

# ESSENTIAL FOODS

Essential Foods is a leading manufacturer of essential and value-added foods in South Africa and comprises two operating divisions:

- Wheat (wheat milling, bakeries and pasta), and
- Other Grains (maize, rice and dried vegetables).

### Business environment

The year was characterised by regression in overall consumer demand and volatile commodity pricing. The latter resulted from local supply discontinuities – specifically in white maize – and a significant weakening of the rand. The overall slowdown in economic growth in South Africa affected demand across the spectrum of product categories, whereas specific product categories such as maize and rice retained volume momentum at an industry level on a full year basis.

The weakening of the rand fed directly into increased input cost, most notably raw materials such as maize,

wheat and rice, which are predominantly imported or trade at dollar-converted import/export parity levels. The local drought affected South Africa's maize crop and resulted in significant price inflation (and supply risk) for white maize. The summer rainfall towards the end of the year will determine the size and price of the 2016 crop.

Retail competitiveness resulted in minor product mix shifts during the year. Investment in additional capacity by other industry players intensified competition in the bakeries segment, resulting in elevated pricing activity.

### Performance overview

Overall performance for the division met expectations despite varied portfolio contributions – the strongest growth generated by the bread category. *Sasko* remains a strong performer, supported by the rigorous implementation of a long-term operational and investment strategy. The division created capacity for growth through a well-managed capital investment plan.

Shakaskraal was commissioned in 2013 and has achieved volume and margin traction ahead of the original investment plan.

Revenue growth for the division was positive despite maize meal deflation during the year. The division's

