KWV

ESTABLISHED 1918

Reg no 2009/012871/06

KWV HOLDINGS
GROUP INTERIM REPORT
(UNAUDITED) FOR THE SIX MONTHS ENDED 31 December 2011

STATEMENT OF FINANCIAL POSITION

	Notes	Unaudited 31 December 2011 R'000	Unaudited 31 December 2010 R'000	Audited 30 June 2011 R'000
ASSETS				
Non-current assets		**301 499**	318 552	304 436
Property, plant and equipment		**198 538**	195 942	198 521
Intangible assets		**20 633**	34 388	19 679
Investment in associates and joint ventures		**15 160**	13 317	14 328
Loans and receivables		**58 135**	62 406	60 757
Deferred taxation		**9 033**	12 499	11 151
Current assets		**1 208 095**	1 180 092	1 151 595
Inventories		**709 904**	694 944	727 231
Trade and other receivables		**325 510**	284 533	243 142
Current income tax assets		**1 053**	3 483	3 924
Derivative financial instruments		**1 363**	5 842	756
Loans and receivables		**9 969**	8 446	7 778
Bank and cash balances		**160 296**	182 844	168 764
Assets held for sale	5	**–**	3 979	–
Total assets		**1 509 594**	1 502 623	1 456 031
EQUITY				
Capital and reserves		**1 258 853**	1 278 331	1 264 735
Share capital		**1**	1	1
Share premium		**425 722**	425 722	425 722
Reserves		**833 130**	852 608	839 012
LIABILITIES				
Non-current liabilities				
Deferred income tax liabilities		**53 396**	73 579	61 532
Current liabilities		**197 345**	150 713	129 764
Borrowings	2	**–**	1 297	–
Trade and other payables		**187 208**	146 685	129 592
Derivative financial instruments		**9 687**	159	110
Current income tax liabilities		**450**	2 572	62
Total equity and liabilities		**1 509 594**	1 502 623	1 456 031
Net asset value per share (cents)		**1 836,7**	1 865,1	1 845,3

	R'000	R'000	R'000
Capital commitments			
Contracted	**5 060**	6 197	5 180
Authorised, not contracted	**25 667**	26 298	27 405

STATEMENT OF COMPREHENSIVE INCOME

	Notes	Unaudited Six months ended 31 December 2011 R'000	Unaudited Six months ended 31 December 2010 R'000	% Change	Audited Year ended 30 June 2011 R'000
Revenue		**426 075**	360 048	18,3	677 766
Cost of sales		**(279 680)**	(230 249)		(454 191)
Gross profit		**146 395**	129 799	12,8	223 575
		34,4%	*36,1%*		*33,0%*
Other income		**4 005**	5 838		10 170
Other gains and losses – net		**(10 137)**	6 692		31 443
Promotion, marketing and distribution expenses		**(106 485)**	(96 848)	10,0	(201 317)
Operational and administrative expenses		**(49 324)**	(40 154)	22,8	(85 736)
Operating profit/(loss)	4	**(15 546)**	5 327		(21 865)
Finance income		**5 587**	6 482		12 255
Finance cost		**(63)**	(337)		(638)
Share of post-tax profits of associates		**765**	2 886		2 832
Profit/(loss) before income tax		**(9 257)**	14 358		(7 416)
Income tax expense		**2 891**	(3 993)		4 468
Profit/(loss) for the period		**(6 366)**	10 365		(2 948)
Other comprehensive income					
Change in foreign currency translation reserve		**486**	(242)		214
Total comprehensive income/(loss)		**(5 880)**	10 123	(158,1)	(2 734)
(Attributable to equity holders of the company)					
		Cents	Cents		Cents
Earnings per share					
– Attributable earnings	3	**(9,3)**	15,1	(161,6)	(4,3)
– Headline earnings	3	**(9,5)**	8,4	(213,1)	(4,3)

