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# PERFORMANCE SUMMARY

FY18 has been a challenging year for RFG, however the Company is beginning to realise opportunities to better capitalise on the breadth of its operations to support a more sustainable business model for the Group and its franchisees.

FY18 REVENUE

**\$374.0m**

FY18 EBITDA (Underlying)

**\$71.4m**

FY18 EBITDA (Statutory)

**(\$354.3m)**

FY18 NPAT (Underlying)

**\$33.3m**

FY18 STATUTORY LOSS AFTER TAX

**(\$306.7m)**

FY18 EPS (Underlying)

**18.4cps**

FY18 EPS (Statutory)

**(169.5cps)**

# CHAIRMAN'S LETTER

During the year ended 30 June 2018 (FY18), RFG faced a number of challenges which contributed to the Company's disappointing performance for the year.

In FY18, a statutory loss after tax of \$306.7m was reported (FY17: Statutory net profit after tax of \$61.9m), reflecting non-cash impairments and write-downs, and provisioning, of \$402.9m recognised in FY18. On an underlying basis, FY18 net profit after tax was \$33.3m, a 56.1% reduction on the prior corresponding period (FY17: \$75.7m).

Whereas actions have been taken to stabilise RFG's operations, and significant progress has been made in implementing a turnaround strategy for the Group, both internal and external factors contributed to the Company's FY18 results.

In June 2017, RFG commissioned a business-wide review to identify improvement opportunities and strengthen the Company's operating model. Key areas of focus included the Group's cost base, including effecting supply chain consolidation and synergy extraction, and a strategic review of the Company's domestic franchise operations and their underlying health in a more difficult retail environment.

Management has implemented an extensive re-engagement program with the Group's franchisee community to better understand and more effectively respond to the challenges facing their businesses.

As the financial year progressed, it became evident that trading results were not meeting management's budget. The Group's performance was being impacted by challenging retail trading conditions, particularly within shopping centres, negative market sentiment towards franchising and RFG in particular arising from negative publicity, the cumulative impact of domestic store closures, and internal challenges in managing what had become an increasingly complex business model following the Gloria Jean's and Hudson Pacific acquisitions.

In response to these factors, the Directors identified a need for RFG to develop a clear turnaround process, to stabilise the business and improve its profitability and return on capital for RFG and its franchisees.

A key to this process was focusing RFG's core strategic direction on the Group's coffee business and retail food franchise systems, which, if supported appropriately, remain capable of generating acceptable future returns for both RFG and its shareholders.

During FY18, the Board also initiated a management transition with the departure of former Managing Director, Andre Nell, and the appointment of Richard Hinson as Group Chief Executive Officer to lead RFG's new management team.

Recommendations from this business-wide review are being implemented to better integrate and streamline RFG's operations, and right-size the operational base of RFG's businesses to support a more sustainable model for RFG and its franchisees. Management has implemented an extensive re-engagement program with the Group's franchisee community to better understand and more effectively respond to the challenges facing their businesses.

Decisive actions have been taken to stabilise RFG's operations, and significant progress has been made in implementing a turnaround strategy for the Group.

In terms of the Company's financial position, the Group reported net debt of \$258.9 million as at 30 June 2018. Subsequent to this date, the Company further negotiated the financial covenants attaching to the Group's debt facilities, with covenants reset effective from 31 August 2018 for covenant periods commencing 1 July 2018. An aspect of this reset was that the term of RFG's senior debt facilities was brought forward to 31 October 2019, and were classified as current in the Company's FY18 financial statements.

The program to restructure the Company's business and build confidence in the franchise brands is progressing, however, the risk that the Group may breach financial covenant thresholds within the next 12 months remains, which could result in the Company's syndicated debt becoming due and payable.

RFG's continuing viability is, therefore, dependent upon the continuing support of its syndicated lenders, and managing the terms of its renegotiated debt facilities.

Having regard to these matters, a key focus for RFG is the reduction of debt and strengthening the Company's balance sheet. The Company is considering a range of options, including potential asset sales and securing potential alternative funding such as a market recapitalisation.

Work on these options began some time ago and is continuing, but, at this date, the Board does not have a definitive position on which option is in the best interests of RFG's shareholders.

Former Chairman, Colin Archer, announced his retirement from the Board, with immediate effect, on 25 September 2018.

Colin Archer was appointed a Director of the Company just prior to RFG's admission to the Official List of the ASX in 2006. On behalf of the Board, I would like to thank him for the significant contribution that he has made to RFG during the past 12 years.

It is also appropriate that I welcome two new non-executive Directors, David Grant and Peter George, each of whom has extensive skills and experience that are relevant to RFG's current challenges. Their appointments demonstrate confidence in RFG's underlying business model and the strategies being implemented to turnaround the Group's performance.

Retail markets are expected to continue to be challenging, and, in the immediate term, trading results are likely to remain subdued until the full impact of turnaround initiatives deliver effective performance outcomes. Your Board fully appreciates the shareholder value restoration challenge the Group continues to face, has a clear strategy and range of options it is exploring with its advisors, and is confident in the steps management is taking under Richard Hinson's new leadership to restore the underlying value in RFG's retail franchise business.

In closing, on behalf of the Board, I would also like to thank the Company's staff, franchisee community, customers and shareholders for their understanding during what has been a difficult year for the Company.

Yours sincerely,



Stephen Lonie  
Chairman of the Board

# CEO'S REPORT

RFG's success depends on the success of its franchisees, so providing an enhanced outcome for them has been my first priority since accepting the role of Group Chief Executive Officer in late May 2018.

Clearly, FY18 has been a challenging year for RFG, however, the Company is beginning to realise opportunities to better capitalise on the breadth of its operations to support a more sustainable business model for the Group and its franchisees.

RFG's business is underpinned by strong, highly recognised Brand Systems, which have delivered sound results over a number of years, complemented by wholesale coffee, manufacturing and distribution businesses which offer additional scale, revenue diversification and vertical integration opportunities. However, the business' rapid expansion, through a series of acquisitions in recent years, introduced a level of complexity that affected organisational effectiveness at a time when our franchisee customers were dealing with challenging trading conditions, particularly within shopping centres.

A business-wide review was commissioned in late 2017 to explore these matters, resulting in recommendations, and ultimately, establishing a process to turnaround the Group's performance.

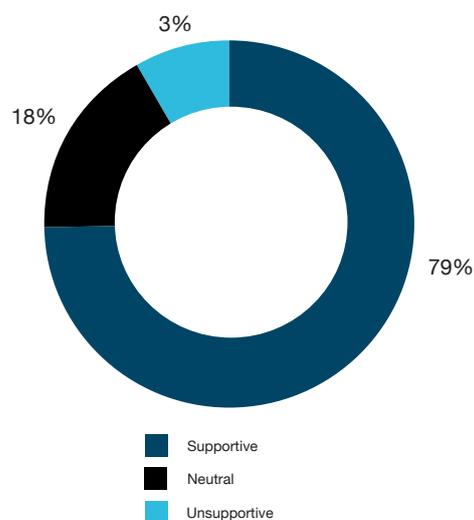
This turnaround will be a concerted journey to simplify RFG's business model, by reducing duplication and inefficiency, and improving the way in which RFG provides support to enhance the performance of its franchisees.

RFG's leadership team is committed to ensuring that the Company delivers on its obligations and commitments as a world class franchisor, whilst continuously focusing the Group's efforts to ensure that it provides the ingredients and innovation to surprise and delight our franchisees and customers.

Recently, I met with approximately 700 of RFG's franchisees during a National Roadshow to listen to their feedback and better understand the challenges facing their businesses. This roadshow was an important step in re-engaging with RFG's franchise community and explaining some of the steps that the Group is taking to support them and enhance the profitability of their businesses, including:

- » Delivery of over \$4.5m in annualised cost of goods savings;
- » Discounted new store and franchise renewal fees;
- » A \$1.5m annualised investment in additional field support; and
- » A \$1.2m annualised investment in enhancing wage entitlement audit and compliance activities.

The overwhelming response to the National Roadshow was positive, with 79% of franchisees responding to a subsequent survey supportive of RFG's future direction, a further 18% neutral, and only 3% unsupportive. While a great deal of work remains to be done, and delivery on RFG's commitments is critical, these results demonstrate that RFG is on the right track in re-building trust and confidence amongst its franchise network.



Post roadshow online survey: 193 franchisee responses

RFG's success depends on the success of its franchisees, so providing an enhanced outcome for them has been my first priority.

RFG has also committed to partnering with its franchisees to identify potential revenue growth and profit generating opportunities that can be implemented across the network. These initiatives include piloting concept stores at Michel's Patisserie, Brumby's Bakery, Donut King and Gloria Jeans, and a digital promotions and loyalty program.

An increased capability and focus to better understand RFG's Brand Systems' shoppers, and changing global trends, will also ensure that the Company not only remains relevant, but becomes a destination of choice in each of the segments in which RFG operates.

### **FY18 Domestic Franchise Performance**

Underlying EBITDA from RFG's domestic franchising operations reduced to \$43.1m in FY18 (FY17: \$78.1m) due to a combination of factors including the cumulative trading revenue impact of store closures over the past two financial years, a decline in revenues from new franchise and renewal activity, and increased costs of franchisee support.

Comprehensive analysis of the domestic network was undertaken as part of the business-wide review, identifying a number of outlets that were not considered sustainable, predominantly as a result of above market rent expectations and declining shopping centre performance. RFG has forecast that up to 250 domestic outlets will either close, or their leases will not be renewed, by the end of FY19. This total includes 123 domestic outlets which closed in the second half of FY18.

### **FY18 International Franchise Performance**

In FY18, RFG's international franchise network grew by a net ten outlets to 880 stores, after 93 new outlets were commissioned during the period. A number of new Master Franchise Agreements were also granted, including for the key territories of the United Kingdom (Donut King & Crust Gourmet Pizza) and Germany (Gloria Jean's), bolstering growth prospects in Western Europe.

At 30 June 2018, the Group enjoyed an international footprint incorporating 87 licensed territories across 11 Brand Systems, and, whilst many of these territories are at an early stage in their development lifecycle, they are expected to generate growing recurrent revenue streams as they mature.

Underlying EBITDA from international franchising operations decreased to \$10.2m in FY18 (FY17:\$19.4m), influenced by prevailing negative sentiment which impacted new Master Franchise sales, together with a reduction in EBITDA margin reflecting additional investment in divisional capability and resourcing, and increased international coffee distribution costs.

