

ASX Announcement

Freedom Foods Group Limited (ASX: FNP)

Financial Year 2014 Results

Freedom Foods Group Limited (FNP) today released the Company's preliminary final results for the full year ended 30th June 2014.

Key Highlights

- Successful year building on the Company's capability and capacities for profitable growth, investing in our brands and establishing key customer relationships in Asia and North America.
- Strong sales growth in the Freedom Foods business unit reflecting growth in Cereals and Non Dairy beverages, with a significant business unit EBDITA increase reflecting sales growth and improved operating efficiencies at Leeton.
- Pactum Australia provided a strong sales and business EBDITA contribution, reflecting increasing non-dairy production volumes, in support of Freedom branded and Private Label products in the fast growing almond beverage category.
- Commencement of commercial operations at Pactum Dairy Group (PDG) in Shepparton in April 2014, with initial volumes ahead of its 3 year business plan, reflecting strong demand from customers from China, SE Asia and Australia.
- Specialty Seafood business made a steady profit contribution, with the Brunswick Sardine brand maintaining its number 1 brand leadership position in Australia and New Zealand.
- A2 Milk Company (a2MC) (17.9% FNP shareholding) reported continued strong growth in the Australian fresh milk business with sales up 24% per cent over the prior year period. a2MC's current market capitalisation implies a value for the Company's 17.9% shareholding of approximately A\$70 million, materially above the book value of A\$10.6 million.
- The Company completed a capital raising of \$30m (gross proceeds) at \$2.10 per share from a placement and entitlements offer in September 2013. The capital raising was significantly oversubscribed with strong demand from a broad range of high quality institutional investors and existing shareholders. In addition, the exercise of options by shareholders and employees raised \$2.2 million.
- Net Cash position including financial assets (loans to PDG associate of \$12.8 million) at June of \$7.9 million. During the period, the Company invested \$19.9 million in capital expenditure, \$4.5 in equity associates and repaid debt of \$12.5m.
- Net assets per share at \$0.81 and net tangible assets of \$0.67 per share. If the a2 Milk Company investment was recorded at market value (as compared to book value of \$10.4 million), the Net Assets per share would be \$1.27.
- The Company is to pay a final dividend for the half year of 1.5 cents fully franked per ordinary share paid on 3rd November 2014. A fully franked converting preference share dividend will be paid on 15th October 2014.



Group Summary Result

The company achieved an Operating EBDITA of \$16.6 million (including interest from Associates), an increase of 43.2% on the previous corresponding period, reflecting increased sales and profitability in the Freedom Foods and Pactum Australia business units and a steady contribution from Specialty Seafood.

Operating Pre-tax Profit was \$13.1 million for the 12 months ended 30 June 2014, reflecting a 73.6% increase on the previous corresponding 12 month period. Net Operating Profit was \$12.5 million, an increase of 97.1%, including a decrease in operating income tax expense to \$0.5 million, against a \$4.8 million tax expense for the prior year period. The result included non-cash employee share option expense of \$252k (post-tax).

The prior year period reported net profit included non-operating pre-tax profit of \$11.8 million from the sale of 40 million shares in a2 Milk Company in December 2012. After a detailed review, the Company has written back an amount of \$3.1 million relating to over accrual of tax on the disposal, which has had the effect of reducing the income tax expense for this period. Going forward, the Company expects a low effective tax rate relating to any capital gain on a sale of shares in a2 Milk Company.

Net assets per share at \$0.81 and net tangible assets of \$0.67 per share, with a2 Milk Company investment recorded at a book value of \$10.6 million.

