**TRANSCRIPTION**

**Company: Australian Agricultural Company Limited**

**Date: 17 November 2022**

**Duration: 22 minutes, 30 seconds**

**Reservation Number: 10026134**

**[START OF TRANSCRIPT]**

Operator: Thank you for standing by and welcome to the Australian Agricultural Company Limited FY23 half year results presentation. All participants are in a listen only mode. There will be a presentation followed by a question and answer session. If you wish to ask a question via the phone, you will need to press the star key followed by the number one on your telephone keypad. If you wish to ask a question via the webcast, please enter it into the ask a question box and click submit. I would now like to hand the conference over to Mr. David Harris, managing director and chief executive officer. Please go ahead.

David Harris: Good morning and welcome to the Australian Agricultural Company's half year results presentation for the financial year 2023. My name is David Harris, managing director and CEO of AACo, and joining me on the call today is Robbie Winckelmann, our group financial controller.

I begin today by acknowledging the traditional custodians of the various lands on which we meet today. In Brisbane, that's the Jagera and Turrbal peoples. I pay my respects to their elders past, present and emerging and extend that respect to any First Nations people joining us for today's presentation.

It gives me great pleasure to present AACo's interim results to you this morning. Firstly, I'd like to run you through the financial highlights for the half, starting with the operating profit, which increased to $38 million versus PCP. This was mainly supported by positive increases in price per kilo of meat sold, as we continue to unlock the full potential of our brands. Our financial position improved, with net assets growing to over 1.4 billion and this increase drove net tangible assets per share, 3% higher to $2.33 per share.

Importantly, the value of our herd grew by $71 million and this has largely come off the back of higher kilogrammes produced through the supply chain as well as higher calf brandings. With this being said, due to the length of our supply chain, a growing herd for the future needs to be invested in today, and this, combined with rising input costs, led to a lower operating cash inflow for the period.

Now, before jumping to how we are progressing against our strategy, I'd like to quickly touch on our purpose on slide six. At AACo, we are evolving together to benefit future generations. This continues to be our purpose and it's why we exist. The land we nurture, the people we develop and the animals we care for, and the exceptional product we create are all hallmarks of our success and we take great pride in that. It's what positions us internationally as producers of exceptional quality Australian Wagyu.

As we push ourselves towards this purpose, we remain laser focused on executing against our strategic pillars and I will elaborate on some of those key achievements in the next part of the presentation.

Moving to slide seven, progress against our strategy. The work our team are doing to unlock the full potential of our brands has been a key driver of our improved operating profit. We've seen Westholme and Darling Downs branded meat sales grow to 88% of our total branded meat sales. North American branded meat sales have increased by 25% and this is combined to support an overall increase in price per kilo of nearly 26% this half. We've also continued momentum with our proactive approach to sustainability by releasing our third sustainability report. We have also progressed our solar bore transitions and we are undertaking numerous research and development initiatives, which I'll touch on in more detail later.

As part of developing our natural resources and assets, we continue to push forward with our gulf farming trials and are undertaking an assessment of how best to maximise our assets and our natural resources into the future.

As with most large natural asset developments, it will take time for us to develop viable projects. However, we are excited with the potential projects that are in the pipeline and look forward to sharing these with you in due course.

Our focus on becoming a simpler and more efficient business has been a consistent approach over the past few years. Within this pillar, we look at improving operational efficiencies throughout the supply chain. At this half, we managed to increase production by 18% with only a 1% increase in cost of production.

Moving onto our meat sales regional performance starting with North America on slide nine. As we've mentioned before, North America is one of our highest priority regions. We achieved consistent demand and strong pricing for our Westholme branded product here and we are pleased with the progress we've seen this half. Overall, the region remains representative of 29% of total meat sales. As we have shifted unbranded commoditized product away from this market, we have increased volume of our Westholme branded meat allocation and we have achieved higher average pricing. Higher pricing in the region was strongly supported by continued recovery of food service as well as an increase of 25% in Westholme sales, which is partly driven by a number of collaborations with high profile US based chefs broadcast across our digital channels.