### **FY18 Di Bella Coffee Performance**

During FY18, RFG completed the consolidation of its four coffee operations into a single, integrated business under the established Di Bella Coffee brand, positioning RFG's coffee operations as Australia's second largest roast and ground coffee enterprise. Despite this initiative, underlying EBITDA for FY18 of \$8.1m (FY17:\$14.2m) was disappointing, influenced by a combination of margin contraction in contract roasting, exit from low-margin grocery contracts, reduced volumes amongst existing customers and losses incurred on sale of assets, as well as c.\$3.5m in non-recurring gains reported in FY17.

Looking forward, Di Bella Coffee will look to leverage its scale, and its established brand and craft coffee pedigree to expand into a range of new market channels, with a focus on strengthening critical commercial and operational capabilities to support business opportunities. The business is also implementing a range of financial, supply chain and procurement initiatives to improve gross margins and cash flow generation.

### **FY18 Manufacturing and Distribution Performance**

Significant investments in new production capacity were completed in FY18, to cater for growing throughput volumes, including commencement of operations at a second Dairy Country facility. Further investment in enhanced sales and management capability, together with product innovation and new customer acquisition, also contributed to enhanced throughput amongst the Dairy Country (+29.7%) and Bakery Fresh (+53.3%) businesses.

The integration of Associated Foodservice Distributors into RFG's existing Hudson Pacific facilities was also completed late in the financial year, consolidating the entirety of the Group's distribution operations at the one site.

# CEO'S REPORT

(CONTINUED)

Underlying FY18 EBITDA for the division was \$10.0m (FY17: \$11.8m), primarily as a result of carrying the costs of additional sites to allow for the integration of Associated Food Services, investment in new capability to drive sales volumes, additional overhead associated with Dairy Country's expansion, and margin reduction on increased wholesale manufacturing sales.

## FY19 Group Priorities

RFG has established a clear roadmap, more particularly detailed in the following diagram, to turnaround performance of the business over three stages.

## OUR STRATEGY

### STABILISE >

#### STABILISE THE BUSINESS AND RETURN TO A PROFITABLE PLATFORM

- » Articulate 3-year business strategies
- » Realign organisation structure
- » Renew and embed franchise and field support model
- » Embed brand revitalisation programs
- » Identify and capture supply chain efficiencies
- » Simplify operational model
- » Embed financial improvements

### OPTIMISE >

#### OPTIMISE OPERATIONS AND ENHANCE PROFITABILITY AND RETURNS FOR RFG AND FRANCHISEES

- » Develop and implement additional revenue growth plans
- » Embed 'Gold Standard' customer training
- » Revise supplier and distribution network
- » Enhance analytical and digital capability
- » Finalise network rationalisation
- » Achieve operational cost efficiencies
- » Launch simplified product portfolio

### RE-INVEST >

#### RE-INVEST TO PRUDENTLY GROW

- » Embed revenue growth plans
- » Enhance sales and marketing operations
- » Enhance integrated planning and analytics
- » Revise employee training and development
- » Initiate corporate owned and operated 'flagship stores'
- » Build on financial and operational improvement

The overwhelming response to the National Roadshow was positive, with 79% of franchisees responding to a subsequent survey supportive of RFG's future direction.

During FY19, we expect that the Company's Brand Systems will stabilise, and are working on a number of initiatives to transform the Group's franchise business, including:

- » Rolling out additional revenue drivers for the Group and each Brand System, a relevant example being recent commencement of the rollout of Gloria Jean's "Good Cup" initiative, which introduces new products, techniques and equipment to revolutionize the brand's coffee offer and shopper experience, whilst driving additional earnings for franchisees;
- » A reinvigorated franchise and field support model which builds on the in-field support capability recently added to the network;
- » A revised distribution model which consolidates 16 current providers to better leverage the Group's buying power;
- » A simplified product portfolio that enhances the quality and value of products provided to franchisee customers; and
- » Enhanced digital and analytical capability, so that RFG has a more detailed understanding of the tastes and consumption patterns of consumers who shop with its franchisees.

Many of the initiatives to integrate and stabilise the Di Bella Coffee business have already been completed, resulting in a consolidated business with an integrated leadership team that has addressed operating inefficiencies and downward trends in performance, and started to roll-out a new brand strategy.

Di Bella Coffee has a market leading brand and pedigree in craft coffee roasting, and the scale to compete and grow the business by taking its crop-to-cup philosophy to a global consumer market. Over the course of this financial year, the business will capitalise on its existing strong foundations by:

- » Putting in place enhanced FMCG sales and marketing capabilities;
- » Improving financial control across the consolidated business;
- » Implementing efficiencies in terms of procurement, production and supply chain;
- » Launching new product portfolios to enter new mass channels; and by
- » Rolling out the Di Bella Coffee brand, product and service portfolio with flagship stores in the USA and New Zealand.

The Company also remains focused on leveraging enhanced capability and capacity within its Manufacturing & Distribution Division to drive additional throughput and enhanced sales volumes, whilst also capturing further efficiencies and investing in new product development that offers additional routes to market.

In closing, I would like to offer my personal thanks to all of the people who have a stake in RFG's continued success – our teams, our valued franchisees and customers, our supplier partners and our shareholders – for their support during a difficult year.

I am encouraged by the initial progress we have made in restoring the performance of the business and building on the strong foundations that are in place, and I look forward to updating you on our progress.



Richard Hinson  
Group Chief Executive Officer

# FY19 OPERATIONAL PRIORITIES



## **Brumby's Bakery**

Brumby's is bringing back the 'heart and soul' of the local bakery. In July 2018, we introduced shoppers to an upgraded store concept which elevates the theatre of daily baking. Through new initiatives such as in-store daytime baking and enhanced customer education, we are connecting with consumers through nostalgia, reminding them of what Brumby's is all about.

We have also enhanced our in-store coffee presence, highlighting to our shoppers this key point of difference to other bakeries. This new and improved merchandising approach is improving the store experience and creating opportunities for our franchisees to re-engage with both loyal and new customers.

## *Michel's*

### **Michel's Patisserie**

Michel's Patisserie is lifting merchandising standards and reinvigorating a menu to surprise and delight our shoppers. Our customers are already benefiting from a unique and refreshed French café experience, along with improved customer service initiatives. The enhanced instore atmosphere, coupled with the roll out of a new, authentic French inspired menu, is proving to be a key competitive advantage. Our concept store pilot was launched in May 2018, showcasing the new menu and improved product presentation, and rollout amongst the wider network commenced during the first half of FY19.

Elevating our coffee credentials has also been a focus, providing customers with a complete café experience. To remain relevant and top of mind, we are seeking to attract younger shoppers through modern product offerings, innovative visual displays and highly targeted marketing campaigns.





## Donut King

Donut King is focused on reigniting the magic of the brand for kids and adults of all ages. We have introduced exciting new products and placed a strong focus on local area marketing initiatives. Increased promotional support for our franchisees has attracted both new and old customers back to the brand.

A concept store pilot was launched in June 2018, showcasing new merchandise displays to grab the attention of shoppers and re-ignite the magic of Donut King. Following a positive reception in the market place, the concept store learnings are currently being implemented in five additional Donut King outlets, to identify opportunities for improved franchise performance across the entire network.



# FY19 OPERATIONAL PRIORITIES

(CONTINUED)

**CRUST**  
LOCAL PIZZA SINCE 2001



## Crust Gourmet Pizza & Pizza Capers Gourmet Kitchen

RFG's Quick Service Restaurant Division, Crust Gourmet Pizza and Pizza Capers Gourmet Kitchen, continue to work closely with our franchisees to develop new restaurant inspired menus for our customers. We placed increased emphasis on customer relationship management so that we may in turn support our franchisees toward better financial outcomes for their stores.

Pizza Capers saw an enhanced focus on local area marketing activity to attract new shoppers and strengthen each franchise territory. Through the continuous improvement of two-way communications with our franchisees, we are listening to the needs of our shoppers and responding faster than ever before.

In September 2018, Crust Gourmet Pizza began the rollout of an ultra-modern brand identity and store design, bringing something new to the QSR market and future proofing our brand for years to come. In designing the new look, we worked closely with our franchise customers to understand the needs and wants of modern day shoppers.



## Gloria Jean's

Gloria Jean's has begun the rollout of its "Good Cup" program, which is about assuring our customers the best possible cup of coffee, every single time. The program incorporates a new coffee menu and upgraded products, equipment, delivery standards, franchise customer support and skills development, and has been well received by franchisees and consumers alike.

The Good Cup program represents a fundamental change in product quality and customer experience for Gloria Jean's stores. It is a comprehensive system designed to change consumer perceptions, drive an internal culture of small business excellence and deliver increased revenue for franchise customers. Through the Good Cup program, we expect to take a leadership position in the space between chain coffee and independent specialty coffee, and in doing so, create a new segment in mass-market specialty coffee.



# Di Bella

GREATNESS IS IN THE DETAIL



## Di Bella

### Di Bella Coffee

Di Bella Coffee purchases more than 3,600+ tonnes of coffee annually and supplies more than 3,000 cafes, restaurants and customers within 37 countries.

In FY18 we focused on consolidating our position in the coffee industry with the consolidation of four coffee businesses under the Di Bella Coffee brand, positioning it as the second largest roast and ground coffee enterprise in Australia. This new model allows the company to scale up for new markets, opportunities and partnerships without losing its core focus on craft roasting.

In July 2018, Di Bella Coffee unveiled its new brand identity, inspired by its vision – ‘Greatness is in the Detail’. The brand refresh comes one month after Di Bella Coffee completed its consolidation. Di Bella Coffee is in the process of a phased rollout of the new brand identity and is targeting the end of the year for completion. The new brand identity was designed to embody the business’ past as a bespoke roaster, while embracing its future as a premium international coffee company providing discerning coffee drinkers around the world with premium Di Bella Coffee. The new identity supports Di Bella Coffee’s brand promise to strive for detail in everything it does, while becoming a global leader in the industry – “Greatness is in the Detail”.



