



FY2019 Full Year Results

28 August 2019

Slide 1 – Welcome

Good morning everyone, and welcome to the results announcement for Bega Cheese for the full 2019 financial year. I am Max Roberts, Chairman of the Board and with me today is CEO Paul van Heerwaarden and CFO Colin Griffin. Paul and I will present the full year result and Paul, Colin and I will be available to answer questions following this presentation.

Before I begin, I would like to mention Barry Irvin our Chairman who is on extended leave due to health issues. I wish him all the best for his recovery and I know he will be back in this seat for the FY2020 half year results presentation.

Slide 2 – Key messages

Ladies and gentlemen, it is important to say up-front that Bega Cheese has delivered a solid result in what has been a challenging year. Both the dairy and FMCG industries have experienced major structural changes in competitive domestic and international environments. While we have maintained a strong competitive position, the ongoing drought resulted in a significant reduction in Australia's milk pool and higher costs across our business. The challenges in dairy and international trade required us to maintain our focus over the year on productive investments, efficiencies and developing markets that support our strong underlying profit contribution.

The acquisition of the Koroit facility in August 2018 provided significant processing capacity and capability into our network and an extra 300 million litres of milk supply. We welcomed over 100 employees with the acquisition and are benefiting from their significant experience and capabilities. Due to Koroit we are now better able to meet the growing industry challenges adding important flexibility, geographic diversity and scale to our network.

I should also mention the closure of the Coburg cheese site in February. It was difficult for those affected but this rationalisation was essential. Our new toll processing arrangement for cheese production has utilised existing capacity in the industry and had a positive impact on our network.

Bega raised \$200 million through an Institutional Placement and Share Purchase Plan finalised in October 2018 resulting in the issue of 27.8 million shares. The funds from the capital raising were applied in reducing total debt following the acquisition of the Koroit facility.

Finally, we look forward to the value to our business of the Enterprise Resource Planning system implemented in FY2019 which is an important factor in our future growth.

The next slide puts the 2019 financial year into context.

Slide 3 – Transformation to becoming ‘The Great Australian Food Company’

It has been great to see the significant growth and development trajectory since our ASX listing in 2011. I have been on the Board of Bega for 36 years and have seen Bega becoming *The Great Australian Food Company*. The move from a supply driven co-op to a market and customer focused organisation has been challenging but ultimately rewarding for the entire Group. Since 2011, the focus has been on establishing corporate wide foundations, diversifying our range of products and strengthening our customer relationships and market shares. Looking to the future we are now focused on investment, innovation, optimisation and strategic alliances that will continue this transformation process.

The next slide details where this growth plan will take us.

Slide 4 – Accelerated growth plan

We are committed to an effective and efficient supply chain network, increasingly diversifying our products and channels to market and prioritising investment in important long-term initiatives.

The acquisition of Bega Foods in 2017 provided Bega Cheese with a new sales and marketing capability. We have launched some exciting new products in 2019, such as gluten free Vegemite, our range of Simply Nuts peanut butter and a portfolio of products under the new Farmers Table brand. The acquisition of Koroit has complimented our range of consumer dairy products, providing us new capacity in butter and milk powders in consumer formats.

The Koroit facility has also expanded our processing capacity and improved access to a strong and growing milk pool in western Victoria. This facility has strengthened our dairy network and will allow us to realise further savings from manufacturing optimisation and efficiency programs. To gain the most value from our integrated supply chain, it is important that we align milk supply with our asset capability and capacity across our network.

I am pleased to say that we have continued to invest in our manufacturing network with increased automation and improved yields. The continuous improvement program which commenced in FY2018 and has continued in FY2019 and has generated significant savings across our supply chain and that program will now extend to other aspects of our supply chain and cost base as we respond to a challenging dairy supply market.

Bega Cheese continued to invest in growth projects. During 2019 the company invested in new consumer lines at our Port Melbourne facility. We also increased the capacity of our lactoferrin plant at Tatura and commenced construction of a new lactoferrin plant at Koroit. We are diversifying our revenue streams, with strong growth in 2019 in our international branded consumer goods business and an expansion of our customer base in nutritionals.

