Freedom Foods Group Limited ABN 41 002 814 235
80 Box Road Taren Point NSW 2229
T: +61 2 9526 2555 **www.ffgl.com.au** /FreedomFoodsGroup

27th February 2020

Freedom Foods Group Limited (ASX: FNP)
2020 Half Year Financial Results Release

Financial Highlights (excluding the impact of Lease Accounting standard)

- Net Sales increased 43.4% to $299.7 million, an increase of $90.7 million
- Operating EBDITA rose 55.6% to $32.7 million, an increase of $11.7 million
- Gross margins increased to 27.1% from 24.7%
- Operating net profit after tax increased 42.1% to $9.1 million. Statutory net profit rose 45.6% to $5.4 million, after abnormals and non-cash expenses
- Interim dividend of 2.25 cents per share (unfranked).

Strategic Highlights

- The Freedom Foods Group (Group or the Company) continues to achieve strong growth through key brands including Australia's Own and Freedom Foods in retail and MilkLab in out of home channels, in the key markets of Australia, SE Asia and China:
  - Net Sales from the Group's Brands represented 49% ($135 million) of total sales compared to 48% ($103m) in the previous corresponding period.
  - Growth achieved in key branded categories and channels, with Australian retail grocery growth of 23%, above category average growth rates (1.3%).
  - Strong sales growth in the MilkLab range of 152% compared to the previous corresponding period and 39% compared to the six months ended 30 June 2019 in the out of home channel and SE Asia
  - Continued growth of Messy Monkeys, with gain of 100% compared to the previous corresponding period and 30% compared to the six months ended 30 June 2019 in the healthy snacks retail channel
  - Growth in Vital Strength and Crankt nutrition brands, building penetration into Pharmacy and convenience channels
  - Launch of 40 new product formats into retail, grocery, out of home and export markets, supported by increased marketing expenditure
  - Launch of specialised Nutritional Ingredients including Lactoferrin (LF), Micellar Casein (MCC) and Whey Protein Isolate (WPI).
  - Growth in key export markets, including exceptional growth in SE Asia with sales revenues of $16.6 million or 58% compared to the previous corresponding period and 53% compared to the six months ended 30 June 2019, reflecting growth in branded and contract products. SE Asia has significant growth potential.
- As one of Australia's leading investors in state-of-the-art food and beverage manufacturing capability, the Group accelerated the final stages of its major capital investment program, including the following:
  - At Shepparton, Victoria, the Group finalised the upgrade to double total processing capacity to 500 million litres per annum, with additional filling and services upgrades being completed.
  - At Ingleburn, NSW, the Group brought forward increases in filling capacity to provide for growth in plant based beverages in Australia and export markets.
  - Fast tracked stage two of a transformational Nutritionals capability, with the planned capacity upgrade for Lactoferrin underway to provide for 40tn of capacity from July 2020 to meet contracted requirements into 2021.
- The half year sales and earnings results have not fully benefited from the key capital expenditure initiatives undertaken since March 2018. The Group expects these capital expenditure initiatives, along with increasing demand, to increase sales and earnings through 2nd half FY 2020 and beyond.

Outlook

Rory Macleod, Managing Director and Chief Executive Officer, commented:

"The Group is well positioned to strategically build into a major global food and beverage business with scale in key food and beverage platforms."

"The Group continues to experience strong demand across its business activities in key channels and markets. This growing demand in dairy, plant-based beverage and cereal and snacks reflects the positive impacts on our expanded operational footprint and increasing brand penetration and market share in key channels and categories in Australia, SE Asia and China."

While the Group expects some short-term disruption to China demand over the next few months as internal supply chains in China return to normal operation, the underlying medium-term demand from key customers in this market remains unchanged, with the Group scheduled to start supply to new China based customers from June 2020. Sales to China represent approximately 15% of our net sales value in the current half year.

The increasing scale and diversification of the Group's activities provides an important hedge to assist in mitigating potential impacts from short term disruption to a particular market. With the new transformational Nutritionals capability, the Group is evolving its scaled dairy capabilities into a high value added protein based ingredients and consumer application platform.

Increasing revenues from the current and expanded capabilities, including ingredients and new consumer applications, are expected to materially positively impact sales and earnings into 2nd half FY 2020 and beyond.

Financial Summary

The Group delivered an improved financial performance with higher sales revenue and earnings. Further investment in innovation, brand and market development assisted in growth in key business divisions and markets.

