GALE PACIFIC LIMITED
(ASX: GAP)

ASX and Media Release

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2018 Annual General Meeting – Managing Director's Address

I would like to start by restating our goal to become a fabrics technology business.

A leader in the development, manufacture and marketing of shade solutions for the retail market, and high performing technical textiles for the commercial sector.

Everything we have been doing over the last four years has been geared towards achieving this goal.

We have operated to a clear strategy, and our entire team is focused on executing this plan.

We have now built a platform to support and sustain growth and have created a strong safety culture, with our performance comparing favourably versus external benchmarks.

After closing four warehouses, relocating and upgrading four others, our facilities are safer, more efficient, and more capable of supporting growth.

In December, we opened a new twelve thousand, five hundred square metre warehouse to support our USA growth plans, in California.

Our brand portfolio has been rationalised from thirteen to three, and we have completed an overhaul of all marketing materials, including logos, packaging, point-of-sale, web sites, and digital content.

We have completed four IT system implementations, with all regions now operating on a single ERP system. The most recent of these was completed at our China manufacturing operations in July this year.

We have exited non-core manufacturing processes, invested in increasing plant capacity, and have transformed all our manufacturing facilities.

We have strengthened the balance sheet and feel confident we have the capacity to continue to invest in our business, research and development, and explore new opportunities for the group.

We have built a positive, values-based culture, as evidenced by our strong employee engagement scores, above global benchmarks on fourteen out of seventeen metrics.

I'd like to take this opportunity to reiterate our strategy and share with you why we believe it is important to our future.

The starting point is to continue the simplification of the operations and focus on our core business.

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We want to do this because our core business, and the products we manufacture, are where we have genuine expertise. In our core products we are able to innovate, adding value to our customers, and creating competitive advantages for our business. Further, by focusing on our core competency we ensure our investments are more targeted and build the platform for a faster-growing, more defendable business.

We will continue to expand our business outside Australia with prioritisation of the USA.

The USA is a large undeveloped market for our product categories, presenting a significant opportunity. Sun protection awareness is building, and yet there is no one leader in the category, nor players doing the DIY shade category well. We have been successful in attracting a customer base made up of many of the world's largest retailers. These associations are driving our reputation in the market and underpin our future success.

We plan to grow our commercial business inside and outside of Australia.

In this area, our focus is on both knitted and waterproof products. The product solutions are unique, and world leading; however, we have been constrained by our capacity to meet the demand for our coated products. As I will share with you later we have invested in additional capacity and feel confident we will be able to meet future demand to support this opportunity. The commercial markets are large, and our progress is closely aligned with our investment in research and development, and our manufacturing capabilities.

We will continue to innovate our core product categories.

This is important, as product innovation will drive profitable sales growth. Without innovation product categories become commoditised. In the retail sector there is limited innovation among our competitors and, in the commercial sector, with customers facing the high cost of product failure, and increasing compliance requirements, there is a need for higher performing products.

We will explore acquisition opportunities aligned with our vision of becoming a fabrics technology business.

We will model any opportunities against robust criteria to ensure any acquisition is value-adding for shareholders.

Finally, we will continue to drive efficiencies at our manufacturing facilities.

As a manufacturer of most of the of the products we sell, having a globally competitive cost position is critical to our success. Our goal is to hunt costs, quality, and service; and build upon our technical capability and manufacturing agility.

In line with our strategy to focus, we have rationalised our product portfolio with close to 95% of our current range now considered core.

We have been exiting non-core products progressively, many of which were marginally profitable, and have reinvested these funds to build a platform for growth.

We are now seeing the benefits of a more focused business in terms of lower logistics costs, a reduced supplier network, improved quality, and more time being spent on our core business.

In addition to the product category exits, we have been exiting non-core manufacturing activities in Australia and China. In the last twelve months we have closed our China weaving, and powder coating operations, both of which were capital intensive and outside our core expertise.

These changes in Australia, and China, have enabled more effective plant layouts and, in the case of China, has supported the consolidation of two facilities into a single manufacturing footprint.

Our strategy in the USA is to sell more of our existing products to existing customers, secure additional store allocations beyond our existing product distribution, sell new products to our existing customers, and add new customers in channels and regions where we are underpenetrated.

We also aim to build awareness of our Coolaroo branded products, highlighting their benefits, and their availability.

Importantly we have been investing in infrastructure that can support and sustain growth in this large market, and will continue to invest ahead of the growth, in sales and marketing, and operations, to ensure we can service the market effectively.

In December, we went live with our new California warehouse, our largest distribution centre across all regions. In addition to the seamless go-live, the new warehouse has already proven to be capable of managing the high seasonal volumes in tight delivery windows.

In the Americas region we continue to drive above-market, customer and category growth. We are becoming a partner of choice for growth for the largest retailers in America. We are partnering to expand the mix in our core window furnishing business across both Home Depot & Lowes. We are gaining more items, in more stores, and driving higher product sell-through rates than ever before. We are gaining additional promotional placements off-shelf, in adjacent aisles, during the key spring and summer periods.

We continue to invest in eCommerce, and grow in our core categories with both the largest pure play site in Amazon, as well as with our brick & mortar customers with eCommerce properties.

In the US spring & summer of 2018 our sell-through rates were higher than customer comp store performance and near neighbour category, and competitor rates - both in unit & dollar terms. We are driving category expansion & driving consumer usage. The best news is that those rates are increasing as we enter the back half of calendar 2018.

We are creating new demand at a higher rate than ever before - and we are getting rewarded for the business performance at our largest partners. We are in the middle of rolling out a national exterior window shade program at Lowes. By the end of December, we will have a significant full time on-shelf presence in a majority of the store network at one of our largest customers.

