Interim Results FY20

Transcript

Investor Relations - Nikki Catrakilis-Wagner

Good morning Ladies and Gentlemen. Thank you for joining us for Tiger Brands' unaudited Group results for the six months ended 31 March 2020. As per usual we will be taking you through the presentation, CEO Noel Doyle will present the results, the financial and operational results as well as the outlook so the agenda is pretty much the same as always. Before we begin, I just want to draw your attention to the forward-looking statements. Once Noel has presented the results we will then move into Q&A. Thank you.

Chief Executive Officer - Noel Doyle

Good morning everybody. Thank you very much for your time this morning. We are presenting a set of numbers that broadly is within the range in terms of headline earnings per share as to what was guided from our trading statement. Two specific call outs that were not envisaged at the time that the trading statement was issued, first of all the settlement agreement in respective of brand rights with the former distributor in Nigeria, as well as a significant gain on foreign-denominated cash resources. The net effect of that was just over a negative 1% on the earnings that we reported. Just important to call that out and I will come back to the settlement in particular a little bit later.

I think what we see when we look at the numbers, I suppose the key feature is continued pressure on volume and broadly speaking a challenge to hold on to market share and recover cost push. It's quite clear that the pre COVID environment the business was already challenged in terms of its ability to grow volume and sustain premiums. And that will place a key focus for us going forward in getting to the correct price points that will allow us to grow at or above market share and to do that clearly requires some re-engineering.

The result in terms of our operating income is down 29% which is an incredibly disappointing result and the HEPS down 35% as you've seen but aligned with guidance.

If we look at the key features and I will talk about the specific category differentiations, but essentially the problem revolves around pricing and recoveries in a market which is already quite challenging from a consumer perspective. Without the volume you end up with under recoveries and it can become a vicious circle in terms of the cost issues. What we've seen continue, and it was something that we would have anticipated, is the level of promotional intensity and the level of volume that sold across the entire market on a pricing platform and through deep cut promotions, continued on some level as previously.

We had specific volume challenges in certain of our categories. Maize is proving quite difficult for us to get above the break-even point, as that market becomes increasingly commoditised. Sorghum and Maize breakfast cereals particularly from a Sorghum perspective relative to other raw materials has become quite an expensive commodity and that portfolio serves the bottom end of the market so, quite a challenge there. And on Rice I'll cover that in a little bit more detail later.

Snacks & Treats, even before the impact of COVID, maybe a small impact for the last couple of weeks as consumer spend was diverted towards more essential foods, but we were seeing some challenges there. That is linked to price competitiveness, particularly in chocolate, a big response to our price positioning which put us under pressure in the period. The Exports pretty good performance out of the market in Mozambique but offset by our inability to export for this period into the Nigerian market, and we will cover that in more detail later.

By and large then, the issue is external but an external issue that we have to address. And it's about hitting the right price points that allow us to get the right level of volume and that comes back to our cost positioning in the market. But there were a couple of internal issues where we could have sold more if we hadn't had those issues; the biggest impacts being in pasta and within condiments & ingredients. No attempt on our part to hide behind the COVID-19 as a rationale for these set of results. As I say we have come out where we guided.

We did see some progress in terms of our market shares in the month of February and March. Those gains in market shares, however in March in particular, were amplified by the weighting of the market towards essential foods and the weighting of Tiger towards essential foods. For the month of March, we certainly sold a lot of volume but at very low margins particularly when you look at our Rice and Wheat business. And I will talk to the Rice and Wheat business and the impact of pricing regulations on those as we go forward.

So, the highlights such as they are, good performance in terms of the top line from VAMP which drove the recovery. I've covered and I am not going to dwell on it, our inability to get fair share of volume at the pricing that we sought based off our cost base. Impairments relating to Exports & International were not necessarily anticipated at the time of the initial trading statement. Those come from two factors, one a significant increase in the WACC rate against which the cash flows are discounted. Essentially we've had to look particularly, when we talk about the Nigerian market and where the oil price is and the possibility of the devaluation or significant inflation in that market, the potential impact of COVID-19, and on a combined basis we have made an assessment that we can expect from our own experiences as we go back to the last devaluation in Nigeria, quite a challenge. A step down in terms of performance, particularly if one looks at the history of UAC in that time period and we have considered that.

