

Foster's Group Limited

Wine Trade Operational Review Investment Market Briefing Question and Answer Edited Transcript

Sydney – 8 June 2004

Panel

Trevor O'Hoy – Chief Executive Officer

Pete Scott – Chief Financial Officer

Walt Klenz – Managing Director – BBWE

Jamie Odell – Managing Director elect – BBWE

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TREVOR O'HOY: I think as you can all see, the flexible and robust sustainable wine model remains our number one priority and absolute focus. The picture of success for us is that we will continue to achieve world-class brands and hopefully world-class financial outcomes. If we can do that then we will have the ability to fully leverage the existing global platform we have which is amongst one of the best and lead the consolidation in the market that still remains today in relative high growth and a market that is still very highly fragmented. That's the prize for us but we have a lot of hard work to do before we get that ability.

Ladies and gentlemen, thank you for attending today and we are happy now to throw the floor open to questions. Can you please state your name and organisation before you ask the question. Are there any questions firstly from the floor?

QUESTION: I guess looking quickly at your guidance and certainly the ability in 05 for 9 per cent growth, that is, high single digit, if you assume that you are getting four and a half from the buy-back category and you are getting second to none in CUB, are you still expecting growth through the wine through F05 before you start getting into these growth initiatives to come true. I guess the question is how long do you think it is going to take the shipments and how are you going to move that without damaging the brands in the short to medium term on the back of if we look at the last two years we have obviously had the drought, a lot more supply out of this so it is a bit harder to do I suspect.

PETE SCOTT: Before we start that, can I reset your comments. You are inferring that the wine division is not showing growth for F05. That would be incorrect. The wine division will show growth in F05.

QUESTION: Can you explain that assuming the capital.....

PETE SCOTT: There will be growth in Beringer as well as CUB and the other operating divisions. I expect the operating divisions to be between mid and high single digit growth for F05. Expect to get leverage over the corporate expense line. We will get significant negative leverage on interest expense. Remember that interest expense in F04 benefited from the fact we didn't have to pay interest on the bonds. So it's a fairly low number. We will not get that benefit in F05. We are going to see some increase in interest expense that my guess right now, is going to take 250 to 300 basis points on what will be pre-tax growth, if you will.

So when I talk about high single digits, I think about high single digits driven roughly equally between growth in earnings and improvements in share capital. We can follow on with the rest of your question but I just wanted to make sure we were clear on that point. Does that help?

QUESTION: In terms of distributor inventories, but how long will that take, you have got on your slide here you think it will take through to first quarter 05. What is the decline expected?

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TREVOR O'HOY: In terms of distributor inventories we will have all the corrections at the end of the financial year. Inventories should remain in balance going forward providing the market growth comes through in line with the assumptions of the model which is high single digit volume growth.

QUESTION: A multi part question on brands. There are a number of brands that had sizeable volume bases that aren't perhaps getting that investment, like Black Opal and there are ones getting secondary investment. So I am just curious as to how the company is going to achieve its top line volume growth targets in those multi-based brands, particularly Black Opal without moving backwards. Another one I may have picked up in the US brands is Founders Estate with a \$10 price on the slide. I always recall that being a \$10 to \$12 brand. Have these been repositioned? If it is, that probably opens up a whole discussion on how you are going to drive or reinvigorate these brands for Beringer. Do you need to reposition them, do you need to tell the consumer that there is a change in quality and value in that statement? That's the first question.

Just a quick one for Pete. The guidance that you are giving does that take into account the utilisation of tax losses and changing tax rates?

PETE SCOTT: First of all the tax question, before Jamie deals with the brand questions. The expectation for the tax rate over the next couple of years will be generally flat at 30 per cent. Obviously as US earnings begin to grow and take a bigger proportion of the total portfolio and total pool of earnings we will have a tendency to migrate up.

JAMIE ODELL: Founders Estate has always just been under US\$10 and supported now by Stone Cellars which is great and very successful. That won't change. I look around the 8 to 12 category as clearly the heartland and primary focus of attention and it is actually also the heartland here in Australia. So the change to more investment range and more emphasis (I think it's fair to say a little bit of emphasis had been taken off, particularly with Stone Cellars coming into the marketplace), will, see not only top line growth but also supply chain efficiencies.

