



## TRADING UPDATE:

# Blackmores downgrades full-year profit expectations to reflect adverse costs in addition to challenges associated with Coronavirus in the second-half

*The financial information in this announcement is subject to auditor review, which will be completed in conjunction with preparation of the Appendix 4D that will be released to the market on 25 February 2020.*

*All figures quoted exclude the impact of AASB 16 Leases so they can be compared like-for-like with the historical outlook previously provided for H1 FY20.*

### SUMMARY

- **First-half revenue of \$303 million, underlying NPAT of \$18 million.**
- **Full-year NPAT expected to be in the range of \$17 million to \$21 million including impacts of Coronavirus.**
- **The Group's transition to manufacturing has put pressure on the second-half result – including approximately \$13 million in expected adverse cost of goods impact (which includes \$9.5 million at the Braeside manufacturing facility).**
- **Costs associated with rollout of new product labels have been adversely impacted by Coronavirus disruptions.**
- **Anticipating at least 2-3 months of China sales and supply challenges due to Coronavirus.**
- **Decision taken to move to more efficient trade promotions, starting in Q4.**
- **The Board has decided not to pay an interim dividend, to conserve cash for operations.**

### DEAR SHAREHOLDER,

Blackmores Limited (ASX: BKL) today released an update on the first-half financial results, which remain subject to auditor review. This includes a change to outlook for the full-year result as a number of cost increases and operational challenges are expected to impact the business in the second-half.

It is expected the Group's first-half statutory NPAT is \$18.3 million with an underlying NPAT of \$18 million. Statutory NPAT includes post-tax one-time items which net to a gain of \$0.3 million (excluded in the underlying trading results shown). The quality of earnings and underlying NPAT has not met expectations during the first-half.

Revenue in the second-half is expected to be similar to that achieved in the first-half, though the significantly higher costs associated with manufacturing and other factors will have a material impact on

the FY20 result. Directors therefore anticipate full-year NPAT will be in the range of \$17 million to \$21 million.

The Board understands and acknowledges that shareholders will be bitterly disappointed with the financial performance of the business. The Board acknowledges that these results are completely unsatisfactory and we have much work to do to restore confidence in Blackmores.

The Board wants to assure shareholders that the matters shared today are being fully and comprehensively addressed by the Board and new Executive Team.

The company has a largely new leadership team, led by myself since joining the business in late 2019. The team has quickly made inroads to identify the challenges facing the business and to progress a plan to return the company to an acceptable level of performance.

There is a lot of work to do to restore the trust of our shareholders and we are resolute in our commitment to doing what it takes to achieve this.

Our new management team is progressing plans to turn around the business, which involves getting better control and visibility of our fixed costs, improving gross margins and significantly improving quality of our earnings in a more sustainable way.

Some of the key factors impacting profitability in the second-half are outlined below.

## 1. BRAESIDE MANUFACTURING SITE

Having taken ownership and management of the Braeside production facility on 25 October 2019, just two months before the end of the half-year, adverse cost variances relating to capacity under-utilisation, increased raw material costs and changes to the manufactured product mix have become apparent.

As Blackmores produces more than 1,000 individual product lines, changes to the volumes and variances between these directly impacts EBIT.

Now that management has full visibility over the cost variances related to the Braeside manufacturing site, it is apparent that the forecast product mix, volumes and material costs will have an estimated combined adverse impact of \$9.5 million on the cost of goods sold in the second-half.

We are confident that the Braeside manufacturing plant will be a key competitive advantage for the Blackmores Group over time, with specific intellectual property and a highly skilled workforce as well as several manufacturing licences and product registrations linked to the site. These continue to be vital for sustainable growth across several Asian markets.

This capability also ensures that we remain proudly Australian when manufacturing complementary medicines – an important quality that underpins our brand. It is critical that we achieve greater efficiencies at the site, by increasing manufacturing volumes and by better managing product mix.

Addressing this key change to operations is expected to take at least 24 months and will include a combination of cost saving initiatives and higher volumes. This will help to ensure the site's contribution to the Group's financial position improves each year.

We are shifting our product development focus onto fewer, bigger and more premium offerings for consumers, which will lead to longer run sizes, positive mix and contribute to greater manufacturing efficiencies.

The final acquisition and working capital payment of approximately \$20 million for the Braeside site will be paid in the second-half.