Summary Financials

12 months to 30 June	2014	2013	% Change
Gross Sales Revenues ('000) (1)	122,772	115,516	+6.28%
Net Sales Revenues ('000) (1)	104,616	98,718	+5.97%
EBDITA (Operating) ('000) (2)	16,611	11,600	+43.2%
EBITA (Operating) ('000) (2)	13,868	8,972	+54.6%
Equity Associates Share of Profit ('000)	-26	819	-103.2%
Pre Tax Profit (Operating) ('000)	13,059	7,524	+73.6%
Pre Tax Profit (Reported) ('000)	12,673	18,524	-31.6%
Net Profit (Operating) ('000)	12,518	6,351	+97.1%
Net Profit (Reported) ('000)	12,132	13,722	-11.6%
Final Ordinary Dividend (cps)	\$0.015	\$0.010	+50.0%
Interim Ordinary Dividend (cps)	\$0.015	\$0.010	+50.0%
Total Ordinary Dividend (cps)	\$0.030	\$0.020	+50.0%
EPS (cents per share)	8.65	14.73	-41.3%
Net Debt / Equity (exc Loans to Assoc)	4.1%	10.0%	-59.5%
Net Assets per Share	\$0.81	\$0.63	+28.8%
Net Tangible Assets per Share	\$0.67	\$0.47	+43.7%

Notes:

(1) Gross Sales Revenues does not include revenues from group associate entities, PDG or A2 Milk Company. Net Sales Revenues in the table above differs from the Appendix 4E, as the above sales includes Pactum sales to Freedom Foods and Freedom Foods to Freedom Foods North America, which is eliminated under consolidation accounting practice, but recognised by the Group as revenue.

(2) Operating EBDITA and EBITA, excludes pre-tax abnormal or non-operating charges with an add back of non cash employee share option expense of \$360k. It includes interest income from Associate PDG.

Freedom Foods

The Freedom Foods business unit continued to build momentum, investing significantly in capability and capacities for future growth including capital expenditure at Leeton and increase in brand marketing.

The business delivered overall gross sales growth of 15% compared to the previous corresponding period. With a focus on its core product portfolio of Cereal, Snacks and Non Dairy Beverage for future growth, the business is progressively reducing its presence in non-core categories including biscuits. The reduction in non-core products impacted sales in the period by approximately \$2.6m, with some resulting impact on manufacturing recoveries.

Growth in Cereal volumes contributed to increased efficiencies at the Leeton manufacturing facility, with further benefits arising from a focus on improving efficiencies in labour, supply chain and distribution. To our knowledge, the Leeton facility is the only integrated large scale manufacturing capability in Australia and overseas producing cereals and snacks “free from” gluten, nuts and dairy to the lowest detectable standards.

Dairy alternative beverage sales continued the strong upward trend from the half year with volume growth of 44% compared to the previous corresponding period, reflecting increased market share of Australia’s Own Organic and Blue Diamond Almond Breeze brands, within a category which is itself growing significantly. As at 30 June 2014, the Almond Milk category accounted for 30% of the retail nondairy category, compared to 16% at 30 June 2013.

The business invested in senior sales & marketing expertise during the year in order to drive growth in retail and other channels in the medium term, as well as marketing investment in building awareness of the brand and products across a broader consumer market.

In North America, our new 80% owned subsidiary Freedom Foods North America, invested in building sales and distribution capabilities, including establishing key relationships with distributors, brokers and retailers within the Specialty and Natural Product Retailer markets. While an operating loss was incurred in this business, this investment now provides a strong base of retail distribution coming on stream into calendar year 2015, building on Freedom Foods unique allergen free and non GMO capabilities.

During the second half of FY 14, the business invested \$6 million in incremental capital expenditure at Leeton, including an upgrade of cereal packaging capabilities to improve efficiencies and provide increased capacity in range and format and additional Cereal extrusion capacity to meet growth requirements in Cereals and other Cereal based products. The investment will significantly increase Freedom Foods production capability, with no material increase in cash overheads and lower cost per case. The commissioning was completed in August 2014.

The impact of sales and efficiency improvements, against increased sales and marketing investment during the period resulted in an increased business unit EBDITA to \$7.1 million. The North American operations reported an EBDITA loss of \$684k from startup operations during the period.

