	—	(518)	(60,619)
Disposals	(247,730)	173,716	34,423	(5,598)	9,584	(35,605)
Classification (to)/from held for sale and disposals of businesses	(110,744)	(279,959)	(53,757)	4,666	(7,022)	(446,816)
At December 31, 2019	**2,659,464**	**2,331,292**	**204,859**	**8,799**	**111,631**	**5,316,045**
Gross value	3,807,484	5,857,392	749,718	78,283	341,863	10,834,740
Accumulated depreciation and impairments	(1,148,020)	(3,526,100)	(544,859)	(69,484)	(230,232)	(5,518,695)
Net carrying amount						
At January 1, 2018	$ **2,436,521**	**2,453,682**	**233,744**	**33,875**	**135,688**	**5,293,510**
Capital expenditure [a]	446,689	282,930	74,808	10,324	36,292	851,043
Acquisitions through business combinations	—	—	3,742	—	(3,610)	132
Depreciation	(107,937)	(319,862)	(72,239)	(13,482)	(50,121)	(563,641)
Impairment of assets (note 17)	—	(55,104)	(6,437)	(6,800)	(105)	(68,446)
Disposals	(140,692)	70,653	12,771	(8,412)	(1,393)	(67,073)
Classification (to)/from held for sale and disposals of businesses	3,991	(164)	880	2,088	—	6,795
At December 31, 2018	**2,638,572**	**2,432,135**	**247,269**	**17,593**	**116,751**	**5,452,320**
Gross value	3,908,302	6,155,356	893,592	170,024	415,389	11,542,663
Accumulated depreciation and impairments	(1,269,730)	(3,723,221)	(646,323)	(152,431)	(298,638)	(6,090,343)

[a] Including borrowing costs.

At December 31, 2019 and 2018, property, plant and equipment included $568,646 and $252,039, respectively, of assets under construction. There were $203,899 and $179,048 in commitments for future capital expenditures as of December 31, 2019 and 2018, respectively.

Impairment of Property, Plant and Equipment

Reviews of the carrying amounts of the Company's property, plant and equipment are performed when there is an indication of impairment. An indicator could be unfavorable development of a business under competitive pressures or severe economic slowdown as well as reorganization of the operations to leverage their scale.

In assessing value in use, the estimated future cash flows are discounted to their present value, based on the time value of money and any risks specific to the asset’s location. The risks specific to the asset are included in the determination of the cash flows.

Impairment of property, plant and equipment arises mainly from plans to optimize industrial manufacturing capacities by closing or selling production facilities as well as underperforming businesses.

Leases – Company as a lessee

The Company assesses whether a contract is or contains a lease at inception of the contract. This assessment involves the exercise of judgment about whether it depends on a specified asset, whether the Company obtains substantially all the economic benefits from the use of that asset, and whether the Company has the right to direct the use of the asset.

The Company recognizes a right-of-use (ROU) asset and a lease liability at the lease commencement date, except for short-term leases of 12 months or less which are expensed in the consolidated income statement on a straight-line basis over the lease term.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease. If this rate cannot be readily determined, the Company uses an incremental borrowing rate specific to the country, term and currency of the contract. Lease payments can include fixed payments; variable payments that depend on an index or rate known at the commencement date; and extension option payments or purchase options, if the Company is reasonably certain to exercise. The lease liability is subsequently measured at amortized cost using the effective interest rate method and remeasured (with a corresponding adjustment to the related ROU asset) when there is a change in future lease payments in case of renegotation, changes of an index or rate in case of reassessment of options.

At inception, the ROU asset comprises the initial lease liability, initial direct costs and the obligations to refurbish the asset, less any incentives granted by the lessors. The ROU asset is depreciated over the shorter of the lease term or the useful life of the underlying asset. The ROU asset is subject to testing for impairment if there is an indicator for impairment, as for owned assets.

ROU assets are included in the heading Property, plant and equipment, and the lease liability is included in the headings current and non-current Financial liabilities.

Description of lease activities

Real estate leases

The Company leases land and buildings for its office and warehouse space and retail stores. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. Leases are typically made for a fixed period of 5-15 years and may include extension options which provide operational flexibility. If the Company exercised all extension options not currently included in the lease liability, the additional payment would amount to $389,158 at December 31, 2019.

Vehicles leases

The Company leases trucks for distribution in specific businesses and cars for management and sales functions. The average contract duration is six years for trucks and three years for cars.

(Dollars in thousands)

Other leases

The Company also leases machinery and equipment and tools, furniture and other equipment that combined are insignificant to the total leased asset portfolio.

Right-of-use assets

	Land and Buildings	Vehicles	Other	Total
Net Carrying Amount				
At January 1, 2019	$ 558,467	152,488	37,645	**748,600**
Additions	89,486	76,628	14,971	**181,085**
Depreciation	(82,231)	(25,665)	(18,089)	**(125,985)**
Impairments	(36,490)	(102,243)	(580)	**(139,313)**
Classification to/from held for sale and change of scope of consolidation, net	(13,964)	(57,204)	(259)	**(71,427)**
December 31, 2019	**515,268**	**44,004**	**33,688**	**592,960**

Additions to right-of-use assets during 2018 were $292,541 and depreciation for 2018 was as follows, Land Buildings: $73,736; Vehicles: $39,957; and Other: $18,948.

Other lease disclosures

A maturity analysis of lease liabilities is shown in Note 12.

The Company incurred interest expense on lease liabilities of $13,337 (2018: $13,552). The expense relating to short-term leases and variable leases payments not included in the measurement of lease liabilities is not significant. The total cash outflow for leases amounted to $181,085 (2018: $205,143).

There are no significant lease commitments for leases not commenced at year-end.

(7) Employee Benefits

Employee Remuneration

The Company's salaries of $2,737 million (2018: $2,689 million) and welfare expenses of $833 million (2018: $865 million) represent a total of $3,570 million (2018: $3,554 million). In addition, certain Company employees are eligible to long-term incentives in the form of equity compensation plans, for which the cost amounts to $144 million (2018: $65 million). Employee remuneration is allocated to the appropriate headings of expenses by function.

Post-employment Benefits

The liabilities of the Company arising from defined benefit obligations, and the related current service cost, are determined using the projected unit credit method. The Company's external actuaries perform valuations on an annual basis. Such plans are either externally funded, with the plan assets held separately from those of the Company in independently administered funds, or unfunded. The deficit or excess of the fair value of plan assets over the present value of the defined benefit obligation is recognized as a liability or an asset on the consolidated balance sheet.

Pension cost charged to the income statement consists of service cost (current and past service cost, gains and losses arising from settlement) and administration costs (other than costs of managing plan assets), which are allocated to the appropriate heading by function, and net interest expense or income, which is presented as part of net financial income/(expense). The actual return less interest income on plan assets, changes in actuarial assumptions, and differences between actuarial assumptions and what has actually occurred are reported in other comprehensive income.

The Company also provides for benefits under defined contribution plans. Contributions to these plans are charged to the consolidated income statement as incurred.

Pensions and Retirement Benefits

In the United States, Nestlé's primary pension plan is a pension equity design, under which members earn pension credits each year based on a schedule related to the sum of their age and service with Nestlé. A member's benefit is the sum of the annual pension credits earned multiplied by an average earning, payable as a lump sum. However, in lieu of the lump sum, members have the option of converting the benefit to a monthly pension annuity. The plan does not provide for automatic pension increases and members do not contribute to the plan. This plan was closed to new entrants at the end of 2015 and replaced by a defined contribution scheme. The pension plan is sufficiently funded on a local statutory basis such that no contributions were required in 2019.

Post-employment Medical Benefits and Other Employee Benefits

The Company maintains medical benefit plans, classified as defined benefit plans under IAS 19, which cover eligible retired employees. The Company's obligations for other employee benefits consist mainly of post-service healthcare benefits, which do not have the characteristics of pensions.

Risks related to Defined Benefit Plans

The main risks to which the Company is exposed in relation to operating defined benefit plans are:

- mortality risk: the assumptions adopted by the Company make allowance for future improvements in life expectancy. However, if life expectancy improves at a faster rate than assumed, this would result in greater payments from the plans and consequently increases in the plans' liabilities. In order to minimize this risk, mortality assumptions are reviewed on a regular basis.
- market and liquidity risks: these are the risks that the investments do not meet the expected returns over the medium to long term. This also encompasses the mismatch between assets and liabilities. In order to minimize these risks, the structure of the portfolios is reviewed and asset-liability matching analyses are performed on a regular basis.

As certain of the Company's pension arrangements permit benefits to be adjusted in the case that downside risks emerge, the Company does not always have full exposure to the risks described above.

(Dollars in thousands)

Plan amendments and restructuring events

During the year, there were individually non-significant plan amendments and restructuring events which have been recognized as past service cost. The related past service costs ($8,388) (2019) and ($1,223) (2018) have been recognized in the income statement primarily under Net other operating expenses.