## 2. INTRODUCTION OF NEW LABELLING

New product regulations imposed by Australia's Therapeutic Goods Administration (TGA) regarding product claims and labelling requirements will be enforced in coming months. In addition, following a

review of all labels to ensure full compliance, Blackmores has taken the opportunity to upgrade label designs for the Blackmores brand in all markets.

This is an ambitious but necessary piece of work. The outcome will not only meet new regulatory requirements but importantly will make it easier for consumers to better navigate our range, with clearer communication on pack and improved presence on-shelf.

While our market research shows refreshed label design will contribute to volume growth in FY21 and beyond, there are costs and revenue phasing effects which have a one-time impact on EBIT in the second-half.

We have revised our forecast of costs related to this transition in the face of disruptions linked to the Coronavirus outbreak.

These costs include actively managing trade inventories of old label product so that new labels are introduced into the market in a coordinated manner, including a full changeover in time for the September 2020 TGA deadline and important customer events, especially in China.

This program of work will have an approximately \$7 million EBIT impact. In conjunction with transition costs we also include estimated costs relating to the disposal of old labels and product.

### **3. ADDRESS MARGIN EROSION**

We're focused on rejuvenating our Australian business and a key component of this is to improve gross margin via better product mix, pricing and promotional effectiveness. While still ensuring that we stay competitive, we have chosen to moderate the depth of our promotional activity, starting in the fourth quarter of FY20.

In previous years, heavy price discounting has been a feature of the final quarter of the year, which has led to overstocking in Australia while at the same time destabilising pricing and customer support in some overseas markets.

While this intervention will provide benefits in sustainable volume and price growth in the next financial year and better price alignment between our markets, it will have a product mix and volume impact in the second-half of FY20 which is expected to adversely affect EBIT.

Nevertheless, it is absolutely the right long-term decision for the business.

### **4. ASSET SALE AND CONTINGENT LIABILITY**

The business expects a pre-tax gain of approximately \$3 million due to the pending sale of a small parcel of land which is non-core to Blackmores' operations.

Blackmores has been in discussions for more than three years with a foreign authority in relation to export classification codes and related exemptions claimed under free trade agreements from 2009 to 2014. The relevant authority issued assessments for approximately \$11 million (AUD) and Blackmores is pursuing all legal avenues of objection. At time of writing, based on legal advice received, no legal liability currently exists in that jurisdiction and, given the uncertainty, no liability has been recorded for FY20 to date. Therefore, neither the half-year result nor the forecast reflects any potential adverse impact. In the 30 June 2019 Annual Financial Report (note 6.5) we disclosed this contingent liability of \$10 million, which has now been adjusted for foreign exchange movement.

### **5. NOVEL CORONAVIRUS**

Our thoughts are with the vast and increasing number of people impacted by the outbreak of the Novel Coronavirus. Our primary focus continues to be on the health of our employees and those in the most affected areas.

While the outbreak has resulted in increased demand for key immunity products in Australia and Asia, the impact of the sales has been countered by supply chain disruptions across the region as a result of the contagion.

In China, local guidance for businesses and schools for people to stay at home for at least the remainder of February has led to a series of interruptions. Channels which rely on free flow of passengers (duty free, small business traders and tourists) have been impacted.

Some e-commerce partners have cancelled or modified February promotions with a slowdown of China inbound and internal freight, which has made it difficult to serve the local market demand with much needed product.

## **INTERIM DIVIDEND**

In light of the significant deterioration in the outlook for the second-half, the Board has made a decision not to pay an interim dividend to conserve cash for operations.

## **BOARD RENEWAL**

The Blackmores Board is committed to a process to renew its composition in an orderly fashion over the medium term, having already announced that Chairman Brent Wallace intends to step down from the Board.

The Board is in advanced discussions to appoint a new, independent non-executive Chairman and to recruit a further independent Non-Executive Director to its ranks.

Upon completion of this transition Blackmores will have a Board comprising an independent, non-executive Chairman and a clear majority of independent, non-executive Directors.

## **LOOKING FORWARD**

Despite challenges in the second-half, the Board and new management team are very confident and optimistic about the future of Blackmores.

Blackmores' brand metrics are the strongest they have been for many years. We have the number one market position in Australia and a number of Asian markets, and we are quickly building a much stronger team in China.

Since the new management team has been in place, we have worked to develop a solid and credible plan for the business going forward. We are building our capability in strategic revenue management which will help stabilise pricing across multiple markets and build back the margin we need to invest in brand and innovation.

