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Company Announcements Office
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Freedom Foods Group Limited (ASX: FNP)
2020 full-year financial results release

$ million	FY20	FY19 (restated)	Change (%)
Revenue	$580.2	$461.8	26%
Adjusted EBITDA (pre-AASB 16)	($86.5)	($88.0)	2%
Adjusted EBITDA (post-AASB 16)	($71.8)	n.m.	n.m.
EBITDA	($96.7)	($118.6)	19%
NPAT	($174.5)	($145.8)	(20%)
Shareholder equity	$61.0	$234.7	(74%)
Net debt[1]	$275.2	$122.0	125%
Net tangible assets per share (CPS)	8.75	66.56	(87%)

Financial Summary

- Total revenue of $580.2m, an increase of 26% on FY19 revenue (restated)
- Adjusted[2] EBITDA loss of $86.5m, compared to a loss of $88m in FY19 (restated)
- Statutory net loss after tax of $174.5m, compared to a loss of $145.8m in FY19 (restated)
- FY19 and prior year accounts restated to reflect past accounting matters and asset impairments
- Net asset write-downs and restatements of approximately $590m for FY20 and prior years
- Dairy and Nutritionals revenue up 37% to $362.9m, with growing demand for lactoferrin
- Plant-based Beverages revenue up 30% to $132.3m, driven by strong MILKLAB growth
- Offshore revenue up 29% to $109.8m, now 19% of overall revenue

Strategic Summary

- The Board and new executive team are focused on addressing past operational and accounting matters
- Comprehensive strategic and operational reviews are underway and operational efficiency programs are being undertaken at all sites
- A simplified business structure and product range will enable Freedom Foods Group to maximise growth opportunities in Dairy and Nutritionals and Plant-based Beverages

[1] Pre-AASB16 lease liabilities
[2] Adjusted for non-trading and non-recurring items, pre AASB 16

- All options are under consideration for the Cereal and Snacks and Specialty Seafood divisions, including divestment
- Group's financial position necessitates a significant recapitalisation. The recapitalisation plan would seek to raise up to $280 million
- A number of recapitalisation alternatives have been assessed to provide the Group a more flexible funding structure to provide runway for the turnaround and future growth
- The recapitalisation process is incomplete and a further update will provided by the end of the calendar year but advanced discussions are taking place with a new investor on supporting both the capital and operational turnaround of the business. The recapitalisation is intended to allow for existing shareholder participation
- The Group has retained the support of majority shareholder, Arrovest, and its banks throughout this process
- The Chairman and the Chair of the Finance and Audit Committee have signalled their intention to retire

Strategy

Freedom Foods Group Limited Interim Chief Executive Officer Michael Perich said:

"This is a deeply disappointing set of results for Freedom Food Group, its people and its shareholders. The results reflect the significant costs of past accounting and operational matters – matters we have identified with the assistance of independent experts and are taking steps to remedy.

"The new executive team, with the support of the Board, is transforming Freedom Foods Group.

"We have implemented a clear focus on operational accountability, improved cashflow reporting, reduced outstanding payables and improved customer and supplier terms. We have reviewed and improved many of the governance frameworks and policies, undertaken a culture review and improved engagement with employees.

"Operationally, we are reviewing the economics of every product line, every site, every sales channel and every market segment to ensure we are focused on those brands with the greatest potential to deliver profitable sales. We will be removing products that are not delivering value and investing in the ones that are.

"Freedom Foods needs to become a simpler business – and that includes identifying parts of our business that may perform better under different ownership.

"We are confident the difficult decisions we have taken today – and further decisions to be made in coming months – will lay the foundations for a simplified but strengthened Freedom Foods Group with enormous growth potential in its key markets of Dairy and Nutritionals and Plant-based Beverages.

"With the right capital structure, culture, people, systems and discipline across all components of the business – from manufacturing to marketing – we remain confident we can reclaim our standing as one of Australia's most successful food and beverages businesses."

Board investigations and restatement of prior year accounts

In March 2020, the Board initiated an investigation into issues regarding the operation and administration of the company's equity incentive plan. Separately, the implementation of a warehouse consolidation program led to the identification in May 2020 of out-of-date, unsaleable and obsolete inventory, as reported to the ASX on 29 May 2020 and 25 June 2020.

In June 2020, the Board expanded the investigation to take a broader look at the Group's financial position and operations with the assistance of external advisors including PwC, Ashurst, Arnold Bloch Leibler and Moelis Australia.