Moving to Asia on slide 10. Revenue wise, Asia is our biggest region. It plays a key role in helping us balance cut allocation across the carcass and Darling Downs continues to be a household name in South Korea. This half, Asia sales as a proportion of total meat sales decreased to 47%. This was driven by an intentional reallocation of volume away from retail into food service markets around the world, as part of our overall global strategy. And despite higher value cuts being allocated to other markets, we were still able to improve average price in the region.

Some of the key activities undertaken in market by our team to grow demand and achieve higher price, included the enhancing of our Darling Downs in-store experience in South Korea and refreshing our Korean Darling Downs website, which has boosted consumer accessibility to online purchases of the product.

Moving to our spiritual home Australia on slide 11. This half, we continue our focus on price premiumization through brand in Australia. Similar to Asia, this resulted in us intentionally reallocating volume away from this region to higher paying regions. Also like Asia, we were able to increase average pricing in this market this half, and this came directly as a result of increasing Westholme sales by 35%, which was driven in part by activations across key venues with influential Australian chefs.

Now I'll move on to Europe and the Middle East on slide 12. Europe and the Middle East is predominantly a food service market and similar to what we saw in North America, this region's meat sales increase strongly this half off the back of increased volume allocation. To support the increase in volume, we undertook a number of brand activations across priority cities in the region and it has been positive to see the consumer activity in the Middle East return to pre-Covid levels.

Moving to further detail on our sustainability agenda on the following slide. Last year we released our sustainability framework and we're happy with the progress we've made against our commitment this half. As I mentioned earlier, we also released our third sustainability report during this period and we have made tangible progress against transitioning our diesel bores to solar by 2024, noting that each bore we convert abates around six tonnes of carbon per year.

We've also undertaken some key research and development initiatives, including completing stage one of our climate risk assessment. This has enhanced our understanding of our impact on the climate and will enable us to take authentic action to addressing it. We also passed the halfway point in our Asparagopsis trial, which will help us understand the potential for reducing methane emissions in Wagyu cattle. And with our partners, we have taken a significant number of core samples to help build our landscape carbon satellite tool, which we hope will be key in bringing down the cost of our participation in soil carbon markets across our extensive land portfolio. We will continue leaning into our sustainability initiatives moving forward and look forward to giving you further updates on our progress as we go.

I'll now hand over to Robbie, who will take you through our financial performance in more detail.

Robbie Winckelmann...: Thank you Dave, and good morning everyone. We appreciate your support of AACo, and I'm pleased to take you through our results for the half.

AACo's trend of positive operating profit has continued this half, and as Dave mentioned earlier, total operating profit improved by 28% to $38.3 million this period. We also achieved a higher operating profit margin of 23.4%, which is up two and a half percentage points versus PCP. The increase in operating profit was strongly supported by a 25.9% increase in the average price per kilogramme of meat sold or a 20.1% price increase when calculated on a constant currency basis. This drove an improvement in meat sales revenue of 18.9% versus prior period. Net tangible assets per share grew by 3% and now exceed $1.4 billion in total, further strengthening our already strong financial position. Operating cash flow has reduced from the comparative as we funded the increased production of live weight kilos produced during the period.

Moving to slide 16 where I'll talk to revenue in more detail. Total revenue improvements of $20.2 million were primarily driven by price performance, and Wagyu meat sales fetched a 25.9% increase in price per kilo sold, adding $24.5 million in meat revenue. Roughly a fifth of this price improvement is attributable to a stronger US dollar relative to the Aussie, and the translation of US dollars nominated sales contributed 5.8% to revenue growth.