# FINANCIAL STATEMENTS



# SUMMARY FINANCIAL INFORMATION

Item	REPORTED			UNDERLYING OPERATIONS <sup>(1)</sup>	
	FY16 (Restated)	FY17	FY18	FY17	FY18
<b>Financial</b>					
Revenue	\$275.1m	\$349.3m	\$374.0m		
EBITDA*	\$92.7m <sup>(2)</sup>	\$106.5m	(\$354.3m)	\$123.5m	\$71.4m
EBIT*	\$86.2m <sup>(2)</sup>	\$97.2m	(\$367.4m)	\$115.5m	\$59.9m
NPAT	\$53.0m <sup>(2)</sup>	\$61.9m	(\$306.7m)	\$75.7m	\$33.3m
Basic EPS	32.3 cps <sup>(2)</sup>	35.7 cps	(169.5 cps)	43.7 cps	18.4 cps
Dividend	27.50 cps	29.75 cps	-		
<b>Operating Performance</b>					
Revenue Growth	30.9%	27.0%	7.1%		
EBITDA Growth*		14.8%	(432.6%)	12.1%	(42.2%)
EBIT Growth*		12.8%	(478.0%)	10.9%	(48.2%)
NPAT Growth		16.9%	(595.2%)	14.0%	(56.1%)
Basic EPS Growth		10.6%	(574.8%)	7.9%	(57.9%)

\* EBITDA, EBIT, Underlying EBITDA, Underlying EBIT & Underlying NPAT are non-IFRS profit measures used by Directors and Management to assess the underlying performance of the Group.

(1) EBITDA and EBIT results from 'Underlying Operations' exclude the pre-tax impact of the following amounts recognised in the Consolidated Statement of Profit or Loss and Other Comprehensive Income:

EBIT - REPORTED

Business turnaround and restructuring costs  
(including acquisition and integration costs)

Impairment and provisions

EBIT - UNDERLYING OPERATIONS

NPAT results from 'Underlying Operations'

NPAT - REPORTED

Post-tax impact of non-underlying EBIT adjustments

NPAT - UNDERLYING OPERATIONS

	FY17	FY18
EBIT - REPORTED	\$97.2m	(\$367.4m)
Business turnaround and restructuring costs (including acquisition and integration costs)	\$13.1m	\$24.4m
Impairment and provisions	\$5.2m	\$402.9m <sup>(3)</sup>
EBIT - UNDERLYING OPERATIONS	\$115.5m	\$59.9m
NPAT - REPORTED	\$61.9m	(\$306.7m)
Post-tax impact of non-underlying EBIT adjustments	\$13.8m	\$339.9m
NPAT - UNDERLYING OPERATIONS	\$75.7m	\$33.3m

(2) FY16 Operating Performance growth measures are based on FY15 Restated Reported results.

(3) Refer to Note 6.

# CORPORATE DIRECTORY

<b>Directors</b>	<p>Mr Colin Archer Chairman and Independent Non-Executive Director</p> <p>Ms Jessica Buchanan Independent Non-Executive Director</p> <p>Mr Stephen Lonie Independent Non-Executive Director</p> <p>Ms Kerry Ryan Independent Non-Executive Director</p> <p>Mr Russell Shields Independent Non-Executive Director</p> <p>Mr Anthony (Tony) Alford Non-Independent Non-Executive Director - Resigned 3 July 2017</p> <p>Mr Andre Nell Executive Managing Director - Resigned 29 May 2018</p>
<b>Company Secretary</b>	Mr Anthony Mark Connors LLB
<b>Registered office &amp; Principal place of business</b>	RFG House 1 Olympic Circuit Southport QLD 4215
<b>Share register</b>	Computershare Investor Services Level 1 200 Mary Street Brisbane QLD 4000
<b>Solicitors</b>	McCullough Robertson Lawyers Level 11, 66 Eagle Street Brisbane QLD 4000
<b>Auditors</b>	PricewaterhouseCoopers 480 Queen St Brisbane QLD 4000
<b>Bankers</b>	National Australia Bank Limited Level 20, 100 Creek Street Brisbane QLD 4000
	Westpac Banking Corporation Level 7, 260 Queen Street Brisbane QLD 4000
<b>Stock exchange listings</b>	Retail Food Group Limited (ASX: RFG) shares are listed on the Australian Securities Exchange
<b>Website Address</b>	<a href="http://www.rfg.com.au">www.rfg.com.au</a>

# DIRECTORS' REPORT

## Overview

The Directors of Retail Food Group Limited (referred to hereafter as the Company) submit herewith the Annual Report of the Company for the financial year ended 30 June 2018 in accordance with the provisions of the *Corporations Act 2001*.

## Information about the Directors

Name	Particulars
Mr Colin Archer	Independent Non-Executive Director and Chairman, Bachelor of Economics, Dip. Financial Planning, Chartered Accountant. Mr Archer joined the Board on 12 April 2006 and was appointed Chairman of the Board on 30 April 2013. Mr Archer is a member of the Company's Audit and Risk Management Committee and Chairman of the Nominations and Remuneration Committees. Mr Archer was re-elected to the Board at the Company's AGM held on 30 November 2017, following retirement by rotations.
Ms Jessica Buchanan	Independent Non-Executive Director. Ms Buchanan joined the Board on 29 May 2012. Ms Buchanan has circa 20 years' experience in branding, marketing and advertising, having commenced her career in the advertising industry working with multi-national agencies such as Wunderman, Young & Rubicam Mattingly and EHS Brann (UK). Ms Buchanan also managed campaigns for various blue chip companies including Ericsson, Tabcorp, Du Pont, Cadbury Schweppes, The Australian Defence Force, British Gas and BMW. Ms Buchanan then went on to become Brand Director at Boost Juice, helping that business grow from 20 to 120 outlets. Subsequently, Ms Buchanan established and then sold a brand agency and digital research business that worked predominantly with retail and franchised groups, including Woolworths, Cotton On Group, Katies, Millers, Healthy Habits, Wasabi Warriors, Mr Rental, Oriental Teahouse, Hairhouse Warehouse and others. Ms Buchanan currently sits on the advisory boards of Narellan Pools (a franchised business) and YomConnect (a Digital Agency), and is a former non-executive director of bakery franchisor Banjo's Bakehouse. Ms Buchanan is a member of the Company's Nominations and Remuneration Committees, and was last re-elected to the Board at the Company's AGM held on 26 November 2015, following retirement by rotations.
Mr Stephen Lonie	Independent Non-Executive Director, Bachelor of Commerce, MBA, FCA, FFin, FAICD, FIMCA. Mr Lonie joined the Board on 24 June 2013. Mr Lonie is a Chartered Accountant by profession and Director of listed corporations, MyState Limited, Corporate Travel Management Limited and Apollo Tourism & Leisure Limited. Mr Lonie is the Chairman of the Company's Audit and Risk Management Committee and a member of the Nominations and Remuneration Committees. Mr Lonie was last re-elected to the Board at the Company's AGM held on 30 November 2016, following retirement by rotations.
Ms Kerry Ryan	Independent Non-Executive Director, Bachelor of Laws and Bachelor of Arts (major in international relations). Ms Ryan joined the Board on 27 August 2015. Ms Ryan's professional background is in commercial law, and she has extensive experience across international markets in the retail and franchise areas. She is a Director of the Richmond Football Club and its health and fitness business Aligned Leisure, and she is a member of the Advisory Board of Lexvoco, a legal services and consultancy business. Ms Ryan is a Fellow of the Australian Institute of Company Directors and a Fellow of the Governance Institute of Australia. She is a member of the Law Institute of Victoria.
Mr Russell Shields	Independent Non-Executive Director, Fellow of The Australian Institute of Company Directors, Director of Eclix and Aquis Entertainment. Mr Shields joined the Board on 18 December 2015. Mr Shields is an experienced banker with extensive knowledge of retail, corporate, institutional and investment banking both in Australia and Asia. Mr Shields has in excess of 35 years' experience in the finance, economics and property industries. Mr Shields is a member of the Company's Audit & Risk Management Committee.
Mr Anthony (Tony) Alford	Non-Independent Non-Executive Director, Bachelor of Business (Accountancy), CPA and CTA. Mr Alford joined the Board on 28 October 2003. Mr Alford was a Chartered Accountant and has in excess of 20 years' experience in public practice. Mr Alford commenced his involvement with Retail Food Group Limited in 1994 in an advisory role, thereafter becoming the Group Financial Controller. Mr Alford was appointed Executive Managing Director of the Group in December 1999, a position held until his transition to Non-Independent Non-Executive Director on 1 July 2016. Mr Alford resigned from the Board on 3 July 2017.
Mr Andre Nell	Executive Managing Director. Mr Nell joined the Board on 1 July 2016. Mr Nell commenced his involvement with Retail Food Group Limited in 2007 following the Group's acquisition of Michel's Patisserie, and subsequently held a variety of key roles within the Company, including Head of Commercial, Chief Operating Officer and Chief Executive Officer – Franchise prior to his appointment to Managing Director on 1 July 2016. Mr Nell is a Chartered Accountant and has a wealth of experience in the successful operation and expansion of franchise networks internationally. Mr Nell resigned from the Board on 29 May 2018.

# DIRECTORS' REPORT

## (CONTINUED)

### Directorships of other listed companies

Directorships of other listed companies held by Directors in the 3 years immediately before the end of the financial year are as follows:

Name	Company	Period of Directorship
Mr Stephen Lonie	Corporate Travel Management Limited	23 June 2010 to present
	MyState Limited	12 December 2011 to present
	Apollo Tourism & Leisure Limited	20 September 2016 to present
Mr Russell Shields	Eclixp Group Limited	24 March 2015 to present
	Aquis Entertainment Limited	7 August 2015 to present

### Directors' shareholdings

The following table sets out each Director's relevant interest in shares and options in shares of the Company as at the date of this report:

Directors	Fully paid ordinary shares Number
Mr Colin Archer	391,084
Ms Jessica Buchanan	11,628
Mr Stephen Lonie	54,195
Ms Kerry Ryan	10,000
Mr Russell Shields	7,752

### Remuneration of Directors and Key Management Personnel

Information about the remuneration of Directors and Key Management Personnel is set out in the Remuneration Report of this Directors' Report.

#### Share options granted to Directors and senior executive management

During and since the end of the financial year, there were no share options granted to the Directors and senior executive management of the Company as part of their remuneration.

#### Performance rights granted to Directors and senior executive management

Performance Rights were granted to senior executive management on 14 July 2016 under the Company's former Performance Rights Plan with respect to the FY16, FY17, FY18 and FY19 performance periods.

### Directors' meetings

The following table sets out the number of Directors' meetings, including meetings of standing Committees of Directors, held during the financial year and the number of meetings attended by each Director, while they were a Director or Committee member. During the financial year, 26 Board meetings, 12 Audit and Risk Management Committee meetings, 4 Remuneration Committee meetings and 5 Nominations Committee meetings were held.