As regards our Deciduous Fruit business, the Far East market has been significantly impacted by both COVID-19, but also by a change in the dynamic in terms of duties between the European Union and the US. Which has made the Chinese market more attractive for fruit producers and brought even more competition into a market that was already heavily traded in a category that globally is in decline.

IFRS16 had a pretty negligible impact and most of what you see in terms of the balance sheet debt comes from our leasing arrangements, specifically Albany's (bakeries) vehicle fleet.

Cash generation was pretty good. We've had really good cash collections in March and that continued into April. We were, to be totally transparent, we did get a benefit that flowed from the big run on stock, particularly Rice, Wheat and Pasta towards the end of the year. That helped our stock position and you can see that in the updates. That doesn't take away from what we believe was a fairly good level of working capital management.

On the interim dividend, just to be as clear as I can, the view that was taken by the Board in passing up on the interim dividend, even though we are in a cash positive position, with significant facilities available to us, that globally the world is in such a state of flux and we are yet to see the full impact as infection rates increase throughout the population, and the view that was taken is lets be prudent and review the position at year end. At year end, all things being equal, based on where we sit today we would make up the dividend in line with our dividend policy so we would declare a final divided based on our 1.75x cover for the year's earnings.

We will skip over this slide which is just a set of facts. Nikki if you don't mind moving us on.

Within the income statement just a couple of things to call out, specifically the impairments I will cover in a little bit more detail. The abnormal items is really the settlement of the dispute, a provision for the settlement of the dispute in

Nigeria offset by a capital gain on a warehouse that was surplus to our requirements. And then the net finance and investment income, you will see there's a significant benefit there that flows through from that forex revaluation on our foreign-denominated cash which was indicated previously.

The impairments, I think I've covered that in a fair amount of detail. It is really about looking at the long-terms prospects of those two markets. In Personal Care we've just assessed some of the tail-end brands in the Personal Care business. It is something we intend to address in terms of cutting the tail and either selling or licensing those brands in the second half of the year.

I don't think there is anything further to add on this slide, except perhaps to say that maybe a sense that a new CEO comes into the position and he decides to clean house. I just want to give you the assurance that that isn't the case. These are impairments having been considered by the Audit Committee and the Board and are valid given our view of the circumstances going forward.

You look at the performance of our Associates, I think in the environment in which we operate globally, not a bad performance particularly out of Carozzi, but it has been impacted by the weakness of the Chilean peso against the rand. It's worth calling out that The National Foods Business operating in probably the most challenging environment of any of our Associates has actually managed to hold its own relative to the prior year.

Volumes, on the next slide, re-illustrate the challenges that the business faced and needs to confront and address head on as we move forward and that is the inability to get both volume and pricing growth in a consumer market that is likely to be even more stretched and strained as we go forward. That significant volume loss in exports is really the fact that we weren't able to trade in Nigeria for the first six months of the year.

At the time of the trading update, we highlighted where we had specific issues. Probably the issue that wasn't called out at that stage was in the Groceries business where we've had a pretty disappointing performance, in terms of our February and March results, notwithstanding the sell-out that was taking place ahead of COVID. And our Snacks & Treats business slowed down significantly in the month of March as people diverted spend, although we were already seeing challenges in the months of January and February in terms of our price positioning particularly in the chocolate category.

Capex, I've been asked quite a few questions around capex as part of a mitigation of the impact of COVID-19, whether Tiger is going to significantly slash its capex projects. That isn't the case, we obviously going to be careful on what we spend. What we are actually seeing in terms of capex is delays in projects as a consequence of the shutdowns that took place in Europe where a lot of the equipment is sourced. We've spent R 500 million so far this year. Expect to spend another R 500 million next year and the guidance for 2021 is still in the region of R 1,5 billion. We call out how we have allocated the spend so far this year.

Attend to the segmental issues. The Grains business, you've really got two big stories within Grains. The first one specifically is within the Wheat to Bread value chain. I believe in terms of market share performance and brand strength we don't have a significant weakness; this is really a category competitive dynamic issue; we haven't seen price increases of any significance in this market for the last two and a half years. One of the impacts I will call out later is the fact that there was a price increase which we were quite confident of it being effective and holding onto it at the end of March, which was superceded by the regulations published by the DTI (Department of Trade & Industry) in the middle of March. So, that business we think is performing quite well, is competitive from a cost perspective against all the benchmarking that we have been able to do but is really operating in a category where the competitive dynamic does not allow for price increases. I think we have done reasonably well to more or less hold onto share in that area.