The Group recorded Net Sales Revenue of $299.7 million, an increase of 43.4% on the previous corresponding period.

Operating EBDITA rose 55.6% on the previous corresponding period to $32.7 million. Gross margins increased to 27.1% from 24.7%.

The result reflected increased sales and earnings contributions from Dairy Beverage, Nutritionals and Plant Beverage business units, offset by reductions in Cereals & Snacks and Specialty Seafood as compared to the previous corresponding period.

The Group achieved an operating net profit after tax of $9.1 million, a gain of 42.1% on the previous corresponding period, reflecting increased operating EBDITA, offset by higher depreciation and amortisation costs as compared to the previous corresponding period.

Statutory net profit after tax was $5.4 million. This included one off non-operating costs of $3.4 million relating to discontinued operations, pre-acquisition costs and unrealised foreign exchange losses .

The statutory income tax expense reflects an effective tax rate of 34%. The higher than normal tax rate is due to the impact of overseas operations including the newly established Chinese wholly owned enterprise (WOFE) and non recognition of losses from changes to the North American operation.

A summary of the key business unit financial performance is outlined below:

- Dairy and Nutritionals operations at Shepparton delivered increased sales growth, reflecting increasing demand in Australia, China and SE Asia. Total earnings contribution improved through the following:
    - increased sales, increasing sales mix to higher margin dairy components and factory utilisation during the period.
    - The integrated dairy nutritionals operation contributed to sales and earnings growth in the segment.
    - Consumer Nutritionals contributed a growth in sales and earnings. Sales growth was impacted on a comparable period with discontinuance of certain bars and drinks formats in 2nd half FY 2019.
    - The Dairy and Nutritionals sales revenues included $22.6 million in bulk milk sales, relating to Spring peak milk not able to be processed at Shepparton due to commissioning of new plant and equipment. In the 1st half period, the bulk milk sales contributed a negative contribution of $2.5m, which was expensed in the result. This is not expected to reoccur.
- Plant-Based operations delivered increased sales, reflecting growth in retail and out of home brands, with operating earnings contribution materially ahead of the prior year period. Total earnings contribution improved through increased sales, increasing sales mix to higher margin channels in out of home and SE Asia and factory utilisation during the period.
- The Cereal and Snacks operations delivered increased branded sales in key branded products in cereals and snacks. Overall the sales and earnings contribution were below the prior comparable period, reflecting the impact of:
    - A decision in FY 2019 to exit a number of major contract manufacturing arrangements for key brand and private label customers in cereals and milling related activities. While the Group has made significant progress in rebuilding these contract sales through its own branded sales, higher trade investment and lower factory utilisation impacted the earnings contribution.
    - Higher trade and promotional costs in 1st half period reflecting expensing of major retail trade promotions in September 2019 associated with Messy Monkeys, Heritage Mill and Arnolds Farm brands.
    - The Group expects ongoing growth in key brands Messy Monkeys, Heritage Mill and Arnolds Farm to drive an increased sales and earnings contribution. A focus on building out the portfolio through snacking formats including in house manufacture of current and new protein snack formats is expected to provide for increased factory utilisation over the medium term.
- Specialty Seafood sales and earnings were down on the previous corresponding period. While the business secured price increases that materially offset the impact of the adverse cost and exchange rate impacts experienced in FY 2019, the impact of significant prices rises for Salmon impacted consumer demand delaying an improvement in earnings contribution.
- With increasing focus on building the Group's brands, the Group increased investments in brand building and marketing as well as in retail and other channel trade activities.
- Group Services costs increased, primarily reflecting a significant investment in sales capability in Australia (retail, out of home), SE Asia and China, quality and finance capability necessary to manage the growth of the Group.
- During the period, the Group established a Chinese Wholly Foreign Owned Enterprise (WOFE) to improve service and efficiency within its China operations. The set up impacted sales for China operations during the period due to timing difference relating to invoicing of sales in China ex warehouse as compared to ex factory in Australia.