Directors	Board of Directors		Audit Committee		Remuneration Committee		Nominations Committee	
	Held	Attended	Held	Attended	Held	Attended	Held	Attended
Mr Colin Archer	26	25	12	11	4	4	5	5
Ms Jessica Buchanan	26	26	-	-	4	4	5	5
Mr Stephen Lonie	26	19	12	11	4	3	5	4
Ms Kerry Ryan	26	26	12	12	-	-	-	-
Mr Russell Shields	26	23	12	11	-	-	-	-
<b>Former</b>								
Mr Andre Nell	25	24	-	-	-	-	-	-
Mr Anthony Alford	-	-	-	-	-	-	-	-

# DIRECTORS' REPORT

## (CONTINUED)

### Company Secretary

The Company Secretary is Mr Anthony Mark Connors. Mr Connors was appointed as Company Secretary on 26 April 2006, having prior to that time and until 2 June 2015 acted as the Company's Legal Counsel. Mr Connors also held the role of Chief Operating Officer, from 2 June 2015 to 9 March 2016 until he was appointed to the role of Director of Corporate Services on 10 March 2016.

### Corporate governance

The Company is committed to achieving and demonstrating the highest standards of corporate governance. The Company has reviewed its corporate governance practices against the Corporate Governance Principles and Recommendations (3rd edition) published by the ASX Corporate Governance Council. The 2018 Corporate Governance Statement is dated as at 30 June 2018 and reflects the corporate governance practices in place throughout the 2018 financial year. The 2018 Corporate Governance Statement was approved by the Board on 31 August 2018. A description of the Group's current Corporate Governance Practices is set out in the Group's Corporate Governance Statement which can be viewed at [www.rfg.com.au](http://www.rfg.com.au).

### Principal activities

The Group's principal activities during the course of the financial year were:

- Intellectual property ownership of the Donut King, bb's café, Brumby's Bakery, Michel's Patisserie, Esquires Coffee Houses (Australia & New Zealand), Pizza Capers Gourmet Kitchen, Crust Gourmet Pizza Bar, The Coffee Guy, Café2U, Gloria Jean's Coffees, It's A Grind and Di Bella Coffee Brand Systems;
- Development and management of the Donut King, bb's café, Brumby's Bakery, Michel's Patisserie, Esquires Coffee Houses (Australia & New Zealand), Pizza Capers Gourmet Kitchen, Crust Gourmet Pizza Bar, The Coffee Guy, Café2U, Gloria Jean's Coffees, It's A Grind and Di Bella Coffee Brand Systems throughout the world, whether directly managed and/or as licensor for all Brand Systems;
- Development and management of the coffee roasting facilities and the wholesale supply of coffee and allied products to the existing Brand Systems and third party accounts under the Di Bella Coffee brand; and
- Development and management of the procurement, warehousing, manufacturing and distribution business under the Hudson Pacific Food Service, Dairy Country, Bakery Fresh and Associated Food Service brands.

# DIRECTORS' REPORT

## (CONTINUED)

### Review of operations and financial condition

#### Important Information:

This review contains forward looking statements, including statements of current intention, statements of opinion and predictions as to possible future events and future financial prospects. Such statements are not statements of fact and there can be no certainty of outcome in relation to the matters to which the statements relate. Forward looking statements involve known and unknown risks, uncertainties, assumptions and other important factors that could cause the actual outcomes to be materially different from the events or results expressed or implied by such statements, and the outcomes are not all within the control of RFG. Statements about past performance are not necessarily indicative of future performance.

Neither RFG nor any of its subsidiaries, affiliates and associated companies (or any of their respective officers, employees or agents) (the 'Relevant Persons') makes any representation, assurance or guarantee as to the accuracy or likelihood of fulfilment of any forward looking statement or any outcomes expressed or implied in any forward looking statement. The forward looking statements in this review reflect views held only at the date hereof and except as required by applicable law or the ASX Listing Rules, the Relevant Persons disclaim any obligation or undertaking to publicly update any forward looking statements, or discussion of future financial prospects, whether as a result of new information or future events.

This review refers to RFG's financial results, including RFG's statutory performance and underlying performance. RFG's statutory performance contains a number of items that when excluded provide a different perspective on the financial and operational performance of the business. Income Statement amounts, presented on an underlying basis such as Underlying NPAT, are non-IFRS financial measures, and exclude the impact of these items consistent with the manner in which senior management reviews the financial and operating performance of the business. Each underlying measure disclosed has been adjusted to remove the impact of these items on a consistent basis. A reconciliation and description of the items that contribute to the difference between statutory performance and underlying performance is provided in the Summary of Financial Information attached to this report.

Certain other non-IFRS financial measures are also included in this review. These non-IFRS financial measures are used internally by management to assess the performance of RFG's business and make decisions on allocation of resources. Non-IFRS measures have not been subject to audit or review. Certain comparative amounts from the prior corresponding period have been re-presented to conform to the current period's presentation.

#### Group overview

The following table summarises the Group's results for the financial years ending 30 June 2018 and 30 June 2017:

Item	FY18	FY17	Change
Revenue	\$374.0m	\$349.3m	\$24.7m
NPAT	(\$306.7m)	\$61.9m	(\$368.6m)
NPAT (Underlying)	\$33.3m	\$75.7m	(\$42.4m)
EBITDA	(\$354.3m)	\$106.5m	(\$460.8m)
EBITDA (Underlying)	\$71.4m	\$123.5m	(\$52.1m)
EPS	(169.50 cps)	35.70 cps	(205.20 cps)
EPS (Underlying)	18.40 cps	43.70 cps	(25.30 cps)
Dividend per Share (DPS)	-	29.75 cps	(29.75 cps)

#### Review of 2018 financial year

RFG commenced FY18 with a focus on consolidating the Group's diversified business platform, with an emphasis on the improving efficiency of the franchise system supply chain and internal Group structure.

In June 2017, RFG had commissioned a business wide review, with the purpose of identifying business improvement opportunities and strengthening RFG's operating model, to better assure a long term future for its business, its franchisees, as well as other stakeholders. This comprehensive review progressed in FY18 and particularly included focus on:

- Examining the Group's cost base, effecting supply chain consolidation, and expediting synergies; and
- Initiating strategic review of the Group's domestic franchise operations.

Other external factors were also affecting franchisee sentiment and commitment through FY18, particularly:

- Fair Work Australia inquiries into other major retail franchise systems and regulatory change arising as a consequence of that; and
- Adverse publicity about franchising in the local and national media.

An adverse public profile for franchising led ultimately to the current Parliamentary Joint Committee on Corporations & Financial Services' Inquiry into the operation and effectiveness of the Franchising Code of Conduct, which is still in progress at the date of this report.

# DIRECTORS' REPORT

## (CONTINUED)

### Review of operations and financial condition (continued)

#### Review of 2018 financial year (continued)

As CY17 progressed, it became evident that trading results were not meeting management's expectation, impacted by challenging retail market trading conditions, especially within shopping centre locations, negative market sentiment towards franchising and RFG in particular, the cumulative impact of 2H17/1H18 store closures, and internal challenges in the management of RFG's business model.

These factors, together with concerns regarding franchisee sentiment and engagement, and the Group's supply chain performance, also contributed to a decline in new store growth, resale and renewal activity, and the number of outlets being passed to RFG management.

At the half year ended 31 December 2017, the Directors reported on:

- The outcome of management's initial review of RFG's retail franchise leases, and the identification of 160 to 200 domestic retail leases which were provisioned for closure;
- The revised outlook for the business in the light of its retail lease review, resulting in a significant impairment write down at 31 December 2017; and
- The trading result and cash flow performance for the first half of the 2018 financial year.

The Directors also determined RFG needed a clear turnaround process to be executed in three stages:

- Stage 1 - **stabilise** the business and return it to a profitable platform, which is still in progress;
- Stage 2 - **optimise** the core business operations and enhance both RFG and franchisee profitability and return on capital outcomes; and
- Stage 3 - **prudently grow** the business, in the retail food franchise systems by developing and operating new stores in selected locations, and in the coffee business by expanding its operation into new market channels in food service and corporate business.

As part of this turnaround strategy, the Board also initiated a management transition within the Group, with the departure of former Managing Director, Andre Nell, and the appointments of Richard Hinson as Group Chief Executive and Chief Executive of RFG's Brand Systems and commercial division, and Darren Dench as Chief Executive of Di Bella Coffee, RFG's coffee business.

The Board is satisfied that RFG's management team is working with its franchisees and customers to improve the underlying and sustainable performance of each of RFG's businesses, and remains confident in the capacity of these businesses to compete in a challenging market place.

Your Directors consider that RFG's core strategic direction lies with its coffee and retail food franchise systems, which, if supported appropriately by RFG and an energised franchisee network, should be able to generate acceptable future returns for both its franchisees and RFG's shareholders.

Clearly, RFG remains challenged today and has much work to do to return to an acceptable level of profitability but, at its essence, the Board sees a robust future for the business where:

- RFG focuses on where RFG and its franchisees can be profitable;
- Di Bella Coffee continues to supply RFG's Brand Systems, and expands its retail and wholesale customer base, both across Australia and internationally;
- RFG delivers a store experience and product fulfilment that its consumers will enjoy, at a cost to franchisees that produces profits for all stakeholders;
- RFG removes internal complexity and simplifies how it does business.

In FY19, RFG expects to see each of RFG's Brand Systems stabilise to a core of profitable, well-run franchisee stores, supported by a field services and supply chain that delivers operational and economic support for RFG's franchisees and other customers.

In the immediate term, RFG's trading results will likely remain subdued until the full impact of RFG's lease restructuring and product and supply chain initiatives deliver the anticipated benefits to RFG's Brand Systems and coffee business.

Cash flow and working capital management also remain a major priority as management pursues outstanding debts and minimises the working capital invested in the Group's manufacturing and logistics chain, as well as improving the velocity of cash flow settlements within each retail food franchise system and the DiBella and Hudson Pacific operations.

RFG's two relationship banks, NAB and Westpac, appropriately continue to closely monitor the Group's turnaround strategy. The Board and senior management are working closely with them and their advisers to this end.

#### Financial position

RFG's current market capitalisation at 24 August 2018 was approximately \$113 million.

In assessing RFG's financial position as at 30 June 2018, and, in particular, the carrying value of RFG's Brand Systems, the Directors have taken a conservative approach, basing their assessment and subsequent impairment position to reflect both the Group's expected FY19 sustainable earnings and the risk profile inherent in RFG's current challenges. The outcome of this assessment was an impairment charge of \$402.9 million for the year, which reduces shareholder funds to \$158.0 million, representing an implied value of \$0.86 per share.