In Rice, we have struggled to get the right price points in Rice. Had a major volume haemorrhage in the first quarter as a result of being aggressive in pricing. Then we were probably a little too passive in pricing in the second quarter which meant that we deferred a price increase that was required as a result of what was happening with the rand until the 1st of April and again got caught in the net of the pricing regulations. What is quite clear though when it comes to Rice, is that there is still significant scope for us to go after re-engineering the cost model both in terms of our procurement and in terms of local versus international packing and in terms of where we have the Rice delivered. Some of our competitors are on a different model delivering to several ports directly and then direct to customers. We still have the model where we deliver into one point of packing and where virtually everything is packed locally.

Pasta, we had some serious problems at our Pasta plant in Isando particularly in January and February. Throughput is up significantly in that space but still some issues. We got a major piece of capex planned for the next couple of months which should give us consistent supply for the remainder of the year.

Jungle and Sorghum cereals, there has been significant cost push due to not a great local crop. High volume of imported oats. Sorghum's pricing relative to Maize is out of sync relative to that target market. So, again challenges in cost recovery for the consumers and you can see where we have attempted to move on pricing. You see almost an immediate response from the consumer in terms of them choosing to switch out of our brands and that's reflected in some of the market share that you see.

Rice in particular, really took a hit in the first quarter. Much better shares for the second portion of the six months. But shares that we gained at an operating loss in that period.

In Consumer Brands - Food, again a challenging performance with some volume declines in our Groceries business offset with some pricing. Overall this is one of the businesses that requires the largest amount of effort and has been receiving priority and I will talk to you a little bit later in terms of cost initiatives as we go forward. Despite that disappointing performance you can see certainly in the top end the market shares have remained reasonably robust, but market shares without Rands in terms of profitability, not really satisfactory. Snacks, Treats and Beverages, Snacks & Treats I have covered before. We find ourselves outpriced particularly in chocolate and we've seen the category come under pressure. It is discretionary spend and we need to reconfigure for the spend that is available, that is one of the categories where we are seeing a very different shopping pattern. People are shopping a lot less, a lot less interaction with convenience stores and therefore we need to provide offerings here in multi packs or larger packs as opposed to the single packs - we've moved a little bit too slowly in that respect. Our Beverage business, the benefits of prior year and the strong brands flowing through there with some investment ahead of the curve. In terms of marketing spend we'll see some of that pull back in the second half of the year, but the Beverage business posted a solid growth in operating profit before marketing. You can see that performance reflected in the market share stats.

VAMP, we've been very pleased with the level of top-line growth within the category or sub-categories where we have decided to participate. It remains an extremely competitive category. Our path to getting this business back to profitability was impacted by non-participation in the deli segment which we've discussed previously. As far as the transaction around VAMP is concerned, we took a view that non-withstanding the fact that we are still involved and hopeful of concluding a deal on the exit of this business that would have the impact of preserving all of the jobs in the business. From an accounting perspective, in terms of the high level of probability required to classify this operation as a discontinued operation, we haven't crossed that hurdle yet. The negotiations have been intense and are still ongoing and as I say we are still hopeful that we may conclude a deal in the next couple of weeks.

Our Home, Personal and Baby business, Homecare we were able to take inflation in the pocket, managed to perform well in terms of our market share, a very good performance. Personal Care remains an incredibly competitive space. As I said our plans are to trim our category participation and take some of our tail brands that may add value to other players and either licence or sell those off in the second six months of the year.

Turning to Exports & International, I think I've covered the sort of impact of the dispute with our previous distributor. Our view in respect of ownership of those brands has not changed and that was communicated previously, However, once wrapped up in extensive litigation the timelines were stretching out ahead of us in terms of following the processes in Nigeria and we've just taken a pragmatic decision around reaching an early settlement of this issue. One, to preserve the long-term value of the brands and two, to get us trading again. The settlement that we've made is less than one year's profitability out of this business and we faced the possibility of being tied up in litigation for a number of years. That explains the decision to make that settlement.

Our business in Cameroon continued to perform quite well. As those of you who know the market well will know that it's been a market with virtually no inflation over the last four to five years. The government has found itself under some serious fiscal constraints and from the 1st of January introduced an excise tax, very similar to GST, of 5% on turnover. That essentially, in terms of a pass through, would be a 5% increase in prices, into a market that's already challenged. That cost of R14 million was absorbed by the business in the first quarter and we are starting to pass that through in the balance of the financial year. We'll see what impact that has on volume, but it is likely to create some challenges for the Cameroon business, Chococam, going forward.

