

CHAIRMAN'S REPORT

Werner Büchner



Introduction

This is my first report as chairman and a great privilege to report on your company's performance over the past year.

I would like to express my heartfelt appreciation to our previous chairman, John Bredin, who has been involved with Clover since its days as a cooperative. It's under John's leadership that Clover transformed to the listed corporate it is today.

As a board, it is our duty to ensure Clover delivers against its strategy and that the long-term vision of the Group resonates with all our stakeholders. Clover's mission remains to reach our widely dispersed consumer base on a daily basis, delivering on our brand promise of providing quality products through our extensive network underpinned by the country's leading dairy business.

Certainly, the overriding objective of Project Cielo Blu and Clover's listing was to give effect to this mission and to continue to build a brand business through development or acquisitions of products that occupy the number one or two category positions.

Project Cielo Blu, our primary capital expenditure programme, is nearing completion and we are particularly proud to have been able to remain on time and on budget. Although the project will only be completed during the next financial year, benefits are increasingly flowing to the bottom line and have helped reduce inflationary cost pressure, especially with regards to fuel and other supply chain costs.

This project will embed our strategy for years to come by reducing supply chain cost and creating manufacturing capacity at the milk source. Our next phase of capital spend is already underway, with significant amounts being invested in both distribution and manufacturing capacity to support growth and efficiency.

In order to achieve our vision of becoming a leading branded foods and beverage group in South Africa and other selected sub-Saharan countries, it is imperative that we build on the existing competencies within Clover. The Social and Ethics Committee Report makes reference to the process we've embarked on to establish a culture of exceptional performance, which will form a beachhead for future market expansion.

I believe that Clover is fulfilling its mission and that it remains well on track to realise its vision.

Operational Overview

It's been a busy year for Clover!

Clover acquired The Real Juice Co. Holdings ("RJC") from AVI Limited and also concluded a transaction with Nestle to establish a new beverage company called Clover Waters. In terms of the transaction, Clover Waters will manufacture and distribute both Clover and Nestle's range of water and ice tea products from August 2013.

These transactions will add value to the existing beverage portfolio and allow Clover to gain market share in this previously underdeveloped portfolio of value added and branded beverages products. For a local African player such as Clover to be entrusted with global brands including Nestlé Pure Life® and Nestea® is an accolade that we are very proud of.

In line with the recapitalisation programme embarked on during 2010, all preference shares were redeemed during June 2013, effectively simplifying our capital structure and marking the final chapter on the legacy structure of our pre-listing days.

We continued to gain market share and experienced volume growth underpinned by Clover's strong brand.

As a relatively newly listed and brand driven FMCG company, we are sensitive to the fact that our "customers" now include both shareholders and consumers, amongst various other stakeholders. Being in the public domain necessitates good transparency and continued delivery on our brand promise. It is therefore very encouraging to be recognised for our efforts in this regard, and it is with great pride that we received the award for the top rated company in the Confectionary and Dairy sector of the Mail & Guardian Top Companies Reputation Index (TCRI) 2013.

The Awards are based on an assessment of the reputation companies have established with South African consumers. 22 different industries are analysed against a list of nine qualities including products and services, financial performance, governance, communication, recognition, workplace environment, corporate social responsibility, vision and leadership and broad-based black economic empowerment.

The overall TCRI is based on the 30 highest advertising spenders (as measured by the Nielsen Ad Index data). Although Clover falls outside the spending bracket, its reputation index would have placed it in the third overall position.

The TCRI award follows Clover receiving the prestigious Investment Analysts' Society (IAS) award for *Best Reporting and Communication: Best Presentation to the Society for a company with a market cap below R5 billion* in June 2013.

I am also proud to report that our reporting on environmental issues is reaching maturity. Our approach to the important matter of environmental impact, health and safety has been to collect extensive data over a number of years via Clover's cloud based Entropy system. After processing this data, we have established clear goals on the reduction of Clover's carbon footprint, water and electricity consumption, which have been incorporated into the respective plant managers' performance measurements.