Underlying vs. Statutory EBDITA

Set out below is a reconciliation of statutory EBDITA to underlying Operating EBDITA

6 Months to 31th December (A$ million)	2019	2018	$ Change	% Change
Underlying Operating EBDITA (1)	32.7	21.0	11.7	55.6%
Other costs not representing underlying performance (2)	(3.4)	(2.7)	(0.7)	
Employee Share Option Expense (non cash) (3)	(0.8)	(1.0)	0.2	
Statutory EBDITA	28.5	17.3	11.2	64.6%

Note:

1. *Operating EBDITA (Earnings before depreciation, interest, tax and amortisation) is a non-IFRS measure as contemplated in ASIC Regulatory Guide 230 Disclosing non-IFRS financial information (RG230). Operating EBDITA is used by management and the directors as the primary measures of assessing the financial performance of the Group and individual segments.*
2. *1H FY 2020 other costs not representing underlying operating performance includes one-off non-operating costs of $1.4 million, acquisition costs of $0.9 million, unrealised foreign exchange loss of $0.4 million and bank facility financing fees of $0.7 million.*
3. *Non cash employee share option expense of $0.8 million* in 1H FY 2020.

Segment Financials

6 Months to 31 December 2019 (A$ million)	Dairy & Nutritionals	Plant Based	Cereal & Snacks	Specialty Seafood	Other	Total
Net Sales Revenue	184.7	64.6	43.4	7.1		299.7
Trading EBDITA	23.9	21.0	2.3	0.1		47.4
Equity Associates (1)					0.7	0.7
Corporate Costs (2)					(15.4)	(15.4)
Operating EBDITA	23.9	21.0	2.3	0.1	(14.7)	32.7
Net Sales Change (YOY %)	+65.2%	+39.5%	0.6%	-9.4%		+43.4%
Net Sales Change (YOY $m)	72.9	18.3	0.3	(0.7)		90.7

Note:

1. *Equity Associates is share of NPAT of Australian Fresh Milk Holding Australia and Australia's Own Dairy (JLL) (10% equity interest held in each by Freedom Foods Group).*
2. *Shared Services costs includes sales and group services, it excludes non-cash employee share option expenses of $0.8 million.*

Key Financials

6 Months to 31 December 2019	2019	2018	
	$'000	$'000	% Change
Net Sales Revenue	299,690	209,041	+43.4%
EBDITA (Underlying Operating) (1)	32,672	21,003	+55.6%
EBDITA (Statutory)	28,480	17,309	+64.5%
Equity Associates Share of Profit (2)	744	240	+210.0%
Pre Tax Profit (Operating)	12,601	8,878	+41.9%
Pre Tax Profit (Reported)	8,410	5,184	+62.2%
Income Tax (Operating)	3,528	2,492	+41.6%
Net Profit (Operating)	9,073	6,386	+42.1%
Net Profit (Reported)	6,687	3,729	+79.3%
Final Ordinary Dividend (cps)	2.25	2.25	-
EPS (cents per share) (Fully Diluted for CRPS)	1.81	1.86	-2.7%
EPS Operating (cents per share) (Fully Diluted)	4.13	2.92	+41.3%
Shareholder Equity	676.5	532.3	+27.1%
Net Debt / Equity	27.9%	30.8%	
Net Assets per Share (cents)	246.3	217.4	+13.3%
Net Tangible Assets per Share (cents)	193.1	165.5	+16.7%

Notes:
1. *Equity Associates is share of NPAT of Australian Fresh Milk Holding Australia and Australia's Own Dairy (JLL) (10% equity interest held in each by Freedom Foods Group).*
2. *Shared Services costs includes sales and group services, it excludes non-cash employee share option expenses of $0.8 million.*

Dairy and Nutritionals Business Group

Dairy Beverages

Branded Portfolio

Dairy based branded beverage sales continued the upward sales and profit trend from FY 2019, reflecting increased sales of the Australia's Own brand and other brands in domestic out of home and export markets.

Australia's Own Dairy Range

Taking the Best of Australia to consumers across Australia, SEA and China.

As part of its strategy to build the Australia's Own brand as a leading beverage brand in Australia and key export markets, the Group launched late in FY 2018 a range of Australia's Own UHT dairy milk products. The expanded portfolio now includes full fat, A2 protein, lite, skim milk and lactose free products in 1 litre and 2 litre formats.

In the Australian domestic retail market, the brand has built a 20.1% (MAT) share of branded UHT white milk in a little over 12 months since launch. The Australia's Own Dairy products are also being expanded into key sales channels in SE Asia, with increasing market penetration in Singapore, Vietnam and Philippines. We see a great opportunity to build Australia's Own across the Asian markets with demand continuing to increase.

