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26 February 2019

Comvita Announces Half Year Result

For the six month period ending 31 December 2018, Comvita (NZX:CVT) today announced a Net Loss After Tax of $2.7m on revenue of $77.7m. This compares to a Net Profit After Tax for the comparable period last year of $3.7m on revenue of $83.6m.

Financial results for the six months to 31 December 2018 (six months to 31 December 2017)

	2018	**2017**
Revenue	$77.7m	$83.6m
EBITDA*	$1.3m	$9.9m
EBITDA%	2%	12%
Net Profit After Tax (NPAT)	($2.7m)	$3.7m
NPAT attributed to non-operating items**	$0.7m	($0.3m)
NPAT excluding non-operating items	($3.4m)	$4.0m
Earnings per share (cents)	(5.91)	8.31
Dividends per share (cents)	Nil	4.0

* EBITDA: earnings before interest, tax, depreciation and amortisation.
**The non-operating item is the revaluation of Comvita's options and convertible loan notes in SeaDragon (NZX:SEA).

Comvita Chairman Neil Craig, said "It has been a challenging 1st half to the FY19 year, which has resulted in a shortfall in revenue and profit to that achieved in the comparable period FY18. It has also been a period where we have implemented some important fundamental changes to the business that will result in long term, sustainable competitive advantage for Comvita."

Strategic Direction

At the end of the FY18 year, the Company made a significant change to Comvita's strategy, and we communicated this at our ASM in October 2018. Management has executed many aspects of this strategy:

- A much greater focus on Manuka honey and propolis (and less on other ingredient platforms).
- Harmonisation of prices across the various sales channels targeting China.
- Growth of Sales and improved margin for our distribution Joint Venture in China.
- Reduced dependence on the Daigou market out of Australia and New Zealand into China.
- Broadened our customer base in North America from dependence on one key customer.
- A step up in marketing activities and packaging to support our premium brand positioning.
- Implementation of a more aggressive plantation strategy using 3rd party capital to provide long term supply security for high UMF Manuka honey.

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We believe the strategic shift to focus on the formal channels into China will provide a sustainable competitive advantage for Comvita. Implementing some of these changes has taken longer to complete than we originally anticipated. Consequently, improved financial performance from implemented changes has been slower to materialise than forecast. In particular, it has taken longer than earlier anticipated to conclude sales agreements with all major CBEC (cross border e-commerce) sellers into China. This strategy, including price harmonisation between channels, was identified by Comvita as the key part of maximising profit in the long term from the Chinese market. We believe that between our China Joint Venture, the formal CBEC channels and the Daigou sellers from New Zealand and Australia into China, we now have 'all bases covered' in order to optimise profit on sales to Chinese consumers in the long term.

This change in approach to China, no orders from one major existing USA customer and another poor pre-Christmas honey harvest, are the main contributors to the poor financial result in the first 6 months.

2018-2019 Manuka Honey Harvest

The Manuka honey harvest season is now effectively complete. We have commenced extraction of honey from the hives but only a small sample of the crop has been tested for quality (UMF activity). From early January to mid-February, we achieved excellent yields from the central and western part of the North Island, which will help counter the poor pre-Christmas crop from Northland and the northern and eastern parts of the North Island. We are optimistic that, while the crop is lower than our budget, it is significantly better in terms of quantity (and quality) than the last two years.

Inventory

Our net bank borrowing at 31 December 2018 was $104m. This use of bank borrowings to purchase high UMF Manuka honey inventory is a targeted use of debt. Today our total inventory is $120m. This provides us with secure honey supply of the highest quality which will grow in value while in storage. As we produce more honey from our own apiaries and generate profit, we expect this net debt to decline. Today, it is at c.$95m with significant bank headroom available.

Further, in the last 6 months we have fully funded from borrowings, at a total cost of c.$19m, our state-of-the-art warehouse and new production facilities, land for plantations and purchased 20% of Apiter (our supplier of high quality propolis in Uruguay). The Apiter purchase has met our expectations in terms of supply and operating performance, in the first 6 months.

CEO Commentary

Comvita CEO Scott Coulter, says "I am confident that significant progress has occurred in the execution of our strategy, the benefit of such will not be fully appreciated until the 2nd half of this financial year and beyond."

Market Outlook

We have seen very good progress being made in our Joint Venture company based inside China. Sales expectations are on target and we are seeing an improved gross profit margin, because of our strategic pricing model approach to our entire business. We have increased our marketing investment inside China, in line with our strategy and we expect to see continued growth in this market.

In our other key market of North America, we have strong sales growth in Canada in the first half of the year, good growth in digital sales channels and have several new wholesale customers including Whole Foods. Despite these positive factors, we have seen a decline in sales overall in North America because an expected replenishment order from our biggest North America customer has not yet been received. This has had an impact in respect of our sales when compared with the same period in FY18.

CEO Comments on Outlook

The interim financial result and prospects for the current financial year ending 30 June 2019 are disappointing, against a backdrop of forecasts we gave at our Annual Shareholder Meeting of revenue and profit growth.

The reality is that:

- Our Manuka honey harvest for this season will be below expectations but better than the last 2 years,
- New revenue opportunities in North America and Europe while still in progress, will materialize either late in FY19 or early FY20, and
- Our strategic approach to price harmonization between channels and markets has impacted Daigou sales in the 1st Half, but has given us margin benefits, particularly inside China.

In effect, the Financial Result is masking strategic gains. In particular, these are:

- The excellent performance of our China Joint Venture which commenced operation in July 2017 and has enabled us to reduce our reliance on the 'informal' Daigou channel out of New Zealand and Australia into China.
- Diversification of our revenue base into North America, away from dependence on very large single company orders.
- With respect to our apiary business, material quantities of high UMF Manuka honey are being delivered from long term leases and plantations we now have in the Central North Island, rather than a dependence on the higher risk 'pre-Christmas' northern geographic regions of the North Island.

Conclusion

Chair Neil Craig, said "The issues outlined above affecting revenue and production of honey in the 1st Half, will impact on our Full Year Result to the extent we now think that we will fall short of Net Profit After Tax of $8.2m we achieved in the FY18. However, we have set up the business from a revenue and margin point of view to deliver strongly in the balance of the 2019 calendar year and beyond. We believe our efforts with respect to price harmonisation between markets and channels and our brand building work in China over the last 12 months will reward us for years to come.

We also believe our approach of a lower cost apiary 'set up' and the targeting of the more stable climate areas in the central North Island including plantation Manuka, is starting to deliver. Our long term strategy of planting c.2000 ha pa of improved high UMF manuka plants on otherwise marginal central North Island high country, is a fundamental tenant to securing our future Manuka honey supply from a sustainable source."

For a more detailed analysis regarding the 1st half of the FY19, please refer to the Financial Statements and Investor Presentation respectively, loaded onto the Comvita website: www.comvita.co.nz

Ends.

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Background information
About Comvita (www.comvita.co.nz)
Comvita (NZX:CVT) is a global natural health company committed to the development of innovative products, backed by ongoing investment in scientific research.