Deciduous Fruit, we've covered the longer-term outlook on that business. But in the short term we saw serious port blockages in the Far East, which was the first area hit by the COVID crisis. That meant that we had to divert some of our products that would have been earmarked for that market to the less profitable markets in the US and in the UK.

So, having posted such an extremely disappointing set of results, the questions that I would guess are going to be: given what's likely to be an even more challenging environment going forward – what is the plan?

So, I think first of all, from a business perspective our expectation is definitely that for the next 18 months at least we are going to see a significant economic downturn, probably the most severe recession that we've seen, certainly in my lifetime. That's going to be compounded by the impact on the economy and our business of a weaker rand in terms of imported products and import parity-driven pricing dynamics. Our core market in the mid-LSMs is definitely going to be impacted by increased levels of unemployment with the impact that has on disposable income and we are going to certainly see some changes in consumer behaviour.

As we go forward and we release down into Level 1 and beyond in terms of the Lockdown alerts, what we are going to see is some of the benefits that we've had in April and May due to limited roots for consumer spend - essentially consumers have had very little choice of where they spend their money and therefore the food sector has certainly gained from that. As markets open up, we're are likely to see less consumer funds dispersed across a broader range of categories and that's definitely going to be a challenge and is going to place an absolute emphasis on value propositions, which will be a challenge for us as Tiger. We hope, not hope, we intend to respond to that appropriately.

There are some upsides to the environment that we find ourselves in. In terms of the Lockdown, but beyond the Lockdown in terms of consumer behaviour, the quantum of in-home consumption is likely to be higher and that's generally good for our brands. We are expecting our first shipments into Nigeria in the month of June and given where the rand is sitting currently, if it sustains itself your local production is likely to be more competitive against international imports and I do think it will provide some opportunities particularly for us in certain categories to go after the efficiencies that might come from participating in the private label sector. This is something that we are exploring with customers. Not to do something opportunistically, but where it makes sense in terms of our category dynamics and our capacity and it makes sense for our customers that we can do something on a sustainable basis, we will be exploring that with our customers.

Risk factors other than the broader macro is that you get a serious second wave globally and that puts some pressure in terms of export bans and pressure on port facilities in terms of import procurement. The National Disaster pricing regulation has had a major impact on us since it was introduced and I'm going to cover that in a little bit more detail and the extent to which that period is extended will be a challenge for us going forward. Of course our primary objective is to continue operating while looking after the men and women who have kept our factories running and kept the shops full for the last three months and that does not come without cost. I don't anticipate that for the remainder of the calendar year we are going to be in a position to reduce any of those costs. We will also have the phenomenon, I think the President discussed last night, that the infection rate increases, even with the best protocols in place, it is inevitable that we will see infections in some of our sites that will require closure resulting in disruption to the supply chain. We have worked hard to build stock but there are certain categories where stock build hasn't been possible and, in those categories, any significant disruption is likely to have an impact on sales out and productivity.

The COVID-19 related costs are likely to be significant. I have tried to give you a sense of these costs and to emphasize that these costs do not include the costs of any disruption in terms of the requirement to close facilities going forward. In the month of April, we were not producing in terms of the regulations in our Home Care factory and in our Malt and Beer powder business at King Foods (sorghum-based products) and the loss of contribution from that is set out clearly. In May we received the go ahead to produce and sell in our Home Care range and therefore that loss declined significantly.
On pricing there will be the cynics amongst you who may say that the R357 million is an opportunity cost, it's a price increase you perhaps you thought you might implement, that you might not get, given what you have seen in the previous three months in terms of the challenge reflected in getting price. The

vast majority of the pricing that we have highlighted as being a constraint imposed by the regulation really relates to Bread where we were quite confident of getting an average price increase through of about 5%, effective at the end of March. We had agreed with our customers a price increase of our Rice business to take us out of an operating loss into a profitable position going forward. The balance relates to annual price increases anticipated to be taken mostly in the Groceries business. So, you may debate the validity of that number but I'm quite confident that between R200 and R250 million of it in Rice and Bread were increases that due to the entire category dynamic would have stuck in the market.