Black Opal is an interesting subject and I didn't mention it as important as it is. It is a brand we have got specific plans for. It has been sitting in the middle of our portfolio between Beringer and Wolf Blass and it needs clearer positioning. Around it you have seen these new Australian concept brands emerging. Black Opal has got to change, I won't tell you what that change will be but you will see a change.

QUESTION: Trevor, just three questions. The growth in Stone Cellars has been quite aggressive, if you believe in that. Is it fair to assume that the two large brands would be flat to down and if that's the case, can we talk a little bit about brand health versus sell through rates. I know that brand health is a leading indicator and volume is quite unrelated but there is a connection at some point in time. I guess the question is firstly, how do you know the core brands are going to respond to consumer spend? Do you have a view on how big a brand is and I am curious how you know those brands are going to respond.

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The second question is I think you said in the release that the Beringer Trade North American revenue was in low double digit. I am just wondering about the components of that top line growth. How much for NPD, how much extensions from existing brands and how much in recovery for existing core brands?

TREVOR O'HOY: I will answer the last one and leave the brand details to Jamie. The model going forward does not have a lot, if any, contribution from innovation factored in. In the model there is 60 to 85 million cost savings with about 50 per cent of that reinvested in brands. We actually included very minimal price increases in the model. We will obviously be trying to get higher price increases and obviously we want that brand investment to work.

JAMIE ODELL: In the wine category, the brands which are the number one brands have up to 6 per cent market share. The bigger brands in key markets are getting bigger. This is led by better brand building, it is led by consolidation in the wine industry, and it is led by consolidation in distributors and retailers and therefore I expect to see the top brands moving towards 10 per cent from 6 per cent.

The brand health of Beringer, I think because of its premium nature and history, is very very strong. The fact of the matter is, as you have seen, it has been undernourished in the last two years.

My confidence is entirely about getting the proper level of investment and from this, consumers buying the product. The whole equity of the Beringer brand is strong. It is still recognised as a great brand. These wine brands have been around for many years, and do not fall out of favour unless people take their eye off the ball and allow them to die. The thing about the wine industry, all the key brands have some sort of history and heritage. All the major brands around the world do and Beringer has got the best position in the US in terms of that background and that potential.

WALT KLENZ: I think the short answer to your question about how confident do we feel about advertising for Beringer, we have done it in the past. Beringer in the context of the American wine market was a heavily advertised brand in a category that is not a beer category and the growth of Beringer in the 80s was directly related to sustained consumer advertising over a significant period of time.

As Jamie said, tactically that was cut back and we are going to basically reinstate that. We track awareness and usage on our brands and all our competitor brands. The brand health in Beringer is still solid. Indeed it has been undernourished, as Jamie said, but we have not seen any significant deterioration in the brand attribute scales that we look at.

JAMIE ODELL: Forgive me using Wolf Blass as an example but when I first joined the business people thought Wolf Blass was a dull and tired brand which was definitely going to die and be replaced with new brands and all our money should be spent on new brands. You will remember across the industry three years ago the proliferation of new brands coming out in different coloured shaped bottles, none of which have stuck in the marketplace.

There is heritage and quality in the wine category. Wolf Blass was in far worse shape in Australia three years ago than Beringer in the US. So it is about getting the plans right for Beringer in the US.

QUESTION: Forgive me for sounding a little bit cynical but go back ten years ago when both Mildara and Beringer were aggressively planting vineyards and getting access to all materials was a key issue for the company. So ten years of planting turns into oversupply and now you are selling the vineyards off. What is going to stop it if it is going back to the same cycle again in five or six years time, are we heading back to a shortage again?

JAMIE ODELL: I will start off with that. The wine industry does move in cycles. You get too much Shiraz and you get too much Chardonnay absolutely. That's why it's fundamental that there is a far better supply/demand process in place. We are putting in place a global sales planning group which is fundamentally the centre of our business, which links all the selling groups in each market and all the demand numbers through the "Manugistics" software program to all the different production sites around the world.

That is a fundamental change in the way we do business and it is very important we have a specialist high calibre capability in the centre of that process.

Ownership, it is funny in the wine industry, we tend to think people in the wine industry have to own vineyards. I challenge that. In most industries, the raw materials do not have to be owned by the brand owner. It is increasingly about the assets being intellectual property and not hard assets. If you look at some premium wines, far more comes not from our vineyards but from our long term contractual relationships.