As part of our early growth phase, Bega Cheese relied on long term strategic alliances to support scale and investment. As the business diversified and invested in new sales and marketing capabilities, we have become less reliant on those traditional alliances. As we further diversify our customer base and become more relevant in global markets, we expect to form new strategic alliances and partnerships, building on our reputation of supplying high quality products and creating shared value.

Slide 5 – Bega Values

During FY2019 the Board and the Executive reviewed and refreshed the values of Bega. These values are important not only for our employees, but to our customers, suppliers and the communities in which we operate. The values are: Passion for the customer, invest in our future, support each other and grow our people. Bega has a proud history built on maintaining a strong reputation amongst our wide range of stakeholders – from farmers, our workforce of over 2,000, our consumers, suppliers, and the Australian public, and our customers in many parts of the world.

I'll now hand over to Paul to take you through the financial results and the details of the operational performance.

Slide 6 - Revenue analysis

Thank you, Max, and before I start, I too would like to mention Barry and wish him well in his recovery.

Overall in FY2019 I am pleased to say we saw strong growth in our core branded consumer and food service business in both the domestic and international markets. Our strong performance in export dairy ingredients and branded product which continues to grow represents 31% of revenue.

Having Koroit in our network with the capacity to process 900 million litres of milk into a range of milk powders and butter products has been and will be fundamental to our servicing domestic and international retail, food service and nutritional customers.

The nutritional and bio-nutrient business has provided strong profit growth with our ongoing diversification of product categories, customers and markets. The increasing trend into goat milk infant formula lead to a processing deal with Bubs. The demand for organic infant formula is also continuing which sees us working with both domestic and international customers on new formulations and supply which will be launched during FY2020.

We have also launched into the domestic market new brands of dairy and spreads products which I will talk about in more detail later.

Slide 7 – Performance highlights

In a very challenging year in the Australian dairy industry, I am pleased to report that Bega Cheese generated a record normalised earnings before interest, depreciation and tax (EBITDA) of **\$115.4 million** in FY2019, being an increase of 5% over the prior year. On a statutory basis Bega Cheese generated EBITDA of **\$89.5 million**, being 3% below the prior year. Milk intake increased by 308 million litres to total a record **1.06 billion litres** in FY2019 and we manufactured a record **280,405 metric tonnes** of dairy and other products.

Bega Cheese generated record revenue of **\$1.42 billion** in FY2019, up by 13%. Export sales increased by 4% to **\$442 million**, with the Group exports to key markets in south east Asia, Japan, China and the Middle East representing the majority of our export business.

Slide 8 – Reconciliation of normalised results

Transaction costs related to the Koroit acquisition, the closure of the Coburg facility, legal costs relating to litigation and management information system deployment all resulted in material abnormal costs to the business. We provide more details on these items in the Annual Report.

On a statutory basis the group generated net profit after tax (NPAT) of **\$11.8 million** in FY2019, being down 59% largely as a result of high depreciation and amortisation from recent capital investments, interest from higher borrowings throughout the year to fund acquisition costs and working capital and a higher effective tax rate from the tax treatment for acquisition costs.

Slide 9 – Balance sheet

The balance sheet as at 30 June 2019 was in good shape, with total assets of **\$1.489 billion**, total liabilities of **\$663 million** and shareholders' funds of **\$826 million**.

Trade receivables and other receivables decreased by \$42 million from the prior year, with the introduction of a Trade Receivables Facility from March 2019 significantly reducing the balance as we derecognised \$188 million of eligible trade receivables as at 30 June 2019.

As foreshadowed in the first half FY2019 Interim Report, the significant seasonal build-up of inventory at the half-year was managed down in the second half, although at 30 June 2019 inventory was still up by \$63 million on the prior year, primarily as a result of the Koroit inventory.

Property plant and equipment and intangible assets increased materially during the year, largely as a result of the Koroit facility acquisition.

Net debt totaled \$288 million at 30 June 2019, being an increase of \$42 million. The group continues to have the strong support of its banks, Rabobank and Westpac, who fund our syndicated debt facility, with Rabobank also providing an Inventory Facility and a Trade Receivables Facility.