Our continued focus on developing demand across our portfolio is yielding encouraging results. All key markets reported in market price improvements on a cut basis and also led to market mixed price improvements. Given current global conditions, it will be remiss to not mention inflation. However, we are pleased that these price achievements are notably exceeding reported inflation levels. Cattle sales revenue of $41.4 million is largely flat on the prior period, due to an 8% sales price uplift that was largely offset as we reduced sales volumes by 6%.

Now turning to our P&L summary on slide 17. As mentioned, operating profit improved by $8.3 million to $38.3 million in the half. This is mainly due to $16.8 million in higher total gross margin, a direct reflection of the increased meat and cattle sales price performance that we spoke about on the previous slide. However, noteworthy, the turmoil seen in the global freight markets have weighed on gross margins. Those global freight issues that we've all seen have led to higher shipping costs incurred during the period as carrier pricing increased and their scheduling uncertainty required us to increasingly rely on air freight in order to ensure on time delivery to our customers.

Net profit after tax was down on the prior period. However, this has been largely impacted by a reduced unrealized mark to market adjustment on the value of our herd and it comes off the back of a softening scene in the Australian cattle market with prices slightly down from the record highs experienced in prior periods.

Moving on to cash flow on slide 18. The business continued to generate positive operating cash flow this period, with net operating cash inflows of $3.4 million. The reduction in operating cash flow is primarily due to three factors outside of those operating profit impacts we've already spoken about. Firstly, we've had increased cash outlays for production costs that are capitalised in operating profit, supporting the 18% increase in live kilogrammes produced. Secondly, the work we've undertaken [inaudible] herd optimization has contributed to a reduction in cattle purchases during the period. And last, our commercial momentum has meant an increase in working capital levels held that period. Separately, I do want to point out that financing costs are slightly down, although effective interest rates incurred were comparable with the PCP and held on similar debt levels. However, that reduction we've seen is thanks to the improved pricing structures at the refinance that we did this time last year.

Turning to slide 19, our balance sheet summary. The increase in brandings and improved live weight kilos produced have driven solid growth in the value of our herd, which rose by $71 million from March. The growth in the value of our herd has supported an increase in overall net assets, taking it to over $1.4 billion, and net tangible assets are now valued at $2.33 cents a share. Our gearing ratio of 22.9% remains well within our targeted range of 20 to 35%. We also have substantial available borrowing capacity which sits at approximately $231 million of available capital, and we continue to maintain substantial headroom within our covenants.

In closing, I'd like to reiterate what we have said before. The strength of our underlying assets combined with the additional optionality that our borrowing capacity provides, positions the business well moving into our next phase of growth. With that I will hand back to Dave to take you through our operating environment and some closing remarks.

David Harris: Thanks Robbie. It's hard for us to look forward without acknowledging the current significant economic uncertainty that exists on a global scale today. Inflation has reached its highest level in several decades. Interest rates are on the rise and there has been a broad based slowdown in economic activity. In Australia, we have also seen increase in biosecurity risk with the emergence of foot and mouth disease and lumpy skin disease close to Australian shores. However, this risk does remain relatively low, with the chance of a foot and mouth disease or lumpy skin disease incursion in the next five years at 11 and 28% respectively. When considering the dynamics playing out in the global beef markets, the USA's herd is certainly being liquidated and so currently price is softening in the short term as increased volumes of lower value product filter throughout the beef system. However, we feel when seasonal conditions improve in the US and that rebuild starts, that the result in lower volumes available for sale, will present real opportunities for Australian producers and more specifically AACo.

More generally, we anticipate sustained demand for quality protein into the future, with the strong rebound of food service to continue in our key markets. And this dynamic will support the continued delivery of the full potential of our brands. Importantly as we have mentioned throughout our presentation today, AACo's herd optimization is continuing to progress, and this positions us well to move into the second half of FY23.

In closing, I'd like to thank the AACo team for their hard work to produce this result, as well as our shareholders for your continued support. This result shows that we are making tangible progress against our strategy and positions us well moving into the full year. However, there is still work to do and we will remain focused on investing back into the business and executing our strategy, as we evolve together to benefit future generations. Thank you very much for joining us this morning. This is the end of our presentation and we are now happy to take questions.