There are a number of elements in vineyard ownership. You only own your own vineyards where there is an absolute need to own vineyards. When there is a long term relationship with contractors, with some of those contractors you can control the farming, depending on the way you structure the deal.

So the ownership of the asset is not important, it is understanding what you need going forward and having enough control to increasing your commitment to contracts. It will be wrong to say that you have to supply all of the wine from your own vineyard. It's about knowing in advance and being ahead of the marketplace in terms of how much fruit you need.

Perhaps I will use an example of the recent vintage here in Australia in terms of introducing some evidence of our improved capability in this respect. We worked out a long time ago there would be too much red coming through, particularly in some areas and particularly at some prices. We actually pre-sold some of our own fruit before the vintage and got rid of that. We managed to maintain a supply and demand balance in the Asia Pacific region. There was quite a lot of tonnage in the overall market.

So, it's not about vineyard ownership any more, it's about brands and having far better market information.

TREVOR O'HOY: Can I add to that, not in a technical sense, but the philosophy has changed significantly as of today. The business has been run for many, many years on the philosophy of never running out of grapes; we will always grow ourselves out of profit declines because we have never seen two bad years in a row.

That changes as of today. Our philosophy is it has to be demand driven. The model is going to change where we will have to mix capital with margin. It is a very complex thing but we have to have a matrix mix of vineyards we own, supply through contracts and outsourcing according to demand. If you happen to get lucky in terms of growth, you may have to give up some margin to the spot market and the growers and that is something the industry has tried to avoid for many, many years. But no longer are we prepared to put this business at risk.

QUESTION: A question following on from what you were talking about Trevor and also some earlier comments from Jamie's presentation. I thought there were two pieces of magic here, one was with lower CAPEX and I sort of expected something like what you have done with Mildara which is sort of much trumpeted, in other words spend some money, get your efficiency up.

The second piece of magic was improved quality with lower grape costs. Isn't that something that everyone else does at the same time if the market price is down and what can you do in sourcing the cut off point to achieve that?

JAMIE ODELL: Well the first point is to understand that California is very different to Australia and I think it would be naive of us to force an Australian production model. The Californian wine makers have far greater influence, the wine makers are far more heralded and to create a US version of Bilyara [Wolf Blass Winery, Barossa Valley, South Australia] is not the right approach. We have a process to deal with our production sites. I am not quite sure what you meant about magic but the efficiency in wine making is about asset utilisation, barrel usage; there is far higher barrel usage in premium wines in California than we currently have in Australia.

That's an example of where we will be sharing best practice and taking costs out of the system. That is not magic, that is producing quality wines and using the best techniques in a winery. We know at the Wolf Blass winery, there is new technology coming through all the time to extract more fruit from the grapes to get more flavour which allows you to obviously sell it for a higher price and to use it to release the wines earlier which clearly helps you with cash and capital efficiency and to use more efficiently things like oak which is a high capital cost in a winery.

That is really without overlaying the principles and processes using Bilyara into some of the sites in California. We are certainly not saying we are going to put the Bilyara model into California because it is a different market and we would make some big mistakes if we just assume that the American wine market can follow the Australian model. Do you have any views on that?

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WALT KLENZ: The two major non-luxury assets, Meridian on the central coast and St Helena are very large plants. Meridian is a 40,000 tonne plant which is not that much smaller than Bilyara. We have scale, especially when we apply some of the production cost reduction issues that Jamie just talked about. So I think we can definitely from an internal production point of view be cost competitive.

We don't necessarily have the same cost as Australia but relative to the North American context, I think it can be very cost effective. With regard to the question of our grape costs, clearly when grape costs go down everyone benefits equivalently. I think a lot of the benefit stream that we see is adjusting the current technological abilities of our wine making team to use a different proportion of insourced grapes and frankly be able to reduce the components of coastal high cost grapes much like here reducing the components of cool climate grapes and go after the higher quality warm climate grapes in an appropriate mix to deliver the product quality at the appropriate price point. That's real change that will benefit disproportionately no matter where the overall market price of grape goes.

JAMIE ODELL: It is not just about the grape, it's about how you make the wine, the techniques you are using, the way you store it, the oak you use, also the age at which you release the wine. The fact is you could sell the right wine at the right price.

As Walt says, improved wine can do that through the blend costs. As to all the wines getting better, that will possibly be happening. That is another reason I think brands are so important. Brands have to be differentiated because it's very hard to have a unique quality standpoint which is not replicable. I think that's the key reason I believe it is the brands which have to take this company forward as well as developing the best quality for each price point. Fundamentally brands, which consumers demand be put on the shelves.