I will now move on to our cashflow.

Slide 10 – Cash flow

Including proceeds from transactions relating to the Trade Receivables Facility, which generated inflows of \$188 million, the Group generated net cash flow from operating activities of \$100 million.

As mentioned earlier the most significant cash outflow in the period related to the acquisition of the Koroit facility, which cost \$251 million, before acquisition costs.

Slide 11 – Group sales

Bega Cheese has had a history of steady growth in revenue, with FY2019 continuing this trend.

Group sales have increased by 13% to \$1.42 billion in FY2019, which was largely due to revenues associated with the Koroit acquisition.

Other key growth initiatives during the year included a further diversification of our customer base in nutritional and innovation in our branded consumer goods business.

Slide 12 – Our consumer brands

The Mondelez Grocery business had a limited innovation pipeline when we acquired it two years ago. We are now starting to see the benefit of our investments in new product development.

During the year we launched 41 new branded products or product variations. We also launched three new brands, Simply Nuts, Farmer's Table and Modern Chef which is an exclusive brand developed for

Woolworths. For the first time these brands expand our retail offerings to cream cheese and butter in the domestic market.

The launch of Gluten Free Vegemite during FY2019 has made this iconic Australian product available to even more consumers. The licencing of the Vegemite brand also saw the successful launch of Arnott's Vegemite Shapes providing further promotion and income generation.

Bega Simply Nuts was launched into the high-growth all-natural peanut butter segment. Our product is made from 100% Australian peanuts sourced from our Kingaroy facility. The range has strong momentum heading into FY2020. Kingaroy continues to play an important strategic role by providing high quality Australian peanuts as an ingredient for our peanut butter and snacking products. The Picky Picky nut snacking product range is now available in Coles and the Dairymont food service brand was also relaunched during the year in the domestic market.

In May this year the Federal Court of Australia ruled on Bega Cheese's right to continue to use its trade dress associated with the peanut butter products acquired from Mondelez. Legal proceedings continue as a result of an appeal by Kraft.

Since the closure of the Coburg facility in March we continued to develop our domestic and international cheddar and mozzarella cheese business, sourcing cheese from our other dairy sites and through our new external toll manufacturing arrangement. This arrangement has provided increased capacity in our network, removing significant costs and importantly avoiding capital expenditure.

Slide 13 – Dairy commodity and farm gate milk prices

Our dairy ingredients business implemented significant changes whilst managing domestic drought conditions and global commodity market challenges. Commodity price volatility was evident early in the year with high European inventory softening skim powder pricing and lower Asian demand depressing butter prices. As the year advanced, the tightening of supply lead to increases in commodity prices of butter, powder and cheese. This improvement during the 2018 spring peak milk season combined with a weaker Australian dollar, supported seasonal rebates and milk price increases for our dairy suppliers.

With the acquisition of Koroit our milk intake was a record 1.06 billion litres. Koroit provided an additional 300 million litres over and above our FY2018 base milk supply which remained at approximately 750 million litres. This is a great outcome in what is a very competitive market. Whilst we expect continued pressure on margins during this drought cycle, we intend to counter this with continued improved efficiencies across our network.

I'll now move to providing an overview of our operations and sites.

Slide 14 – Operations review

As the company grows, we consistently focus on maintaining the most efficient manufacturing footprint and logistics network possible and making the necessary ongoing changes to ensure we remain globally competitive. The closure of our Coburg facility and the subsequent entry into a toll processing arrangement was part of our broader ongoing consolidation program.

As mentioned earlier, a core component of our success has been the sustained focus on continuous improvement. We achieved significant savings in FY2019 from a range of initiatives including waste reduction, yield improvement, capacity enhancement, labour efficiency and overhead reduction.

Safety performance continues to improve year on year with a 15% reduction in the total recordable injury frequency rate.

Our recently implemented new ERP system replaced four separate systems and required an enormous effort and commitment from every part of the company. Importantly this new system provides a platform for supply and network efficiencies and information systems that will support our ambitious plans well into the future.