Operator: Thank you. If you wish to ask a question via the phone, you will need to press the star key followed by the number one on your telephone keypad. If you wish to ask a question via the webcast, please type your question into the ask a question box.

Your first phone question comes from Jonathan Snape with Bell Potter. Please go ahead.

Jonathan Snape: Yeah, thanks. Hey guys, can you hear me okay?

David Harris: We can hear you, Jono.

Jonathan Snape: Yep. Great. Hey, can I just ask two questions if I can? One around sales volume. Last year you produced more than you sold. This year it looks like you produced more than you sold. If memory serves me right, it's a three to three and a half year progeny cycle, so would it be reasonable to assume that volumes can start to grow again in 2024 of your available stock, the sell volume starts to show up again then?

David Harris: Thanks Jono. I look I suppose in the right here and now we were slightly down on PCP for volume and that was principally around just Covid impacts and processing capabilities. We had a few floods in southeast Queensland earlier on in the year that affected those. We feel that we'll normalise for the second half. As I'm sure you appreciate, we don't necessarily give guidance out into the future, but I think what I can say is that we're really comfortable with our production metrics and we've got some really good production capacity over the last couple of years and production results and so I look forward to continuing to build the business into the future.

Jonathan Snape: Okay. Look, if I can ask around past to me, you obviously have your COGS level and your cost to production, but you've been building that into an animal that takes three years to grow. Now, if memory serves me, the big jump in your cost structures back in '18 and '20 and you're probably cycling through a fair bit of that stock now, should we see the benefit I guess, of the cost reductions that came through a couple years ago and the containment that's going on now, start to build through in a couple of years time? Am I reading into that right, just on those life cycles?

David Harris: Yeah, thanks Jono. Look, it's an interesting one. I think part of that is accurate. The challenge is that over that amount of time, as you acknowledge three, three and a half years, there's a lot of changes moving through there and look, there's no doubting we're going to come up against some inflationary headwinds in the short term, so I think you're right in that there is great examples of those efficiency gains and cost of production gains that we've made over previous years and we'll continue to work towards starting to filter through the system, noting that in the near term there are certainly examples where our costs and our input costs are going to be challenged in the short term. What beyond that looks like, who knows, but those input costs, diesel, electricity, certainly commodities, there's some tough asks there that we've got to keep working with and that will be absorbed as well.

Jonathan Snape: All right, great. Thanks, guys. Cool

Robbie Winckelmann: I might just had one additional piece of context, Jono. If you recall, some of those increased costs from 2018 and 2019 were incurred late in the supply chain and would've already flushed through in prior years. I think we've spoken about that a couple years ago for you.

Jonathan Snape: Thank you.

Robbie Winckelmann: No worries.

Operator: Thank you. Your next question is a webcast question from Eric Lowe who asks, what is the number of cattle and is the cattle station still suffering from drought?

David Harris: Thanks very much for the question, Eric. Look, I think it's important to note that at the half year we don't give specifics about cattle volumes. That's a end of year one for us. I will reiterate though, what I said to Jono there before. We are getting some really good production figures coming through the business and I think we're certainly on the road to business as usual post those couple of really significant effects in the past.

In relation to the second part of your question, are we still suffering from drought? Look, there is no doubting, we have not had brilliant seasons in the real north of the country for some years now and so central Queensland is certainly in a really good position, but the northern properties over the last two years have only been average at best and so having a few less cattle on hand has certainly helped us work through that. I would not say we're out of the woods, but what I would say is we've got a really nice start to the season up there now, so hopefully fingers crossed this year will be a better scenario for us right in the north.

Operator: Thank you. There are no further questions at this time and that does conclude our conference for today. Thank you for participating. You may now disconnect.

**[END OF TRANSCRIPT]**