Asset-liability Management and Funding Arrangement

The Company's investment committee is responsible for determining the mix of asset classes and target allocations of the Company's plans with the support of investment advisors. Periodic reviews of the asset mix are made by mandating external consultants to perform asset-liability matching analyses. Such analyses aim at comparing dynamically the fair value of assets and the liabilities in order to determine the most adequate strategic asset allocation.

The overall investment policy and strategy for the Company's funded defined benefit plans is guided by the objective of achieving an investment return which, together with the contributions paid, is sufficient to maintain reasonable control over the various funding risks of the plans. As those risks evolve with the development of capital markets and asset management activities, the Company addresses the assessment and control process of the major pension investment risks. In order to protect the Company's defined benefit plans funding ratio and to mitigate the financial risks, protective measures on the investment strategies are in force.

Reconciliation of assets and liabilities recognized in the consolidated balance sheet is as follows:

	2019			2018		
	Defined benefit retirement plans	**Post-employment medical benefits**	**Total**	**Defined benefit retirement plans**	**Post-employment medical benefits**	**Total**
Present value of funded obligations	$ 4,058,259	—	4,058,259	3,722,182	—	3,722,182
Fair value of plan assets	(4,460,906)	—	(4,460,906)	(4,062,813)	—	(4,062,813)
Excess of assets over funded obligations	(402,647)	—	(402,647)	(340,631)	—	(340,631)
Present value of unfunded obligations	445,411	576,965	1,022,376	450,388	551,900	1,002,288
Net Defined Benefit Liabilities	$ **42,764**	**576,965**	**619,729**	**109,757**	**551,900**	**661,657**
Liabilities from cash-settled share-based transactions			$ 121,857			$ 115,195
Liabilities from non-current deferred compensation and other			578,039			557,751
Net Liabilities			**$ 1,319,625**			**$ 1,334,603**
Reflected in the consolidated balance sheet as follows:						
Employee benefit assets			$ (402,647)			$ (340,631)
Employee benefit liabilities			1,722,272			1,675,234
Net Liabilities			**$ 1,319,625**			**$ 1,334,603**

(Dollars in thousands)

The movement in the present value of defined benefit obligations is reflected as follows:

	2019			2018		
	Defined benefit retirement plans	**Post-employment medical benefits**	**Total**	**Defined benefit retirement plans**	**Post-employment medical benefits**	**Total**
At January 1	$ 4,172,570	551,900	4,724,470	4,684,953	610,967	5,295,920
of which funded defined benefit plans	*3,722,182*	—	*3,722,182*	*4,196,745*	—	*4,196,745*
of which unfunded defined benefit plans	*450,388*	*551,900*	*1,002,288*	*488,208*	*610,967*	*1,099,175*
Service cost	136,485	12,482	148,967	180,413	13,188	193,601
of which current service cost	*144,873*	*12,482*	*157,355*	*178,643*	*16,181*	*194,824*
of which past service cost	*(8,388)*	—	*(8,388)*	*1,770*	*(2,993)*	*(1,223)*
Interest expense	169,635	21,943	191,578	157,095	20,498	177,593
Actuarial (gains)/losses	462,579	26,032	488,611	(358,058)	(62,625)	(420,683)
Benefits paid on funded defined benefit plans	(379,829)	—	(379,829)	(441,967)	—	(441,967)
Benefits paid on unfunded defined benefit plans	(57,770)	(35,392)	(93,162)	(49,866)	(30,128)	(79,994)
At December 31	**$ 4,503,670**	**576,965**	**5,080,635**	**4,172,570**	**551,900**	**4,724,470**
of which funded defined benefit plans	*$ 4,058,259*	—	*4,058,259*	*3,722,182*	—	*3,722,182*
of which unfunded defined benefit plans	*445,411*	*576,965*	*1,022,376*	*450,388*	*551,900*	*1,002,288*

The movement in the fair value of defined benefit assets is reflected as follows:

	2019	2018
	Defined benefit retirement plans	**Defined benefit retirement plans**
At January 1	$ 4,062,813	4,435,319
Interest income	165,227	154,019
Actual return on plan assets, excluding interest income	612,695	(317,905)
Employer contributions	57,770	283,213
Benefits paid on funded defined benefit plans	(437,599)	(491,833)
At December 31	**$ 4,460,906**	**4,062,813**

(Dollars in thousands)

The major categories of plan assets as a percentage of total plan assets are as follows:

	2019	2018
December 31:		
Equities	23.99%	15.90%
Debts	63.30	64.69
of which government debts	*32.97*	*33.52*
of which corporate debts	*30.33*	*31.17*
Alternative investments	12.71	19.41
Total	100.00%	100.00%

Equities and government debts represent 57% and 49% of the plan assets in 2019 and 2018, respectively. Almost all of them are quoted in an active market. Corporate debts, real estate, hedge funds and private equities represent 43% and 51% of the plan assets in 2019 and 2018, respectively. Almost all of them are not quoted in an active market.

Expenses recognized in the consolidated income statement are as follows:

	2019			2018		
	Defined benefit retirement plans	Post-employment medical benefits and other benefits	Total	Defined benefit retirement plans	Post-employment medical benefits and other benefits	Total
Service cost	$ 130,560	12,011	142,571	173,697	12,843	186,540
Net Interest expense	6,729	21,245	27,974	5,115	19,859	24,974
Administration expenses	10,945	—	10,945	10,348	—	10,348
Defined benefit expenses	**148,234**	**33,256**	**181,490**	**189,160**	**32,702**	**221,862**
Defined contribution expenses			93,721			93,122
Total expenses			**275,211**			**314,984**

The expenses for defined benefit and defined contribution plans are allocated to the appropriate headings of expenses by function.

Remeasurement of defined benefit plans recognized in the consolidated statement of comprehensive income is reflected as follows:

(Dollars in thousands)

	2019			2018		
	Defined benefit retirement plans	**Post-employment medical benefits**	**Total**	**Defined benefit retirement plans**	**Post-employment medical benefits**	**Total**
Actual return on plan assets, excluding interest income	$ 612,695	—	612,695	(317,905)	—	(317,905)
Experience adjustments on plan liabilities	(14,803)	31,434	16,631	(41,334)	8,117	(33,217)
Change in demographic assumptions on plan liabilities	65,909	6,762	72,671	—	14,576	14,576
Change in financial assumptions on plan liabilities	(513,685)	(64,228)	(577,913)	399,663	39,932	439,595
Remeasurement of defined benefit plans	**$ 150,116**	**(26,032)**	**124,084**	**40,424**	**62,625**	**103,049**

	2019	**2018**
Principal financial actuarial assumptions:		
Discount rates	3.25%	4.25%
Expected rates of salary increases	3.00%	3.00%
Medical cost trend rates	5.0% – 6.5%	5.0% – 6.75%

Life expectancy as reflected in the following table is based upon the PRI-2012 mortality table for 2019 and the RP-2014 mortality for 2018.

	Life expectancy at age 65 for a male member currently aged 65 (in years)		Life expectancy at age 65 for a female member currently aged 65 (in years)	
Mortality table	**2019**	**2018**	**2019**	**2018**
PRI-2012 (2019)/ RP-2014 (2018)	20.7	20.9	22.7	23.0

(Dollars in thousands)

Sensitivity Analyses on Present Value of Defined Benefit Obligations

The table below presents the present value of the defined benefit obligations when major assumptions are changed.

		2019	2018
As reported	$	5,080,635	4,724,470
Discount rates			
Increase of 50 basis points		4,791,848	4,470,683
Decrease of 50 basis points		5,395,639	4,997,889
Expected rates of salary increases			
Increase of 50 basis points		5,120,444	4,761,609
Decrease of 50 basis points		5,041,336	4,687,825
Medical cost trend rates			
Increase of 50 basis points		5,086,021	4,724,681
Decrease of 50 basis points		5,075,123	4,712,101
Mortality assumption			
Setting forward the tables by 1 year		4,972,147	4,633,624
Setting back the tables by 1 year		5,177,544	4,802,214

All sensitivities are calculated using the same actuarial method as for the disclosed present value of the defined benefit obligations at year-end.

Weighted average duration of Defined Benefit Obligations

At December 31, 2019, the weighted-average duration of the defined benefit obligation was 12.3 years.

(8) Investments in Associated Companies

Associates are companies where the Company has the power to exercise a significant influence but does not exercise control. Significant influence may be obtained when the Company has 20% or more of the voting rights in the investee or has obtained a seat on the board of directors or otherwise participates in the policy making process of the investee.

Associates are accounted for using the equity method. The net assets and results are adjusted to comply with the Company’s accounting policies. The carrying amount of goodwill arising from the acquisition of associates is included in the carrying amount of investments in associates.