The FY20 audit by Deloitte and a forensic accounting investigation by PwC identified a range of accounting matters going back a number of years.

Most significantly, the reviews determined that most of the costs capitalised during the commissioning phase of the Group's capital investment program should be more appropriately treated as expenses. These accounting treatments contributed to decisions on new products and expansions that were based on unrealistic assessments of market opportunities and margin assumptions that were not realised. As a result, too many Group products were sold at prices that did not fully recover their costs.

These matters have resulted in a material restatement of the Group's FY19, FY18 and prior period accounts and material write-downs and adjustments.

The total impact of the adjustments and write-downs for FY20 and prior periods is approximately $590 million.

Key impacts include:

- $372.8 million from a reduction in asset values reflecting changes to accounting policies and practices related to the capitalisation of capital works costs;
- $75.9 million in write-downs of goodwill and brands;
- $60.1 million in write-downs of out-of-date, unsaleable and obsolete inventory; and
- $38.9 million from a reduction in the value of capitalised new product costs reflecting changes to accounting policies and practices.

The Group is cooperating with the Australian Securities and Investments Commission in relation to investigations into these matters. ASIC has formally requested documents from the Group through the issue of a Section 30 notice under the *Australian Securities and Investments Commission Act*.

Financial Summary[3]

The Group made a statutory net loss after tax for FY20 of $174.5 million (FY19 loss of $145.8 million). Net sales increased 26% to $580.2 million, with domestic sales up 25% to $470.2 million and export sales up 29% to $109.8 million. Adjusted EBITDA[4] losses decreased slightly to $86.5 million from $88.0 million in FY19.

[3] All FY19 figures restated
[4] Adjusted for non-trading and non-recurring items, pre AASB 16

While higher profitability was obtained from the Group's plant-based products – particularly from MILKLAB – and from the commencement of sales of lactoferrin and similar nutritionals products, these contributions were outweighed by a poor performance from Cereal and Snacks and Specialty Seafood and losses from the operations of UHT dairy.

Despite the impact of COVID-19 on international trade, overall export sales to Southeast Asian markets rose by 261% to $34.4 million, reflecting increasing market acceptance of the Australia's Own and MILKLAB dairy brands. Export sales of UHT milk products to China rose by 8% to $60.1 million led by increased sales to contract partners.

Net assets fell to $61 million, compared to $234.7 million in FY19, reflecting the operating performance of the business and asset and goodwill impairments.

As part of cost-management initiatives, the Group initiated a warehouse rationalisation program and implemented a redundancy program with 62 roles being made redundant in May and June 2020. The Group has also restricted capital expenditure, with its major capital investment programs now largely complete.

As at 30 June 2020, net debt (pre-AASB 16 lease liabilities) was $275.2 million. This is expected to increase to approximately $335 million at the time of the recapitalisation. The Group has negotiated a standstill agreement with its lenders to enable it to stabilise the Company; investigate and remedy the operating and accounting issues; and pursue the recapitalisation plan. The standstill agreement has been extended until 29 January 2021 to enable the completion of the recapitalisation plan.

Dividends

On 27 February 2020, directors declared an unfranked interim dividend of 2.25c per share to the holders of fully paid ordinary shares in respect of the half year financial results ending 31 December 2019. On 29 May 2020, the Company announced that it was cancelling the dividend. No dividend has been or will be paid in respect of FY20.

Operational summary[5]

Segment	Revenue			Adjusted EBITDA[6]		
$ million	FY20	FY19 (restated)	% change	FY20	FY19 (restated)	% change
Dairy and Nutritionals	$362.9	$264.8	37%	($46.1)	($35.6)	(29%)
Plant-based Beverages	$132.3	$101.5	30%	$17.2	($3.2)	n.m.
Cereal and Snacks	$69.9	$80.9	(14%)	($32.1)	($31.6)	(2%)
Specialty Seafood	$15	$14.5	4%	$0.2	($2.9)	n.m.

Dairy and Nutritionals

A leading producer of long-life UHT dairy milk, nutritional products and performance powders

Revenue rose 37% to $362.9 million, with the business experiencing an unprecedented spike in

[5] All FY19 figures restated

[6] Adjusted for non-trading and non-recurring items, pre AASB 16

demand for UHT milk as a result of pantry stocking caused by the COVID-19 lockdowns, a rise in exports to Asia and increased industrial nutritionals sales.