Australia's Own Kids Milk

Largest imported kid's milk brand in China

The "Australia's Own" branded "Kid's Milk" product continued to grow sales and distribution during the period, with the product remaining the largest imported kid's milk brand in China.

The brand continues to be supported with marketing investment including point of sale promotion, sampling and sponsorship of leading China (CCTV) national children's TV programmes. The brand is well established in key cities and provinces in China, with further distribution expansion expected into 2020.

The Group currently supplies a range of formats including 200ml base format, 200ml leaf format for exclusive use in e-commerce channels and an A2 Protein Milk variant. Further product innovation to build on this strong consumer brand is planned for FY 2021 with further growth expected into 2020.

Australia's Own Dairy Company China (trading as JLL)

The Group subscribed in May 2018 for an initial 10% investment in AO China for a consideration of RMB22 million (AUD$4.7 million). It retains an option to subscribe for up to an additional 20% of AO China within three years from the date of the initial subscription.

The AO China business has continued to grow strongly since its inception, with sales in in the year ended 31 December 2019 in the order of RMB 350 million (AUD$76 million). The business has invested significantly in sales and marketing and achieved a small profit contribution in the 2nd half of calendar 2019.

Contract Manufactured Dairy – Australia, China and South East Asia

Largest Australian supplier of UHT Dairy to Australia, China and SEA Contract Customers

Sitting alongside our brand expansion, Freedom Foods is the largest Australasian supplier of contract manufactured milk to the Australian, Chinese and SE Asia markets. We have a range of long standing as well as new relationships with key brand owners and retailers across all jurisdictions.

In Australia, the Group supplies a number of long-term retail customers that provide a strong base of underlying volume and earnings support. The Group continues to supply a number of key relationship customers in China including major dairy manufacturers and brand owners. In SE Asia, the Group has developed customer relationships in markets such as Singapore, Malaysia, the Philippines and Vietnam. A number of new customers are expected to start supply as new filling capacities come online during CY 2020.

Shepparton UHT Operations

During the period, volume throughput at Shepparton increased as additional retail, other contract customers and Group branded product supply commenced. Additional volumes will commence through calendar year 2020, reflecting demand in Australia, SE Asia and China and increased capacity.

Total dairy milk volume processed in the period was in excess of 150 million litres compared to 107 million litres in the previous corresponding period. The Group estimates dairy milk volume processed in FY 2020 to be upwards of 350 million litres. Sales of dairy based components including cream will also increase.

New Capacity

Largest investor in UHT dairy technology and capacity in Australia

During the period, the Group finalised the upgrade to double total processing capacity to 500 million litres per annum, with additional filling and services upgrades being completed.

This doubling of processing capacity aligns and supports growth in UHT filling capability at Shepparton to meet demand in domestic and export markets including SE Asia and China.

The Group expects the remaining filing and services upgrades to be completed by June 2020, bringing to completion all the UHT expansion initiatives planned.

Dairy Supply – Australian Fresh Milk Holdings (AFMH)

Australia's largest dairy milking operation

AFMH operates Moxey Farms, a fully integrated dairy farming operation located in the Lachlan Valley, New South Wales and Coomboona Farms in the Goulburn Valley in northern Victoria.

The Coomboona Farms operation in northern Victoria was acquired in January 2019, expanding AFMH's production platform in a renowned dairy farming region. In November 2019, AFMH acquired the Torrumbarry Aggregation comprising 4,083 hectares on the Murray River, 100km north of Shepparton. The acquisition included significant water rights.

The purchase of the Torrumbarry Aggregation provides the opportunity to develop a scaled young stock operation enabling accelerated growth plans at Moxey Farm and Coomboona Farms to support increased capacity in milking cows.

With the acquisition of the Torrumbarry Aggregation, AFMH is the largest dairy producer in Australia with current operations forecasting over 190 million litres of production annually by the year ending 30 June 2021.

Freedom Foods is utilising a growing proportion of the dairy milk output from Coomboona Farms for its Australia's Own Kid's Milk and other dairy product formats.

AFMH is a strategic partnership owned by the Perich and Moxey families, New Hope Dairy Group and Freedom Foods Group. FNP has a 10% equity shareholding in AFMH.