Slide 15 – Our manufacturing sites

With the acquisition of Koroit and the closure of Coburg in FY2019, Bega now has a stronger, integrated and flexible dairy manufacturing network. This network provides opportunities to create further value by consolidating the manufacture of certain products on our most efficient assets, such as butter and certain powder products, and to help optimise the value we extract from milk solids.

Bega Cheese continues to invest in a range of capital projects to maintain and enhance our asset base, to provide a safe workplace for our people and to improve our sustainability performance. We also continue to invest in growth and efficiency projects, with investments to support innovation in our consumer goods business during the year, including a new dips line and the Simply Nuts jar line. The company also commissioned an upgrade to the lactoferrin plant at Tatura during the year.

Slide 16 – Our approach to corporate social responsibility

Over the past year we have developed a comprehensive sustainability framework aligned to the United Nations' Sustainable Development Goals to ensure we are constantly improving and meeting community, customer and shareholder expectations. Our key focus areas with detailed and targeted performance measures out to 2030 include improving food nutrition, in particular the reduction of

salt, supporting an increase in the diversity of our people, a reduction in greenhouse gas emissions, improved water conservation and a reduction in packaging waste.

We have established an ambitious energy reduction program with initiatives across all sites which are targeted to deliver up to a 20% reduction in energy use over four years.

We have seen improvements in gender diversity in FY2019 with women now representing 46% of our staff in professional roles, up from 36% in the prior year. We will continue to focus on further increasing diversity across the business.

As a member and signatory to the Australian Packaging Covenant Organisation, we achieved 'Leadership' level for post-consumer recovery and waste diversion criteria.

As a regionally focussed business, the sustainable use of water has always been important for us. We will continue to ensure effective water management in our operations, including initiatives to reduce water consumption and decrease wastewater. A highlight in FY2019 was the reuse of 38% of water used in our manufacturing operations.

Slide 17 – Where are we today?

Our entry into retail dairy and other spreads will provide further growth in profitability along with continued growth in international markets.

Total milk production across Australia is forecast to further decline in FY2020, continuing the pressure on margins. We are already seeing this pressure with record opening milk prices announced by all processors in recent months. Whist aggressive competition for milk will continue, Bega Cheese is well placed to maintain strong supplier relationships through our 9/3 seasonal milk pricing initiative, the Bega Supply Premium and our strong reputation in the marketplace amongst farmers.

We remain focused on growth through investment and other profit improvement initiatives. Our ongoing focus on working capital management will continue to ensure our balance sheet is resilient.

Slide 18 – Our priorities

In everything we do at Bega we ensure that we are relevant to our customers and globally competitive. The pressure on earnings in FY2019 will continue in the new financial year and it is imperative that we focus on executing our growth initiatives and the further rationalisation and optimisation of our manufacturing footprint and logistics network.

In FY2020 we will continue to invest in our brands, develop new products and extend our reach as we grow our consumer and food service markets in Australia and overseas. Our product innovation pipeline developed since early FY2018 and our marketing and execution capability will support this growth.

Our capital investment program will focus on reducing the overall supply chain costs and support growth categories with increased capacity and capabilities. This includes the new lactoferrin facility at Koroit which is scheduled to be commissioned in early 2020 and will provide a positive return in the second half of FY2020 into FY2021.

We will continue to firmly defend the legal actions brought by Fonterra in the Supreme Court of Victoria, due to be heard in late 2019. This case relates to the rights to use the Bega brand in Australia and our cross claim on Fonterra regarding the non-performance of their obligations in accordance with the Bega trademark licence agreement.

As I look to the future, I expect the competitive challenges impacting the dairy industry to continue, which may provide further potential consolidation opportunities. We remain focused on diversifying and aligning our milk supply to ensure long term success. Notwithstanding these challenges I am confident in our strategy and capability to accelerate our growth plans and reset our cost base in FY2020.

Importantly, in FY2020 we will continue the transformation we began a couple of years ago to become The Great Australia Food Company.

Slide 19 – Questions

Thank you and we will now take any questions.