Adjusted EBITDA losses increased to $46.1 million ($35.6 million loss for FY19) due to a number of factors, including selling prices not fully recovering costs for some products, losses from the sale of surplus milk and delays to the commissioning of the lactoferrin plant and UHT expansion in Shepparton. The under-utilisation of plant and equipment meant overheads were not fully recovered.

The state-of-the-art Shepparton plant is now operating on a much-improved basis, with utilisation improving, focused controls around yield and recovery implemented and a review of product lines underway. All old, unsaleable and overvalued inventory has been written off.

The Group is focused on returning the segment to profitability in FY21.

In Australia, retail UHT sales increased significantly during panic buying in the peak COVID-19 lockdown period during March and April, however, sales of cream to other manufacturers were affected by an economy-wide reduction in demand, resulting in a decline in normally strong prices achieved at this time of year. Demand for cream and butter remains lower than normal levels but the Group expects to see an improvement with the continued reopening of restaurants and cafes.

Dairy exports to China and South East Asian markets remain strong, with sales of Group brands and contracted customer brands currently tracking ahead of the previous corresponding period.

Sales of consumer nutritionals, including Vital Strength and UPROTEIN, were affected by gym and specialty store closures, with demand for the Group's products falling in the peak lockdown period. The re-opening of these facilities in most states has been reflected in an increase in demand and the Group expects further improvement following the re-opening of Victoria.

Plant-based Beverages
A leading producer of long-life UHT products including soy, rice and almond milk and liquid stocks

Revenue increased 30% to $132.3 million as the plant-based beverages segment experienced strong growth across all channels and all brands, particularly MILKLAB.

Adjusted EDITDA of $17.2 million compared to an EBITDA loss of $3.2 million in FY19.

The strong performance came despite the impact of COVID-19, which caused major disruption to out-of-home demand during the peak lockdown periods. Volumes have since recovered and profitability continues to improve as economies of scale increase.

MILKLAB has been at the forefront of the shift towards consumption of plant-based products, generating strong brand loyalty in a high-margin channel for the Group, leading to increased profitability.

Launched less than five years ago, MILKLAB's range of plant-based milks is now sold in approximately 8000 cafes, including the Starbucks and Muffin Break chains, with further significant growth expected this financial year. In September 2020, MILKLAB was introduced in all McDonalds' McCafe outlets.

Freedom Foods Group continues to produce Almond Breeze milk under licence from Blue Diamond Growers. The Company is involved in legal disputes with Blue Diamond over this contract, which the Company has previously announced to the market. The Group disputes Blue Diamond's claims and is defending its position.

Cereal and Snacks
The market-leading producer of allergen-free and healthy breakfast cereals and snack bars

While Freedom Foods Group retained its leading position in the growing health food cereal category, overall revenue declined 14% to $69.9 million ($80.9 million in FY19), with the adjusted EBITDA loss rising slightly to $32.1 million ($31.6 million loss in FY19).

Revenues declined due to the exit from some contract manufacturing and reduced sales to Asia, offset by increased grocery sales, which benefited from panic buying during COVID-19. Dependence on lower-margin grocery sales reduced profitability, which was also affected by lower production levels and higher input costs due to the impact of the drought.

The Group's key brands of Messy Monkeys, Heritage Mill and Crankt delivered an increase in sales during the year, however Arnold's Farm was affected by reduced demand from China.

An operational review of Cereal and Snacks has determined that the business has been overly reliant on trade marketing to support new products, some of which have not achieved anticipated returns.

In line with its company-wide product rationalisation program to reduce the number of low-margin or loss-making product lines, the Group has adopted a more focused approach to new product development decisions.

Freedom Foods Group and its advisers are reviewing all strategic options for the Cereal and Snacks businesses. While actively pursuing a 'fix and retain' strategy, the Group is also exploring a potential divestment.

Specialty seafoods
A leading producer of a range of canned seafood, including sardines and salmon

Revenue was broadly flat $15 million ($14.5 million in FY19), with the segment returning to profitability with adjusted EBITDA of $0.2 million, compared to an EBITDA loss of $2.9 million in FY19.

While Brunswick Sardines maintained its brand leadership position in Australia and New Zealand and Paramount Salmon performed well, sales were affected by reduced grocery sales caused by necessary price increases. The price increases were driven by higher input prices due to movements in exchange rates, which also constrained profitability.