(Dollars in thousands)

The Company has the following investments in associated companies:

	Ownership interest		Net book value	
	2019	2018	2019	2018
Freshly, Inc.	20%	20%	$ 25,288	33,950
Williams Inland Distributors, LLC	—	45%	$ —	4,874
Total investments in joint ventures and associated companies			**$ 25,288**	**38,824**

The Williams Inland Distributors, LLC. partnership was dissolved as of October 17th, 2019.

(9) Deferred Taxes

Deferred taxation is the tax attributable to the temporary differences that arise when taxation authorities recognize and measure assets and liabilities with rules that differ from the principles of the consolidated financial statements. It also arises from temporary differences stemming from tax losses carried forward.

Deferred taxes are calculated under the liability method at the rates of tax expected to prevail when the temporary differences reverse, subject to such rates being substantially enacted at the reporting date. Any changes of tax rates are recognized in the consolidated income statement unless related to items directly recognized in other comprehensive income. Deferred tax liabilities are recognized on all taxable temporary differences excluding non-deductible goodwill. Deferred tax assets are recognized on all deductible temporary differences provided that it is probable that future taxable income will be available.

Deferred tax assets by types of temporary differences are as follows:

	2019	2018
Employee benefits	$ 403,889	376,626
Inventories, receivables, payables, accruals, and provisions	181,064	199,113
Financial instruments	11,398	—
Net operating losses	11,582	4,029
Others	191,395	1,098
Total deferred tax assets	**$ 799,328**	**580,866**

(Dollars in thousands)

Deferred tax liabilities by types of temporary differences are as follows:

		2019	2018
Tangible fixed assets	$	537,644	522,296
Goodwill and other intangible assets		747,794	695,441
Financial instruments		—	6,152
Total deferred tax liabilities	**$**	**1,285,438**	**1,223,889**

At December 31, 2019 and 2018, deferred taxes were recognized for all temporary differences, unless an exception from the general principal applied. Additionally, the Company had net operating losses and tax credits, which can be carried forward to the extent taxable income will be generated. In earlier years, a portion of the net operating losses and tax credits that the Company does not expect to realize were transferred to unrecognized deferred tax assets. These unrecognized deferred tax assets, all of which expire in more than five years, total $5,819 as of December 31, 2019 and 2018. Excluding the unrecognized deferred tax assets, a benefit has been fully recognized based on the Company's expectation of probable taxable profits before the unused tax losses expire.

(10) Goodwill and Intangible Assets

Goodwill

Goodwill is initially recognized as a result of the accounting for a business combination (Note 19). Subsequently, it is measured at cost less impairment.

Intangible Assets

This heading includes intangible assets that are internally generated or acquired, either separately or in a business combination, when they are identifiable and can be reliably measured. Internally generated intangible assets (essentially management information system software) are capitalized provided that there is an identifiable asset that will be useful in generating future benefits in terms of savings, economies of scale, etc.

Indefinite life intangible assets mainly comprise of operating rights which can be renewed without significant cost and are supported by ongoing marketing activities. They are not amortized but tested for impairment annually or more frequently if an impairment indicator is triggered. Any impairment charge is recorded in the consolidated income statement under Other trading expenses. The assessment of the classification of intangible assets as indefinite is reviewed annually.

Finite life intangible assets are amortized over the shorter of their contractual or useful economic lives. They comprise mainly management information systems and rights and customer lists. Finite life intangible assets are amortized on a straight-line basis assuming a zero residual value: management information systems over a period ranging from 3 to 8 years; and other finite intangible assets over the estimated useful life or the related contractual period, generally 5 to 20 years or longer, depending on specific circumstances. Useful lives and residual values are reviewed annually. Amortization of finite life intangible assets starts when they are available for use and is allocated to the appropriate headings of expenses by function in the consolidated income statement. Any impairment charge is recorded in the consolidated income statement under Other trading expenses.

(Dollars in thousands)

		Goodwill	Total Intangible Assets
Gross Value:			
At January 1, 2018	$	20,925,843	2,406,825
of which indefinite useful life		—	*188,202*
Expenditure		—	174,238
Disposals		—	(134,693)
Acquisition of businesses [a]		987,514	4,380,200
Reclassified as held for sale		(1,755,817)	(1,174,533)
At December 31, 2018		**20,157,540**	**5,652,037**
of which indefinite useful life		—	*4,275,500*
Accumulated Amortization and Impairments:			
At January 1, 2018		(4,758,575)	(1,057,989)
of which indefinite useful life		—	—
Amortization		—	(70,542)
Impairments (Note 17)		(260,000)	(8,288)
Disposals		—	67,042
Disposal of businesses		513,421	16,255
At December 31, 2018		**(4,505,154)**	**(1,053,522)**
of which indefinite useful life		—	—
Net at December 31, 2018	$	**15,652,386**	**4,598,515**
of which indefinite useful life		—	*4,275,500*
Gross Value:			
At January 1, 2019	$	20,157,540	5,652,037
of which indefinite useful life		—	*4,275,500*
Expenditure		—	80,206
Disposals		—	(22,863)
Acquisition of businesses [a]		34,920	1,983
Reclassified as held for sale		(1,400,968)	—
At December 31, 2019		**18,791,492**	**5,711,363**
of which indefinite useful life		—	*4,275,500*
Accumulated Amortization and Impairments:			
At January 1, 2019		(4,505,154)	(1,053,522)
of which indefinite useful life		—	—
Amortization		—	(57,507)
Impairments (Note 17)		—	(23,181)
Disposals		—	20,880
Disposal of businesses		—	—
At December 31, 2019		**(4,505,154)**	**(1,113,330)**
of which indefinite useful life		—	—
Net at December 31, 2019	$	**14,286,338**	**4,598,033**
of which indefinite useful life		—	*4,275,500*

[a] Acquisitions are primarily related to the licensed Starbucks business in 2018 (Note 19).

(Continued)

Impairment of Goodwill and Intangible Assets

Goodwill and intangible assets with an indefinite life are tested for impairment at least annually and when there is an indication of impairment. Finite life intangible assets are tested when there is an indication of impairment.

The annual impairment tests are performed at the same time each year and at the cash generating unit ("CGU") level. The Company defines its CGU for goodwill impairment testing based on the way that it monitors and derives economic benefits from the acquired goodwill. For indefinite life intangible assets, the Company defines its CGU as the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. The impairment tests are performed by comparing the carrying value of the assets of these CGU with their recoverable amount, based on their value in use, which corresponds to their future project cash flows discounted at an appropriate pre-tax rate of return. Usually, the cash flows correspond to estimates made by management in financial plans and business strategies covering a period of five years after making adjustments to consider the assets in their current condition. They are then projected to perpetuity using a multiple which corresponds to a steady or declining growth rate. The Company assesses the uncertainty of these estimates by making sensitivity analyses. The discount rate reflects the current assessment of the time value of money and the risks specific to the CGU (essentially country risk). The business risk is included in the determination of the cash flows. Both the cash flows and the discount rates include inflation. An impairment loss in respect of goodwill is never subsequently reversed.

Impairment Charge during the year

There was no Goodwill impairment charge during 2019. The 2019 Intangible Assets impairment charge relates to Operating Rights and Others and Management Information Systems.

The 2018 Goodwill impairment charge relates to the Infant Nutrition CGU, which is reported in the Nutrition Segment.

The Infant Nutrition CGU is composed mainly of goodwill and intangible assets. These have arisen mainly from the acquisition of Gerber Products Company. An annual impairment test for the Infant Nutrition CGU was conducted in the second half of 2018. While Infant Nutrition continued to be a clear leader and innovator in the US baby food category, sales and market share decreased during 2018. Formula sales were adversely impacted by changes in government-sponsored contracts. The combination of these factors resulted in an overall downward revision of projected cash flows and a recoverable amount of the CGU lower than its carrying amount. Consequently, a goodwill impairment charge amounting to $260,000 was recognized under the heading of Net other operating expenses in the consolidated income statement in 2018. The 2018 carrying amount of the Infant Nutrition CGU amounted to $765,481, which included $760,981 of goodwill and $4,500 of intangible assets with indefinite useful life.

The recoverable amount of the CGU has been determined based upon a value-in-use calculation. A pre-tax discount rate of 8.2% (2018: 8.2%) was used in this calculation. There was no impairment of the carrying amounts of the other assets of the CGU.

(Dollars in thousands)

Annual Impairment Tests

Impairment reviews have been conducted for goodwill and intangible assets with indefinite useful life items allocated to seven cash generating units (CGU).

The Petcare CGU has been considered as significant with regard to the total goodwill for which detailed results are presented.. Nestlé Starbucks Coffee US is considered significant with regard to total intangible assets with indefinite useful life.