We are also exploring a number of new ventures and growth opportunities to help to deliver consistent and higher quality earnings for the Blackmores Group in FY21 and beyond, and we look forward to outlining some of these initiatives when we release our full first-half year results on 25 February.

Your faithfully,



**Alastair Symington**  
Chief Executive Officer

## INCOME STATEMENT

Half-year ended 31 December 2019	Statutory (subject to review) <sup>1</sup>	Underlying	H1 FY19	% Underlying var to pcp
<b>Sales Revenue</b>	<b>302.7</b>	<b>302.7</b>	<b>319.4</b>	<b>(5%)</b>
Other income	6.5	0.8	1.1	<b>(29%)</b>
<b>Revenue and other income</b>	<b>309.2</b>	<b>303.5</b>	320.4	<b>(5%)</b>
Cost of raw materials and consumables used	124.1	122.3	124.2	<b>(2%)</b>
<i>% of sales revenue</i>	<i>41.0%</i>	<i>40.4%</i>	<i>38.9%</i>	
Selling and marketing expenses	30.3	30.3	32.0	<b>(5%)</b>
Operating expenses	128.1	122.8	113.8	<b>8%</b>
<b>Total Expenses</b>	<b>282.5</b>	<b>275.4</b>	<b>270.0</b>	<b>2%</b>
<b>EBIT</b>	<b>26.7</b>	<b>28.0</b>	<b>50.5</b>	<b>(44%)</b>
<i>% of sales revenue</i>	<i>8.8%</i>	<i>9.3%</i>	<i>15.8%</i>	
Net interest expense	2.3	2.3	2.2	<b>2%</b>
Income tax expense	5.9	7.5	14.1	<b>(47%)</b>
<i>% effective tax rate</i>	<i>24.2%</i>	<i>29.1%</i>	<i>29.3%</i>	
Non-controlling interest	0.2	0.2	(0.2)	<b>(202%)</b>
<b>NPAT</b>	<b>18.3</b>	<b>18.0</b>	<b>34.3</b>	<b>(48%)</b>

1. Amounts shown exclude the recognition of increases to interest expense (\$0.3m) and depreciation (\$3.8m) and a decrease to operating lease cost (\$3.9m) relating to adoption of AASB 16 Leases based on the modified retrospective approach.

<i>Cost of goods sold (COGS)</i>	<i>140.4</i>	<i>138.6</i>	<i>133.9</i>	<i>4%</i>
<b>Gross profit</b>	<b>162.2</b>	<b>164.1</b>	<b>185.5</b>	<b>(12%)</b>
<i>% sales revenue</i>	<i>53.6%</i>	<i>54.2%</i>	<i>58.1%</i>	
<i>Operating expenses exc. COGS</i>	<i>111.7</i>	<i>106.4</i>	<i>104.1</i>	<b>2%</b>

## RECONCILIATION OF STATUTORY RESULT (SUBJECT TO REVIEW) TO UNDERLYING RESULT

A\$m	H1 F20	H1 F20
	EBIT	NPAT
<b>Statutory Result (subject to review)</b>	<b>26.7</b>	<b>18.3</b>
<b>Adjust for Significant items:</b>		
Bargain Purchase Adjustment	(5.7)	(5.7)
Catalent Acquisition Gross Margin Adjustment	1.8	1.3
Catalent Acquisition Stamp Duty	1.8	1.8
Transformation/Restructuring Cost	3.6	2.5
<b>Underlying Result</b>	<b>28.0</b>	<b>18.0</b>

## SEGMENT REVENUES

A\$m	H1 F20	H1 F19	% Var
ANZ	115.5	144.2	(20%)
BioCeuticals Group	57.0	56.8	0%
China	61.7	65.4	(6%)
Other Asia	68.4	52.9	29%
<b>Total Revenue</b>	<b>302.7</b>	<b>319.4</b>	<b>(5%)</b>