# DIRECTORS' REPORT

## (CONTINUED)

### Review of operations and financial condition (continued)

#### Financial position (continued)

In the Directors' report to shareholders for the half year ended 31 December 2017, the Directors identified a number of recapitalisation initiatives that RFG was minded to pursue and, in conjunction with RFG's advisers, RFG continues to explore these options, together with the continuation of the core business turnaround strategy.

At this date, your Directors are confident that RFG has a feasible turnaround strategy, the management team to implement it successfully, the core franchisee cohort to support their own and the Group's investments in the respective Brand Systems, and the current support of RFG's bankers and other key stakeholders to complete the turnaround job.

Shareholders will particularly take note of the classification of RFG's core debt as current as at 30 June 2018 on the basis of the current revised covenant relief conditions provided by the Group's relationship bankers, NAB and Westpac, as at 30 June 2018.

RFG will be seeking to reduce its debt through a combination of its turnaround strategy, potential asset sales and plans to obtain funding (by way, for example, of a market recapitalisation when the business performance has stabilised). Work on all these options commenced some time ago and continues, but, at this date, the Board has no definitive position on which options are preferable.

#### Going concern

These financial statements have been prepared on the basis that RFG is a going concern, able to realise assets in the ordinary course of business and settle liabilities as and when they are due.

The Group has experienced challenging operating conditions over the year and as announced with the release of its operating results for the half-year ended 31 December 2017, has instituted a restructure of its franchise brand systems networks to right-size the operation base of its respective businesses and set a course for growth in both domestic and international franchise activities. During the year ended 30 June 2018, the Group incurred a loss after income tax of \$306.7 million, which included business turnaround, restructuring costs and impairment losses of \$427.3 million as a result of the provisioning for the closure of circa 250 franchise stores and the impairment impacts arising from the revised profitability forecasts associated with the reset franchise networks going forward. The Group has a net current liability position of \$231.3 million at balance date. Despite these challenges, the Group generated a positive cashflow from operating activities of \$10.8 million and a positive Underlying EBITDA of \$71.4 million. Management and the Board are focussed on implementing the restructuring plan through FY19 and continuing to execute initiatives which are expected to boost operating earnings and reduce costs in future periods.

As referred to in Note 19 of the Financial Statements, the Group's secured syndicated loans totalling \$265 million are classified as current liabilities at the balance date. The Group had breached one of its lending covenants under its syndicated lending facility agreement at 30 June 2018. However, the Group has received a conditional waiver from the syndicate lenders. In addition, subsequent to the year end, agreement has been reached between the Company and its lenders to reset the covenants effective from 31 August 2018 for covenant testing periods commencing 1 July 2018. The Group's syndicated loan facility reduced from \$309 million to \$285 million and the maturity date was brought forward to 31 October 2019.

Despite the program to restructure the franchise businesses and build confidence in the franchise brands by consumers and potential franchise investors, there remains significant risk that the Group may breach financial covenant thresholds under its financing agreements within the next twelve months. A breach of one or more of these financial covenants may result in all the syndicated debt becoming due and payable. The continuing viability of the Group and its ability to continue as a going concern is dependent upon the Group maintaining the continuing support of the syndicated lenders, and managing the covenants and the terms of the renegotiated facility.

Achieving this outcome also depends upon:

- (1) The Group's ability to implement successfully an asset sales program over the next twelve months to realise funds to assist in paying down the syndicated debt;
- (2) The Group's ability to obtain additional funding (by way, for example, of a capital raising or accessing alternative sources of finance);
- (3) The Group's ability to execute successfully the restructuring initiatives previously referred to.

As a result, there is a material uncertainty that may cast significant doubt on whether the Group will continue as a going concern and, therefore, whether it will realise its assets and settle its liabilities and commitments in the normal course of business and at the amounts stated in the financial report. However, the Directors, after taking into account all relevant factors, have concluded that there are reasonable grounds to believe both that the secured syndicate financiers will continue to support the Group and that the business will remain a going concern for the next twelve months.

Accordingly, the Directors have prepared the financial report on a going concern basis. As a consequence, no further adjustments have been made to the financial report relating to the recoverability and classification of the assets carrying amounts or the amounts and classifications of liabilities that might be necessary should the Group not continue as a going concern.

RFG's auditor continues to work with the Board and management through these issues and has included an emphasis of matter paragraph in its audit opinion on the financial statements as at 30 June 2018 on the basis of material uncertainty associated with the syndicated debt facility and the various recapitalisation initiatives. Your Directors understand and accept the position taken by the auditor at this date, as RFG's relationship bankers are still considering the impacts of RFG's turnaround strategies that are currently in progress.

# DIRECTORS' REPORT

## (CONTINUED)

### Review of operations and financial condition (continued)

#### Review of Operations

Revenue for FY18 was \$374.0 million, representing a 7.1% increase (or \$24.7 million) on the prior corresponding period (PCP). The increase in revenue is primarily attributable to the following factors:

- A \$66.5 million increase from a full 12 months of Commercial Food Services segment revenue from both the HPC and AFS acquisitions; offset by
- A \$10.0 million decrease in Di Bella Coffee revenue, primarily attributable to competitive conditions in the contract roasting sector, and exit of low-margin Grocery contracts; and
- A \$31.8 million decrease in Brand System segment revenues (Bakery/Café, OSR and Coffee Retail), attributable to significantly lower transactional revenues from new outlet growth and franchisee renewals, and a decrease in Brand System coffee and allied product sales compared to the PCP.

The reported EBITDA loss of \$354.3 million and reported NPAT loss of \$306.7 million was significantly attributable to the \$402.9 million (pre-tax) non-cash provisioning and impairment as discussed previously. Underlying EBITDA of \$71.4 million and Underlying NPAT of \$33.3 million for FY18 excludes \$22.8 million (pre-tax) in restructuring costs associated with the business-wide review, and acquisition and integration costs attributable to the Hudson Pacific Corporation (HPC) and Associated Foodservice (AFS) acquisitions, \$1.6 million amortisation of acquired intangible assets. The FY18 costs excluded from Underlying EBITDA also include \$402.9 million (pre-tax) of non-cash provisioning and impairment of assets as discussed previously.

#### Financial Position and Cash Flows

Net Assets of \$158.0 million have decreased by \$307.1 million (or 66%) from 30 June 2017, primarily as a result of non-cash provisioning and impairment of assets. Further details on these adjustments are included in Note 6 of the financial statements as at 30 June 2018.

Cash inflows from operating activities for FY18 were \$10.8 million (FY17: \$63.8 million), with the decrease in net operating cash inflow attributable to cash outflows arising from business turnaround and restructuring costs incurred in the year, as well as a significant increase in working capital balances as a result of the growth in wholesale customer sales in the Commercial Food Services segment. The cash conversion to EBITDA ratio for the year was affected by the significant \$402.9 million non-cash provisioning and impairment of assets mentioned previously.

The Group received \$22.0 million (before costs) in cash arising from the issue of shares from the DRP Shortfall Placement on 17 October 2017.

#### Debt Structure

As at 30 June 2018, the Group's total gross debt increased to \$273.9 million, including ancillary facilities. The increase in gross debt was predominantly due to the timing of working capital cash flows, continued investment in property, plant and equipment and acquisition earn out payments for the Di Bella and Hudson Pacific Corporation acquisitions attended to during FY18.

In December 2017, the Group extended its three-year debt facilities totalling \$150 million, due to mature in December 2018, into longer dated maturities as follows:

- \$100 million extended to facilities maturing in January 2020; and
- \$50 million extended to facilities maturing in December 2020.

In addition, RFG reduced the existing debt facilities, maturing in December 2020, by \$25 million.

The Group received a conditional waiver from its senior debt lenders on 29 June 2018, for testing of financial covenants for the period ended 30 June 2018.

Subsequent to 30 June 2018, the Company further negotiated its financial covenants attaching to the Group's debt facilities that support the Group's restructuring plans with its senior debt lenders. Agreement has been reached between the Company and its lenders to reset the covenants effective from 31 August 2018 for covenant testing periods commencing 1 July 2018.

# DIRECTORS' REPORT

## (CONTINUED)

### Review of operations and financial condition (continued)

#### Debt Structure (continued)

The key terms of the covenant reset are:

Financial covenants and conditions	Revised 31 August 2018	Previous covenants
Covenant testing	Quarterly on 31 March, 30 June, 30 September and 31 December	Quarterly on 31 March, 30 June, 30 September and 31 December
Operating Leverage ratio (Secured Net Debt/EBITDA)	5.0x to December 2018; 4.5x to March 2019; 4.0x from 1 April 2019 onwards;	3.0x to December 2018; 2.5x from 1 January 2019;
Interest cover ratio	3.0x	4.0x
Gearing ratio	Covenant removed	Less than 50%
Financial Guarantor EBITDA and Assets ratios	Covenant removed	Greater than 90%
EBITDA performance to budget	Covenant removed	20% variance to budget
Mandatory prepayment – asset sales	100% of net proceeds	60% of net proceeds
Mandatory amortisation	Requirement removed	\$12.5m repayment by 2 March 2019
Total senior debt facilities	\$285 million	\$309 million
Tenor of facilities	31 October 2019	January 2020 and December 2020

In addition, the Group's restructuring program is subject to a review process with the lenders after 31 December 2018.

These revised banking arrangements will also come at an increased cost to the Group, which has been factored into future cash flows.

#### Operating Segment Review

The Group is managed through five major reportable segments under AASB 8, as follows:

- Bakery/Café Division (incorporating Michel's Patisserie, Donut King, and Brumby's Bakery Brand Systems);
- QSR Division (incorporating Crust Gourmet Pizza and Pizza Capers Brand Systems);
- Coffee Retail Division (incorporating Gloria Jean's Coffees, Esquires, Café2U and The Coffee Guy Brand Systems);
- Di Bella Coffee (incorporating Wholesale Coffee operations); and
- Commercial Food Services Division (incorporating procurement, warehousing, manufacturing and distribution operations).

All Brand System segments, with the exception of Di Bella Coffee, and Commercial Food Services, are referred to collectively by management as Franchise Operations.

#### Brand System Operations

Underlying Franchise Operations EBITDA for FY18 was \$53.3 million (FY17: \$97.5 million), representing a decline of 45.3% (or \$44.2 million).

FY18 new outlets established comprised of 101 in total, including 93 in international territories, and 8 domestically, with the prevailing negative sentiment surrounding the franchise industry, resulting in no new outlets being recognised in 2H18.

FY18 outlet closures were 305 in total, including 83 in international territories, 217 domestic traditional outlets, and 15 mobile vans. Domestic outlet closures are discussed in further detail under the heading *Domestic outlet analysis & consolidation*.