QUESTION: I am trying to get an understanding of what effect this review is going to have on 04 and 05 earnings. If you have a look at the \$22 million, your shipment adjustment, consensus numbers for the US trade was \$164 million, that was 04 overall earnings consensus for Beringer Trade North America. I know that because your guys told me that. Does that mean that now it is going to be around \$140 million for 04 because presumably that \$22 million comes straight off this year's forecast earnings.

PETE SCOTT: The \$22 million does come off this year's earnings, that's right. The other adjustment that I would suggest you consider would be the Services adjustment. That is an important element. Remember that Services generated over the fiscal year 03 was in the order of \$35 million EBITA; we are talking about a \$20 million number this year. From my stand point we are taking \$22 million plus the \$15 million out of what would have been the wine group base and those are the two elements that you need to consider when we think about 04.

QUESTION: I was speaking specifically on US trade and consensus was \$164 million for that segment. Is that going to be now around \$140 million for this year because that \$22 million was in the US, not Australia?

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PETE SCOTT: That's right. I am not going to comment on the specific amount. The \$22 million comes off US trade number.

QUESTION: I would like to know what that \$22 million actually is and what are you going to do with it because 20 per cent margin is around 100 million of sales, thereabouts which is probably about 2 million cases, a significant amount of shipment. What are you going to do with that?

PETE SCOTT: Don't think about the 20 per cent margin because it's only the direct brand contribution that's attributable to this \$22 million. Effectively the overheads stay the same, so it is a higher percentage.

QUESTION: I am a little surprised you are pulling numbers down by \$22 million and clear effectively the shipment and why you don't get a stronger rebounding growth in 05 when you say you are still going to be under double digits. You effectively pulled off quite a significant portion in 04 so you are starting off a lower base.

PETE SCOTT: Correct, and I think one of the things I mentioned was that there would be a significant increase in brand investment in F05, a significant increase.

QUESTION: Just a couple of quick ones, your guidance on EPS, you said you were probably down \$15 million EBITA on Services, you are down \$22 million here on the shipments, so that's 35 million EBIT which presumably is about \$25 million NPAT down, yet your EPS guide has only gone from 2.9 percent to 1 percent. I would have thought that say \$25 million NPAT on around 500 million NPAT, that is 5 percent negative NPAT growth, yet you are only bringing the EPS down by about 1.92 per cent. So are there other businesses that are doing better to offset that?

PETE SCOTT: Prior to those adjustments, you're right, we would have been growing mid single digit on a continuing business basis. Obviously the rest of the business continues to do pretty well.

QUESTION: Is that better than what you thought at the half year? You said 2.1 percent.

PETE SCOTT: What I said was we did 2.9 percent growth in the first half 04. We thought we would do better in the back half and therefore better for the full year. We expected actually to exceed the 2.9 per cent.

QUESTION: To labour the point on F05 and the benefit from the Stone Cellars inventory, I am presuming that is something that inches the growth off the lower base. If you can quantify that for us in 05 and 06? The second question is more for Jamie in relation to the Asia Pacific business which is being held up as the model. The feedback from the trade domestically is there has been a significant increase in the aggressiveness and deals from Beringer in the current six month period. Can you perhaps comment on trading in that business, whether that signals an issue of the model that is being held as the footprint please. Thanks.

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ANDREW LEYDEN: The Stone Cellars adjustment of the total surplus wine taken as a write down is around 25 per cent of that write down. So we can return that brand to an outsource model using the original blends that were destined for that brand. That will return benefits in F05 and F06 to the tune of somewhere between \$15 million and \$20 million. That benefit stream will effectively end in F06 [and the benefits of the future supply blend will kick in at that point. Is that clear enough?

JAMIE ODELL: In terms of Australian wines, I don't know who your sources are. Last year for example we were doing 3 for 10 promotions which we haven't done this year. We launched some litres last year so that may have moved slightly from litre to actual activity but not a shift in terms of our expenditure.

I can guarantee that there is a lot more money going above the line and that's what we plan to do. It is more about being on display at a price point rather than discounting. I can assure you that there is no change in what we are doing here and the results are in line as indicated to you previously.

TREVOR O'HOY: Are there any questions on the line?