	Goodwill	
	2019	**2018**
PetCare	$ 8,813,712	8,815,865
Subtotal	**8,813,712**	**8,815,865**
Other CGU's	5,472,626	6,836,521
Total	**$ 14,286,338**	**15,652,386**

	Intangible assets with indefinate useful life	
	2019	**2018**
Nestlé Starbucks Coffee US	4,271,000	4,271,000
Subtotal	**4,271,000**	**4,271,000**
Other CGU's	4,500	4,500
Total	**4,275,500**	**4,275,500**

For these CGUs, the recoverable amount is higher than their carrying amount. The recoverable amount has been determined based upon a value-in-use calculation. Cash flows have been projected over the next five years. They have been extrapolated using a steady or declining terminal growth rate and discounted at a pre-tax weighted average rate.

(Dollars in thousands)

The following table summarizes the key assumptions for each significant CGU:

	2019				
	Period of Cash Flow Projections	Annual Sales Growth	Annual Margin Evolution	Terminal Growth Rate	Pre-Tax Discount Rate
PetCare	5 years	3.1% to 5.5%	Declining	2.0%	8.2%
Nestlé Starbucks Coffee US	5 years	3.7% to 4.7%	Improvement	2.3%	7.7%

	2018				
	Period of Cash Flow Projections	Annual Sales Growth	Annual Margin Evolution	Terminal Growth Rate	Pre-Tax Discount Rate
PetCare	5 years	0.8% to 2.0%	Declining	2.0%	8.2%
Nestlé Starbucks Coffee US	5 years	3.6% to 4.5%	Stable	2.5%	8.0%

- The pre-tax discount rate has been computed based on external sources of information.
- The cash flows for the first five years were based upon financial plans approved by Nestlé Group Management which are consistent with the Nestlé Group's approved strategy for this period. They are based on past performance and current initiatives.
- The terminal growth rates have been determined to reflect the long-term view of the nominal evolution of the business.

Management believes that no reasonably possible change in any of the above key assumptions would cause the CGU's recoverable amount to fall below the carrying value of the CGUs.

(11) Financial Instruments

Financial Assets – Classes and Categories

The classification of financial assets is generally based on the business model in which a financial asset is managed and its contractual cash flow characteristics. The Company classifies financial assets in the following categories:

- measured at amortized cost;
- measured at fair value through the consolidated income statement (abbreviated as FVTPL, fair value through profit or loss).

For an equity investment that is not held for trading, the Company may irrevocably elect to classify it as measured at FVOCI. This election is made at initial recognition on an investment by investment basis.

Financial Assets – Recognition and derecognition

The settlement date is used for initial recognition and derecognition of financial assets as these transactions are generally under contracts whose terms require delivery within the timeframe established by regulation or convention in the marketplace (regular-way purchase or sale). Financial assets are derecognized when substantially all of the Company's rights to cash flows from the financial assets have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

Financial Assets – Measurement

Financial assets are initially recognized at fair value plus directly attributable transaction costs. However, when a financial asset measured at FVTPL is recognized, the transaction costs are expensed immediately. Subsequent remeasurement of financial assets is determined by their categorization, which is revisited at each reporting date.

Commercial paper and time deposits are held by the Company's treasury unit in a separate portfolio in order to provide interest income and mitigate the credit risk exposure of the Company. The Company considers that these investments are held within a business model whose objective is achieved by collecting contractual cash flows. The contractual terms of these financial assets give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. These assets have therefore been classified as measured at amortized cost.

Investments in equities, debt funds, and equity funds as well as other financial assets not giving rise on specified dates to cash flows that are solely payments of principal and interest are classified at FVTPL. These investments are mainly related to self-insurance activities.

Financial Assets – Impairment

The Company assesses whether its financial assets carried at amortized cost and FVOCI are impaired on the basis of ECLs. The analysis requires the identification of significant increases in the credit risk of the counterparties. Considering that the majority of the Company's financial assets are trade receivables, the analysis also integrates statistical data reflecting the past experience of losses incurred due to default. See Note 3 for impairments related to trade receivables.

The Company measures loss allowances for investments in debt securities and time deposits that are determined to have low credit risk at the reporting date at an amount equal to 12 month expected credit losses.

The Company considers a debt security to have low credit risk when its credit rating is "investment grade" according to internationally recognized rating agencies. To assess whether there is a significant increase in credit risk since initial recognition, the Company considers available reasonable and supportive information such as changes in the credit rating of the counterparty. If there is a significant increase in credit risk the loss allowance is measured at an amount equal to lifetime expected loss.

ECLs are a probability-weighted estimate of credit losses. Credit losses are measured as the present value of all cash shortfalls due to a credit default event of the counterparty (i.e. the difference between cash flows due to the entity in accordance with the contract and the cash flows that the Company expects to receive).

Loss allowances for financial assets measured at amortized cost are deducted from the gross carrying amount of the assets.

Impairment losses on other financial assets related to treasury activities are presented under Net financial expense.

The model and some of the assumptions used in calculating these ECLs are key sources of estimation uncertainty.

Financial Liabilities at Amortized Cost

Financial liabilities are initially recognized at the fair value, net of transaction costs incurred.

Subsequent to initial measurement, financial liabilities are recognized at amortized cost. The difference between the initial carrying amount of the financial liabilities and their redemption value is recognized in the consolidated income statement over the contractual terms using the effective interest rate method. This category includes the following classes of financial liabilities: trade and other payables, commercial paper, bonds, lease liabilities, and other financial liabilities.

Financial liabilities at amortized cost are further classified as current and non-current depending whether these will fall due within 12 months after the balance sheet date or beyond.

Financial liabilities are derecognized (in full or in part) when either the Company is discharged from its obligation, they expire, are canceled or replaced by a new liability with substantially modified terms.

Supplier finance agreements

The Company participates in supplier finance agreements under which suppliers may elect to receive early payment by factoring their receivables from the Company. The due dates of the payments by the Company are based on agreed trade terms with the suppliers, are compliant with the applicable regulations, and remain consistent with the normal operating cycle of its business.

The Company continues to present invoices eligible to be settled through these programs as Trade payables considering that the original liability is neither legally released nor substantially modified on entering into such arrangements. Related payments are included within operating cash flows because they remain operational in nature.

(Dollars in thousands)

Financial Assets and Liabilities by Class and by Category:

		2019	2018
By class:			
Cash and cash equivalents [(a)]	$	322,711	368,045
Trade and other receivables, net		17,370,403	16,606,655
Derivative assets (Note 5)		1,223	26,464
Bonds and debt funds		310,871	1,431,878
Equity and equity funds		333,809	328,929
Investments in life insurance company general accounts		585,922	576,854
Loans to Affiliates		323,179	64,072
Other financial assets [(b)]		42,458	121,170
Total financial assets		**19,290,576**	**19,524,067**
Trade and other payables		2,724,071	3,101,547
Financial liabilities – current		7,122,540	6,064,089
Derivative liabilities (Note 5)		308,701	292,990
Financial liabilities – non-current		14,582,326	16,389,379
Total financial liabilities		**24,737,638**	**25,848,005**
Net financial position	**$**	**(5,447,062)**	**(6,323,938)**

[(a)] Includes bank balance of $322,711 (2018: $368,045).

[(b)] Includes short-term investments.

		2019	2018
By category:			
At amortized cost:			
Loans and receivables (including cash and cash equivalents)[(c)]	$	18,034,648	17,123,281
At fair value to the income statement:			
Derivative assets (Note 5)		1,223	26,464
Financial assets		1,254,705	2,374,322
Total financial assets		**19,290,576**	**19,524,067**
Liabilities at amortized cost [(c)]		24,428,937	25,555,015
Derivative liabilities at fair value to the income statement (Note 5)		308,701	292,990
Total financial liabilities		**24,737,638**	**25,848,005**
Net financial position	**$**	**(5,447,062)**	**(6,323,938)**
of which at fair value		*947,227*	*2,107,796*

[(c)] Carrying amount of these instruments is a reasonable approximation of their fair value. For bonds included in liabilities at amortized cost, see the Bonds table.

Fair Value Hierarchy of Financial Instruments

The Company classifies the fair value of its financial instruments in the following hierarchy, based on the inputs used in their valuation:

- Level 1: The fair value of financial instruments quoted in active markets is based on their quoted closing price at the balance sheet date. Examples include exchange-traded commodity derivatives and financial assets such as investments in equity and debt securities.

- Level 2: The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques using observable market data. Such valuation techniques include discounted cash flows, standard valuation models based on market parameters for interest rates, yield curves or foreign exchange rates, dealer quotes for similar instruments, and use of comparable arm's length transactions. For example, the fair value of forward exchange contracts, currency swaps and interest rate swaps is determined by discounting estimated future cash flows.

- Level 3: The fair value of financial instruments that are measured on the basis of entity specific valuations using inputs that are not based on observable market data (unobservable inputs). When the fair value of unquoted instruments cannot be measured with sufficient- reliability, the Company carries such instruments at cost less impairment, if applicable.