A number of exciting new products and packaging options were launched during the year. I would like to single out our achievement of bringing fresh milk with a minimum 18 day shelf life to the market, and the introduction of ultra-pasteurised milk with a shelf life of 30 days, another industry first. I believe that these initiatives will play the biggest role in providing quality nutrition to our consumers.

Dairy industry overview

High maize prices and a weakening rand impacted negatively on the landed cost of animal feeds during the year under review. Administered inflation, especially relating to fuel and electricity, was at a much higher level than CPI. Lacklustre market conditions further exacerbated the negative effect on farm productivity. Inflationary costs will have an impact on food inflation in the coming year as costs filter through to consumers.



Product focus

Individually wrapped processed cheese (IWS) slices project

- Installed a new Bosch – Sapal IWS filling line from Switzerland.
- The filling line produces 1 000 individually wrapped slices per minute (almost 17 each second), generating approximately 1 tonne of cheese per hour.
- The plant is the only UHT processed cheese production facility in South Africa.
- Each slice is electrostatically charged to ensure that the slices do not slide off each other as they are stacked on top of each other. The charge only holds for the couple of seconds needed to transport the stack of slices to the downstream equipment.
- Each stack of slices is enveloped in an inert atmosphere containing a mixture of nitrogen and carbon dioxide to reduce product degradation by exposure to oxygen.
- New storage and gas pipeline distribution network for supplying liquid nitrogen and carbon dioxide to the process were installed.
- Constructed a new raw material cold room.
- Upgraded the electricity supply transformer to the site.
- Created 9 new jobs.

In contrast, at the time of writing, the New Zealand drought saw international supply lower and dairy commodities commanded high prices, creating export opportunities as the seasonal high production months approaches in the southern hemisphere.

Clover has successfully managed its supply side risk through its unique milk procurement system (CUMPS) and has recently enhanced this system by creating opportunities for dairy exports and a bigger exposure to the international ingredients market through Clover Fonterra Ingredients.

Increased local competition, especially in the UHT market, has led to reduced selling prices. I believe that these factors will contribute to continued on-farm pressures which will impact supply for the foreseeable future. As the country's largest buyer of dairy, we continue to monitor the situation and will react responsibly.

Although, consolidation in the primary industry continues, we still believe that dairy farming is sustainable. The total production output is increasing, ensuring security of supply in the short to medium term at least. Land redistribution remains largely an unsolved issue in South Africa and we expect the status quo to remain. The impact on producers is hard to quantify. I believe that a focus on national food security is necessary to ensure sustainability of supply.

The South African dairy exports to the sub-Sahara region have grown at a phenomenal rate, partly driven by the expansion of South African retailers into the rest of Africa. Apart from these markets, Clover has established a presence and relationships in Nigeria over a number of years and continues to explore opportunities in Angola. The Board believes that sufficient local knowledge and experience has been gained to take more decisive steps in these markets and we have begun considering various options in that regard. In the longer term, it is envisaged that these initial countries will be used as springboards into other countries.

Macro-Economic Overview

The global economic outlook remains uncertain on the back of a fragile Euro zone experiencing muted recovery. More recently, signs of economic recovery in the US were offset by concerns over a slow-down in some sectors in China. From a South African perspective, it is undeniable that investor confidence was shaken by a number of factors including labour unrest, low productivity, increased costs and rand volatility.

South African consumers experienced enormous increases in living expenses, mainly as a result of rises in utility and transport costs. Coupled with the high level of unsecured domestic debt, consumers' disposable income has contracted leading to reduced discretionary spending.

Despite these pressures, we continued to gain market share and experienced volume growth underpinned by Clover's strong brand, but at lower than anticipated selling prices.

On the labour front, I am happy to report that Clover reached a settlement with representative unions on an average staff cost increase to Clover of 7,1% per annum. Clover is aware of and sensitive to the fact that inflationary pressures have the biggest impact on lower salary earners – as a result our lowest paid workers will receive an annual increase of between 20% and 25%, relieving some of this burden.

Financial overview

In spite of a disappointing first half, the commendable efforts and strategic measures put in place by the management team delivered significant results and a much improved financial performance in the second half.