Freedom Foods Group and its advisers are reviewing all strategic options for the Specialty Seafood business, including divestment.

Recapitalisation plan

Freedom Foods Group has been reviewing options to recapitalise the business – through debt, equity or a combination of both – with any proceeds used to retire debt and for general corporate purposes. The Board undertook an extensive process to select the right capital solution for the

Group given the uniqueness of its current situation. The proposed approach is focused on raising the necessary capital by way of an ASX-listed convertible note, protecting the incoming capital as secured debt while providing equity-linked optionality and flexibility.

The Group received several offers from credible parties and is now in exclusive, advanced discussions with a new investor to support the capital and operational turnaround of the business. It is anticipated that the capital raising will total up to $280 million, and the raising intends to provide existing shareholders with an opportunity to participate.

Freedom Foods Group's majority shareholder, Arrovest, has indicated its support for the recapitalisation plan and the Board intends to provide all the Group's shareholders with an opportunity to participate in any capital raising. The Board has pursued capital solutions that have the least dilutive effect on existing shareholders.

It is anticipated that further announcements on the recapitalisation will be made before the end of calendar 2020.

People and Culture

During the year, there were a number of executive management changes, including the appointment of Interim Chief Executive Officer Michael Perich on 6 August 2020 and a new Chief Financial Officer, Josee Lemoine.

Justin Coss commenced as Group General Counsel and Company Secretary on 23 June 2020. Scott Standen, who was initially intended to cease his role as Company Secretary on 30 November 2020, will now remain as joint Company Secretary until 31 December to ensure a smooth transition.

It is anticipated that further announcements will be made following the completion of the recapitalisation process as the Board moves to strengthen the management team.

In parallel to the executive changes, the Board and management are reinforcing internal systems and protocols and focusing on cultural improvements through a redesign of governance frameworks to promote the optimal employee behaviour and uphold corporate values. This includes aligning remuneration incentives with the interests of the Group and its shareholders.

Board renewal

Freedom Foods Group is undertaking a board renewal process. During the year, two new independent Non-executive Directors were appointed to the Board – Genevieve Gregor and Jane McKellar. Timothy Bryan was appointed as Alternate Director for Anthony M. Perich and Ronald Perich.

Non-Executive Chairman Perry Gunner has indicated he will retire and not stand for re-election at the next Annual General Meeting and Non-executive Director Trevor Allen, who is Chair of the Finance and Audit Committee, has indicated his intention to retire at or around the time of the AGM. It is anticipated that further board changes, including the appointment of additional non-executive directors, will be announced following the completion of the recapitalisation process.

Voluntary share suspension

The Company's shares will remain in voluntary suspension until after it has announced its proposed recapitalisation, which is anticipated mid-December.

Annual General Meeting

Freedom Foods Group advises that its Annual General Meeting will be held on 29 January 2021 at 11am (AEDT). The AGM will be held virtually, with full details to be provided in the Notice of Meeting. In accordance with Listing Rule 3.13.1, the closing time and date for receipt of nominations from persons wishing to be considered for election as a Director of Freedom Foods Group is 11am (AEDT) on 7 December 2020.

Way forward

Interim Chief Executive Michael Perich said:

“Despite the significant challenges of the past year and the impact of COVID-19, particularly on out-of-home sales, the potential of Freedom Foods Group can be seen in the sales growth in key segments delivered over the full year.

“We are tapped into rapidly growing markets that provide strong tailwinds for Freedom Foods Group. These include the rise in demand for plant-based beverages and the growing recognition of the health benefits of lactoferrin.

“We anticipate continued sales growth in Dairy and Nutritionals and Plant-based Beverages in FY21, with increased penetration of MILKLAB in the out-of-home market, growth of Vital Strength and other nutritionals brands and increasing inroads in Asian export markets.

“We are committed to restoring the Group to sustainable and long-term profitable growth.”

Investor and analyst briefing

Freedom Foods Group Chairman Perry Gunner, Interim CEO Michael Perich and Non-executive Directors Trevor Allen and Genevieve Gregor will provide a webcast and conference call briefing to investors in relation to the FY20 results.

Date: Monday 30 November 2020

Time: 5pm AEDT

Listen-only webcast: https://www.openbriefing.com/OB/4022.aspx

Registration for dial-in conference call: https://s1.c-conf.com/diamondpass/10011248-nc7ew3.html

Investor inquiries

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