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2019 and 2018

(Dollars in thousands)

		2019	2018
Fair value hierarchy of financial instruments:			
Derivative assets	$	—	8,064
Bonds and debt funds		—	1,184,092
Equity and equity funds		—	10,036
Other financial assets		2,523	20,433
Derivative liabilities		(1,742)	(20,308)
Prices quoted in active markets (Level 1)		**781**	**1,202,317**
Time deposits		—	—
Derivative assets		1,223	18,400
Bonds and debt funds		301,439	244,461
Equity and equity funds		237,649	224,188
Investments in life insurance company general accounts		585,750	576,854
Other financial assets		18,024	12,500
Derivative liabilities		(306,959)	(272,682)
Valuation techniques based on observable market data (Level 2)		**837,126**	**803,721**
Valuation techniques based on unobservable input (Level 3)		**16,033**	**101,758**
Total financial instruments at fair value	**$**	**853,940**	**2,107,796**

There have been no significant transfers between the different hierarchy levels in 2019 and in 2018.

NESTLÉ HOLDINGS, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2019 and 2018

(Dollars in thousands)

Changes in liabilities arising from financing activities

	2019	2018
At January 1	$ (22,721,934)	(15,742,010)
Currency retranslations and exchange differences	(28,341)	176,381
Changes in fair values	5,790	12,191
Imputed Interest on financial debt	(151,731)	(207,984)
(Inflows)/Outflows on interest derivatives	(47,162)	(50,921)
Inflows from bonds and other non-current financial debt	(153,572)	(8,673,800)
Outflows from bonds and other on-current financial debt	1,976,457	1,533,453
Outflows from current financial debt	(885,518)	230,756
At December 31	(22,006,011)	(22,721,934)
of which current financial debt	(7,122,540)	(6,064,089)
of which non-current financial debt	(14,582,326)	(16,389,379)
of which derivatives hedging financial debt	(301,145)	(268,466)

(Dollars in thousands)

Bonds

	Comments	Coupon	Effective interest rate	Year of issue/ maturity	2019	2018
USD 500,000		2.00	2.17	2013-2019	$ –	499,195
USD 500,000		2.25	2.41	2013-2019	–	499,844
USD 400,000		2.00	2.06	2014-2019	–	399,823
AUD 250,000	(b)	4.25	4.43	2014-2020	174,572	179,008
NOK 1,000,000	(b)	2.75	2.85	2014-2020	113,650	116,359
USD 650,000		2.13	2.27	2014-2020	649,967	649,007
AUD 175,000	(b)	3.63	3.77	2014-2020	125,024	126,794
GBP 400,000	(a)	1.75	1.82	2015-2020	524,852	508,524
GBP 100,000	(b)	1.75	1.68	2016-2020	132,453	128,690
USD 550,000		1.88	2.03	2016-2021	549,027	548,224
USD 600,000		1.38	1.52	2016-2021	598,648	597,782
GBP 500,000	(a)	1.00	1.17	2017-2021	654,949	633,965
USD 650,000		2.38	2.50	2017-2022	648,427	647,687
USD 300,000		2.25	2.35	2017-2022	299,315	299,035
USD 800,000		2.38	2.55	2017-2022	796,108	794,821
EUR 850,000	(a)	0.88	0.92	2017-2025	950,126	969,599
CHF 550,000	(a)	0.25	0.24	2017-2027	568,224	558,517
CHF 150,000	(a)	0.55	0.54	2017-2032	154,962	152,305
USD 1,000,000		3.10	3.17	2018-2021	998,900	998,290
USD 600,000	(c)	3.13	3.28	2018-2023	597,212	596,404
USD 1,500,000	(c)	3.35	3.41	2018-2023	1,496,937	1,496,179
USD 900,000	(c)	3.50	3.59	2018-2025	895,842	895,200
USD 1,250,000	(c)	3.63	3.72	2018-2028	1,241,274	1,240,444
USD 1,250,000	(c)	3.90	4.01	2018-2038	1,231,220	1,230,560
USD 2,100,000	(c)	4.00	4.11	2018-2048	2,060,084	2,059,380
Other bonds issued by Nestlé Purina PetCare Company:						
USD 63,210		9.30	6.46	1991-2021	65,511	67,116
USD 78,963		8.63	6.46	1992-2022	82,378	83,833
USD 43,927		8.13	6.47	1993-2023	45,921	46,489
USD 51,164		7.88	6.45	1995-2025	54,216	54,671
Other Bonds					1,804	1,814
Total carrying amount [d]					**$ 15,711,603**	**17,079,559**
of which due within one year					*1,720,515*	*1,398,862*
of which due after one year					*13,991,088*	*15,680,696*
Fair value [d] of bonds, based on prices quoted (level 2)					16,755,589	17,115,420

[a] Subject to an interest rate and currency swap that creates a U.S. dollar liability at fixed rates.

[b] Subject to an interest rate and currency swap that creates a U.S. dollar liability at floating rates.

[c] Sold in the United States only to qualified institutional buyers and outside the United States to non-U.S. persons.

[d] Carrying amount and fair value of bonds exclude accrued interest.

Several bonds are hedged by currency and/or interest derivatives. The fair value of these derivatives is shown under derivative assets of $0 (2018: $16,764) and under derivative liabilities of $285,465 (2018: $251,502).

(12) Financial Risks

In the course of its business, the Company is exposed to a number of financial risks: credit risk, liquidity risk, market risk (including foreign currency risk and interest rate risk, commodity price risk, and equity price risk). This note presents the Company's objectives, policies, and processes for managing its financial risk and capital.

Financial risk management is an integral part of the way the Company is managed. The Board of Directors of Nestlé S.A. determines the financial control principles as well as the principles of financial planning. The Chief Executive Officer organizes, manages, and monitors all financial risks, including asset and liability matters.

A Nestlé S.A. Asset and Liability Management Committee ("ALMC"), under the supervision of the Chief Financial Officer of Nestlé S.A., is the governing body for the establishment and subsequent execution of Nestlé S.A.'s Financial Asset and Liability Management Policy. It ensures implementation of strategies and achievement of objectives of Nestlé S.A.'s Financial Asset and Liabilities Management Policy, which are executed by the Centre Treasury, the Regional Treasury Centres, and in specific local circumstances, by the subsidiaries. Approved Treasury Management Guidelines define and classify risks as well as determine, by category of transaction, specific approval, execution, and monitoring procedures. The activities of the Centre Treasury and of the Regional Treasury Centres are monitored by an independent Middle Office, which verifies the compliance of the strategies and/or operations with the approved guidelines and decisions taken by the ALMC.

Credit Risk

Credit Risk Management

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Company. Credit risk arises on financial assets (liquid, non-current and derivative) and on trade and other receivables.

The Company aims to minimize the credit risk of liquid assets, non-current financial assets and derivative assets through the application of risk management policies. Credit limits are set based on each counterparty's size and risk of default. The methodology used to set the credit limit considers the counterparty's balance sheet, credit ratings, risk ratios and default probabilities. Counterparties are monitored regularly, taking into consideration the evolution of the above parameters, as well as their share prices and credit default swaps. As a result of this review, changes on credit limits and risk allocation are carried out.

The Company avoids the concentration of credit risk on its liquid assets by spreading them over several institutions and sectors.

Trade receivables are subject to credit limits, control, and approval procedures in all the subsidiaries. Due to its large geographic base and number of customers, the Company is not exposed to material concentrations of credit risk on its Trade and Other Receivables, net (Note 3). Nevertheless, commercial counterparties are constantly monitored following the similar methodology used for financial counterparties.

(Dollars in thousands)

The maximum exposure to credit risk resulting from financial activities, without considering netting agreements and without taking into account any collateral held or other credit enhancements, is equal to the carrying amount of the Company's financial assets.

Credit rating of financial assets

Financial assets include liquid assets, non-current financial assets and derivative assets. The credit risk of the financial assets is assessed based on the risk of the counterparties including the associated country risk. The Company uses an internationally recognized credit scale to present the information. The Company deals mainly with financial institutions located in Switzerland, the European Union, and North America.

		2019	2018
Investment grade (A- and above)	$	1,149,127	2,410,642
Investment grade (BBB+, BBB and BBB-)		44,891	29,891
Non-investment grade (BB+ and below)		30,321	28,273
Not rated (*)		372,655	365,083
Total financial assets (excluding receivables and inter-group loans)	**$**	**1,596,994**	**2,833,889**

(*) Mainly equity securities and other investments for which no credit rating is available.

Liquidity Risk

Liquidity Risk Management

Liquidity risk is the risk that a company may encounter difficulties in meeting its obligations associated with financial liabilities that are settled by delivering cash or other financial assets. Such risk may result from inadequate market depth, disruption, or refinancing problems. The Company's objective is to manage this risk by limiting exposures in financial instruments that may be affected by liquidity problems and by maintaining sufficient back-up facilities.