The total investment in AFMH at 31st December 2019 was $22.9 million, with an additional $4m invested in the period as part of the equity contribution to the acquisition of the Torrumbarry Aggregation.

Direct Dairy Milk Supply and Outlook

During the period, the Group continued to build on its "Freedom Farmers" sourcing strategy, establishing direct supply contracts with dairy farmers in Victoria and southern New South Wales that produce consistent high-quality dairy milk.

The direct supply strategy seeks to align a multi-year volume, quality and pricing relationship that supports the growth demands of the Group and provides our farming partners with certainty and a stable revenue basis to invest in their farms.

As at 31st December 2019, the Group had more than 60 direct suppliers supplying in excess of 300 million litres per annum. With the existing long term contracted supply of 100 million litres from Australian Consolidated Milk (ACM), total supply in FY 2020 expected to be 400 million litres per annum.

The Group's partnership with AFMH provides a level of underwriting of further growth in milk supply in the medium to long term, with an ability to increase offtake, reducing any reliance on recruitment of new suppliers. A number of other current larger direct suppliers also intend to grow their supply within this time frame.

The Group has established supply relationships based on multi-year contracts at prices broadly in line with average prices being offered by other processors. Some increases in milk price arrangements during the period to encourage growth in supply are being materially offset through increased UHT dairy milk pricing and higher prices for dairy components including cream.

The Group remains confident in its ability to access milk in relation to its long term growth strategy, with milk supply in FY 2021 expected to be around 430 – 440 million litres.

No direct milk supply source was impacted by the recent bush fires in Victoria and New South Wales.

The Group noted retailers implementing higher retail pricing for all dairy products (including fresh and UHT) in Australia to assist in building a sustainable supply future.

Nutritionals Business Group

The Group is leveraging its significant and growing dairy capabilities to build a branded high margin product portfolio in specialty nutritional products.

As part of this, the Group completed through calendar 2019 the first stage of a specialised nutritionals platform aligned to the dairy UHT operations at Shepparton. The platform provides for protein standardisation and the ability to manufacture high grade protein components for use in our branded products and for sale to strategic customers.

Following MCC production commencing late in FY 2019, the Group commenced sales of Native Whey Protein Isolate (WPI) and Lactoferrin (LF) during the period. As awareness grows of the new capabilities, the Group continues to see strong customer demand for the broad range of protein streams, aligned to previously announced long term contractual commitments.

The Group is well progressed on commercialising a number of these key ingredients into applications under its own brands, including in Sports Performance, Diet and Adult Nutrition as well as consumer applications for Lactoferrin.

Performance Nutrition Brands

Vital Strength is the leading brand in Chemist Warehouse

The Vital Strength brand is recognised as a leader in high quality nutrition products, sold through retail grocery, pharmacy and fitness retailers in Australia.

During the period, the Vital Strength brand increased sales and profit contribution from key customers and channels. Into the 2nd Half FY 2020, the Vital Strength range will be expanded across its core portfolio and through new product formats including pre-workout shots and pre-workout powders specifically formulated and sized for different channels. A new “Pure” range based on internally produced Native WPI will also be launched into the Performance retail channel.

Crankt Protein Brand

Fast growing brand in Petrol and Convenience

The Crankt Protein beverage and snack bar range is sold through petrol and convenience chains, fitness retailers and retail grocery outlets in Australia and New Zealand.

The Crankt brand performed well in the latest period, with growing sales through increased distribution and consumer uptake in both retail supermarket and petrol and convenience chains. The range was expanded with innovation in protein snacking formats.

The Crankt range has further growth opportunities through expansion into out of home and petrol and convenience channels.

Vital Life Health

In February 2020, the Vital Life Health brand was launched through VITAL LIFE™ Immune Shot with Lactoferrin.

The new product contains Lactoferrin, manufactured by the Group, providing a new innovative way to access an ingredient that helps to fight bacteria and viruses, providing comprehensive immune support.

The new Shot packaging delivery format is based on innovative technology that provides for delivering an easy to consume liquid combination with a long shelf life. This provides a new consumer experience beyond traditional pills and powders.

A range of new products to be launched under the Vital Life brand will seek to provide high value added scientifically proven ingredients in innovative consumer formats that assist in improving overall health and wellness. The core functional ingredients will be based on high grade protein components sourced from our Shepparton Nutritionals capability.

The Vital Life Immune Shot will initially be launched for online sale, with retail distribution expected to be launched from late April 2020.