QUESTION: Thank you very much, a lot of good information in the review. I have a couple of questions on the North American business as well. Jamie, can you give any specific targets on how many new products you plan to introduce in 05 or 06 and maybe a follow up on that and can you give us any further clarity in what your current level of market is as a percentage of sales and what you plan to change that to.

JAMIE ODELL: I will answer the first one. We expect about four to five new products coming through in the US in the next 12 months. I also want to make it clear we are a business which focuses. I don't want to give an indication we are going to have a scatter-gun approach to new product development. What we have really done, and I mentioned this before in my presentation, we have formed an innovation group and that global structure is really led from the hub here in Asia Pacific which is a combined CUB and Beringer Blass innovation group working across all of the alcoholic beverage categories in terms of gathering consumer insights and working through the trade, that is the sort of activity you see in recent launches in Asia Pacific as well as the CUB launches we have been seeing here in Australia.

That has been supplemented with innovation people in the US and in Europe, specifically people who form part of that group and are using common processes and common insights. There is far more emphasis on new products going forward. The wine category is one, which I said earlier, where secondary brand innovation has proven to be more successful than pure innovation.

Don't think of innovation as new brands and new bottles coming through. Think of it as new approaches to existing assets. Saltram would be a good example. Saltram is a winery which has been around for many years with recognition built through completely rebuilding that brand and going about it in a different manner. We got back into growth rates as I indicated earlier. That is some feel for innovation but you will see four to five products come out next year certainly. The first two I have already

alluded to be sparkling white Zinfandel and the new Zinfandel 187 ml. Perhaps that's an example that not all innovation is going to be earth shattering, some of it is going to be entering new segments and new consumer drinking opportunities.

ANDREW LEYDEN: Specifically to the question on brand building, the profile of brand building varies clearly on a region-by-region basis.

We intend to double the amount of spending between F04 and F05 in marketing. The kind of range that would apply is somewhere between 7 and 11% (as a percentage of sales) which is a very strong rate of investment. 7 to 11%, depending on the market.

QUESTION: Up from three, four today?

ANDREW LEYDEN: My initial statement was our levels at the moment are probably sub 6, but they are different by market.

QUESTION: I just have a couple of more follow up questions on the history supply issues. You mentioned that you are past the worst. What kind of yield assumptions do you have in your model going forward?

WALT KLENZ: From a California perspective, we basically try to look at long term yields on a region by region basis and try to take a five year average or something like that. Obviously depending on which regions inherently have higher or lower yields, depending on their climate and whatever, so the yield across the whole state can vary depending on where the growth is going to come.

Frankly, most of the growth in the next couple of years, although in a declining rate, is coming out of the coastal area in California so actually some of the yields may decline across the whole acreage because yields in the central coast are inherently lower. We basically try to do a five year average, knowing that you are going to have big ones and small ones and they are frankly very difficult to forecast.

JAMIE ODELL: Yields are important in terms of what is the effect in the industry and supply coming through the industry. Let me talk about how our supply model is flexible. We can actually go through each brand at each price point and the different inputs into those different blend structures. We look at the amount of fruit already in the supply chain, the amount of planting in the ground and the amount that is likely to come through looking at averages as a base but acknowledging the latest information we are getting from the vineyard growers backed down based on the amount of fruit available to the amount we commit to.

Sometimes that will be as low as 50 per cent. If, for example, we know there is a lot of Cabernet to be brought in the marketplace at low price points we would back down on our future commitments. If we know there is a shortage of high price Riesling, up to 90 per cent, never to 100 per cent, up to 90 per cent because as Trevor said, the model is changing in that you have to balance the balance sheet with the P&L.

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If there is a penalty paid for that ten per cent, that's the penalty we pay. We believe that will be mitigated in terms of where the supply and demand is. Let's say we sold above our own demand model, then we would go out and pay current prices but far better to do that than end up with some of the surpluses that we have currently witnessed.

QUESTION: Last year's yield on average would be below the five year average. Did you have a think about that?

WALT KLENZ: In California they were perhaps marginally below but not enormously below.

QUESTION: Maybe one final question for Pete. I think I saw under rule 7.33, maximum price for the shares of 4.65. Is that right and secondly, does that mean you will be buying back shares at current prices?

