



## Dairy Business

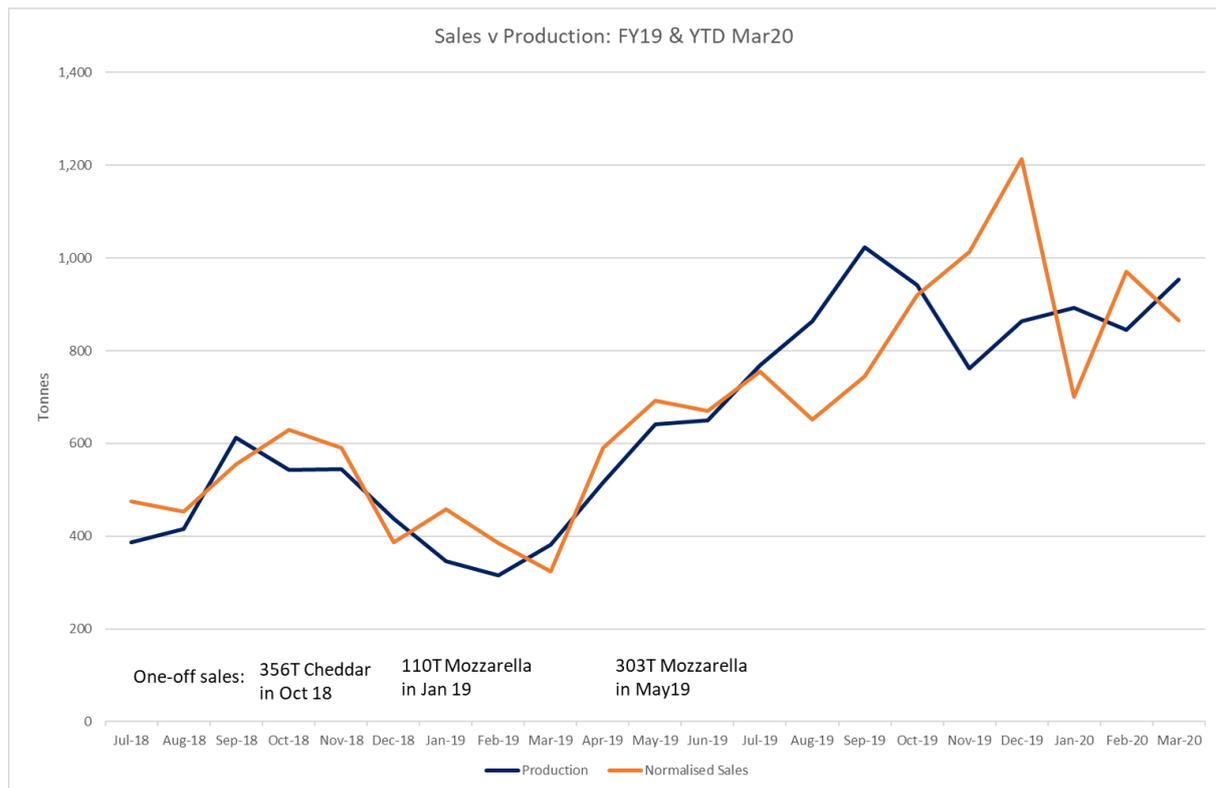
The following chart is an extension of the chart which I included in my January letter to include mozzarella and cheddar production and sales to March 2020.

You can see some of the seasonal impacts on our dairy business in the chart.

November/December sales ramp up for the traditional festive season demand and to pull inventory into the supply chain ahead of the drop off in January, as many distributors close for several weeks. February sales rebound as distributors re-open and inventories in the supply chain need replenishing.

However, we do see in March the first signs of a dip in sales caused by COVID-19.

The blue production line reflects the seasonal milk supply peak coming off from November 2019 with a low point in February before the autumn calving. Demand remained strong through to 31 March 2020 with most milk received is being produced to cheese.



Total YTD March 2020 cheese production 7,915T: Mozzarella 6,951T; Cheddar 964T

- **Production 99% higher than for YTD March 19 which was 3,984T**

Mozzarella sales YTD March 2020: 6,523T

- **Sales 149% higher than for YTD March 19 which was 2,618T**

Total revenue from dairy factories

- **YTD March 20: \$67m: \$61m of produced goods and \$6m of milk sales**
- **YTD March 19: \$56m, \$36m of produced goods and \$20m milk traded out**

From around the second week in April, we began to see a decrease in sales and forward orders from our food service channel customers. This channel accounts for about 30% of our Mozzarella sales and has fallen by about 70% over the last 3 weeks. That would translate to a 20% reduction in ongoing product sales, without the benefit of stronger retail demand and increased export sales.

We are taking a cautious approach to managing our path through this period.

Retail demand has remained strong and our key supermarket customers are taking their full contracted volumes. Export sales' inquiries have increased and I am pleased to be able to report that we have signed a new contract for 1,000T per annum supply to a large customer in China. We will be producing for this order in May, with first shipment to be made late May.