Plant-Based Business Group

Branded Portfolio

Strong growth in Australia's Own, MilkLab and Blue Diamond brands in Plant-based beverages

Plant-based branded beverage sales continued to grow, with significant volume growth of 27% and sales revenue growth of 42% compared to the previous corresponding period, reflecting growth in the Australia's Own range, MilkLab range and the licenced Blue Diamond Almond Breeze brand in retail and out of home channels.

The trend towards plant-based food and beverages is increasing in Australia and global markets, driven by a desire for healthier and "cleaner" lifestyles which is motivating consumers to focus on fruits, vegetables, nuts, seeds, grains and other botanicals.

In retail grocery, the Group remains the largest supplier of almond beverages, including products under the Australia's Own brand, our licensed Blue Diamond Almond Breeze brands and private label offers.

The Group continued to experience strong growth in the high margin out of home channel with both MilkLab and Almond Breeze Barista having established a clear market leadership in the almond segment of the milk for coffee market. Increased channel penetration and consumer demand is expected to continue to drive growth, with the Group expanding the range of plant based beverage products under the MilkLab brand.

The Group has also secured distribution with a number of major speciality food chains & quick service restaurants, reflecting the capability to provide a range of options for plant beverages as well as complementary dairy offers including lactose free dairy milk.

During the period, the Group invested in sales and distribution to develop new channels in SE Asia and the Middle East, with increasing sales of the Australia's Own range and MilkLab.

The MilkLab brand is experiencing strong demand across existing markets in Australia and new markets into SE Asia, the Middle East and has the potential to be a leading global plant-based beverage brand in the milk for coffee markets.

UHT facility at Ingleburn, south west Sydney

The state-of-the-art UHT facility at Ingleburn in south west Sydney has performed well since start-up and commissioning in December 2017. Increasing volume growth in plant based beverages continues to validate the decision to build a facility with capability to provide for long term growth.

With the increasing growth in plant based beverages in Australia and export markets, the Group brought forward increases in faster and more efficient filling capacity, with these installations and upgrades to be completed by June 2020. The investments will bring total filling capacity to 210 million litres per annum, with further scope for growth within the facility over the longer term.

A significant advantage in working with major customers including speciality food chains is the ability to provide scaled manufacturing capacity over the longer term.

Capabilities for yoghurt processing completed during 2019 provided for domestic and product launches in SE Asia during the period. While China's demand for yoghurt is strong, sales are subject to receiving Chinese government accreditation for the Ingleburn facility for yoghurt production at some stage in the future.

Cereal and Snacks Business Group

Australia

Number 1 health food cereal brand and growing

The Freedom Foods business is the category leader in the cereal and snacks segment found in the health food sections of retail supermarkets. Freedom Foods branded products delivered sales growth in its branded Cereal and Snacks segments compared to the prior year period.

The Messy Monkeys brand continued an impressive growth trajectory, supported by strong trade and external marketing activity. The brand is the No 1 selling "new" brand in the health food section of supermarkets and has expanded its core range with popcorn and extruded snacks variants. During the period, the Messy Monkeys brand was launched into the mainstream cereal & bar category and has been performing well since launch.

The Freedom Foods Arnold's Farm brand performed well in its oat based cereal products through its exclusive distribution in Australia with Woolworths supermarkets. The brand's footprint has expanded in domestic retail & now includes snack bars.

In June 2018, the Group launched an expanded range of Freedom Foods branded cereals and snacks in the mainstream retail channels in Coles Supermarkets under the brands Heritage Mill and Brekky Heroes. Since introduction, the products have performed well. The Heritage Mill brand has already achieved a 30.1% share (MAT) of the breakfast cluster and muesli category in Coles Supermarkets.

The Group is confident that the growth and opportunities provided by a focus on its own brand strategy & exiting a number of major contract manufacturing attrangements in FY19 will provide for increased financial returns in the medium to long term. Strong demand in the Heritage Mill and Arnold's Farm brands and increased demand in exports markets provides a strong foundation for success.

China, South East Asia and Other Regions

Leading cereal brand on Alibaba's Tmall International

Within the online cereal category, sales have progressed well, with further growth achieved and increasing brand recognition in this small but growing category in China.