STATEMENT OF CASH FLOWS

	Notes	Unaudited Six months ended 31 December 2011 R'000	Unaudited Six months ended 31 December 2010 R'000	Audited Year ended 30 June 2011 R'000
CASH FLOW FROM OPERATING ACTIVITIES				
Cash flows from operations before changes to working capital		**(7 916)**	8 376	(16 215)
Changes in working capital		**1 260**	7 122	(841)
Cash inflow/(outflow) from operations		**(6 656)**	15 498	(17 056)
Interest received		**4 740**	5 119	12 255
Finance costs		**(305)**	(370)	(1 614)
Taxation refunded/(paid)		**74**	5 124	(65)
Net cash flow from operating activities		**(2 147)**	25 371	(6 480)
CASH FLOW FROM INVESTING ACTIVITIES				
Acquisition of property, plant and equipment		**(10 465)**	(9 682)	(24 582)
Proceeds on disposal of property, plant and equipment		**361**	12 053	27 137
Acquisition of software		**(1 725)**	–	(407)
Acquisition of Golden Kaan brand		**–**	–	(357)
Investment sold		**–**	–	17 605
Loan repayments received		**3 859**	9 452	12 496
Dividends received		**1 920**	1 991	2 947
Investment in joint venture and associate		**(271)**	(3 734)	(4 799)
Net cash flow from investing activities		**(6 321)**	10 080	30 040
CASH FLOW FROM FINANCING ACTIVITIES				
Issue/(repurchase) of shares		**–**	127	125
Dividends paid		**–**	(23 152)	(23 303)
Net cash flow from financing activities		**–**	(23 025)	(23 178)
Net increase/(decrease) in cash and cash equivalents		**(8 468)**	12 426	382
Cash and cash equivalents at beginning of the period	2	**168 764**	169 121	168 382
Cash resources at end of the period *		**160 296**	181 547	168 764
Cash resources at end of the period				
Cash and cash equivalents		***160 296***	*182 844*	*168 764*
Other short-term borrowings		***–***	*(1 297)*	*–*
		160 296	*181 547*	*168 764*

STATEMENT OF CHANGES IN EQUITY

	Notes	Unaudited Six months ended 31 December 2011 R'000	Unaudited Six months ended 31 December 2010 R'000	Audited Year ended 30 June 2011 R'000
Share capital		**1**	1	1
Share premium		**425 722**	425 722	425 722
Reserves				
Common control reserve	2	**787 230**	787 969	787 230
Retained earnings		**44 812**	65 005	51 745
Balance at the beginning of the period		**51 745**	80 301	80 301
Net (loss)/profit attributable to ordinary shareholders		**(6 366)**	10 365	(2 948)
Equity accounted earnings transferred to equity reserve		**(567)**	(2 443)	(2 389)
Profit on sale of treasury shares		**–**	85	84
Dividend paid		**–**	(23 303)	(23 303)
Treasury shares		**(2 923)**	(2 924)	(2 923)
Balance at the beginning of the period		**(2 923)**	(2 965)	(2 965)
Treasury shares sold by the group		**–**	41	42
Equity reserve		**2 956**	2 445	2 391
Balance at the beginning of the period		**2 389**	2	2
Transfer of equity accounted earnings from retained earnings		**567**	2 443	2 389
Currency translation reserve		**1 055**	113	569
Balance at the beginning of the period		**569**	355	355
Movement for the period		**486**	(242)	214
Total reserves at the end of the period		**833 130**	852 608	839 012
Total equity		**1 258 853**	1 278 331	1 264 735

NOTES TO THE INTERIM REPORT

for the six months ended 31 December 2011

1. BASIS OF PREPARATION

The interim consolidated financial statements for the half-year ended 31 December 2011 have been prepared in terms of IAS 34: Interim Financial Reporting and should be read in conjunction with the annual financial statements for the year ended 30 June 2011, which have been prepared in accordance with IFRS and in accordance with the Companies Act (No. 71 of 2008), as amended. The interim financial statements have not been audited or independently reviewed and were prepared under the supervision of the financial executive, DP Smit CA(SA).

The accounting policies used in the preparation of the interim financial statements are consistent with those applied in previous financial periods as well as the following statements, amendments and interpretations to IFRS that became effective during the current reporting period:

- Amendments to IFRS 1: First-time Adoption of International Financial Reporting Standards
- Amendments to IFRS 7: Financial Instruments: Disclosures
- Amendment to IAS 24: Related Party Disclosures
- Amendment to IFRIC 14: Prepayments of a Minimum Funding Requirement
- Improvements to IFRSs 2010
- Revision of AC 504: IAS19 (AC 116) – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction in the South African Pension Fund Environment

The various changes in accounting standards had no material effect on the reported results for the period.

The following new standards, new interpretations and amendments to standards and interpretations have been issued but are not effective yet and have not been early adopted:

- IFRS 9: Financial Instruments
- Amendment to IAS 12: Deferred Tax – Recovery of Underlying Assets
- IFRS 10: Consolidated Financial Statements
- IFRS 11: Joint Arrangements
- IFRS 12: Disclosure of Interest in other Entities
- IFRS 13: Fair Value Measurement
- Amendment to IAS 27: Separate Financial Statements
- Amendment to IAS 28: Investments in Associates and Joint Ventures
- Amendment to IAS 19: Employee Benefits
- Amendment to IAS 1: Presentation of Financial Statements
- IFRIC 20: Stripping Costs in Production Phase Surface Mine
- Amendments to IAS 32: Offsetting Financial Assets and Financial Liabilities
- Amendments to IFRS 7: Disclosures – Offsetting Financial Assets and Financial Liabilities

2. RESTATEMENT OF COMPARATIVE AMOUNTS

Certain amounts of the prior interim period to 31 December 2010 are restated in accordance with disclosure as per the annual report and in order to make them more comprehensive and to improve comparability. The major changes are:

- The KWV Research and Development Trust is now consolidated as per the latest interpretations of the consolidation requirements of IFRS.