The focus for the business into 2015 remains on increasing sales in Australia through building on its category leadership in the health channel and further growth in distribution channels, while establishing key products, channels and distribution for expansion of product into export markets in North America and Asia.

An exciting innovation pipeline has been developed which will be launched into 2015, through new products in Cereals, Non Dairy Beverages, Nutritional Snacks and new formats for convenience and food service channels.

The additional \$9 million upgrade to Freedom Foods nutritional snack capabilities at Leeton will materially improve efficiencies on current business and provide the ability to meet demand for nutritious allergen free snacks in a range of formats in Australia and internationally. The new capabilities will come on line in 2 stages between November and March 2015.

Our capital investment at Leeton has been made to improve operating efficiencies, increase production capability and improve quality. This investment, aligned with ongoing marketing investment in building awareness of the brand and products across a broader consumer market open to healthier digestive and nutritional products, provides a strong base for growth.

In North America, the business is focused on building sales within a core base of retail distribution that has been established in in 2014. The business has obtained ranging in excess of 3,000 Stores that is either on shelf or due to be ranged over the next few months in retailers such as Sprouts, Whole Foods, PCCC, Raleys, Wegmans, HEB and Kroger's, reflecting Freedom Foods unique proposition in Allergen Free and Non GMO. The business remains focused on delivering its medium term sales target of up to 1 million cases of Freedom Foods branded Cereals and Cereal snacks per annum.

With the launch of the Australia's Own brand in China in late 2014, via our licensing agreement with Shenzhen JLL Group (JLL), Freedom Foods will be looking to develop and grow a range of high quality and safe food products relevant to the Asian consumer. The initial launch will comprise Dairy products, manufactured through Pactum. The existing and new capabilities with Freedom Foods and Pactum's manufacturing facilities will provide superior capabilities to customise food and beverage products for these markets.

Specialty Seafood

The Specialty Seafood business performed broadly in line with the previous corresponding period, with business unit EBDITA of \$2.4 million

Brunswick sardines maintained its No 1 brand leadership position in Australia and New Zealand.

In salmon, the Paramount brands full year sales result was impacted by SKU ranging reductions implemented during 2nd half FY 2013, although the effect on profitability of these reductions was reduced in the FY 2014 year through management of promotional spend and improved cost of goods against plan. The impact of this SKU reduction impacted sales in the full year by approximately \$2.5m.

The business remains focused on driving growth into 2015 through category leadership of the specialty seafood channel, including new product opportunities aligned to consumer demand for convenience and superior health benefits.

As part of this the business is introducing revitalized packaging for the Brunswick brand in 1st half FY 2015 and for Paramount during 2015.

The business continued to utilise the procurement power of Bumble Bee Foods of North America, with Bumble Bee securing 2014 / 15 inventory requirements through priority access to salmon and sardine catch volumes.

Pactum Group Business

Pactum Food and Beverage

The Pactum business unit continued to build momentum investing significantly in capability and capacities for future growth including the new Pactum Dairy Group (PDG) facility at Shepparton and investment in additional value added format capability.

Pactum provides innovative solutions in long life (UHT) food beverages for private label and proprietary customers and delivered a business EBDITA contribution of \$9.7 million.

Pactum's non-dairy production volumes increased during the period to support the growth of the Australia's Own and Blue Diamond brands, as well as external private label requirements in the fast growing almond beverage category.

The business continued to see the benefit of increasing its mix of value added UHT products to a range of private label and proprietary customers. Dairy milk production has been transferred to the PDG facilities in Shepparton.

During the 2nd half 2014, Pactum expanded its capabilities with the installation of 250ml Prisma Format and 330ml Prisma Dreamcap formats. The packaging capability is currently owned by Pactum and operated at PDG's Shepparton facility. Both capabilities will be for domestic customers, with a significant proportion of capacity being allocated to PDG dairy based export customers into 2015. The total investment of approximately \$15 million will provide an initial earnings contribution in FY 15.