We have also incurred costs related to additional supervision and additional PPE in the plants. We are providing additional staff transport that's under our control in terms of the passenger loading and in terms of the sanitisation regime. And of course, so far to the end of May in responding to the social needs we have ramped up our social investment by R13 million with a number for the remainder of the year yet to be determined.

So, the impact for the second six months, assuming the pricing regulations apply for the entire period, we anticipate being somewhere north of R500 million and again I just want to emphasise that excludes the cost of any future disruption which is difficult to predict.

In addressing the challenges that we face, there is no one size fits all solution for Tiger. The approach we have been taking in both in terms of how we structure ourselves to deal with the challenges that we face as well as the focus that we bring, means that we are looking at the category dynamics in each individual category and trying to address those specific issues with as great a degree of speed as we possibly can. What I have set out in the next couple of pages, are the drivers for us over the next six to 18 months, but particularly the next six months in terms of us rebasing our cost base in order to get to a premium that is going to be sustainable in what is going to be an ever more challenging market.

I am happy in the Q&A to respond to those specific issues.

So really, we are just addressing this, based on the categories with the biggest challenges in a methodical, very category specific dynamic. There are some over-arching themes, but even those themes have very definitive and clear subsets in the individual business. Therefore, in terms of some of the restructuring that we are doing, we are changing some of the lines of accountability that I believe may have been blurred as we moved towards a matrix that we can have very clear lines of accountability, in terms of the day-to-day execution within the business. Key areas where we are going to get efficiencies like our logistics, like our procurement and key areas around compliance in the areas of food safety and financial controls. Areas where we have to and we have highlighted the need for a proper capital allocation model like our innovation funnels, we are preserving our investment in those spaces and preserving the central control, but we are trying to free up the category teams to push for fast execution of the key themes we have identified previously. The business model quite clearly in this environment has to work from the appropriate selling price down and we have to keep focusing and keep re-engineering until we find a business model with costs that allow us to sustain market share at the right price points.

In terms of what you can expect to see delivered by the end of the financial year, I think you will see in the next couple of months the completion of the structural alignment internally. We have already started down the road in terms of cost saving. Between our corporate office and two of the key challenged categories we anticipate annualised savings and having those implemented in the last quarter, of R250 million. Getting into the level of detail required and getting to site has been an issue. We are working through the most challenged categories methodically and we will have completed that work in its entirety by the end of the year.

Concluding the VAMP exit, we are quite confident that we will not be operating in the VAMP business by the end of this year. We have announced, after many years of challenges and volatility in the Deciduous Fruit business, that we don't believe we are necessarily the best owner for this business, and we have started a process to explore taking Deciduous Fruit out of our portfolio. And we have also started a process within our Personal Care business to rationalise the expansive tail in terms of those brands.

So Ladies and Gentlemen thank you for hearing me out. It's certainly not a pretty story that I am telling you, but I am confident that we have some very specific plans already in place and we are starting to create some momentum to drive a better performance, a better underlying performance as we go forward. In the very short term, that R500 million COVID costs is a real millstone that we will have to deal with and is definitely going to have a significant impact on our earnings for the full year.

If I can hand over to Nikki, I think you'll moderate the questions.

Nikki Catrakilis-Wagner
Are there any questions on the conference call?

Moderator
Yes, the first question comes from Myron Raj from Mibfa. Please go ahead.

Question:
Hi guys. Thanks for the opportunity to ask questions. I've got two if I may. So the first one you said leading into the Lockdown before your period end you certainly saw sales because of people stocking up but you've guided in February before you knew there was going to be a Lockdown a certain range

and you had a budget. It looks like even with the benefit of the Lockdown you have underperformed. You come at the bottom end of the budget. Can you give us what happened or is there something I am missing? Can you explain a little more perhaps? Thanks, and I've got one more question.

Answer - Noel Doyle:
In response to that question, what we saw in that second six weeks in March we saw an increase in volumes in Rice, Pasta and Maize and Wheat, particularly Wheat and Rice. And those are categories where we make extremely low margins. At the same time we saw a pretty significant slowdown in Snacks & Treats, Beverages where there seemed to be a bias towards sales out towards carbonated beverages as opposed to concentrates and in the Personal Care and Home Care business they slowed down. We had a lower rate of sale in high margin businesses and a higher rate of sale in very low margin businesses.