### Financial performance

Revenue  
**R11 335m**

**6%**

2014: R10 652m

Operating profit  
**R1 278m**

**31%**

2014: R976m

Operating profit margin

**11.3%**

2014: 9.2%

Capital spend

**R447m**

2014: R323m

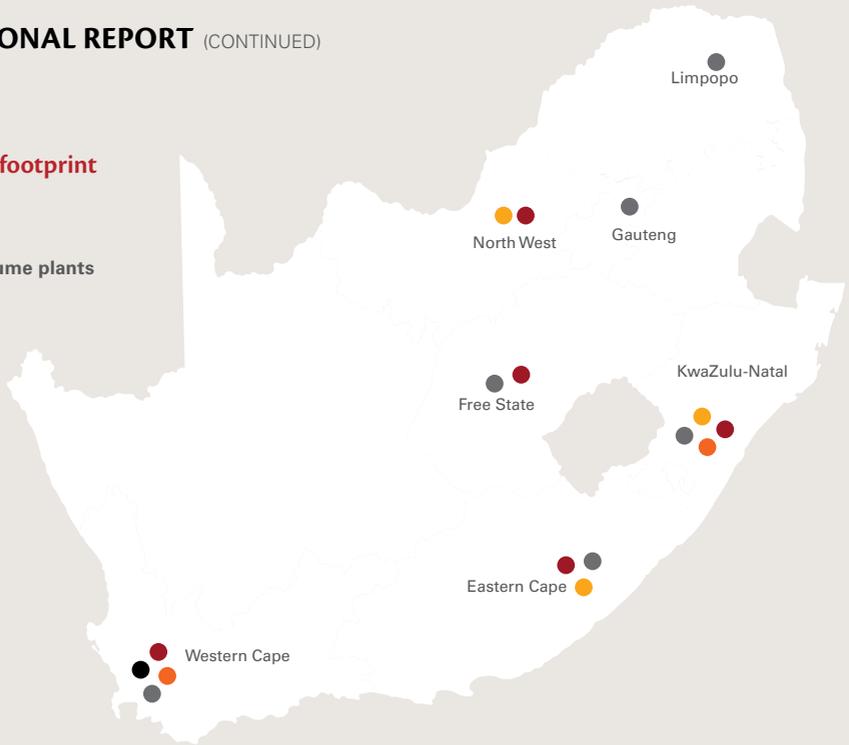


Category	Price change	Volume change	Performance
<p><b>Wheaten flour products</b></p> <p>A large portion of flour produced is transferred to the Group's bread bakeries and pasta plant, and the remainder contributes to a variety of branded and industrial flour products under the <i>Sasko</i> brand.</p>	<b>1.9%</b>	<b>0.0%</b>	<p>Wheat volume performance was under pressure during the year. On a rolling 12-month basis the category performed negatively at an industry milling level (-0.5%). Top-end grocer ("TEG") flour volumes however increased with 4.9% with <i>Sasko</i> gaining share in this trade channel.</p> <p>Essential Foods' volumes were affected by challenges in the Malmesbury wheat mill start-up and the loss of key industrial business in a very competitive environment.</p>
<p><b>Maize products</b></p> <p>Maize is manufactured into a variety of staple foods, including maize meal, samp, maize flour and instant porridge, with <i>White Star</i> super maize meal as the flagship brand.</p>	<b>0.4%</b>	<b>4.0%</b>	<p>The maize category excelled amid a highly volatile pricing environment, resulting in very challenging volume and margin management. Industry milling volumes increased by 2.4% and total TEG volume was up by 6.3%.</p> <p>Solid performance by <i>White Star</i> across all trade channels contributed to Essential Foods' overall divisional performance.</p>
<p><b>Rice</b></p> <p>The Group imports rice products to South Africa, which it markets through its extensive distribution footprint, with <i>Spekko</i> as the flagship brand.</p>	<b>(0.2%)</b>	<b>14.2%</b>	<p>Competitive activity among brand leaders intensified with TEG volume up by 5.1%.</p> <p>Essential Foods delivered sound volume growth and an improved financial contribution. Increased depth of distribution brought further benefits.</p>
<p><b>Bread</b></p> <p>The Group supplies fresh bread to the South African market through more than 35 000 delivery points every day.</p>	<b>4.0%</b>	<b>9.6%</b>	<p>Total TEG plant bread volumes increased by a mere 0.3%.</p> <p>Essential Foods' bread category excelled with strong volume gains in select regions and trade channels. This was enabled by a deliberate strategy of increased marketing investment and the revitalisation of the <i>Sasko</i> brand initiated in 2014.</p> <p>Operating profit increased by 70% (2014: 54%).</p>
<p><b>Pasta</b></p> <p>A range of wheat-based pasta products are manufactured using local and imported ingredients. The Group produces South Africa's first pasta made from white maize.</p>	<b>3.3%</b>	<b>(9.1%)</b>	<p>Total TEG volume was up by 1.9%, with private label participation remaining at high levels.</p> <p>Essential Foods' pasta category continued to contribute positively to the overall financial performance, despite lower volumes and some operational issues.</p>
<p><b>Beans and legumes</b></p> <p>The Group is a major supplier of South Africa's branded beans and legumes.</p>	<b>(6.1%)</b>	<b>(5.9%)</b>	<p>Total TEG volume increased by 11.7%.</p> <p>Despite being a smaller contributor to Essential Foods with lower volumes in 2015, the category makes a positive profit contribution.</p>

## OPERATIONAL REPORT (CONTINUED)

### Production footprint

- 5 wheat mills
- 3 maize mills
- 2 rice and legume plants
- 1 pasta plant
- 15 bakeries



ability to balance price, volume and margin through the volatile supply cycles enabled further operating margin expansion.

Essential Foods experienced some operational challenges in pasta pack conversion and the initial deployment of the new Malmesbury wheat mill. The consolidation of the Malmesbury and Paarl mills is now complete and the targeted short-term benefits were achieved.

The major capital investment expenditure projects for 2015 included equipment upgrades and maintenance at the Duens bakery in Epping. Further capital was allocated to process improvements and the replacement of the bakeries distribution fleet with new generation trucks that offer fuel efficiency, lower maintenance and fleet optimisation across multiple routes.

### Sustainability progress

Electricity consumption is a focus area for the division due to high use, especially in mills. Efficiencies and opportunities to explore alternative energy sources are investigated and developed in association with Energy Partners. In the Essential Foods milling environment, generators are generally not a feasible option, resulting in production losses, product waste and mechanical and electronic damage due to load-shedding. In the Western Cape, the business participates in load curtailment initiatives to reduce downtime.

Essential Foods supports responsible nutrition and food safety. The division is set to meet the sodium (salt) reduction targets for 2016 and 2019 as set out in the Department of Health's foodstuff regulations.

The availability and quality of water is increasingly becoming a strategic sustainability issue requiring management. Essential Foods relies on process water

(as a product ingredient) and water for use in daily operations. During the year, Shakaskraal bakery's supply was maintained through available groundwater sources, but urban development and ageing infrastructure in all areas poses an increasing risk to water supply for the business.

All product information, including genetically modified organisms ("GMO"), is responsibly disclosed on product labels.

 Read more in the sustainability section from page 57.

### Innovation

Innovative range extensions were launched under the following brands:

- *Sasko Plus* speciality bread ranges
- *Champion* instant maize porridge

### Outlook

Sustainable growth for the Essential Foods division depends on significant, strategic capital investment decisions. These projects typically have a multi-year horizon from the investment decision to full production. In the past year this entailed a R105 million expenditure, which was allocated to the replacement and upgrade of the Epping bakery, due for completion in 2016.

In the next financial year, the division will embark on a R330 million replacement and capacity expansion of the Aero-ton bakery in Gauteng. This will further enhance manufacturing and distribution efficiency in support of future growth in key markets. The expansion is expected to be completed during 2017.

The division will continue to manage costs and margins with the focus on incremental growth. Economic conditions are set to limit consumer spending power. Essential Foods has a responsibility to consumers to be as efficient and competitive as possible to ensure affordable price points for staple foods.

The Group's largest value unlock opportunity has been in the bakeries segment where excellent progress has been made – with further growth and improvement opportunities ahead.

### Brands

- *White Star*
- *Sasko*
- *Spekko*
- *Select Rice*
- *Nice Rice*
- *Blue Bird*
- *Champion*
- *Pasta Grande*
- *Imbo*
- *Crossbow*

### Revenue contribution