The Freedom Foods Arnold's Farm brand remains one of the top three oat cereals on Tmall International. With increasing consumer awareness of this developing category in China, the Group is innovating to provide for ongoing growth in the category. Sales in offline channels in China reduced as the business transitioned to new arrangements for offline sales through its partnership with Theland. Sales are expected to increase into 2020 as our new offline distribution structure commences.

In North America, reflecting a focus on building our Australian and Asia platform, the Group will discontinue its current operations to be managed through a new distribution arrangement with Atlantic Natural Foods. Under the arrangement, Freedom Foods product ranges including Allergen Free Cereal, Messy Monkeys Snacks and other private label business will be maintained and sold through Atlantic Natural Foods, acting as exclusive distributor for this product range and other products developed in the North American market. All sales, marketing and distribution expenses will be managed by Atlantic Natural Foods.

Specialty Seafoods

Number 1 sardine brand in Australasia and stable salmon market share

Brunswick Sardines maintained its No. 1 brand leadership position in Australia and New Zealand, with some growth achieved in the latest period following innovations introduced in FY 2019.

The Paramount Salmon brand maintained market share, however, sales were impacted by a declining category reflecting significant consumer price increases late in FY 2019.

While the business secured price increases that materially offset the impact of the adverse cost and exchange rate impacts experienced in FY 2019, the impact of significant price rises for Salmon impacted consumer demand, delaying an improvement in earnings.

Innovation Capabilities

The Group will continue to be a leading innovator in its chosen product and channel segments.

As part of this, the Group continues to invest significantly in its innovation capabilities across its business groups. This investment, aligned to its significant capital investment in manufacturing capabilities, provides a strong base to accelerate new product development pipelines. In the last five years, the Group has invested in excess of $62 million in product development.

Expenditure of $7.6 million on product development in the period materially reduced from the prior year period expenditure of $13.2 million. Amortisation of new product development costs capitalised in previous periods now exceeds the expenditure being incurred on new product development. Sales from new product development initiatives since 2017 contributed $93.0 million (31% of total sales) in the latest half year period, up from $58.9 million in the prior corresponding period.

A total of 41 new products were launched from July 2019 into retail grocery, out of home and export markets, supported by increased marketing expenditure.

The Group continues to receive awards for product development innovation, including the recognition *as* Product of the Year for Messy Monkeys bars and Australia's Own Like Milk and additional awards for Barley Plus and Active Balance breakfast cereals by Healthy Food Magazine.

Capital Expenditure

As one of Australia's leading investors in state-of-the-art food and beverage manufacturing capability, the group accelerated the final stages of its major capital investment program, with key programs including:

- At Shepparton, the Group finalised the upgrade to double total processing capacity to 500 million litres per annum, with additional filling and services upgrades being completed.
- At Ingleburn, NSW, the Group brought forward increases in filling capacity to provide for growth in plant based beverages in Australia and export markets.
- Fast tracked stage two of a transformational Nutritionals capability, with the planned capacity upgrade for Lactoferrin underway to provide for 40tn of capacity from July 2020 to meet contracted requirements into 2021.

As noted in August 2019, the FY 2019 year reflected a peak in the five year investment cycle with capital expenditure expected to materially reduce. The Group expects a large proportion of its remaining investment program to be completed in FY 2020, bringing forward some aspects of timed FY 2021 expenditure. The Group anticipates FY 2021 capital expenditure to be less than the depreciation expense for that period.

The capital expenditure program provides a strong operational platform to significantly increase the Group's sales and operating financial returns.

Depreciation of capital equipment was $9.9 million in the half compared to $5.1 million in the previous corresponding period, reflecting the transfer of an increasing proportion of development capital expenditure to fully operational capital equipment.

Corporate and Group Management

Talent and Technology

The Group continued to make investments in people and capability to ensure the Group can implement and manage growth. During the period, we invested in talent and capability in sales and innovation as well as increased capability in operations including reliability and quality processes.

We are developing our people and talent identification processes to align with the Group's rapidly expanding sales and operational platform. During the period, the Group further progressed the transformation of its IT / ERP systems. Further investments in technology is required to ensure we increase efficiency and productivity.

Capital Management

Liquidity and Finance Facilities

Cash generated from operations represented a material improvement from the prior corresponding period. With the winding down of the significant capital expenditure period, the Group is working to improve the management of inventory holdings including packaging and raw materials, while maintaining capability to manage velocity in key areas of the business.