These ranges will be stocked year-round and represents a considerable increase in the number of items, stores and overall points of distribution for our window shade business in the home centre channel in the Americas. We expect this new ranging will enable further increases in sell-through in spring and summer 2019.

We are positioned well to grow and are preparing for a record spring and summer.

We continue to build the marketing infrastructure to support growth, investing in product engineering, product management, and marketing communications.

We have invested in a dedicated eCommerce channel account management resource as we see this as a high growth channel requiring unique skills.

The new ranging wins are significant, but we won't necessarily see the full returns on these wins in the first year due to investments in in-store racking and inventory clearance.

To date our commercial product focus, outside Australia, has been on non-coated, knitted fabrics.

As mentioned earlier, our manufacturing capacity has constrained our ability to market coated or waterproof products outside of Australia.

Knowing this, we have focused our efforts on servicing existing customers in existing markets.

With new production capacity coming on stream in March, we are well progressed in the implementation of plans to launch our coated fabrics in northern hemisphere markets.

Last week, our USA team launched new knitted, and coated fabrics, at the key industrial fabrics show in Texas, and the Middle East North Africa team will be launching at the largest construction show in the region, in Dubai, in November.

Our strategy is to focus on our most unique products where we believe we will have the greatest advantages when compared to incumbent products.

Our new $8 million extrusion line will arrive into Melbourne in December and is planned to commence production in March 2019. Importantly, we are on track.

As I said earlier, innovation in our product categories is key to driving profitable growth.

Whilst our origins are in High Density Polyethylene and Polypropylene-based products, we will not be constrained by that in the development of future products.

Our strategy is to explore new materials and technologies that provide improved performance and create new applications for our fabrics, and fabric-related products.

We have established strong technical alliances with groups that have technologies we can adapt to our own applications and markets.

These technical partners are also assisting us to take our ideas and bring them to life.

Some of these developments take time, particularly in the proofing of the concepts, however, we are well progressed.

It is pleasing to be able to report that some of these product launches are imminent.

In the USA, this year, we launched solar motorised blinds and will also launch this program in Australia this summer. This is a good example of taking a technology and applying it to our products. In this category we are competing with the custom-made market, with a ready-made DIY item at a considerably lower price point, providing exceptional value for consumers.

In addition, our commercial fabric developments include knitted fabrics that are either flame retardant, or non-combustible, as we believe the market will trend quickly towards fabrics with improved flame retarding properties.

Our new coating line also has complimentary capabilities to our existing coating line, enabling broader product development potential.

Finally, we have increased our investment in research and development, and product engineering, by 250% over the last four years, and have been successful in being granted more patents in the last three years than at any time in the last fifteen.

Our wholly-owned manufacturing facilities in China have undergone perhaps our greatest transformation.

We have invested substantially in bringing the plant to a new, much higher, standard and have seen improvements in service, waste reduction, safety and, importantly, culture.

Our strategy is to hunt cost outs aggressively, supported by our new IT system. We will continue to drive improved labour productivity and are implementing low cost automation in labour-intensive areas to support this.

We have numerous other initiatives in place to support our efficiency drive, including product range rationalisation, and more global product alignment.

In September, our non-core manufacturing exits enabled us to relocate our cutting, sewing and packing functions into our main facility, and we're pleased with the improvements, and optimistic about the efficiencies this will deliver over time.

We're proud of what we've achieved so far, but more excited about our future.

Our plan is simple, and clearly defined. We have a strong team, and we now have the requisite infrastructure in place to support our growth aspirations.

Now, in terms of outlook.

In the Americas, we will see the completion of the rollout of the expanded Lowes window shade program until December, and will commence the rollout of another new, additional window shade program at Home Depot in the second half of the year.

We are investing to grow, and the opportunity is big.

We are being presented with opportunities for broader ranges now and, whilst pursuing these, we are working hard to execute our current and new programs effectively.

In Australia and New Zealand, we are well prepared for the summer selling season that is commencing now. We have just launched the new solar motorised window shade program which will be ranged in more than 110 stores.

As foreshadowed, in the commercial sector, drought conditions have continued to impact the grain harvest, particularly on the eastern seaboard, and we are expecting another difficult year. Somewhat offsetting this is an uplift in water retention fabrics and architectural shade fabrics. We are confident of growth in the underlying commercial business.

Turning to the Middle East, we see this market as attractive, despite current challenges and economic uncertainty. We remain committed to it and are confident of our ability to achieve growth, particularly given our new products, and our expansion into coated fabrics.

In Eurasia, we continue to pivot the business away from low value, low margin products, to branded core retail and commercial products. Whilst small, we believe this market to have growth potential, and we have a great team.

Like most suppliers of China-made products to the USA, we have been keeping a close eye on tariffs. Some of our products will incur higher duties than currently and we are working through this issue to recover the duty impact. We currently pay duties on some of our products but are unable to be definitive on the impact of these changes, offset by the cost recovery strategies we would employ.

We have continued to see a stabilisation of resin prices over the last few months and the currency headwinds we confronted last year have now abated.

In terms of revenue, we are off to a strong start in FY2019.

Sales in the USA have been particularly pleasing and the strong sales out results give us a level of confidence in the future of this region.

As per previous years, second half performance is expected to be significantly greater than in the first half due to seasonality.

Regarding earnings, it is too early to provide detailed guidance. We have started the year well but there are still many uncertainties and a long way to go.

I would like to conclude by again thanking our customers for their support, and our suppliers and other partners for the role they play in helping us achieve our goals.

Our employees around the world have made a huge contribution throughout the year. I would like to thank them, sincerely, for their efforts.

And, finally, I would like to thank our shareholders for your continued support of GALE Pacific.

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