(Dollars in thousands)

	2019					
	1st year	2nd year	3rd to 5th year	After the 5th year	Contractual amount	Carrying amount
Trade and other payables	$ 2,724,071	—	—	—	2,724,071	2,724,071
Commercial paper	5,062,630	—	—	—	5,062,630	5,049,753
Bonds	2,165,179	3,273,800	4,833,980	10,161,052	20,434,011	15,711,604
Lease liabilities	118,161	116,181	268,366	336,188	838,896	721,844
Other financial debt	218,866	—	—	—	218,866	218,866
Other financial liabilities	—	—	—	2,800	2,800	2,800
Total financial debt	**7,564,836**	**3,389,981**	**5,102,346**	**10,500,040**	**26,557,203**	**21,704,867**
Financial liabilities (excluding derivatives)	**10,288,907**	**3,389,981**	**5,102,346**	**10,500,040**	**29,281,274**	**24,428,938**
Non-currency derivative assets	716	—	—	—	716	716
Non-currency derivative liabilities	(18,165)	(5,294)	—	—	(23,459)	(23,218)
Gross amount receivable from currency derivatives	726,040	673,818	32,031	1,694,673	3,126,562	2,997,069
Gross amount payable from currency derivatives	(876,879)	(723,444)	(150,762)	(1,811,079)	(3,562,164)	(3,282,044)
Net derivatives	**(168,288)**	**(54,920)**	**(118,731)**	**(116,406)**	**(458,345)**	**(307,477)**
of which derivatives under cash flow hedges	*$ (162,982)*	*(54,920)*	*(118,733)*	*(116,404)*	*(453,039)*	*(169,737)*

	2018					
	1st year	2nd year	3rd to 5th year	After the 5th year	Contractual amount	Carrying amount
Trade and other payables	$ 3,101,547	—	—	—	3,101,547	3,101,547
Commercial paper	4,451,153	—	—	—	4,451,153	4,438,186
Bonds	1,876,245	2,149,004	7,863,726	10,392,977	22,281,952	17,079,559
Lease liabilities	129,666	126,052	311,672	368,002	935,392	815,915
Other financial debt	111,908	—	—	—	111,908	111,908
Other financial liabilities	—	—	—	7,900	7,900	7,900
Total financial debt	**6,568,972**	**2,275,056**	**8,175,398**	**10,768,879**	**27,788,305**	**22,453,468**
Financial liabilities (excluding derivatives)	**9,670,519**	**2,275,056**	**8,175,398**	**10,768,879**	**30,889,852**	**25,555,015**
Non-currency derivative assets	9,067	—	—	—	9,067	9,067
Non-currency derivative liabilities	(31,878)	(5,591)	(2,260)	—	(39,729)	(39,067)
Gross amount receivable from currency derivatives	100,263	665,020	675,499	1,712,895	3,153,677	2,969,724
Gross amount payable from currency derivatives	(158,562)	(833,672)	(823,925)	(1,861,359)	(3,677,518)	(3,206,250)
Net derivatives	**(81,110)**	**(174,243)**	**(150,686)**	**(148,464)**	**(554,503)**	**(266,526)**
of which derivatives under cash flow hedges	*$ (78,084)*	*(154,444)*	*(150,686)*	*(148,129)*	*(531,343)*	*(131,187)*

Market Risk

The Company is exposed to risk from movements in foreign currency exchange rates, interest rates, and market prices that affect its assets, liabilities, and future transactions.

Foreign Currency Risk

The Company is exposed to foreign currency risk from transactions. Transactional exposures arise from transactions in foreign currency. They are managed within a prudent and systematic hedging policy in accordance with the Company's specific business requirements through the use of currency forwards and swaps.

Interest Rate Risk

Interest rate risk on financial debt is managed based on duration and interest management targets set by the ALMC through the use of fixed rate debt and interest rate swaps.

Taking into account the impact of interest derivatives, the proportion of financial debt subject to fixed interest rates for a period longer than one year represents 71% (2018: 77%).

Price Risk

Commodity Price Risk

Commodity price risk arises from transactions on the world commodity markets for securing the supplies of green coffee, cocoa beans, and other commodities necessary for the manufacture of some of the Company's products.

The Company's objective is to minimize the impact of commodity price fluctuations and this exposure is hedged in accordance with the policies set by the Company's management and the Nestlé Group policy on commodity price risk management.

The Global Procurement Organization is responsible for managing commodity price risks on the basis of internal directives and centrally determined limits, generally through the use of exchange-traded commodity derivatives.

The commodity price risk exposure of future purchases is primarily managed using a combination of derivatives (mainly futures and options) and executory contracts.

As a result of the short product business cycle of the Company, the majority of the anticipated future raw material transactions outstanding at the balance sheet date are expected to occur in the next year.

Equity Price Risk

The Company is exposed to equity price risk on investments. To manage the price risk arising from these investments, the Company diversifies its portfolios in accordance with the guidelines set by the Board of Directors of Nestlé S.A.

Value at Risk ("VaR")

Description of the Method

The VaR is a single measure to assess market risk. The VaR estimates the size of losses given current positions and possible changes in financial markets. The Company uses simulation to calculate VaR based on the historic data for a 250-day period.

The VaR calculation is based on a 95% confidence level and accordingly, does not take into account losses that might occur beyond this level of confidence.

The VaR is calculated on the basis of unhedged exposures outstanding at the close of business and does not necessarily reflect intra-day exposures.

Objective of the Method

The Company uses the described VaR analysis to estimate the potential one-day loss in the fair value of its financial and commodity instruments.

The Company cannot predict the actual future movements in market rates and prices, therefore, the below VaR numbers neither represent actual losses nor consider the effects of favorable movements in underlying variables. Accordingly, these VaR numbers may only be considered indicative of future movements to the extent the historic market patterns repeat in the future.

VaR Figures

The VaR computation includes the Company's financial assets and liabilities that are subject to foreign currency, interest rate, and price risk.

The estimated potential one-day loss from the Company's commodity price risk sensitive instruments is not significant.

Capital Risk Management

The Company's capital risk management strategy is to maintain a sound capital base to support the continued development of the Company's operations, utilizing various funding sources available to it. Substantially all of the Company's debt is guaranteed by Nestlé S.A., which allows the Company to borrow from third parties at lower interest rates. In order to ensure that the return on invested capital is optimized, the Company establishes strict limits on annual additions of property, plant and equipment.

(Dollars in thousands)

(13) Assets Held for Sale

Non-current assets held for sale and disposal groups are presented separately in the current section of the consolidated balance sheet when the following criteria are met: the Company is committed to selling the asset or disposal group, an active plan of sale has commenced, and in the judgment of Company management it is highly probable that the sale is expected to be completed within 12 months. Immediately before the initial classification of the assets and disposal groups as held for sale, the carrying amounts of the assets (or all the assets and liabilities in the disposal groups) are measured in accordance with their applicable accounting policy. Assets held for sale and disposal groups are subsequently measured at the lower of their carrying amount and fair value less cost to sell. Assets held for sale are no longer amortized or depreciated.

As of December 31, 2019, assets held for sale and liabilities directly associated with assets held for sale are mainly composed of the Ice Cream business and certain DSD network assets which historically supported Frozen Pizza and Ice Cream.

Building on the experience of the Nestlé Group in 2016 with the creation of the joint-venture Froneri, the US Ice Cream business (part of the Brands segment) has been sold at end of January 2020 to Froneri to create a global leader in ice cream. The US Ice Cream business and related DSD assets have been therefore disclosed as held for sale as at December 31, 2019. The estimated result on disposal, to be recognized under the heading other operating income in the income statement in 2020, amounts to a gain of approximately $2 billion.

	2019	2018
Inventories	$ 164,757	—
Trade and other receivables, prepayments, accrued income and other assets	34,844	—
Property, plant, and equipment	511,709	—
Goodwill	1,400,968	—
Assets held for sale	2,112,278	—
Financial liabilities	15,169	—
Trade and other payables, accruals, and deferred income	8,212	—
Deferred taxes	103,669	—
Liabilities directly associated with assets held for sale	127,050	—
Net assets held for sale	**1,985,228**	**—**

(Continued)

(Dollars in thousands)

(14) Accruals

Accruals consist of expenses relating to the current year, which will not be invoiced until after the balance sheet date.

