



ASX/media release

18th January 2011

MARKET UPDATE

Retail Food Group Limited (ASX:RFG) provides the following operational update:

1H11 Guidance:

RFG announced during its 2010 Annual General Meeting that it anticipated 1H11 NPAT from Core Operations to be in the range of 10% to 15% over that reported in 1H10 (being \$12.5 million).

Based on unaudited management accounts the Company remains confident that the said guidance remains valid, however, 1H11 NPAT from Core Operations will likely fall within the lower part of the indicated range given the impacts arising from:

- the significant number of franchisees who did not trade on some or all of the four designated or declared public holidays over Christmas as a result of the significantly increased wage cost brought about by the recently introduced Modern Awards under the FairWork Act; and
- continued inclement weather in Queensland and New South Wales.

Acquisition of Esquires Coffee Houses (Esquires)

On the 29th of December 2010 RFG announced that it had reached two separate agreements by which it shall acquire the intellectual property, franchisor and licensor rights of the Esquires Coffee Houses (Esquires) system for Australia and New Zealand.

Settlement of both transactions remains scheduled for mid February 2011.

Queensland & Northern New South Wales Flooding:

RFG has conducted a preliminary assessment of the impact of recent and continuing flood events affecting Queensland and Northern New South Wales.

Given the nature and extent of these events, a significant portion of the Company's franchised outlet population within the affected territories has been adversely impacted either directly or indirectly. This will necessarily have flow on affects for RFG.

RFG has allocated significant financial, logistical and personnel resources toward provision of necessary and appropriate relief and support for the franchisee community such that, where possible the resumption of trading may be achieved at the earliest juncture.

In the interim, the Company advises that some 320 outlets are situated within Queensland and Northern NSW. The vast majority of these outlets have or will be impacted in some measure by the recent and continuing flooding and its aftermath.

Flood impacts vary considerably and range from stock shortages and staffing issues through to total store closure, and in limited cases, outlet destruction.

To date, 108 outlets have been directly affected resulting in outlet closure, comprising:

- 56 Brumby's outlets (including Brumby's Go! and 13 Big Dad's Pies outlets);
- 31 Donut King outlets;
- 14 Michel's Patisserie outlets; and
- 7 bb's café outlets.

Pleasingly, as of today there remains only 8 Brumby's outlets (including 5 Big Dad's Pies outlets) which remain closed:

- 6 outlets have sustained significant flood damage; and
- 2 outlets are inoperable due to shopping centre/site closure.

The immediate future of each of these outlets is presently the subject of further assessment. In certain instances it may well be determined that rectification works in order to facilitate recommencement of trade will be uneconomical.

In any event, the fact that 100 of those impacted outlets have already recommenced trading is a direct consequence of the amazing and unselfish support provided by RFG personnel, franchisees and their staff, together with members of the community, to ensure damaged outlets were reopened and trading within the shortest possible timeframe. RFG extends its sincere thanks and appreciation to those persons for their valued assistance.

Franchisees are obliged by their franchise agreements to maintain appropriate insurance coverage (including in respect to business interruption, flood and physical damage).

It is understood that all affected franchisees maintain insurances, however, the Company appreciates that those policies may in many cases not provide sufficient or appropriate cover, or indeed, may be the subject of exclusionary clauses. Ultimately, the availability and sufficiency of insurance cover will be assessed on a case by case basis, but in any event, there will likely be delays in the claims process. In the interim RFG will continue to liaise with, and provide assistance to, its franchisee community and their continuing needs arising from the floods and their affect.

At a corporate level, RFG anticipates the loss of franchise service fee and other revenue in the immediate and medium term as a consequence of the floods and their affect on the Company's franchise networks.

Additionally, RFG does not discount the potential for:

- permanent outlet closures and latent lease and make good liabilities which may arise, particularly in circumstances where the franchisees concerned are incapable of meeting financial obligations otherwise owed by them;
- additional personnel and other corporate costs necessary to manage franchisee distress and service or support impacted franchisees;
- increase in bad debts, and provisioning for doubtful debts, amongst franchisees financially incapable of meeting their obligations under their franchise agreements;
- significant impact to programmed new outlet growth amongst flood affected regions within Queensland and Northern NSW; and

- reduction in new outlet growth amongst flood affected regions given the imperative for rectification works and reinvigoration of existing communities and trading spheres.