More financial details can be found in the Chief Financial Officer's report on page 32.

Governance and the Board

The Group is committed to the highest corporate governance standards in its dealings with all its stakeholders and supports the Code of Corporate Practices and Conduct as recommended by the King III Report on Corporate Governance for South Africa.

Our approach to governance is elaborated on in the Corporate Governance Report later on in this integrated annual report but I am particularly pleased with the progress made at our Centre of Excellence on Consumer Protection and Competition legislation which has seen continuous training programmes being implemented.

Remuneration of executives and other employees is an equally important aspect. The Group endeavours to attract and retain individuals of the highest standard as we strive to align management's long-term incentives with those of our shareholders. More details can be found in the Remuneration Report on page 56.

There have been a number of changes in the composition of the board during the past year. Most notably was a reduction in the total number of directors. The Board now has an equal number of independent non-executive and non-executive directors. Two long-serving non-executive directors, namely John Bredin, the previous chairman, and Harry du Preez stepped down during November 2012 and will not be replaced.

As was the case with John Bredin, our previous chairman, I am not independent in terms of King III, since I also supply raw milk to Clover. In the opinion of the Board, it is in the interest of the Group to maintain a close relationship with its raw milk suppliers. As recommended by King III, Tom Wixley will continue as Lead Independent Director to fulfil the functions of the Chairman whenever a conflict arises and in the other circumstances as envisaged in King III.

Manie Roode retired from his executive position and as a member of the Board on 30 June 2013. The Board has decided not to replace Manie Roode, resulting in the number of executive directors serving on the board reducing to three. Subsequent to the financial period Peter Mageza indicated

Our achievement of bringing fresh milk with a minimum 18-day shelf life to the market, is an industry first.



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that he will resign as the director of the Company at the Annual General Meeting due to a conflict of interest. Geoff Elliott will also resign from the Board of Directors at the Annual General Meeting. I would like to thank Geoff and Peter for their dedication and continued contributions to the Board.

As required by the Companies Act, Jacques van Heerden was appointed as Company Secretary on 1 October 2012. For a detailed report on the Board, its composition and that of its sub-committees, refer to the Corporate Governance Report on page 42 of this integrated report.

Social and environment

As mentioned in the outset of this report, our environmental impact controls are maturing. Clover Mama Afrika, our award-winning social investment project is now in its ninth year and growing from strength to strength. More details on these important sustainability drivers, together with health and safety initiatives are contained in the Report on Sustainability on Clover's website www.clover.co.za.

Transformation – B-BBEE Update

We subscribe to the National Government's priorities with regards to transformation and empowerment and embraces the principles of B-BBEE as we seek to remain a positive and constructive contributor to the country in this regard.

Clover is currently a Level 6 B-BBEE contributor. The Group is aligning its overall business strategy with a B-BBEE strategy to migrate to Level 4 compliance by 2015.

More information on this strategy is available in the Report on Sustainability, at www.clover.co.za.

The Future/Outlook

The successful implementation of Project Cielo Blu will deliver benefits for Clover now and over the long term and help to mitigate input and high transportation costs. Factors that impacted on Clover during the first six months of the year do not negatively affect our long-term strategy; to the contrary, these continuous investments ensure the relevance of our brands in the minds and hearts of consumers.

New principal business, synergies from the Clover Waters and RJC transactions and new product development will further drive revenue as we continue to invest and explore areas where we have competitive expertise, both in South Africa and selected sub-Saharan emerging markets.

The Board is convinced that the investment in well needed infrastructure will provide Clover with a time-to-market advantage in its defined market space.

Appreciation

I would like to thank my fellow Board members for their support during the past year. On behalf of Clover, a sincere thank you is extended to the outgoing Chairman, John Bredin as well as to Harry du Preez and Manie Roode for the decades of service and helping to make Clover truly "Way Better".

In particular, I would like to commend Johann Vorster for his visionary leadership which has yet again enabled the Clover team to deliver a very balanced performance in light of the challenges faced during the past year.

The dedication and diligence of the executive management and all staff cannot go unmentioned, and on behalf of the Board I thank you.

Werner Büchner

11 September 2013