Accruals are as follows:

		2019	2018
Accrued payroll	$	509,052	419,451
Accrued trade spend and promotional expenses		493,979	579,010
Accrued interest		163,521	175,831
Other accrued expenses		627,031	433,902
Total accruals	$	**1,793,583**	**1,608,194**

(15) Provisions and Contingencies

Provisions

Provisions include liabilities of uncertain timing or amount that arise from restructuring plans, environmental, litigation, and other risks. Provisions are recognized when a legal or constructive obligation stemming from a past event exists and when the future cash outflows can be reliably estimated. Provisions are measured at the present value of the expenditures unless the impact of discounting is immaterial. Obligations from restructuring plans are recognized when detailed formal plans have been established and when there is a valid expectation that such plans will be carried out by either starting to implement them or announcing their main features. Obligations under litigation reflect Company management's best estimates of the outcomes based on the facts known at the balance sheet date.

Contingent Assets and Liabilities

Contingent assets and liabilities are possible rights and obligations that arise from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not fully within the control of the Company.

(Dollars in thousands)

Provisions

Provisions are as follows:

		Restructuring	Environmental	Legal	Other	Total
At December 31, 2018	$	194,952	22,445	11,532	42,296	271,225
Provisions made in the year		179,083	3,676	2,525	115,400	300,684
Amounts used		(126,606)	(2,254)	(1,185)	(77,907)	(207,952)
Reversal of unused amounts		(16,648)	(146)	(800)	(6,875)	(24,469)
Unwind of discount		—	881		18	899
At December 31, 2019	$	230,781	24,602	12,072	72,932	340,387
of which expected to be settled within 12 months	*$*	*229,202*	*1,729*	*5,572*	*52,393*	*288,896*

Restructuring

Restructuring provisions arise from a number of projects across the Company. These include plans to optimize production, sales, and administration structures. Restructuring provisions are expected to result in future cash outflows when implementing the plans (usually over the following two to three years).

During 2019, the Company initiated and continued with a number of reorganizations within all of the operating segments to reduce structural costs and to optimize production. As part of these actions, net increases to restructuring provisions of $162,435 were recorded in the consolidated financial statements.

Environmental

Situations where the Company is found liable for remediation or cleanup efforts by the U.S. environmental Protection Agency ("EPA") or other governmental agencies on specific sites represent known liabilities. In these instances, it is the Company's policy to accrue for environmental cleanup costs when they are assessed. As assessments and cleanups proceed, these liabilities are reviewed and adjusted as additional information becomes available regarding the nature and extent of contamination, methods of remediation required, other actions by governmental agencies or private parties, and the amount, if any, of available coverage by the Company's insurance carriers.

Legal

Legal provisions have been set up to cover legal and administrative proceedings that arise in the ordinary course of the business. They cover numerous separate cases whose detailed disclosure could be detrimental to the Company interests. The Company does not believe that any of these cases will have a material adverse impact on its financial position. The timing of outflows is uncertain as it depends upon the outcome of the cases. Company Management does not believe it is possible to make assumptions on the evolution of the cases beyond the balance sheet date.

Other

Other provisions are mainly constituted by onerous contracts and various damage claims having occurred during the year but not covered by insurance companies. Onerous contracts result from termination of contracts or supply agreements above market prices in which the unavoidable costs of meeting the obligations under the contracts exceed the economic benefits expected to be received or for which no benefits are expected to be received.

Contingencies

Litigation

The Company is exposed to a number of asserted claims and unasserted potential claims encountered in the normal course of business. In the opinion of Company management, the resolution of these matters will not have a material impact on the Company's consolidated financial position.

Exposure for Environmental Matters

The Company has contingent liabilities related to environmental matters where the Company has received "Notices of Potential Liability" from, or has been identified as a "Potentially Responsible Party" by, the EPA or other government agencies regarding the alleged disposal of hazardous material at various sites around the country that allegedly require environmental cleanup.

These proceedings are being vigorously defended or resolutions are being negotiated. Although the outcome of these proceedings is unknown, Company management does not believe that any resulting liability would be material to the consolidated financial position of the Company.

(16) Net Financial Income/(Expense)

Net financial income/(expense) includes net financing cost of net debt and net interest income/(expense) on defined benefit plans.

Net financing cost of net debt comprises the interest income earned on cash and cash equivalents, and short-term investments, as well as the interest expense on financial debt (including leases). These headings also include other income and expense such as exchange differences on net debt and results on related foreign currency and interest rate hedging instruments. Certain borrowing costs are capitalized as explained under the section "Property, Plant and Equipment".

(Dollars in thousands)

	Note		2019	2018
Interest income		$	531,841	426,133
Interest expense			(757,456)	(614,454)
Net financing cost of net debt			**(225,615)**	**(188,321)**
Interest income on defined benefit plans	7		14,209	14,347
Interest expense on defined benefit plans	7		(42,183)	(39,321)
Net interest expense on defined benefit plans			**(27,974)**	**(24,974)**
Other			(107)	896
Net financial expenses		$	**(253,696)**	**(212,399)**

Interest expenses on amounts due to affiliated and associated companies, and bonds and commercial paper guarantee fees to Nestlé S.A. amounted to $(80,046) and $(73,094) in 2019 and 2018, respectively. Interest income on amounts due from affiliated and associated companies amounted to $520,371 and $385,940 in 2019 and 2018, respectively.

(17) Net Other Trading and Operating Income/(Expenses)

Net Other Trading Income/(Expense)

These comprise restructuring costs, impairment of property, plant and equipment and intangible assets, litigation and onerous contracts, result of disposal of property, plant and equipment, and specific other income and expenses that fall within the control of operating segments.

Restructuring costs are restricted to dismissal indemnities and employee benefits paid to terminated employees upon the reorganization of a business. They do not include dismissal indemnities paid for normal attrition such as poor performance, professional misconduct, etc.

Net Other Operating Income/(Expense)

These comprise impairment of goodwill and results on disposals of businesses (including impairment and subsequent remeasurement of businesses classified as held for sale), as well as other directly related disposal costs like restructuring costs directly linked to businesses disposed of and legal, advisory and other professional fees), acquisition related costs and other income and expenses that fall beyond the control of operating segments and relate to events such as natural disasters.

(Dollars in thousands)

Net other trading income/(expenses) is as follows:

		2019	2018
Return on company-owned life insurance	$	101,015	27,943
Reversal of unused restructuring provisions		16,648	10,114
Franchise and royalty income		—	185
Miscellaneous trading income		—	235
Other trading income		**117,663**	**38,477**
Restructuring costs		(165,019)	(127,339)
Impairment of property, plant and equipment and intangible assets		(223,113)	(78,041)
Litigation and onerous contracts [**]		(153,388)	(37,362)
Result on deferred compensation		(70,444)	(18,548)
Loss on real estate operations		(41)	—
Miscellaneous trading expenses		(26,957)	(2,688)
Other trading expenses		**(638,962)**	**(263,978)**
Total net other trading expenses	$	**(521,299)**	**(225,501)**

[**] Relating principally to a number of separate legal cases, liabilities linked to voluntary product withdrawals and various separate onerous contracts.

In 2019, other trading expenses are mainly comprised of $464 million of one-off costs representing impairment charges related to property, plant, restructuring costs, and onerous contracts and other expenses related to the decision taken by the Company in the second quarter of 2019 to exit of Direct-Store-Delivery (DSD) network for Frozen Pizza and Ice Cream.

Net other operating income/(expenses) is as follows:

		2019	2018
Gain on disposal of businesses [a]	$	—	853,353
Miscellaneous operating income		186,271	56,212
Other operating income		**186,271**	**909,565**
Loss/expenditures on disposal of business [a]		(4,966)	(2,222,157)
Impairment of goodwill [b]		—	(260,000)
Miscellaneous operating expenses		(349,128)	(104,608)
Other operating expenses		**(354,094)**	**(2,586,765)**
Total net other operating expenses	$	**(167,823)**	**(1,677,200)**

[a] See acquisitions and disposals of businesses (Note 19).

[b] See goodwill and intangible assets (Note 10).

(Dollars in thousands)

(18) Income Tax Expense

The Company files a consolidated return with Nestlé US Holdco Inc. However, the Company also records its own tax expense and liability as if it filed on a standalone basis. Taxes and fiscal risks recognized in the consolidated financial statements reflect Company management's best estimate of the outcome based on the facts known at the balance sheet date. These facts may include, but are not limited to, changes in tax laws and interpretations thereof in the United States. They may have an impact on the income tax as well as the resulting assets and liabilities. Any differences between tax estimates and final tax assessments are charged to the consolidated income statement in the period in which they are incurred, unless anticipated.

Taxes include current taxes on income and other taxes such as taxes on capital and adjustments relating to prior years. Income tax is presented within the consolidated income statement, except to the extent that it relates to items directly taken to other comprehensive income.

Income from associates and the share of other comprehensive income of associates are shown net of tax effects.