Same Store Sales (SSS) and Average Transaction Value (ATV) metrics for FY18 exclude the contribution from stores closed in the comprehensive domestic outlet network analysis.

Operationally, weighted Same Store Sales (SSS) and Average Transaction Value (ATV) growth of -1.4% and +2.7% represented a disappointing outcome, heavily impacted by the performance of those Brand Systems with significant shopping centre exposure, most significantly the Michel's Patisserie network.

This performance is contrasted with the QSR Division's performance, where credible SSS and ATV metrics of +2.0% and +2.9% were underpinned by disciplined pricing, menu innovation, alignment with delivery aggregators and a focus on operational excellence.

In 2H18, management implemented many of the initiatives, noted previously, in the review of domestic franchise operations and continued extensive engagement with the franchisee community, including:

- A restructuring of the Company's field support model, including employment of additional field based personnel fully operational;

# DIRECTORS' REPORT

## (CONTINUED)

Review of operations and financial condition (continued)

Operating Segment Review (continued)

*Brand System Operations (continued)*

- Further enhancing RFG's franchisee wage entitlement audit framework and compliance activities;
- Delivering cost of goods savings to franchisees;
- Offering discounted new store and renewal term franchise fee structures;
- Commencing store closure and landlord negotiation programs; and
- Continued reduction in head office and shared service resources;

Group Chief Executive Officer, Richard Hinson, completed an extensive Franchisee roadshow in July 2018, visiting 6 cities and c. 700 franchisees, communicating the future direction of the Group's franchise operations.

To improve the underlying and sustainable performance of each of its Brand Systems, "concept store" pilots have also been launched in the Michel's Patisserie, Brumby's Bakery, Donut King and Gloria Jeans Brands.

*Domestic outlet analysis & consolidation*

As announced in March 2018, a comprehensive domestic outlet network analysis was undertaken in February 2018, referencing three-year quantitative sales, lease and performance information and qualitative store-by-store assessment. As a result of that analysis, the company was forecasting in March 2018 (as announced) that between 160 and 200 outlets were not sustainable and would therefore likely close (or their leases would not be renewed) on or before 30 June 2019. The domestic outlet network analysis was recently revisited, having regard to the franchisee assistance activities and landlord rental negotiations undertaken in 2H18. The Company is now forecasting, as a consequence, that by 30 June 2019, circa 250 of the existing outlets will close (or their leases will not be renewed on expiry).

In July 2018 the domestic outlet network analysis was revisited, including consideration of franchisee assistance activities, and landlord rental negotiations undertaken in 2H18. As a result of the July 2018 review, circa 250 outlets are now forecast to either be closed or lease renewal not sought on expiry, on or before 30 June 2019.

RFG is seeking to renegotiate improved rental outcomes, where possible, to minimise closures, and will work constructively with impacted stakeholders.

*Brand system operations - International*

During FY18, the Group granted 9 new international master licenses, most notably the Donut King and Crust Brand Systems in the United Kingdom and Gloria Jean's in Germany, bolstering growth prospects in Western European markets.

Development of the UAE joint venture arrangements has been suspended indefinitely by mutual consent, to be reviewed at such time when RFG's turnaround strategy is further progressed. The joint venture arrangements were entered into in 1H18, to accelerate Brand System expansion within the Gulf, and establish a coffee enterprise throughout the Middle East & North Africa (MENA) region.

RFG now has 87 international licensed territories across 11 Brand Systems and, while many of these territories are in the early stages of their development cycle, they are expected to provide growing recurrent revenue streams as they mature.

*Di Bella Coffee*

During FY18, the Group appointed a new Chief Executive, Darren Dench, to take control of what was Retail Food Group's Coffee and Allied Beverages (CAB) division, and is now the Company's consolidated Di Bella Coffee business.

Underlying Di Bella Coffee Operations EBITDA for FY18 was \$8.1 million (FY17: \$14.2 million), representing a decrease of \$6.1 million on PCP. The decrease in EBITDA on PCP was due to \$2.6 million loss of margin in the contract roasting sector on new customer acquisition and cost pressures, and exit of low-margin Grocery contracts, with \$3.5 million due to non-recurring gains in FY17, and losses on sale of assets in FY18.

During FY18, RFG completed the restructuring and alignment activities which underpin the 1H18 repositioning of its CAB Division under the Di Bella Coffee brand, consolidating the Group's four coffee businesses into a single, integrated coffee enterprise under the Di Bella Coffee name.

Ongoing activity is focused on strengthening critical commercial and operational capabilities under a single leadership team, implementing financial and operational initiatives across supply chain and procurement to improve gross margins and cash flow generation, positioning the business to be commercially competitive.

RFG will ultimately exit its existing low-margin capsule operations, following non-renewal of the Group's domestic capsule supply agreement and a failure to achieve adequate business for the professional machine program, which has been significantly impacted by technical and manufacturer related issues.

*Commercial Food Services*

The Commercial Food Services Division EBITDA was \$10.0 million (FY17: \$11.8 million), primarily attributable to costs associated with carrying additional sites to allow for integration of the May 2017 AFS acquisition.

# DIRECTORS' REPORT

## (CONTINUED)

### Review of operations and financial condition (continued)

#### Operating Segment Review (continued)

##### *Commercial Food Services (continued)*

Investment in sales and management capability has driven an increase in foodservice customers since 30 June 2017, and new business secured for Dairy Country, largely commencing in 2H18. New product innovation and customer acquisition also drove growth in Bakery Fresh throughput to c.4.6 million kg for the period.

The integration of the Associated Food Services acquisition into the existing Hudson Pacific facilities was completed in Q418, with the resultant logistical, lease exit, asset disposal and redundancy costs included in Integration Costs for the year.

Significant investment in new production capacity was completed during FY18, including:

- Commencing operations at a second facility for Dairy Country, including a \$5.2 million capital investment in new production lines, with additional cold storage. Operating and overhead costs of this additional facility commenced during the year;
- Upgrading equipment to increase efficiency and capacity, including a \$1.1 million capital investment at the existing Dairy Country facility;

The business continues to tender for additional production volumes with existing and new customers to drive economic returns from this asset investment.

##### *Organisational efficiency*

In recent years, RFG rapidly expanded through acquisitive activity. This growth has delivered many benefits, but has also led to a complexity which impacted focus on RFG's franchise business and has affected head office and shared service resource efficiency and effectiveness.

A key focus of the business-wide review has been the reduction of duplication and inefficiency, better integration of support structures, and improving alignment of the Company's resources with core revenue drivers.

The review resulted in a range of operational cost saving initiatives being undertaken in FY18, the impact of which is likely to be felt in FY19. Further efficiencies will be delivered in FY19.

##### **Looking forward**

Your Directors are not in a position to provide any specific guidance on the 2019 financial year at this date, although we do remain confident in the strategies being pursued by management and the other options to reduce debt being considered by RFG and its advisers.

The focus will remain to *stabilise* then *optimise* and then **prudently grow** the performance of the business.

##### **Dividend**

Under its current arrangements with its relationship banks, NAB and Westpac, and its underlying trading results, there will be no dividend for RFG as at 30 June 2018, nor is a dividend payment likely in the foreseeable 12 month outlook, until RFG's turnaround strategy returns the business to an acceptable profitable position.

##### **Board renewal**

Your Directors have also reflected on their performance in this difficult past twelve months and note that they have been proactive in both identifying the performance issues within the business and taking the initiative to address them, including the development of a feasible turnaround strategy and the appointment of a new senior leadership team that can develop and implement this plan successfully.

Your Directors have also taken the opportunity to seek out new talent to join the Board, and your Directors hope that they will be able to announce some new appointments once the 30 June 2018 financial year reporting process has been cleared.

##### **Acknowledgements**

It has been a challenging and disappointing year for RFG and its shareholders and your Directors can only assure you that they are trying to regenerate the underlying value that they consider RFG represents, but also accept that the proof is ultimately in the results RFG delivers and, with a depressed share price and no dividend on offer, there is much value to recreate.

RFGs' management team and its many staff have continued to work hard with us to identify and address the many challenges dragging the business down and we acknowledge and praise their efforts, and note management's optimism that RFG has a positive and profitable future.

# DIRECTORS' REPORT

## (CONTINUED)

### Dividends

Dividends paid or declared by the Company to members since the end of the previous financial year were:

Company	FY18		FY17	
	Cents per share	Total \$'000	Cents per share	Total \$'000
<b>Declared and paid during the financial year</b>				
Fully paid ordinary shares				
Final dividend - fully franked at 30% tax rate <sup>[1]</sup>	15.00	26,510	14.50	23,920
Interim dividend - fully franked at 30% tax rate <sup>[2]</sup>	-	-	14.75	25,968
	15.00	26,510	29.25	49,888
<b>Declared after the end of the financial year</b>				
Fully paid ordinary shares				
Final dividend - fully franked at 30% tax rate <sup>[3]</sup>	-	-	15.00	26,510

(1) In respect of the financial year ended 30 June 2017, as detailed in the Directors' Report for that financial year, a final dividend of 15.00 cents per share, based on 176,736,066 shares on issue at 29 August 2017, franked to 100% at 30% corporate income tax rate, was paid on 17 October 2017. The final dividend was approved by the Directors on 29 August 2017 and, therefore, was not provided for in the Company's financial report. It was resolved that the 2017 final dividend would constitute an eligible dividend for the purpose of the Company's Dividend Reinvestment Plan. The issue price of the shares was \$4.47.

(2) The Directors resolved not to declare an interim dividend in FY18.

(3) The Directors have resolved that no final dividend will be paid in respect of FY18.

### Environmental regulations

The Group, due to the nature of its operations, is not required to be environmentally licensed nor is it subject to any conditions which have been imposed by an environmental regulator specifically related to the Group or its operations.

In circumstances where the nature of the Group's operations requires, the Group is committed to compliance with all prescribed environmental laws and regulations.

### Indemnification of Officers and Auditors

During the financial year, the Company entered into a contract insuring the Directors of the Company, the Company Secretary, and all executive officers of the Company and of any related body corporate against a liability incurred as a Director, Secretary or executive officer to the extent permitted by the *Corporations Act 2001*. The contract of insurance prohibits disclosure of the nature of the liability and the amount of the premium.

The Company has also entered into a Deed indemnifying the Directors, officers and certain other parties in respect of certain claims that may be raised against them relative to the operations of the Company, its former and current subsidiaries.

To the maximum extent permitted by the *Corporations Act 2001*, the Deed indemnifies those persons from liabilities incurred as a consequence of the acts of those persons.