Question:
Great, thank you. The second question is sort of an overarching question. Recently, I was lucky enough to attend the presentation where they explained to us that in the South African markets similar to sort of global markets the price premium that food producers get for the brand leader you get is shrinking and it's shrinking all the time. This is true overseas and in South Africa. You can see that in your Foods business as well as Grains business. Even specially on the Grains business it was pointed out to us what the familiar quality metrics look for in Bread, softness, freshness, tastiness and so on. It appears that the brand premium is coming down but that the competition has caught up with Tiger Brands and in fact some of your peers are outdoing you in consumer taste tests on these attributes. So just a general question, Noel if you don't mind. Is the brand premium coming down? Is this something that's going to be a constant feature and therefore is this just now that is all that's left for you to pull is the cost lever so that you can actually be reasonably profitable?

Answer – Noel Doyle
So I think the point that you raise around brand premiums is certainly relevant and probably more pronounced in basic foods, like Bread and Rice and Pasta. We recognise that and you can see it in our numbers. You know as you attempt to inflate pricing you can see there is a switch off in terms of volume. That is why getting the cost base right to allow us to get that price premium in those categories is important. And it is particularly important in the short term because the other levers to pull are really about what you put into the market that is different and how you modify consumer perception of value on existing product ranges in terms of price points. So, on price points and different pack formats I think we can make some progress on that in the short term. The real innovation, having done a regroup around our innovation, that takes a little bit longer. So, in the short term, when I say the short term in the next 12 months, the focus has to be on taking out cost because of that dynamic which we don't

see changing dramatically. To be honest, is likely to intensify given the kind of post-Lockdown health of the consumer and the higher levels of unemployment. So, you are right, in the short term the biggest lever has to be re-engineering our cost, both for the volumes that we are getting. Cost is not just our operating expenses, we are going to have to revisit all of our procurement models, we are going to have to revisit all of our formulations as well.

Question:
Thank you. Just a clarification before I leave you. You mentioned a figure of R250 million saving from property and other related cost cutting. Is that a quarterly number or annual number?

Answer - Noel Doyle
That's the annualised number that we have identified and which we will start to put into execution right now. Only in respect of the corporate office and two of the categories in which we operate.

Investor
Thank you so much Noel.

Noel Doyle
What we've been doing whilst managing through the COVID crisis is tackling sort of the areas where we thought there were the greatest levels of opportunity or risk and we have got plans that I'm very comfortable to stand behind for two categories plus the corporate office that will deliver annualised savings of R250 million.

Nikki Catrakilis-Wagner
Is there another question on the call?

Operator
No, we have no further questions.

Nikki Catrakilis-Wagner
This question is from Michael Klopper. How do you assess the success of promotions? That is, are volume increase the end goal? Do you seek the maximum Rand EBITDA from the promotion?

Noel Doyle
So, each promotion will have different objective depending on the category that is being promoted. Depending on whether we are responding to a perception of brand weakness or whether we are launching a new concept. But the overriding requirement is that a promotion gives us better rand EBITDA. So, if we looked across the wide range in terms of promotional valuation, we look to promotions that make us more Rands. We are starting to be more judicious about which promotions we engage in and having some robust discussions

with some of our retailers, where based on empirical evidence, we are not participating in promotional activity which doesn't give the payback.

Nikki Catrakilis-Wagner
The second question is from Steven Hurwitz from 36One. Why is Tiger Brands unable to put through pricing increases in Bread? Don't the pricing regulations prohibit you from increasing margins not from putting through price increases to recover input costs.

Noel Doyle
Specifically, to Bread, if I can just step back. The regulations allow you to put through price increases for cost push that you have over the reference period and after the dates of the regulations which was the 15th or 16th of March. In the case of Bread, the price increase we were seeking to put through was a price increase not linked to cost push now but to historical cost push. Therefore, putting through that price increase would have had the impact of correcting both gross and operating margins. The guidance that we've received when we looked for clarification, is that if you increase your gross margins or your operating margins without there being a specific cost push, post the date of the regulations that you would be in breach of the regulations. So, what we have been able to do successfully is put through cost push linked price increases in both Rice and Wheat in May. We've got more increases going through in those categories in June and probably one in Pasta. But all they do is allow you to hold your margins at the level that they were at previously. The reference period for us being December of 2019 and January and February. They are two of our poorest months so for example, in that reference period we actually lost money in Rice. The price increase that we were due to put through in Rice on the 1st of April was to correct those losses and the impact of not being able to put through that price increase which was not driven by raw material cost push is almost R100 million for the second six months of the year. Even though we've able to recover subsequent cost push. The Com-Com (Competition Commission) have also guided very clearly that if you end up with leverage as a result of volume, the benefits of that leverage have to be offset against any raw material cost push that you seek to push through. So, effectively the impact of the regulations is to freeze your profitability and your margins at the level of the reference period, which is the three months ending February 2020.