PETE SCOTT: Without commenting specifically on rule 7.33, as I think you have all observed, we have been out of the market recently from a share buy-back stand point, certainly with regard to this meeting and the importance of this meeting. As we think about the remainder of the fiscal year and going forward, I think what we will end up doing is probably let this information digest for a day or two and then we will be most likely back in the market. Obviously that comment is always caveated by market conditions etc., but that would be our intent. As I mentioned, we will continue to pursue the buy-back program as we go into fiscal year 05.

QUESTION: A couple of questions. The first one again on North America, specifically with reference to your assumptions. You are assuming your market share is going to improve, you are going to out-perform the market in general but what you are indicating here today is obviously very similar to what your competitors sort of kicked up probably six, twelve months ago. So can you give us an idea of why you think you are going to do this any better than the other big companies specifically? Where does your marketing spend relative to the likes of Constellation Gallo, sort of why should we come out of here convinced that you are going to do a better job than them given that more recently you have been falling behind.

Also I suppose as sort of an extension on the topic of distribution, it appears in the US that the bigger you are, the more advantage you have and it seems to be becoming increasingly the case for the likes of Constellation Gallo, is that an issue for you going forward and is there something you plan to address?

Just on the cost side, are you being conservative in terms of what costs you can strip out? There is a comment in the costs under review. Is it possible therefore you will come back in the future indicating there are additional costs that are going to be pulled out. Also, in terms of the costs that you have given us, could you give us a bit of an idea in terms of the break down, where that is coming from.

TREVOR O'HOY: On the last one, I envisage and hope that we don't come back in this forum ever again. From here on in its normal day-to-day operations. We have set on our targets and we will come back and report back on that but I don't believe we will change the model to this degree again.

JAMIE ODELL: I am very confident in our ability to deliver the lower cost of goods. Those are actions in which there are improvements to be made and continuous improvement is what we are about.

In terms of distribution, again I call on Walt because he has been dealing with that for a long time.

We have very strong distributors and strong partnerships with the distributors. In all markets there are two powerful forces at play, one is brands and one is distribution and we are looking to increase our distribution strategy in a number of markets to actually increase our spread because we know if we get our product on to the shelves then it sells.

Our distribution base is extraordinarily solid at the moment, we have great distributors and very strong distributors.

WALT KLENZ: Particularly in the last year, particularly the east coast we made two major moves in New York and Massachusetts to align our portfolio with the prime distributors in the market. We have an objective with our distributors (remember distributors in the US, because of consolidation, are often multi-divisional distributors), it is to be the anchor wine company in the division in which we are, and in every major market around the US I think we qualify as the major anchor tenant, as it were, in supermarket or shopping mall context. That is something that is very very important and that is a critical negotiating point when we sit down and talk to distributors about where to move or where we want to be and we want to be anchor tenant. That doesn't mean we are not going to be the only wine company, we want to be the major wine company in that division which is one of the reasons typically we are not in the Gallo House, Gallo has typically semi-control powers. We are not a Gallo House. We are with Diageo in Cleveland, we are typically the anchor tenant in the other Diageo division.

As Jamie said, I feel that our national distribution strength, looking at the quality of our distributors and where we are located with those distributors is as good as I have seen it in the last 10 or 15 years.

ANDREW LEYDEN: I want to deal specifically with the questions on costs. We have disclosed a range of \$60 to \$85 million benefit streams in F07 to F09. We have discussed those because we are confident we can deliver them. The extent that we can increase the amount of cash we can dedicate to our brand building, I don't quite know what that is going to be. We will target a bigger number than that.

In terms of breakdowns, I can give you some guidance around that. In terms of excess inventory, a significant write down. This is a permanent exit of supply from

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the supply chain. It delivers a minimal stream for us, and therefore is of negligible value.

In terms of future supply, we anticipate a benefits range of somewhere between \$15 million and \$25 million. In terms of consolidation of infrastructure and more efficient use of oak treatments, we anticipate somewhere between \$35 and \$40 million.

Then we have a series of benefits relating to purchasing and other initiatives not related to some of the write downs. Those benefits are between \$10 and \$20 million. Hopefully that gives you a better feel for the range of benefits.

QUESTION: Andrew, if you can just clarify that \$15 to \$25 million that you are referring to in terms of the inventory write down. Isn't that what is going to kick in in 05? This is Stone Cellars?

ANDREW LEYDEN: For the Stone Cellars fruit realignment we will get a \$15 to \$25 million benefit in each of F05 and F06 only. That is really an exit. [Future supply starts to deliver from F06 onwards – *what are we saying here????*].