RFG CEO Tony Alford said, “notwithstanding that the vast majority of the Company’s franchised outlets have recommenced trade, it would be naïve to suggest that normal trading conditions will resume as a matter of course”.

“Many franchisees will experience a long period of revenue reduction, and in some cases, this may result in a permanent reduction in retail sales within those communities worst affected by flood. This may have long term adverse affects for those franchisees concerned”.

“Conversely, there are positives that have emanated from these devastating floods with significant uplift in sales amongst some outlets due to demand for consumer staples such as bread and stock shortages amongst supermarket vendors. Indeed, we have reports of customer lines extending beyond shopfront doors amongst a number of Brumby’s outlets”, Mr Alford said, “these situations provide a unique opportunity for the Brumby’s system to convert new customers to the brand whilst also reinforcing the community based profile of the Brumby’s network”.

“The floods also present an opportunity for significantly damaged Big Dad’s Pies outlets to progress opportunities for stronger realignment of their outlets to the Brumby’s brand consistent with the Company’s intent upon acquisition of that system. We shall continue to engage with those franchisees in connection with this opportunity”.

“Importantly, we are relieved to confirm that franchisees, staff and their families are safe. That said the financial and emotional toll on those families and their businesses may be significant and be prolonged”, Mr Alford said.

“Quite apart from the consequential direct loss of revenue RFG will suffer as a result of the floods, the Company has resolved to provide necessary ongoing financial and resource assistance to impacted franchisees. Whereas RFG has no contractual obligation to do so, and leaving aside the compelling moral obligation, it is in the medium to long term economic interests of all stakeholders, including shareholders, that this assistance be provided”, he said.

Victorian Flooding:

Whilst the Company continues to monitor the flood events taking place within Victoria, it is pleased to announce that no outlets have been affected within that State at this juncture.

FY11 Guidance

Although RFG is not presently furnished with sufficient information and understanding of the flood impact on affected franchisees and the communities in which they conduct their retail operations, it is evident that there will be a consequential adverse impact on RFG revenues in the short to medium term.

That reduced revenue, allied with the Company’s preparedness to financially assist distressed franchisees and their families, will result in a lower FY11 Net Profit after Tax (NPAT) than would otherwise have been anticipated had normal trading conditions applied.

Given the continuing nature of the flood crisis, together with the prevailing volatile retail environment subsisting both prior to and post it, it would at this juncture be both premature and imprudent to provide full year guidance, or to quantify the likely extent of the affect the matters addressed herein will have on FY11 NPAT.

That said, RFG remains committed to, and is confident of achieving, positive FY11 NPAT growth from Core Operations over that reported in FY10 (being \$26.4 million). Ultimately, however, RFG's likely FY11 NPAT result is a matter that will be influenced by unique and highly unusual circumstances whose full impact is not yet capable of assessment.

RFG continues to monitor these unfolding events and circumstances and will keep the market informed concerning this matter.

About Retail Food Group Limited

Retail Food Group is a leading Australian retail food brand manager and franchisor. It is the franchisor and intellectual property owner of the Donut King, Michel's Patisserie, Brumby's Bakeries (including Big Dad's Pies), and bb's café franchise systems.

About Esquires Coffee Houses (Esquires)

The Esquires Coffee Houses system originated in Canada and was first established in New Zealand by way of master franchise in 2001. The New Zealand network has a current footprint of 46 outlets and is the largest franchised coffee chain within that country.

Esquires is yet to be established within Australia.

The Esquires Coffee House system is similar to, and is a direct competitor of, the bb's cafe system in New Zealand.

Following settlement of the transactions, further information will be provided to the market including import and effect for RFG's existing franchise system network and in particular the alignment with, and future development of, the bb's café franchise system.

Total consideration in respect of the acquisitions will be circa AUD\$9.0 million (assuming all vendor performance obligations are fulfilled).

