



Australian Agricultural Company Limited
ABN 15 010 892 270

Wednesday, 4 April 2018

AACo Market Update and Operational Review

The Australian Agricultural Company (ASX:AAC) has today released a market update in relation to its FY18 results. CEO Hugh Killen will discuss the market update on a conference call scheduled for 9.30am AEST today (details provided below).

Based on preliminary and unaudited results for the 12 months to March 2018 AACo expects to report:

- Operating EBITDA¹ in the range of \$12 million to \$16 million. This compares with FY17 Operating EBITDA of \$45.0 million;
- Statutory EBITDA loss in the range of \$(30) million to \$(40) million. This compares with FY17 Statutory EBITDA of \$133.2 million;
- Significant items related to Livingstone Beef in the range \$(60) million to \$(65) million. These significant items reflect (i) an impairment charge against the carrying value of Livingstone Beef and (ii) an onerous contract provision taken in relation to Livingstone Beef. These charges are non-cash in nature and taken through the income statement below the EBITDA line;
- Negative Operating Cash Flow in the range of \$(38) million to \$(42) million. This compares with positive FY17 Operating Cash Flow of \$29.3 million; and
- A positive asset revaluation reserve adjustment of \$32 million to \$36 million, relating to the revaluation of AACo's property portfolio.

The FY18 result expectations set out above are unaudited and preliminary in nature. AACo's FY18 audited results are subject to a number of factors including review by AACo's auditors, finalisation of the livestock market valuation, finalisation of the Livingstone Beef impairment charge including to reflect any conclusions from the Strategic Review (see below) and Board approval.

Operational Review

CEO Hugh Killen said "We have undertaken a comprehensive Operational Review focused on diagnosing the current business model and identifying the changes that need to be made to improve shareholder returns, increase profitability and drive cash flow generation across our supply chains. Decisions reached through the Operational Review include:

¹ Operating EBITDA is a measure that uses a standard price for the cattle component of cost of goods sold rather than utilising a market price, which is subject to volatility. For further explanation of this measure refer to AACo's FY17 Annual Report.

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1. **Livingstone Beef Strategic Review** – We have begun a Strategic Review process to assess all available options and determine the optimal path to deliver shareholder value from Livingstone Beef.

While this Strategic Review is underway, management will continue to focus on the controllable aspects of the production process, including further improving the operational efficiency of the plant.

Deloitte have been engaged to assist with the Strategic Review. We will provide a fulsome update on the review at the time of our FY18 results announcement.

2. **Process & Efficiency Review** – AACo has initiated a Process & Efficiency Review of its supply chains, with a primary focus on identifying opportunities to improve processes, realise cost savings and improve profit margin.

Premium (non-wagyu shortfed) supply chain

AACo's Premium (non-wagyu shortfed) supply chain has underperformed expectations, primarily due to (i) its reliance on external service providers in the later stages of the value chain and (ii) its level of exposure to commodity beef price fluctuations.

The first substantive outcome of the review is a decision to simplify this supply chain by transitioning to a cattle sale model, rather than selling beef, which will increase the profitability and cash flow from this supply chain. The change will occur after a short transition period and will be adopted going forward subject to a material change in market conditions.

The impact of this decision on AACo's financial profile will be a reduction in the volume of beef sales in the Premium supply chain and an increase in the volume of cattle sales. Based on current market conditions and various other assumptions, management expects the sustainable impact of this initiative to be an improvement in Operating EBITDA and Operating Cash flow of more than \$5 million per annum. FY19 is expected to benefit from a greater improvement than this due to one-off timing benefits associated with moving to a cattle sale revenue model.

Luxury/Prestige (wagyu) supply chain

While the Luxury/Prestige (wagyu) supply chain continues to deliver strong margin performance, AACo believes there is an opportunity to unlock further margin through cost efficiencies in addition to our focus on driving revenue growth through our branding and marketing.

Wylarah and Westholme brand launch preparation plans continue to progress in multiple markets. AACo expects to undertake its next formal brand launch before the end of calendar 2018.

AACo is currently in the process of scoping the process and efficiency review and will provide the market with a further update at the time of our FY18 results announcement."

FY18 Earnings Performance

As foreshadowed in the announcement of AACo's H1 FY18 results in November 2017, AACo's performance in H2 FY18 has been affected by external challenges including (i) increased competitive dynamics in certain markets, (ii) a higher Australian dollar, (iii) higher input prices, and (iv) an elevated cattle price environment for Livingstone Beef.

- Livingstone Beef continued to be affected by the elevated cattle price environment resulting in higher cattle procurement costs. Livingstone Beef is expected to contribute an FY18 Operating EBITDA loss of \$(18) million to \$(22) million. This compares with an FY17 Operating EBITDA loss of \$(12.5) million.

AACo's primary operational focus remains on improving the efficiency of the plant and dynamically managing throughput volumes. AACo will continue to focus on these areas while the Strategic Review process is underway.

In order to provide greater transparency to the market, AACo intends to include segment disclosure for Livingstone Beef in its FY18 audited results.

- Cost of Production increased in FY18, impacted by the one-off attrition cost (announced at the H1 FY18 results), unfavourable seasonal conditions and higher input costs continuing through H2 FY18.
- Both the Luxury/Prestige and Premium brand segments delivered year-on-year price growth for FY18, and the performance of the Singapore and Taiwan markets continues to be pleasing following the launch of the Wylarah and Westholme brands.

However, we experienced some price softness in parts of the product portfolio in H2 FY18 driven by increased competitive dynamics and strength of the Australian dollar.

- The value of live cattle sales undertaken in H2 FY18 was less than half the amount undertaken in H2 FY17. This decline reflects management's decision to focus on sustainable financial performance rather than current-period profitability and cash flow generation.
- The FY18 Statutory EBITDA expectation also reflects a decline in cattle prices relative to the end of FY17, resulting in an expected decrease in AACo's livestock inventory market valuation in the range of \$70 million to \$80 million. This impact is based on preliminary information and is subject to final livestock valuation through the audit process.

FY18 Cash Flow Performance

Expected FY18 Operating Cash Flow is impacted by the above EBITDA drivers as well as the following key factors:

- An increase in working capital, reflecting a normalisation of working capital levels following a material reduction at the end of FY17.
- An increase in livestock inventory kilograms on the balance sheet, resulting in a proportion of Operating EBITDA being non-cash in nature.
- Higher finance costs, including interest payments and the settlement of interest rate swaps as part of the debt refinancing process completed in September 2017.

Net debt at year end was \$348 million, with a Gearing Ratio (net debt divided by total equity plus net debt) of approximately 26%, at the lower end of AACo's stated target range of 20% to 35%.

FY18 Results Announcement

AACo's audited FY18 results will be released to the market on 23 May 2018. A full market update will be provided at that time.

Investor Conference Call

AACo will host a conference call with the investment community including a Q&A session from 9.30am AEST today. A recording of the call will be available on the AACo investor relations website <https://aaco.com.au/investors-media/media> later in the morning.

Participants should dial one of the numbers below and quote **conference ID 231422**.

Dial in numbers

Australia Toll Free:	1800 908 299	Australia Local:	+61 2 9007 8048
Australia Alt. Toll Free:	1800 455 963	Australia Alt. Local:	+61 7 3145 4005
Canada/USA Toll Free:	1855 624 0077	China Toll Free:	1080 0140 1776
Hong Kong Toll Free:	800 968 273	New Zealand Toll Free:	0800 452 795
Singapore Toll Free:	800 101 2702	Taiwan Toll Free:	0080 112 7377
UK Toll Free:	0800 051 1453		

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