QUESTION: The answer to the question in terms of why should we feel confident you can do it better?

JAMIE ODELL: The key point is we have done this before, both in Asia Pacific and also in North America. Let's not underestimate the great brands we have in Australia and in the US. When the US have been given money to spend, these people have done it effectively. It will be supplemented by more global ability across the Foster's Group.

You have talked about our competitors. We differentiate ourselves. We have premium margins, different price points, there are different consumers buying those price points. We are not actually trying to sell at the very bottom end of the market. We are trying to sell at the premium price points of the market. That is a differentiating point.

Our ability to spend effectively, yes, clearly we have a great deal of confidence in supply chain activity. Revenue growth is the key variable, the key initiative, the one which I keep reinforcing that we have to drive through. I can guarantee in terms of the money we are releasing to brand investment, it is going to be controlled effectively, released effectively, it is not going to be thrown at the wall in a "hit and hope" fashion. This is going to be professionally planned, the way we have done in Asia Pacific. A focus on core brands in key markets such as the US where we want to increase distribution, where we want to increase consumer pull through.

So it will be done as a very highly focused initiative across the business. But yes, revenue growth is fundamental and it is one of those areas that until I can show you the value add and until I can show you the numbers, will you never believe me. But we have better credentials than anybody in terms of major wine players to show growth at premium price points.

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WALT KLENZ: As I said before, regarding the Beringer brand, I know what the spending has been and I know what the projected spending is - it is going to get us back to comparable spending at the time when Beringer was growing very significantly. Frankly, in the US context the only real player who has spent more is Gallo. Gallo is the only one that has significantly out spent the competitive. Gallo has been more than competitive in terms of its consumer spending over a period of time. That is the model that this plan gets us back to.

TREVOR O'HOY: We will take one last question from the floor and go back to the telephone.

QUESTION: This is a two part question. How did you do this review? Did you start and build yourself up to what you thought was sustainable, or did you start with your existing operation and this is the deck of cards that has been dealt, - "we will try and maximise what we can get"?

The second question, just in relation to 2004, your Australian vintage is up on 2003. I look at it and say the Australian industry is up 25 per cent, the major competitors are up in the 20s. What is your expectation, what did you mould into the competitive set as far as price versus volume, the Australian market and the Australian exports particularly into the US over the next couple of years to try and clear a sizable amount of vintage that you don't have sitting in your tanks or do you have quite a bit hanging over from 2003 that you are going to be releasing against your competitors in 2004?

TREVOR O'HOY: In terms of the first question, clearly the basis for this review and the one going forward has been around, but not totally, the successful Asia Pacific model.

JAMIE ODELL: How did we approach the review? What we did fundamentally, we started with the outcomes we wanted, which I have shown you, the financial outcomes in terms of high cash generation 70 to 80 per cent and vastly increased returns profile. Then we worked back through the P&L and the balance sheet.

Then we overlaid the optimum models to what we have and then we investigated areas we didn't need in the model going forward. We tried to deliver an optimum model for the future overlaid with what we have currently got, to change the model to be more demand driven and more consumer driven, more brand driven in the future.

It was done as a team and done ultimately to drive the financial outcomes of the business but also drive sustainability.

Again about sustainability, this is not a one-off fix. You have to have replicable growth and to do that you have a really solid base and get back to the fundamentals. That's what we have tried to do here, we have to provide a sustainable growth from top line growth, high utilisation of capital assets and better cash generation. That's the process we went through.

In terms of the Australian vintage, I am actually quite proud to say we are 8 per cent up. I want to mention we got rid of predicted surplus before the vintage occurred. This all again comes down to increased capability in terms of SOP [Sales and

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Operational Planning]. We will make sure that we do not end up with surpluses and that is a priority for us. Please get that message.

In terms of the market, we can't control the market. There is going to be a lot of Australian wine in the marketplace. There always has been,. There has never been a time when you have gone to a bottle shop and have not been able to buy a bottle of wine. There has always been a lot of wine around. What is happening, actually, is that there is better and better quality around the world as wine making techniques improve and there is particularly some new countries that invest more and more in wine infrastructure.

That is going to continue. There is going to be more and more products trying to be sold and they are going to find it harder and harder to get in because the number of gatekeepers is going to be reducing. We have to succeed with our premium brands regardless, frankly, of how much other product comes into the marketplace.