The Company has not, otherwise, during or since the end of the financial year, indemnified or agreed to indemnify an officer or auditor of the Company or of any related body corporate against a liability incurred as such an officer or auditor.

### Non-audit services

Details of the amounts paid or payable to the auditor for non-audit services provided during the year by the auditor are outlined in Note 34 to the financial statements.

The Directors are satisfied that the provision of non-audit services, during the year, by the auditor, or by another person or firm on the auditor's behalf, is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*.

The Directors are of the opinion that the services, as disclosed in Note 34 to the financial statements, do not compromise the external auditor's independence, based on advice received from the Audit and Risk Committee, for the following reasons:

- All non-audit services have been reviewed and approved to ensure that they do not impact the integrity and objectivity of the auditor; and

# DIRECTORS' REPORT

## (CONTINUED)

### Non-audit services (continued)

- None of the services undermine the general principles relating to auditor independence, as set out in Code of Conduct APES 110 Code of Ethics for Professional Accountants issued by the Accounting Professional & Ethical Standards Board, including reviewing or auditing the auditor's own work, acting in a management or decision-making capacity for the Company, acting as advocate for the Company or jointly sharing economic risks and rewards.

### Auditor's independence declaration

The auditor's independence declaration is included on page 27 of the financial report.

### Rounding off of amounts

The Company is a company of the kind referred to in *ASIC Corporations Instrument 2016/191* and, in accordance with that Class Order, amounts in the Directors' Report and the Financial Report are rounded off to the nearest thousand dollars, unless otherwise indicated.

### Remuneration report

The Directors present the Retail Food Group Limited 2018 remuneration report, outlining key aspects of the Company's remuneration policy and framework, and remuneration awarded this year.

This Remuneration Report, which forms part of the Directors' Report, sets out information about the remuneration of Retail Food Group Limited's Directors and its senior executive management for the financial year ended 30 June 2018.

The prescribed details for each person covered by this report are contained below under the following headings:

- Key Management Personnel;
- Remuneration Policy;
- Relationship between Remuneration Policy and Group Performance;
- Remuneration of Directors and Senior Executive Management;
- Key Management Personnel equity holdings;
- Key terms of employment contracts;
- Loans to Key Management Personnel; and
- Other transactions with Key Management Personnel and Directors of the Group.

#### 1. Key Management Personnel

The Company does not directly remunerate any of its Directors, Key Management Personnel or specific executives. Rather, the Directors, Key Management Personnel and specific executives are remunerated through subsidiaries of the Company.

The Directors and other Key Management Personnel of the consolidated entity during or since the end of the financial year were:

Executive and Non-executive Directors	Position
Mr Colin Archer	Chairman and Independent Non-Executive Director
Ms Jessica Buchanan	Independent Non-Executive Director
Mr Stephen Lonie	Independent Non-Executive Director
Ms Kerry Ryan	Independent Non-Executive Director
Mr Russell Shields	Independent Non-Executive Director
Mr Anthony (Tony) Alford	Non-Independent Non-Executive Director - Resigned 3 July 2017
Mr Andre Nell	Executive Managing Director - Resigned 29 May 2018
Senior executive management	Position
Mr Richard Hinson	Group Chief Executive Officer - Appointed 29 May 2018
Mr Peter McGettigan	Chief Financial Officer
Mr Anthony Mark Connors	Company Secretary, Director Corporate Services
Mr Michael Gilbert	Chief Executive - International - Resigned 13 June 2018
Mr Gary Alford	Chief Executive Officer - Resigned 15 September 2017
Mr Darren Dench	Chief Executive Officer - Di Bella Coffee - Appointed 4 December 2017

The term 'senior executive management' is used in this Remuneration Report to refer to these persons.

These named persons were senior executive management throughout the financial year and since the end of the financial year.

Mr Richard Hinson was appointed to Chief Executive Australia on 22 January 2018, and was promoted to Group Chief Executive Officer on 29 May 2018.

Mr Michael Gilbert was appointed to Chief Executive - International on 21 June 2017. Prior to this appointment, he held the position of Chief Franchise Officer (was not classified as KMP) and resigned from this position on 13 June 2018. He will cease employment on 12 September 2018.

Mr Anthony (Tony) Alford became a Non-Independent Non-Executive Director on 1 July 2016 and resigned from this position on 3 July 2017.

Mr Andre Nell was appointed executive Managing Director on 1 July 2016, and resigned from this position on 29 May 2018.

# DIRECTORS' REPORT

## (CONTINUED)

### Remuneration report (continued)

#### 1. Key Management Personnel (continued)

Mr Gary Alford was appointed as Chief Executive Officer of the Company on 1 July 2016, and retired from this position on 15 September 2017.

Mr Darren Dench was appointed to Global Head of Coffee on 4 December 2017. He was subsequently appointed Chief Executive Officer - Di Bella Coffee on 29 May 2018.

#### 2. Remuneration Policy

The Board considers that it is critical to its long term success, and the building of shareholder value, that it attracts, retains and motivates appropriate personnel to lead, manage and serve the Group in an increasingly competitive marketplace for senior executive talent.

The objectives of the Group's remuneration policy are to:

- Motivate executive and non-executive personnel to successfully lead and manage the Group, with a focus on driving long term growth and shareholder value;
- Drive successful performance and achievement of long and short term goals and otherwise reinforce the objectives of the Group;
- Deliver competitive remuneration packages necessary to attract and retain appropriate personnel;
- Ensure fair remuneration, having regard to duties, responsibilities and other demands;
- Ensure flexibility, to enable the Group to cope with planned or unforeseen threats and opportunities;
- Ensure compliance with relevant laws; and
- Ensure sustainable value for all stakeholders.

When determining executive remuneration packages, the Board may have regard to:

- The need to attract, retain and motivate appropriate personnel;
- Market practices;
- Alternative benefits including incentive programs, fringe benefits and equity schemes;
- Assessment of individual performance against set goals and targets; and
- The scope of responsibility, duties and other demands.

Executive remuneration shall generally take the form of a base salary plus superannuation, however, may comprise performance bonuses and other benefits or rewards in certain circumstances.

When determining non-executive remuneration packages, the Board may have regard to:

- The need to attract, retain and motivate appropriately qualified and experienced Directors with diverse backgrounds and experiences to ensure the Board is comprised of a range of skills necessary to properly understand the business environment in which the Group operates;
- The scope and complexity of the responsibilities assumed by such Directors in connection with the oversight and leadership of the Group;
- Comparative market practices;
- Assessment of individual performance against set goals and targets; and
- Alternative benefits, including equity schemes.

#### Role of the Remuneration Committee

The Board has a Remuneration Committee to assist the Board and report to it on remuneration and issues relevant to remuneration policies and practices, including those policies and practices for senior executive management and non-executive Directors.

The functions performed by the Remuneration Committee are to:

- Review and evaluate the market practices and trends on remuneration matters;
- Make recommendations to the Board in relation to the Group's remuneration policies and practices;
- Oversight of the performance of the Managing Director, Chief Executive Officer, Chief Financial Officer and other members of senior executive management and non-executive Directors; and
- Make recommendations to the Board in relation to the remuneration of senior executive management and non-executive Directors.

The Remuneration Committee has adopted the following policies to which it will continue to have regard when determining the remuneration of executives and senior executive management members, being to:

- Annually review executive and senior executive management member packages by reference to Group performance, executive performance, comparable information from industry sectors and other listed companies;
- Reward performance which results in long-term growth in shareholder value;
- Link all bonuses and incentives to pre-determined performance criteria; and
- Reference any changes to measurable performance criteria.

# DIRECTORS' REPORT

## (CONTINUED)

### Remuneration report (continued)

#### 3. Relationship between Remuneration Policy and Group Performance

The following compensation structures are designed to attract suitably qualified executives, reward the achievement of strategic objectives and achieve the broader outcome of long-term success and the building of shareholder value. The compensation structures take into account:

- The capability and experience of the executive;
- The executive's ability to manage and deliver the Group's forecast results;
- The attainment of pre-determined KPIs developed specially for the executive's role;
- The Group's overall performance including:
  - The Group's earnings;
  - The growth in earnings per share and return on shareholder wealth; and
- The relative size of incentives within each executive's remuneration package.

Remuneration packages include a mix of fixed and variable compensation and short-term and long-term performance-based incentives. The mix of these components is based on the role the individual performs.

In addition to their salaries, the Group also provides non-cash benefits to its executives and contributes to a post-employment superannuation plan on their behalf, in accordance with its statutory obligations.

#### Fixed Compensation

Fixed compensation consists of base compensation, which is calculated on a total cost basis and includes any fringe benefits tax (FBT) charges related to employee benefits including motor vehicles, as well as employer contributions to superannuation funds.

Compensation levels are reviewed annually by the Remuneration Committee and the Group Chief Executive Officer (and formerly, the executive Managing Director), through a process that considers the individual responsibilities and the achievement of pre-determined KPIs, and the overall performance of the Group.

Remuneration is also reviewed on promotion.

Executives receive a superannuation guarantee contribution required by the Government, which is currently 9.5% (2017: 9.5%) and do not receive any other retirement benefits. Some individuals, however, have chosen to sacrifice a further part of their salary to increase payments towards superannuation.

#### Performance-linked Compensation

Performance linked compensation includes both short-term and long-term incentives and is designed to reward executives for meeting or exceeding their defined role objectives. The short-term incentive (STI) is an 'at risk' bonus provided in the form of cash, while the long-term incentive (LTI) is provided as performance rights which can convert to ordinary shares of the Company on vesting under the rules of the Company's Performance Rights Plan. The decision to grant Rights to executives is based on past performance. In respect of the Performance Rights granted, there are performance criteria required to be achieved in order for the Performance Rights to vest.

#### Short-term Incentive Bonus

Each year, the Remuneration Committee sets pre-determined key performance indicators (KPIs) for certain key executives. The KPIs generally include performance measures relating to the Group and the individual and include financial, people, customer, strategy and risk measures. The measures chosen directly align the individual's reward to the KPIs of the Group and to its strategy and performance. The Group undertakes a rigorous and detailed annual forecasting and budget process. The Board considers that the achievement of the annual forecast and budget is, therefore, the most relevant short-term performance condition.

The financial performance objectives may include but not be limited to "Net Profit", "Revenue", "Franchise Revenue", "Corporate Expenditure" and "Minimum Earnings Per Share" compared to budget and forecast amounts. The non-financial objectives vary with position and responsibility and include measures such as achieving strategic objectives, compliance with governance and regulatory requirements, new store commissions, growth in network sales from effective brand marketing and promotions, growth in average weekly sales, growth in customer counts, customer satisfaction and staff development.