While some progress has been made, the Group sees further opportunity to improve working capital and expects a further material improvement in operating cashflow in the 2nd half of FY 2020.

The Group held net total borrowings of $188.5 million, comprising term facilities, equipment finance leases and working capital facilities, with a net debt to equity ratio of 27.9%.

In December 2019, the Group entered into a new secured syndicated and bi lateral banking facility with its long term banking partners HSBC and NAB, replacing the existing club facility which was due to expire in December 2020. The new facility provides a more flexible finance and liquidity structure to assist in the ongoing growth of the Company over the medium term. The term of the new $407 million facility is three years. The Group does not utilise any form of reverse factoring (ie supply side financing).

During the period, the Group invested $66 million in capital expenditure relating to the balance of construction and equipment payments, commissioning and related costs for the capital expenditure on plant and equipment at Shepparton, Ingleburn and Leeton, technology platform development, and deposits for capital expenditure relating to expanded capital projects committed to in the 1st half of FY 2020. Capital expenditure also included payments for assets that would previously have been acquired and funded as operating leases.

Dividends

The Group will pay an unfranked interim dividend of 2.25 cents per ordinary share on 22nd May 2020.

As noted in FY 2019, the Group intends to pay an unfranked dividend for any dividends relating to FY 2020, reflecting likely reduced tax payments as the Group utilises tax losses from acquisitions and accelerated tax depreciation benefits from the current investment phase. The Group anticipates a return to paying fully franked dividends from increased profits after FY 2021.

The record date for determining entitlements is 27th March 2020 and the payment date is 22nd May 2020. The Group's Dividend Reinvestment Plan (DRP) is no longer open.

The Group will pay an unfranked interim convertible redeemable preference share dividend in accordance with the terms of the convertible redeemable preference shares. The record date for determining entitlements is 27th March 2020 and the payment date is 22nd May 2020. There are 101,130 converting preference shares remaining on issue at 31st December 2019.

Group Outlook

Building a Global Food and Beverage business based in Australia

The Group is well positioned to build into a major global food and beverage business with scale in key food and beverage platforms, providing strong diversification in sales, together with earnings growth, from key markets and channels in Australia, China and SE Asia.

Our key brands Australia's Own and Freedom Foods will be at the forefront of driving our returns from our innovation and manufacturing capabilities in Australia and international markets. New brands recently launched also have the potential to be global success stories; MilkLab and Messy Monkeys have been extremely well received and are expanding at a strong rate.

The growth in sales and financial returns in our Plant beverage business reflects the investment in brands and new capabilities at the Ingleburn site in Sydney. This business is expected to materially contribute to profitability over the medium term as the Group focuses on driving its brands in retail and higher margin out of home channels and into SE Asia and China.

With a large and significantly increasing base of dairy volume within the Group, the focus is on driving the dairy business towards specialty and high value-added products. New product revenue streams from the Nutritionals capability are expected to materially positively impact sales and earnings into FY 2020 and beyond.

The cereal and snacks business are strategically well positioned to build a growth platform in multiple products, channels and distribution across Australia, China and SE Asia. The decision to exit a large a number of major contract manufacturing arrangements has released capacity and capability for our own brand strategy and provide for increased financial returns in the medium to long term.

The Group continues to experience strong demand across its business activities in key channels and markets. This growing demand in dairy, plant-based beverage and cereal and snacks reflects the positive impacts on our expanded operational footprint and increasing brand penetration and market share in key channels and categories in Australia, SE Asia and China.

While the Group expects some short-term disruption to China demand over the next few months as internal supply chains in China return to normal operation, the underlying medium-term demand from key customers in this market remains unchanged, with the Group scheduled to start supply to new China based customers from June 2020. Sales to China represent approximately 15% of our net sales value in the current half year. The increasing scale and diversification of the Group's activities provides an important hedge to assist in mitigating potential impacts from short term disruption to markets.

We expect the Group to deliver higher sales and earnings growth in the second half of FY 2020, reflecting seasonality and further growth across key business activities.

For further information, please contact:

Rory J F Macleod
Managing Director and CEO
Freedom Foods Group Limited
+612 9526 2555

Stephanie Graham
Group GM, Corporate Development
Freedom Foods Group Limited
+612 8543 3525

Media Enquiries:

Ian Pemberton
P&L Corporate Communications
+ 61 402 256 576

FNP Forward Looking Statement

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