Once again you don't compare in other categories how much beer we sell and how much beer is available. We talk about what the consumers need to pull through, the price points, manage the distributors to make sure they can grow your brand over anybody else's.

We actually focus on why consumers are going to be trying our brands. Consumers have a lot of choice from other countries, not only just Australia.

TREVOR O'HOY: Thanks, Jamie. We are coming to a close. Can we take some questions from the telephone and we can answer some more questions after we close that. There are no questions from the phones. Some final ones from the floor.

QUESTION: Just on outsourcing, to what degree are you outsourcing or going to outsource Stone Cellars and if it is a full outsource or are you buying a finished good from a second or third party and what does that do to bring up the capacity in the manufacturing process and storage processing?

WALT KLENZ: I think as Andrew and Jamie said, we will be returning fairly shortly with the initiatives to the full outsource model on Stone Cellars. Some of the benefit streams, as Andrew related, some of the minor benefit streams of rationalising the inventory models is to get rid of outside storage cost. So it isn't so much we are going to free up internal capacity but more we will not have to go out and buy capacity to make aged wines that we didn't need but had to take because of the relatively inflexible inputs. So that will be the benefit there. It isn't like we are going to have 20,000 tonnes of excess capacity.

ANDREW LEYDEN: The other points, we have a similar model in Australia with products like Eaglehawk, somewhere between 90 and 95 per cent of Eaglehawk will be outsourced. So a very similar model in terms of outsourcing.

WALT KLENZ: You will recall White Zinfandel and Blush remains 100 per cent outsourced of that very large and profitable business.

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QUESTION: Just quickly, I guess looking again at the increase in the Australian supply, I guess given once again that you are holding that business up as the example of growth based on the domestic and international growth, by indicating that you are only increasing by 8 per cent I would suggest you still have inventory here, you have significant inventories otherwise you are not expecting any future growth from that business.

Secondly, given the level of write downs you have done here, obviously that is done on previous margins and when you target a cashflow of 70 to 80 per cent of EBITDA, should we be looking at that 07, 08 target?

JAMIE ODELL: I will handle it first. The best way to work out who has got too much inventory is go to the shelves and see who has got the oldest vintages. You will find our vintages are about the youngest, particularly white wines. You get those wines out. In sparkling Yellow we have already got wine from vintage and Yellow is the number one sparkling SKU here in Australia.

We got to the point where it was about 12 weeks after we picked that we had that product on the shelves. That's a unique model. It is difficult *with* our vintage intake to understand our whole business because of the increased level of outsourcing and increased product like Eaglehawk and Saltram using outsourced fruit.

This is more a replication of some of the more premium fruit coming through and the contract growers. It is also a recognition of the market place. It is a buyer's market at the moment. We have the ability to go to the marketplace and to buy more as we need it. But we certainly don't want it in our tanks at this particular time and we have controlled the extent of amount we have in this vintage.

ANDREW LEYDEN: Just to re-emphasize Jamie's point, the growth of 8 per cent in vintage, our demand profile is greater, shows you how important the outsource model is. Regarding the question on cash flow, we are reaching 70 per cent of EBITDA in F06 so it is a little earlier than your question indicates.

TREVOR O'HOY: We have time for one more.

QUESTION: You have discussed this inventory. The other one is the barrel contract which is \$35 to \$40 million. Can you give an indication how that flows through to lower cost and time-frame? You mentioned of the cost reductions, \$35m, \$40m is oak barrels. Is that a case you have taken the hit now, that will help you in 05 and then on that will afford cost reductions?

ANDREW LEYDEN: The flexibility with the oak, we are reducing the amount of oak we use in our premium business, that is a permanent change in terms of the wine maker and the amount that we are taking in 04 represents the cost of actually doing that, making it one of change to the amount of oak that we have in our system. So that's what the \$35 to \$40 million represents. It's a one-off charge this year. We will make a permanent reduction.

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In terms of cost savings, clearly there is somewhere between a one and two year lag, depending on the wine that is being processed, we see a P&L benefit. That is a consequence of not having the same level of oak in our program but we will see P&L benefits starting to roll through about one and a half years after action. On average, that really depends on the mix of wines.

TREVOR O'HOY: Thanks Andrew. I think at that point we will close. Thank you all here today and on the line for your participation. The test is delivering on what we are promising. Thank you.

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