Nikki Catrakilis-Wagner
The next question is from Muneer Ahmed. Are you able to give some guidance on when you expect VAMP deal to close and can we expect the second half losses to be the same as the first half? Has the sourcing of raw materials been impacted by global Lockdowns?

Noel Doyle
I'll take the second questions first. By and large we've been successful in keeping a consistent supply chain through this period. It's been tight in some

of our categories but that's been more demand related than supply related. There are certain isolated instances, where for very specific parts or components or ingredients we've had some delays. But that's not been a major disruption in terms of our ability to supply so far. It is something to watch quite carefully and what would be more concerned about is port congestion particularly if you end up with port closure as a result of higher infection rates that might occur at the port itself. So that is an issue.

As regards to VAMP we are sort of deep in negotiations with the parties who have expressed an interest. I am still hopeful that within the next weeks rather than months we will reach a successful conclusion to the deal but as I said, we are not in a position yet where I could express that as a high probability. Losses in the second six months likely to be slightly less than the first six months and as I say we do intend to ensure we go into the next financial year without carrying those losses.

Nikki Catrakilis-Wagner
The next question is from David Oberholzer. Good day, in the April trading statement it was stated that a 5% depreciation of the rand from your budgeted level of R 15,50 amounts to an annualised impact of R600 million increase in costs. Does this still hold true for the second half of the year now that you are re-engineering your cost base? Or will TBS rely on cost recovery to make up for the rand depreciation?

Noel Doyle
That dynamic and those sensitivities will still apply. We're still living off the benefit of some procurement positions, so the full impact is only likely to be felt in the first quarter of new financial year. There is a limited amount of work that we can do in terms of changing that cost base. So I would say the majority of that rand exposure is still an issue that will need to be recovered in the marketplace. The cold comfort is that is likely to be a cost pressure that will be borne right across the segment and across our competitors and the sustainability of not recovering it from an overall category perspective must be quite limited, especially given the operating margins that a lot of our competitors operate at which are lower than ours.

Nikki Catrakilis-Wagner
The next question is from Kgosi Ragube. Thank you for the opportunity. Panic buying – are you seeing a slowdown in staple categories as sales even out between pantry loading? And the second question – what are some of the challenges that you are facing on the disposal of VAMP?

Noel Doyle
We've certainly seen a slowdown, but we are still seeing quite positive volumes out of the base carbohydrates, essential carbohydrates. Some of that may be coming from the fact that effectively because of the pricing regulation in the base period we have been locked into a very competitive pricing

position. But there definitely is, and we expect further slowdown in that growth. Very strong growth which I think I shared previously in the month to middle April slowing somewhat but still reasonably robust performance in the month of May.
With regards to VAMP, the complexities of dealing with multiple inter-related parties is part of the complexities of doing the deal. As is, quite frankly, attempting to sell a loss-making business into quite a challenging macro-economic environment.

Nikki Catrakilis-Wagner
The next question is from Nick Webster. Good morning. You have always said that at no point would you consider private label. What has changed and what categories and what possible timing. Thank you

Noel Doyle
So, what's changed, I think first of all in terms of private label we've certainly said it's not a priority while in certain categories like the VAMP business we do significant private label business. But there is definitely a change in focus. We have to accept the reality of where we are and the fact that private label is going to grow. We have got volume hungry facilities and private label can allow us to reduce unit costs for our branded offerings as well as put us in a competitive position relative to other players in the category. There are more opportunities now, potentially with a weaker rand given that position that's likely to be sustained. At this stage we are not commenting on the specific categories, but we should be in a position within the next month or so to give more clarity after we've concluded discussions with some of our retailing partners.

Nikki Catrakilis-Wagner
There are no further questions. A lot of them have been covered by previous questions and I will revert to the other more detailed questions. Thank you for joining us and you are welcome to follow up with me if you have additional questions. Thank you.

Noel Doyle

Thank you

Ends