With increasing demand from its private label and proprietary customer base for increased capacity and product format capability across dairy and non dairy categories, Pactum invested significantly in capability and capacities for future growth including additional capacity at the Shepparton facility and planned expansion at a new site in South West Sydney.

Pactum's planned new facility in Ingleburn in South West Sydney will provide for significant expansion in capacity and efficiency improvements compared to current operations, including providing more efficient and lower cost warehousing and logistics compared to current arrangements.

Pactum will acquire approximately 66,000 sq. metres of land in Ingleburn for an acquisition price subject to final adjustments, of approximately \$16.6 million. Settlement is expected on or around February 2015, once final sub divisions and other approvals have been obtained.

The new facility will provide superior capabilities to customise food and beverage products for local and export markets with efficiency and speed to meet the growing demand for high quality safe foods from Australia marketed under the Company's brands "Australia's Own" and "Freedom Foods" and leading brands of key customers in Australia and internationally.

Construction of the facility is expected to commence in 2nd half FY 2015, with production commencing from 2nd half FY 2016. The acquisition of land, associated building and capital requirements is expected to be funded from Freedom Foods Group existing finance facilities and other assets.

Pactum Dairy Group (PDG)

PDG was established in 2013 to operate UHT dairy milk operations for supply into both the domestic and export markets. PDG is a joint venture between Pactum and Australian Consolidated Milk (ACM), a major Australian dairy milk supply group.

Pactum manages PDG on behalf of the joint venture partners, with sales to key customers undertaken as an integrated contract packaging offer.

The facility was established in the northern Victorian city of Shepparton, for a total investment of approximately \$45 million, with initial capacity for 100 million litres of dairy milk production, with capability to be increased up to 300 million litres in the longer term. The facility was completed over a construction period of approximately 9 months, with the project largely on budget.

The plant commenced operations in April 2014, with commencing volumes ahead of its 3 year business plan, with strong demand from customers for 1 Litre and Portion pack volume from South East Asia and China. These customers are expected to grow beyond their initial volumes as demand for milk increases, with Australian milk products providing highest quality and safety at a comparative cost advantage compared to locally sourced milk.

To date, key relationships include Bright Dairy (Shanghai), New Hope Dairy (Chengdu), Shenzhen JLL (Guangzhou) and online retailer Yihaodian. Each of these relationships is complementary with significant diversification in local market distribution, product range and capability.

PDG has also developed other relationships for China and SE Asia including A2 Milk Company (for exclusive UHT supply into Australia, China and SE Asia) and selected retailers and distributors in China, SE Asia and Australia.

Total dairy milk volume processed in 2015 is expected to be over 100 million litres, with the site total capacity estimated at 300 million litres, based on current planning configuration.

To meet expected expansion in milk volumes over the medium term, PDG is evaluating additional processing and filling capacity expansion, including expansion of warehousing and logistics capability.

Opportunities to vertically integrate into other value added dairy products streams are also being reviewed, consistent with our customer's long term requirements.

With the commencement of operations and significant resourcing to meet the expected ramp up in volumes, the business recorded a loss in FY 2014. FNP equity accounted 1% of the loss in line with the current ownership structure. The Company has the capacity to obtain a 50% interest in PDG by converting convertible notes issued to it as part of its original investment. This is expected to occur in FY 15.

Strategic Equity Associates

A2 Milk Company Limited (a2MC), 17.9% Equity Interest

The Company is the largest single shareholder in the A2 Milk Company Limited (a2MC). a2MC owns and commercialises unique and comprehensive intellectual property rights relating to a2™ brand milk and related dairy products in international markets.

a2™ branded milk is the fastest growing milk brand in the Australian market and the major driver of category growth nationally, accounting for approximately 9% of grocery channel market share by value. a2MC also markets a2™ Platinum™ infant formula to consumers in Australia and China. a2MC's plan to enter the North American fresh milk market is progressing, with a launch expected to commence during calendar 2015.