2. RESTATEMENT OF COMPARATIVE AMOUNTS (continued)

Prior period results have been restated as follows:

	As reported previously R'000	Restatement R'000	Restated amounts R'000
Statement of changes in equity			
Common control reserve	777 207	10 762	787 969
Statement of financial position			
Borrowings	12 059	(10 762)	1 297
Statement of cash flows			
Cash resources of subsidiaries at beginning of the period	158 359	10 762	169 121

3. EARNINGS PER SHARE

	Unaudited Six months ended 31 December 2011 Number '000	Unaudited Six months ended 31 December 2010 Number '000	Audited Year ended 30 June 2011 Number '000
Number of shares			
– issued	**68 538**	68 538	68 538
– used in the calculation of earnings per share	**68 537**	68 537	68 537
	R'000	R'000	R'000
Reconciliation of headline earnings			
Net profit/(loss) attributable to ordinary shareholders	**(6 366)**	10 365	(2 948)
Adjusted for:			
– profit on sale of property, plant and equipment	**(135)**	(4 588)	(16 595)
– impairments of non-current assets	**–**	–	14 355
– profit on sale of joint-venture company	**–**	–	(12 394)
Headline earnings	**(6 501)**	5 777	(17 582)
Adjusted for:			
– Retrenchment cost	**9 271**	–	–
– Costs associated with Pioneer offer	**–**	–	6 264
Adjusted headline earnings	**2 770**	5 777	(11 318)
	Cents	Cents	Cents
Earnings per share			
– Attributable earnings	**(9,3)**	15,1	(4,3)
– Headline earnings	**(9,5)**	8,4	(25,7)
– Adjusted headline earnings	**4,0**	8,4	(25,7)

	Unaudited Six months ended 31 December 2011 R'000	2010 R'000	Audited Year ended 30 June 2011 R'000
4. SEGMENTAL ANALYSIS			
Functional analysis of sales	**426 075**	360 048	677 766
Wine	**196 993**	178 038	343 382
Spirits	**175 182**	162 763	296 750
Other	**53 900**	19 247	37 634
Regional analysis of sales	**426 075**	360 048	677 766
South Africa	**229 594**	204 941	374 795
Europe and the United Kingdom	**131 431**	98 273	202 046
Rest of the world	**65 050**	56 834	100 925
Operating profit of wine and spirits	**(15 546)**	5 327	(21 865)
Trading profit: South Africa	**13 866**	22 968	20 701
Trading profit: Europe and the United Kingdom	**15 231**	5 130	(1 620)
Trading profit: Rest of the world	**10 813**	4 853	3 177
Items not allocated to segments:			
Other income and other gains and losses	**(6 132)**	12 530	41 613
Operational and administrative expenses	**(49 324)**	(40 154)	(85 736)

5. ASSETS HELD FOR SALE

The group sold its 50% interest in its joint-venture company, Vititec (Proprietary) Limited ("Vititec"), as well as some assets that Vititec rented from KWV in the prior year.

Assets classified as held for sale	
Property, plant and equipment	1 373
Investment in associates and joint ventures	2 606
	3 979

6. EVENTS FOLLOWING THE INTERIM PERIOD

Shortly before the end of the interim period, on 21 December 2011, HCI (Hosken Consolidated Investments) and KWV jointly announced a mandatory offer by HCI to all KWV shareholders. The offer resulted from the fact that HCI's indirect shareholding in KWV increased beyond 35% in December 2011.

A circular with details of the mandatory offer, required in terms of the Companies Act, was distributed to shareholders on 20 January 2012. Shareholders who wish to accept the offer have to submit the relevant documentation to the transfer secretary by Friday 2 March 2012. The offer follows approval by the Competition Commission in April last year for the acquisition of control of KWV by HCI.

7. OPERATING RESULTS

The sales volumes for the six months under review increased by 19,7%, and revenues increased by 18,3%. Of the 18,3% increase in sales revenue 8,2% relates to contract bottling.

Total wine sales volumes remained flat and the increase in sales (10,6%) stemmed from price increases and the favourable movement in the exchange rate.

Sales of spirits were satisfactory when one considers that the South African brandy market is a declining category, with turnover growing by 7,6% (volume growth of 4,9%).