Our focus remains on the production of Mozzarella, and its associated by-products, in preference to the less profitable cheddar-based products.

We are selling some milk above previous planned levels to balance production and demand and maintain appropriate cash flow through this period.

Whilst COVID-19 has had some impact on product mix and sales at this time, we do not expect a material revenue impact overall, unless of course, the situation in Australia significantly worsens, which at the time of writing would seem to be unlikely.

### **Milk Supply**

Pleasingly, milk supply in the January-March period was stronger than we had anticipated. Rather than the 10% drop against our previous forecast levels I alluded to in my January letter, milk supplies were slightly higher than expected. We are putting this down to an earlier autumn calving, as well as signs that some farmers are beginning to reinvest in their herds with improving on-farm conditions.

Farm gate milk prices remain high and are likely to continue to have a dampening effect on gross margins but product prices were generally rising in response. There has been some weakness in spot prices for some by-products through late April, but we believe this is due to the flow on impacts of COVID-19 dairy demand reduction, combined with an earlier autumn milk flush.

We expect competition for FY21 milk supply to remain strong and we are targeting a further increase in milk supply to the factories for FY21, in line with our strategic growth plan.

## **Lactoferrin**

I am also pleased to report that the existing Lactoferrin plant is back in production following the successful resin replacement and re-commissioning. We are now back to producing Lactoferrin of 95% purity which commands the higher pricing in the market; and are noting a continued increase in demand for this product.

## **Business Development**

Inquiries from overseas for our products have increased significantly over the last two months. No doubt this is in part due to businesses in China and other regions, beginning to come out of their COVID-19 lockdown, aided also by the lower Australian dollar.

International business development can have a long gestation period. The contract I referred to earlier, for 1,000T pa to a major Chinese buyer, has been one we have worked on for some time further to the review of our sales team and capabilities. Management has a positive outlook with regard to further growth opportunities for export sales.

## **Farms' Sale and Leaseback**

We continue to make good progress with the farm sale and leaseback process, notwithstanding that the COVID-19 restrictions have impacted the various parties' due diligence processes and slowed negotiations to an extent.

The timing of settlement is therefore likely to be a little later than we had initially expected because of delays resulting from the COVID-19 restrictions on travel etc.

As advised at our AGM in November 2019, the purpose of the sale and leaseback is to redeploy \$30+m of capital invested in the farms to our factories where we can achieve higher rates of return, per kilogram of milk solids processed. The proceeds will also significantly reduce bank debt and reset balance sheet gearing.

This will place BFC in a better position to undertake non-organic growth should opportunities arise in the shorter term.

## **Lactoferrin from Skim Milk**

The BFC Board has approved the expansion of our dairy protein (Lactoferrin) plant at Jervois. The project which will commence as soon as funding permits. The total cost of this important upgrade will be in the order of \$12m, with a pay back of less than 24 months.

This exciting project also provides a solid platform for a later expansion of production capabilities into other nutraceutical products, further "stretching" the value we can extract from our milk intake.

## Strategic Imperatives

As presented at the AGM; there are 5 key strategic initiatives which are in the process of implementation. A brief update is provided below –

<b>Strategic Imperatives</b>	<b>Comment</b>	<b>Status</b>
<b>Capacity Utilisation</b>	Nearly all milk received being processed to cheese.	<b>Good</b>
<b>Sales Pipeline</b>	Strong demand for mozzarella domestically and internationally, although current COVID-19 impacts in domestic food services	<b>Good</b>
<b>Enhanced Product Mix</b>	Mozzarella sales at 80% of total cheese production. Lactoferrin production from existing plant recommenced. New product development to add to margins.	<b>Good</b>
<b>Grow Milk Supply</b>	Critical focus area in 2H20 for FY21.	<b>In Progress</b>
<b>Dairy Nutraceuticals</b>	Current production capability restored. Lactoferrin from skim milk will expand capacity and significantly add to earnings.	<b>In Progress</b>

## Provincial Food Group

PFG has benefitted from the stronger retail demand for its meat-based products caused by the COVID-19 situation. This stronger demand has seen PFG move from a loss-making position, as previously advised, to at least a break even position with a solid order pipeline, currently, for the balance of the year.

The team at PFG have also been working hard to drive further improvements in the production process and cost reductions which supports enhanced growth in their operating results.

Management and the Board are continuing to drive the transition of the core dairy and meat businesses from start-up phase to commercially sustainable enterprises and a lot has been achieved over the last 18 months.

We look forward to Australia and the world gradually recovering from this pandemic – and from BFC's perspective, we continue to focus on positioning the Company so that its strength will be in its ability to rebound faster, stronger and better than before, once these challenges presented by the current COVID-19 situation are under control.

We will continue, of course with our energetic focus on delivering on the strategic imperatives.

I look forward to your continued support through the remainder of FY20 and as we prepare for FY21.

Kind Regards



Jonathan Hicks  
Chief Executive Officer

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