The Company is the largest single shareholder in a2MC with a fully diluted shareholding of 17.9%. a2MC is listed on the main board of the New Zealand Stock Exchange (NZX: ATM), with a current market capitalisation of approximately NZ\$429million (A\$391 million) implying a value for the Company's 17.9% investment of around A\$70 million, materially above the book value of A\$10.6 million. The Company did not recognise any equity accounted profit from a2MC during the year, compared to \$819k in the prior year period.

While the Company intends to maintain a strategic shareholding in the medium term, it will retain the option to realise capital from the investment to support growth opportunities.

Capital Management

The Company held cash of \$4.8m at the full year, with total borrowings of \$9.8 million, comprising mainly equipment finance leases. Net debt at 30th June 2014 was \$4.9m. Net debt excludes financial assets and loans to Associate entities. At 30th June 2014, the Company had lent \$12.8 million to Pactum Dairy Group to support further capital investment and working capital requirements. The loan attracts interest at a rate of 8.0% per annum.

Net cash flow from operations was \$7.2m, reflecting improved operating performance and increased working capital from change in product mix and inventory build for capital installation. During the period, the Company invested \$19.9m in capital expenditure, \$4.5m in equity associates and repaid debt of \$12.5m. The capital expenditure of \$19.9 million comprised normal operating expenditures, commitments to expansion at Freedom's Leeton facility and expansion of Pactum's packaging capabilities at Shepparton.

The Company completed a capital raising of \$30m (gross proceeds) from a placement and entitlements offer in September 2013. The capital raising was significantly oversubscribed with strong demand from a broad range of high quality institutional investors and existing shareholders. The proceeds of the Placement and Entitlement Offer is being used to fund the Company's growth strategy including acceleration of new capital projects within Freedom Foods, Pactum Australia, new product initiatives, acceleration of international sales activities and additional working capital requirements.

The Company has approximately 152,127 convertible redeemable preference shares (CRPS) on issue, which are convertible 1 for 1 into ordinary shares at election of the holder at any time.

Dividends

Consistent with the continued improvement in group performance, the Company will pay a final fully franked dividend of 1.5 cents per ordinary share, an increase of 0.5 cents on the final dividend paid in November 2013. The record date for determining entitlements is 3rd October 2014 and the payment date is 3rd November 2014.

The Company's dividend reinvestment plan (DRP) remains open.

The Company will pay a fully franked converting preference share dividend to be paid in accordance with the terms of the converting preference shares. The record date for determining entitlements is 3rd October 2014 and the payment date is 15th October 2014. There are 152,127 converting preference shares on issue.

Outlook

The Company will continue to build on its capability and capacities for growth, investing in our brands and establishing key customer relationships in Asia and North America through its Freedom Foods and Pactum businesses.

Freedom Foods is expected to continue to deliver improved results from growth through innovation in new products, expansion of distribution channels in Australia and international markets, aligned with increasing manufacturing efficiencies from volume and cost efficiencies arising from the capital investment program at the Leeton facility. This, aligned with investment in building awareness of the brand across a broader consumer market open to healthier products, provides a strong base for growth into future years.

The expansion of capabilities in Pactum will result in an increase in sales and profitability, with further growth opportunities through meeting the increasing demands of its private label and proprietary customer base, including under the Company's brands "Australia's Own" and "Freedom Foods" and leading brands of key customers in Australia and internationally.

The investment in Pactum Dairy Group provides a material opportunity to increase exposure to the growing demand for high quality and safe dairy products from South East Asia, including China aligned with our key strategic customers. PDG is expected to provide a material profit contribution in FY 2015.

The strategic investment in a2 Milk Company provides the Company and its shareholders a potentially significant value creation opportunity through a2 Milk Company's growth in Australia and international markets.

Overall the Company anticipates growth in sales, operating profitability and improving return on funds employed in FY 2015.

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