The components of income tax (expense) from continuing operations are as follows:

		2019	2018
Current tax	$	(468,808)	(1,009,958)
Deferred tax		40,721	314,221
Taxes related to other comprehensive income		14,860	26,318
Income tax (expense)	$	**(413,227)**	**(669,419)**

The components of deferred tax (expense)/benefit by type are as follows:

		2019	2018
Tangible fixed assets	$	(65,775)	162
Goodwill and other intangible assets		(119,709)	184,698
Employee benefits		23,514	(25,162)
Inventories, receivables, payables, accruals, and provisions		(6,435)	(9,921)
Financial instruments		17,550	788
Net operating losses		8,257	(3,326)
Other		183,319	166,982
Deferred tax benefit	$	**40,721**	**314,221**

(Dollars in thousands)

Taxes recognized in other comprehensive income/(loss):

		2019	2018
Tax effect relating to:			
Fair value adjustments on cash flow hedges	$	16,799	(11,430)
Fair value of available-for-sale assets		—	10,883
Fair value changes on equity instruments		(328)	145
Defined benefit plan actuarial losses		(31,331)	(25,916)
Total taxes recognized	**$**	**(14,860)**	**(26,318)**

Reconciliation of income from continuing operations before income taxes multiplied by the applicable tax rate to income tax (expense) is as follows:

		2019	2018
Tax at theoretical rate	$	(356,895)	(115,013)
Tax effect on non-deductible amortization and impairment of goodwill and other intangible assets		(75)	(393,524)
Permanent differences on company-owned life insurance policies		30,030	2,230
Tax effect of non-deductible or non-taxable items		2,383	(632)
Prior years' taxes		(76,608)	(160,401)
Transfers form unrecognized deferred tax assets		—	8,257
Other taxes		(12,062)	(10,336)
Income tax (expense)	**$**	**(413,227)**	**(669,419)**

(19) Acquisitions and Disposals of Businesses

Business Combinations

Business combinations are accounted for using the acquisition method. Where not all of the equity of a subsidiary is acquired, the non-controlling interests are recognized at the non-controlling interest's share of the acquiree's net identifiable assets. Upon obtaining control in a business combination achieved in stages, the Company remeasures its previously held equity interest at fair value and recognizes a gain or a loss in the consolidated income statement.

(Continued)

Modification of the Scope of Consolidation

Acquisitions

There were no acquisitions in 2019.

At the end of August 2018, the Company acquired the perpetual rights to market, sell and distribute certain Starbucks' consumer packaged goods and foodservice products in the United States (Nestlé Coffee Partners) including roast and ground coffee, whole beans and instant and portioned coffee (Brands).

None of the other acquisitions in 2018 were significant.

Disposals

There were no disposals in 2019.

In 2018, the main disposals during the year were:

- U.S. Confectionery business, confectionery, (Brands), 100%, March.
- Gerber Life Insurance, insurance, (Other), 100%, December.

Acquisitions of Businesses

The Starbucks Alliance transferred control over the existing businesses mainly in the United States. It excludes Ready-to-Drink products and all sales of any products within Starbucks coffee shops. Consumer and foodservice products include *Starbucks*, *Seattle's Best Coffee*, *Teavana*, *Starbucks VIA Instant*, *Torrefazione Italia* coffee and *Starbucks* branded *K-Cup* pods. Through the Starbucks Alliance, the Company and Starbucks will work closely together on the existing Starbucks range of roast and ground coffee, whole beans as well as instant and portioned coffee. This partnership with Starbucks significantly strengthens the Company's coffee portfolio in the United States premium roast and ground and portioned coffee business. This creates synergies that result in goodwill being recognized, which is expected to be deductible for tax purposes.

(Dollars in thousands)

The major classes of assets acquired and liabilities assumed at the acquisition date were:

	2019	2018
	Total	**Total**
Property, plant and equipment	$ -	$ 3,742
Intangible assets	-	4,380,200
Inventories, prepaid inventories and other assets	-	180,000
Employee benefits, deferred taxes and provisions [1]	12,523	-
Other liabilities [1]	(47,443)	-
Fair value of identifiable net assets	$ **(34,920)**	$ **4,563,942**

The goodwill arising on acquisitions and the cash outflows were:

	2019	2018
	Total	**Total**
Fair value of consideration transferred	$ -	$ 5,551,456
Fair value of identifiable net assets [1]	34,920	(4,563,942)
Goodwill	$ **34,920**	$ **987,514**

	2019	2018
Fair value of consideration transferred	$ -	$ 5,551,456
Cash and cash equivalents acquired	-	-
Cash outflow on acquisitions	$ **-**	$ **5,551,456**

[1] Relates to an unfavorable contract relating to the licensed Starbucks business identified during the measurement period.

Acquisitions planned after December 31, 2019

On January 27, 2020 the Nestlé Group announced that it has entered into an asset purchase agreement with Allergan to acquire the gastrointestinal medication Zenpep. This move aims to expand Nestlé Health Science's (Nutrition Segment) medical nutrition business and complement its portfolio of therapeutic products. Zenpep, available in the United States, is a medication for people who cannot digest food properly because their pancreas does not provide enough enzymes to break down fat, protein, and carbohydrates.

(Dollars in thousands)

The transaction is expected to close in the first half of 2020 concurrent and dependent upon the merger of Allergan and AbbVie.

(a) Disposals of Businesses

In 2019, the expenditures on disposals of businesses of $8,358 are primarily due to additional costs related to the Gerber Life Insurance business disposed in 2018.

In 2018, the loss on disposals of businesses is mainly composed of the disposal at the end of December 2018 of the Gerber Life Insurance business (part of the Other businesses segment).

		2019	2018
		Total	Total
Property, plant and equipment	$	-	(8,588)
Goodwill and intangible assets		-	(2,400,674)
Inventories		-	(27,564)
Assets Held for sale		-	(390,016)
Other assets		-	(221,888)
Non-current financial assets		-	(3,486,748)
Financial liabilities		-	3,886
Other liabilities		-	2,500,526
Net assets disposed of	$	**-**	**(4,031,066)**
Cumulative other comprehensive income items, net reclassified to income statement		-	(171,282)
Disposal costs		(8,358)	(77,655)
Consideration received	$	-	2,911,199
(Loss)/profit on current year disposal		**(8,358)**	**(1,368,804)**

(Dollars in thousands)

(20) Transactions with Related Parties

Compensation of Key Company Management Personnel

Key Company management personnel comprise five high-ranking officers in each of the following subsidiaries: Nestlé USA, Inc., Nestlé Purina PetCare Company, and Gerber Products Company. These officers hold the positions of Chief Executive Officer, Chief Financial Officer, Head of Human Resources, General Counsel, and Head of Sales or Sales/Marketing. The Chief Executive Officer and the Chief Financial Officer of Nestlé USA, Inc. are directors of NHI. There is one non-executive director.

The compensation paid or payable to key Company management for employee services is shown below:

		2019	2018
Salaries and other short-term employee benefits	$	12,861	13,999
Share-based payments		10,243	12,615
Post-employment benefits		1,169	1,310
Total compensation	**$**	**24,273**	**27,924**

(Dollars in thousands)

Loans with Related Parties

		2019	2018
Loans to Nestlé S.A.:			
At January 1	$	—	198,790
Loan repayments		—	(198,790)
At December 31	**$**	**—**	**—**
Loans to NIMCO US, Inc. (Parent):			
At January 1	$	12,096,267	8,432,307
Loans granted during year		405,327	3,663,960
At December 31	**$**	**12,501,594**	**12,096,267**
Loans from affiliates:			
At January 1	$	—	25,945
Loans received during year		78,594	—
Loan repayments		—	(25,945)
At December 31	**$**	**78,594**	**—**
Loans to affiliates:			
At January 1	$	2,559,735	1,469,215
Loans granted during year		955,781	1,506,596
Loan repayments		(296,714)	(416,076)
At December 31	**$**	**3,218,802**	**2,559,735**

The above loans with related parties are in the trade and other receivables, trade and other payables, and current and non-current financial liabilities headings of the consolidated balance sheet.

(21) Events after the Balance Sheet Date

On March 11, 2020, the World Health Organization declared the Coronavirus (COVID-19) outbreak to be a pandemic in recognition of its rapid spread across the globe, with over 150 countries now affected. Many governments are taking increasingly stringent steps to help contain or delay the spread of the virus. Currently, there is a significant increase in economic uncertainty which is, for example, evidenced by more volatile asset prices and currency exchange rates, and rising unemployment claims.

For the Company's December 31, 2019 consolidated financial statements, the Coronavirus outbreak and the related impacts are considered non-adjusting events. Consequently, there is no impact on the recognition and measurement of assets and liabilities. Due to the uncertainty of the outcome of the current events, the Company cannot reasonably estimate the impact these events will have on the Company's financial position, results of operations or cash flows in the future.

The Company was not aware of any other specific events or transactions occurring after December 31, 2019, and up to March 31, 2020 that could have a material impact on the presentation of the accompanying consolidated financial statements, except the estimated gain on the disposal of the US Ice Cream business mentioned in Note 13 Assets held for sale.