## BALANCE SHEET

A\$m	Dec-19 (subject to review)	Jun-19	\$ Chg	% Chg
Cash <sup>1</sup>	33.7	24.5	9.2	38%
Receivables <sup>1</sup>	117.1	143.9	(26.7)	(19%)
Inventories <sup>2</sup>	129.3	125.1	4.2	3%
Other current assets	12.4	12.0	0.4	3%
<b>Current Assets</b>	<b>292.6</b>	<b>305.5</b>	<b>(12.9)</b>	<b>(4%)</b>
Property, plant and equipment <sup>3</sup>	140.3	80.8	59.6	74%
Other non-current assets <sup>6</sup>	110.9	104.6	6.2	6%
<b>Total Non-Current Assets</b>	<b>251.2</b>	<b>185.4</b>	<b>65.8</b>	<b>36%</b>
<b>Total Assets</b>	<b>543.8</b>	<b>490.9</b>	<b>52.9</b>	<b>11%</b>
Trade and other payables <sup>4</sup>	136.6	131.8	4.8	4%
Other current liabilities <sup>6</sup>	17.9	18.7	(0.8)	(4%)
<b>Total Current Liabilities</b>	<b>154.5</b>	<b>150.5</b>	<b>4.0</b>	<b>3%</b>
Interest bearing liabilities <sup>5</sup>	153.0	119.0	34.0	29%
Other non-current liabilities <sup>6</sup>	19.9	13.7	6.2	46%
<b>Total Non-Current Liabilities</b>	<b>172.9</b>	<b>132.7</b>	<b>40.2</b>	<b>30%</b>
<b>Total Liabilities</b>	<b>327.5</b>	<b>283.2</b>	<b>44.2</b>	<b>16%</b>
<b>Total Equity</b>	<b>216.4</b>	<b>207.7</b>	<b>8.7</b>	<b>4%</b>

1. Cash and receivables balances reflect the impact, in Dec 2019, of a sale of receivables of \$23m to an unrelated entity in exchange for cash. This sale was made at competitive rates.

2. Inventories include \$19m of inventory held at the Braeside site, like-for-like inventory at 31 Dec 2019 was \$110m.

3. Property, plant & equipment increase includes \$49.5m resulting from the acquisition of the manufacturing facility at Braeside.

4. Trade and other payables includes \$24m relating to the estimated balance owed to Catalent for the acquisition of the manufacturing site at Braeside.

5. Increase in debt includes \$33m relating to the funding for the acquisition of the manufacturing site at Braeside.

6. Amounts at Dec 2019 exclude the recognition of right-of-use assets (\$17.6m) and lease liabilities (current \$7.1m, non-current \$10.7m) relating to adoption of AASB 16 Leases based on the modified retrospective approach.



## CASHFLOW STATEMENT

A\$m	Dec-19 (subject to review)	Dec-18	\$ Chg	% Chg
Cash generated from operations <sup>1,4</sup>	42.7	33.6	9.1	27%
Interest and taxes	(13.3)	(18.6)	5.4	(29%)
<b>Net Cash from Operating Activities</b>	<b>29.4</b>	<b>15.0</b>	<b>14.4</b>	<b>96%</b>
<b>Net Cash used in Investing Activities<sup>2</sup></b>	<b>(47.8)</b>	<b>(18.2)</b>	<b>(29.6)</b>	<b>163%</b>
<b>Net Cash from Financing Activities<sup>3,4</sup></b>	<b>27.3</b>	<b>3.5</b>	<b>23.8</b>	<b>687%</b>
<b>Net increase in cash / cash equivalents</b>	<b>8.9</b>	<b>0.2</b>	<b>8.7</b>	<b>3560%</b>
Cash and cash equivalents at start of year	24.5	36.5	(12.0)	(33%)
Effects of FX	0.3	1.4	(1.1)	(77%)
<b>Cash and cash equivalents at end of year</b>	<b>33.7</b>	<b>38.1</b>	<b>(4.4)</b>	<b>(11%)</b>
<i>EBITDA</i>	32.8	55.8	(23.0)	(41%)
<i>Cash Conversion %</i>	130%	60%		70 pts
<i>Cash Conversion % (adj. for receivables financing)</i>	60%	60%		-

1. Cash generated from operations in H1 FY20 includes a \$23m inflow related to sale of receivables.

2. Cash used in investing activities in H1 FY20 includes a \$33m outflow related to payment made to Catalent for manufacturing facility at Braeside.

3. Cash from financing activities in H1 FY20 includes \$34m proceeds from borrowings which predominantly was used to fund payment made to Catalent for manufacturing facility at Braeside.

4. Amounts shown in H1 FY20 exclude a \$3.8m impact relating to adoption of AASB 16 Leases based on the modified retrospective approach. This would have the effect of increasing cash generated from operations and decreasing cash from financing activities by the same amount.