TIGER BRANDS

Adding value to life

STRATEGIC REVIEW UPDATE
MAY 2017

Key highlights

Drive sustainable growth by growing the core and expanding into adjacent categories and geographies

Adopt a category-driven approach in the rest of Africa based on market attractiveness, strategic fit and right to win

Build distinctive capabilities required to win with consumers, customers and business partners

Deploy an operating model that provides the capabilities needed to deliver on our growth objectives at the right cost profile

Provide the fuel for growth by driving indirect spend excellence through **zero-based spend** (ZBS) **and zero-based budgeting** (ZBB)

Build a **best-in-class** integrated supply chain to leverage scale and create fuel for growth

Lawrence Mac Dougall – Chief executive officer's statement

The global recession triggered a change in consumer behaviour, reducing established brand loyalty and revenue in the consumer packaged goods (CPG) industry. This led to a reduction in relative spending on consumer products. Declining revenues are forcing manufacturers to turn to mergers and acquisitions (M&A) as a growth catalyst.

Despite declining revenues, the global CPG industry has had a long run of solid, profitable growth. This positive trend can be largely attributed to the industry embarking on strategic cost reduction projects, including local and international sourcing and procurement strategies, as well as operational optimisation initiatives. Large players are also responding by strengthening and focusing on their core portfolios.

In addition, the impact of socio-economic challenges such as constrained economies and macro-economic volatility, emerging consumer and shopper trends, the evolution of the retail landscape and the emergence of new channels, as well as an increasingly agile competitive set, have spurred manufacturers to review their portfolios, processes and strategies.

Similarly, Tiger Brands operates in an intensely competitive industry where increasing market share against well-funded and established participants requires the full commitment of an experienced and expert team working towards a clear strategy. The first step in addressing these challenges was a thorough strategic review, the outcome of which is the development of a strategy for sustainable profitable growth, driven by three focus areas, namely portfolio and growth strategy; creating a cost-conscious culture and an advantaged integrated supply chain; operating model and organisational design. Each of these areas became the focal point of separate workstreams.

We are confident that the strategy builds on our strengths and will enable the group to create predictable value in the form of stable financial returns to those who provide our capital, and tangible value for all our stakeholders through real benefits and constructive partnerships.

Driving sustainable growth

1. Portfolio and growth strategy

The purpose of this stream of work was to develop a strategic, full potential plan for stronger top-line growth, enhanced margin and improved return on net assets (RONA) through optimisation of the portfolio.

Historically, the pursuit of geographic diversification has led to a loss of focus and thinly spread resources. The intention is to reverse this cycle of underperformance by creating fuel for growth through focusing the portfolio and distorting investment where appropriate. Defining the core is therefore critical to building portfolio strength and performance.

Tiger Brands has defined its core as the manufacturing, marketing and distribution of everyday branded food to middle-income consumers. This already accounts for 70% of Tiger Brands' current sales. These consumers are a growing proportion of the South African market, are more brand loyal, have similar shopping destinations and utilise the media in a similar manner. Food is a large, attractive core that offers strong growth potential, allowing us to build on our resilient positions and good adjacencies. The core will be supported and protected by leveraging relevant adjacencies where these support our vision of being the best fast moving consumer goods (FMCG) company in South Africa and the most desirable growth company on the continent.

Efficient capital allocation and business management is critical to reaching full potential. To this end, we will adhere to six strategic principles to achieve sustainable growth by protecting and leveraging our core categories. In addition, we will adopt a hybrid model of master and standalone brands, aligned with our core focus. This will be concluded after extensive consumer testing. A hybrid model will help facilitate an increase in marketing investment and ensure optimal spend.

Six strategic principles

1. Continually strive to reach full potential and grow the core business. The following growth drivers will help achieve full potential:
   - Increase availability and achieve our fair share in the modern and general trade
   - Appropriate management of price
   - Relevant pack size architecture
   - Unmet needs and addressing emerging trends by enhancing our "big idea" innovation
   - Brand health

2. Pursue adjacencies to protect and leverage the core
3. Optimise portfolio for current performance and future potential
4. Simplify and support clear growth and RONA winners
5. Focus on a defined set of growth drivers
6. Drive an embedded Tiger Way

In line with best practice, the portfolio will be continuously reviewed with the intention to best position our businesses for growth, which may, in some instances, be outside the group. This will be done in the right way at the right time. Similarly, expansion will be complemented by targeted growth through M&A activities that leverage our core capabilities.

The immediate priority is to rejuvenate the domestic business to deliver sustainable, profitable growth. Importantly, Africa and emerging markets remain a key part of our growth strategy. We have refined our approach to our African strategy by exiting non-core categories in Kenya and Ethiopia. Looking ahead, we will prioritise core category opportunities based on market attractiveness, strategic fit and our right to win. Similarly, the role of associates will be reviewed continuously.