Other sales relate mainly to contract bottling. These sales have more than doubled and although this is low-margin business, it improves the group's cost base and capacity utilisation.

The above factors are also visible in the regional sales. Stable volumes in Europe, coupled with a weaker euro and increased prices, resulted in an increase of 33,7% in revenue. Volumes and revenues from South Africa were disappointing with the main source of growth being contract bottling. Sales to the rest of the world grew satisfactorily mainly due to growth in exports to the African market.

The reason for the slight decline in the group's gross margins is the significant increase in contract bottling business. In general, the margins across product ranges and markets have performed satisfactorily and the focus on improving margins are starting to gain traction. Excluding contract bottling, the gross profit increased from 38,1% to 39,2%. The product mix sold affects margins and in future gross margins is not dependent on sales of lower-margin products.

Rent received and dividend income form part of other income. The decrease in other income is due to a decline in rent received, stemming from the disposal of these assets.

Other gains and losses consist mainly of exchange rate profits and losses and profits on sale of assets. The prior period contained a one-off profit on sale of non-core assets of R4,8 million and exchange profits of R2,1 million. In contrast, in the current period there were negligible sale of assets and exchange rate losses amounted to R9,5 million. These losses were due to a strategic decision to hedge most of the budgeted sales for the 2012 financial year in advance. Of the total exchange rate loss on interim, R5,8 million relates to the mark-to-market adjustments on budgeted sales for the remainder of the year.

Continued investment in the group's brands, distribution channels as well as in its new RTD business, is reflected in the 9,9% increase in selling and promotional expenses. Sales expenses are 27,7% of revenue, excluding contract bottling, as compared to 28,1% in the previous period.

7. OPERATING RESULTS (continued)

Administrative and operational expenses increased by 23% due to retrenchment cost of R12,9 million and the restructuring process that was effected in the past six months. Excluding these costs, the group's overhead expenses are being managed downward according to plan.

The headline earnings for the period under review amounted to a loss of R6,5 million (9,5 cents per share), compared to a profit of R5,8 million in the comparative six months. Adjusted headline earnings, as detailed in note 3, deteriorated from R5,8 million to R2,8 million.

8. ASSETS AND FUNDING

The group's total assets and net asset value remain largely unchanged and it continues to hold substantial net cash resources of R160,3 million.

The group's accounting policy is to state property, plant and equipment at historical cost less accumulated depreciation and not to revalue these assets to market value. As a result, the market value of appreciating assets like land and buildings and certain works of art are more than their carrying values in the financial statements.

The board considers the current accounting policy to be appropriate and does not intend revaluing properties on a regular basis, but in the light of the mandatory HCI offer it has been resolved to disclose the valuation of properties and works of art on a one-off basis.

Recent valuations, some of which were updated as part of the fair and reasonable reporting process, estimate the values of KWV's art collection at R40 million (carrying value negligible); and R152 million for non-operational properties (carrying value about R15,6 million). In addition, the most significant operational properties which are required if KWV is to continue as a going concern have also recently been valued at about R230 million, whereas their carrying values are R24 million.

If adjusted in the financial statements, the revaluation of the non-operational properties and works of art would result in an increase of about R2,52 (after tax) per share in the net asset value of the business. As previously indicated, the board has no intention to sell these assets in future.

The group's investing activities show a cash outflow of R6,3 million, whereas there were significant inflows from the sale of assets and loan repayments in the comparative period.

9. BUSINESS ENVIRONMENT

KWV's export sales remain weighted towards conventional, developed economies in Europe and North America, where volumes are starting to stabilise again, although growth prospects remain limited and consumers continue to trade down.

South African consumers, in particular, are facing increasing inflation, which is likely to put further pressure on liquor consumption and margins. In addition, increases in excise duties continue to be significantly above inflation and will contribute to products being less affordable. Possible changes in legislation to implement more stringent controls over the marketing of alcohol could also affect sales negatively.

In this challenging environment, KWV remains committed to its strategy of product diversification, brand focus and a global footprint and will therefore maintain its levels of investment in advertising and promotions. KWV also continues to invest in its distribution and marketing infrastructure and will continue to fund the expansion of products like Ciao and Jimmijagga. The investment in these new products and markets will likely consume cash resources in the short term before the anticipated benefits start to realise.
This requires a longer-term view of the business and demands a strong focus on process optimisation and improved execution and implementation.

The group's return on assets remains very low and it is not expected that this will improve substantially in the short term as the focus remains on the portfolio of products and not on the restructuring of the balance sheet.

Signed on behalf of the board of directors.

Marcel Golding	**André van der Veen**
Chairman	*CEO*

Paarl
21 February 2012

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