2. Creating a cost-conscious culture and an advantaged integrated supply chain

Zero-based spend (ZBS)

The ZBS workstream was focused on achieving indirect spend excellence in order to identify and deliver savings in sales activities as well as in general and administrative (SG&A) costs in line with those achieved by other global organisations and utilise those savings as fuel to unlock Tiger Brands' growth strategy. The key to success is creating cost transparency and establish a cost-conscious mindset and culture to ensure sustainability of cost savings going forward.

Our aim is to achieve sustainable savings based on spend transparency, clear policies and compliance.

Although benchmarking revealed that expense ratios are generally below the median for our peer group, a detailed bottom-up process identified significant savings. Execution of ZBS will be based on principles such as rigorous governance, compliance with new guidelines and policies as well as the establishment of a bottom-up budgetary discipline beginning with the 2018 budgeting process (ZBB). This will be supplemented by effective change management and communication to embed behavioural change as well as ongoing, frequent tracking.

Supply chain

In terms of our supply chain, we envisage an integrated supply chain that is agile and dynamic and can deliver the required growth while unlocking cash. The following three initiatives will deliver our supply chain vision:

Supply chain initiatives

1. Fuelling growth	• Manufacturing optimisation • Logistics and customer service • Reducing supply chain waste
2. Unlock cash	• Inventory reduction • Creditor terms
3. Agile and dynamic supply chain	• Establishment of a procurement operational centre (POC) • Customer service excellence • Standardisation and simplification of processes, systems and practices

Manufacturing plants were assessed through top-down benchmarking and a bottom-up analysis. The manufacturing scope included the entire conversion process from raw materials to finished goods. Manufacturing elements assessed included cost, equipment, products, labour, facility layout and manufacturing capability and capacity.

Our manufacturing transformation aims to improve gross margins, unlock capacity to support future growth and implement a standardised organisational blueprint. This will be delivered through:

- conversion cost improvement, underpinned by manufacturing optimisation and consolidation
- a new logistics model with centralised distribution and order management, underpinned by technology
- a progressive reduction plan in credit notes, both in volume and value
- inventory optimisation initiatives spanning finished goods, raw materials and packaging.

3. Operating model and organisational design

The objective of this workstream was to design the optimal operating model and identify the required capabilities to enable our strategy and growth ambitions.

The process identified a need for upskilling, as well as process and system enhancement, while a number of inefficiencies in how we are organised and operate were identified.

The future operating model will refocus on the consumer, reignite innovation and leverage our scale as one Tiger Team resulting in an agile, lean organisation that responds quickly and is aided by simple ways of working. A key enabler will be improved processes and enhanced systems.

Operating model vision[1]

[1] The operating model vision is subject to consultations in terms of the Labour Relations Act.

To achieve this, we will be required to move from a federated to an integrated operating model, while maintaining our commercial edge. It means moving from independent business units under a common umbrella to a consolidated category model focused on driving our brands and products, while remaining focused on delivering superior financial results. "Big idea" innovations will be facilitated by concentrated innovation capabilities, with a deeper understanding of our consumers, a renewed focus on R&D, and a forward-looking innovation portfolio.

Engagement with Tiger Brands will become easier through a unified sales team and an integrated supply chain that can truly leverage the breadth and power of our product basket. Further efficiencies will be extracted from an improved shared service organisation, delivering repeatable activity at the right quality and cost and enabled by automation and continuous improvement.

The corporate centre will set the strategic direction and play a bigger part by providing centralised expertise in the form of centres of excellence to harness our skill base as well as to facilitate synergies.

Measures of success

Key performance indicator	Five-year target	FY2016 Restated[†#]
Net sales	Category growth +1% – 2% per annum	R30,6 billion
Gross margin	+150bps* – 180bps*	31,8%
Marketing investment (% of NS)	+100bps* – 160bps*	2,5%
Operating margin before IFRS 2 charges	+100bps* – 160bps*	13,7%
RONA	>35%	30,7%

* *Basis points (bps).*

[†] *Restated for early adoption of IFRS 15 Revenue from Contracts with Customers. Refer note 7 in results announcement.*

[#] *Restated as required by IFRS 5 in relation to the treatment of East Africa Tiger Brands Industries Plc. (EATBI) and Haco Tiger Brands (E.A.) Limited (Haco) as discontinued operations.*

The company has put in place plans to generate significant savings over the next five years. These savings will primarily be derived from gross margin improvements and by driving efficiencies through ZBS. It is intended that these savings will provide the necessary source of funding for reinvestment in the core and to take advantage of future growth opportunities. The net impact is an anticipated increase in the operating margin (before IFRS 2 charges) of between 100bps and 160bps over the five-year period to 2022.

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