At the end of the financial year, the Remuneration Committee assesses the actual performance of the Group and the relevant individual against the KPIs set at the beginning of the financial year. No bonus is awarded where performance objectives are not achieved. The Group Chief Executive Officer, recommends to the Remuneration Committee, the performance bonus amounts for individuals, for approval by the Board. This method of assessment was chosen as it provides the Remuneration Committee with an objective assessment of the individual's performance.

# DIRECTORS' REPORT

## (CONTINUED)

### Remuneration report (continued)

#### 3. Relationship between Remuneration Policy and Group Performance (continued)

##### Long-term Incentive Bonus

In terms of long term incentive arrangements, in August 2015 the Directors approved and adopted a Performance Rights Plan. Under this plan, Performance Rights were granted to certain Key Management Personnel on 14 July 2016 with respect to the FY16, FY17, FY18 and FY19 performance periods. Shareholders also approved the grant of Performance Rights to former Managing Director, Andre Nell, at the Company's 2016 Annual General Meeting. In any case, the following Key Management Personnel were granted Performance Rights under the above plan:

- Mr Andre Nell;
- Mr Gary Alford;
- Mr Peter McGettigan;
- Mr Anthony Mark Connors; and
- Mr Michael Gilbert.

The Plan was designed to focus executives on delivering long-term shareholder returns. Under the plan, participants are only granted shares if performance conditions pertaining to the earnings per share (EPS) growth and relative total shareholder return (TSR) are met and the employee is still employed at the end of the vesting period.

The Directors have determined that performance conditions have not been met for the FY16, FY17 and FY18 rights performance periods, and accordingly nil performance rights eligible for vesting 1 July 2018 will vest.

Whereas the above Plan will continue to operate in respect of historical Performance Rights which may have been granted under it, in the 1H18 the Directors approved a replacement Rights Plan (Replacement Plan) in connection with future long term incentive remuneration. The Replacement Plan contemplates the grant of performance rights which are measured over a three year performance period commencing on 1 July in the financial year in respect to which the incentive is granted, and are subject to vesting conditionings based (in equal measure) on indexed total shareholder return and return on equity. A copy of the Group's Long Term Incentive Plan Policy & Procedure, and RFG's Rights Plan Rules, which apply under the Replacement Plan, are available on the Company's website, [www.rfg.com.au](http://www.rfg.com.au).

At the Company's 2017 Annual General Meeting, shareholders approved the proposed grant to former Managing Director Andre Nell of 117,014 performance rights under the Replacement Plan. Despite shareholder approval, the aforesaid rights were not granted to Mr Nell having regard to the performance and circumstances of the Group. Following Mr Nell's departure, the requirement to issue the approved rights became redundant.

The Company's arrangements with senior executive management contemplate the grant of Performance Rights under the Replacement Plan which equates to 30% of the relevant executive's total fixed remuneration. Having regard to recent performance of the Group, Performance Rights in respect to FY18 long term incentive remuneration have yet to be granted as at the date of this Report.

Participation in the Plan was at the Board's absolute discretion and no individual has a contractual right to participate in the Plan.

Note the summary information in relation to the Group's earnings and movements in shareholder wealth for the five years to 30 June 2018 in accordance with the requirements of the Corporations Act as follows:

Metrics	FY14	FY15	FY16	FY17	FY18
Share price at start of financial year	\$3.95	\$4.54	\$5.43	\$5.53	\$4.70
Share price at end of financial year	\$4.54	\$5.43	\$5.53	\$4.70	\$0.54
Interim dividend	10.75 cps	11.50 cps	13.00 cps	14.75 cps	-
Final dividend	11.25 cps	11.75 cps	14.50 cps	15.00 cps	-
Basic EPS (Underlying)	26.5 cps	35.6 cps	40.5 cps	43.7 cps	18.4 cps
Basic EPS <sup>(1)</sup>	26.5 cps	22.1 cps	37.4 cps	35.7 cps	(169.5 cps)
Diluted EPS <sup>(1)</sup>	26.5 cps	22.1 cps	37.4 cps	35.7 cps	(169.5 cps)

(1) EPS figures are as historically reported.

# DIRECTORS' REPORT

## (CONTINUED)

### Remuneration report (continued)

#### 4. Remuneration of Directors and Senior Executive Management

The following tables show details of the remuneration expense recognised for the Group's Directors and Senior Executive Management for the current and previous financial year measured in accordance with the requirements of the accounting standards.

FY18 Name	Short-term Benefits			Long-term Benefits			Termination Benefits	Total
	Salary & fees <sup>(1)</sup>	Bonus	Other	Super-annuation	Performance Rights	Other <sup>(2)</sup>		
	\$	\$	\$	\$	\$	\$		
<b>Non-Executive Directors</b>								
Mr Colin Archer	217,884	-	-	19,578	-	-	-	237,462
Ms Jessica Buchanan	111,517	-	-	3,944	-	-	-	115,461
Mr Stephen Lonie	127,854	-	-	12,146	-	-	-	140,000
Ms Kerry Ryan	109,589	-	-	10,411	-	-	-	120,000
Mr Russell Shields	109,589	-	-	10,411	-	-	-	120,000
<b>Senior Executive Management</b>								
Mr Richard Hinson <sup>(3)</sup>	219,617	-	796	10,024	-	-	-	230,437
Mr Darren Dench <sup>(4)</sup>	173,934	-	1,038	11,018	-	-	-	185,990
Mr Peter McGettigan	451,598	55,000	1,800	20,049	12,538	19,824	-	560,809
Mr Anthony Mark Connors	307,266	46,800	1,800	20,049	7,894	8,189	-	391,998
Mr Michael Gilbert <sup>(5)</sup>	342,405	45,000	1,819	20,049	4,010	-	-	413,283
<b>Former</b>								
Mr Anthony (Tony) Alford <sup>(6)</sup>	7,092	-	-	674	-	-	-	7,766
Mr Gary Alford <sup>(7)</sup>	147,847	-	-	14,715	-	2,582	-	165,144
Mr Andre Nell <sup>(8)</sup>	737,003	100,000	3,441	20,049	-	43,520	750,000	1,654,013
	<u>3,063,195</u>	<u>246,800</u>	<u>10,694</u>	<u>173,117</u>	<u>24,442</u>	<u>74,115</u>	<u>750,000</u>	<u>4,342,363</u>

Key management personnel were granted a cash bonus of \$246,800 during the year ended 30 June 2018 in respect of their performance for the year ended 30 June 2017. The bonuses were approved by the Board.

- (1) Salary and fees include Short-term benefits as per Corporations Regulation 2M.3.03(1) Item 6 comprising of cash salary and annual leave entitlements.
- (2) Other long-term benefits as per Corporations Regulation 2M.3.03(1) Item 8. The amounts disclosed in this column represent the movements in the associated long service leave provisions.
- (3) On 29 May 2018 Richard Hinson was appointed as Group Chief Executive Officer and as a result of this appointment, is now considered to be a KMP. The remuneration of Richard Hinson is proportioned for the period that he is considered a KMP.
- (4) On 4 December 2017 Darren Dench was appointed as Global Head of Coffee and as a result of this appointment, is now considered to be a KMP from this date. He was subsequently appointed Chief Executive Officer - Di Bella Coffee on 29 May 2018. The remuneration of Darren Dench is proportioned for the period that he is considered a KMP.
- (5) Resigned on 13 June 2018 and will cease employment on 12 September 2018.
- (6) Ceased employment on 3 July 2017.
- (7) Ceased employment on 3 July 2017.
- (8) Ceased employment on 29 May 2018.

# DIRECTORS' REPORT

## (CONTINUED)

Remuneration report (continued)

### 4. Remuneration of Directors and Senior Executive Management (continued)

FY17 Name	Short-term Benefits			Long-term Benefits			Termination Benefits	Total
	Salary & fees <sup>(1)</sup>	Bonus	Other	Super-annuation	Performance Rights	Other <sup>(2)</sup>		
	\$	\$	\$	\$	\$	\$		
<b>Non-Executive Directors</b>								
Mr Colin Archer	203,798	-	-	18,411	-	-	-	222,209
Ms Jessica Buchanan	112,000	-	-	-	-	-	-	112,000
Mr Stephen Lonie	118,904	-	-	11,296	-	-	-	130,200
Ms Kerry Ryan	102,929	-	-	9,778	-	-	-	112,707
Mr Russell Shields	101,159	-	-	9,610	-	-	-	110,769
Mr Anthony (Tony) Alford	221,745	242,000	-	12,537	-	498,787	-	975,069
<b>Executive Directors</b>								
Mr Andre Nell	648,220	121,911	1,800	19,828	20,414	44,503	-	856,676
<b>Senior Executive Management</b>								
Mr Gary Alford	433,981	102,431	-	47,680	8,334	36,743	-	629,169
Mr Peter McGettigan	341,634	112,074	1,800	30,100	10,403	23,149	-	519,160
Mr Anthony Mark Connors	266,057	121,293	1,800	19,716	7,489	4,503	-	420,858
Mr Michael Gilbert <sup>(3)</sup>	13,433	-	69	771	259	-	-	14,532
	2,563,860	699,709	5,469	179,727	46,899	607,685	-	4,103,349

Key Management Personnel were granted a cash bonus of \$699,709 during the year ended 30 June 2017 in respect of their performance for the year ended 30 June 2016. The bonuses were approved by the Board.

- (1) Salary and fees include Short-term benefits as per Corporations Regulation 2M.3.03(1) Item 6 comprising of cash salary and annual leave entitlements.
- (2) Other long-term benefits as per Corporations Regulation 2M.3.03(1) Item 8. The amounts disclosed in this column represent the movements in the associated long service leave provisions.
- (3) On 21 June 2017 Michael Gilbert was appointed as Chief Executive - International and as a result is was considered to be a KMP from that date. The remuneration of Michael Gilbert is proportioned for the period that he was considered a KMP.

The relative proportions of remuneration that are linked to performance and those proportions that are fixed are as follows:

	Fixed		Short-term Incentive		Long-term Incentive	
	FY18 %	FY17 %	FY18 %	FY17 %	FY18 %	FY17 %
<b>Non-Executive Directors</b>						
Mr Colin Archer	100.0	100.0	-	-	-	-
Ms Jessica Buchanan	100.0	100.0	-	-	-	-
Mr Stephen Lonie	100.0	100.0	-	-	-	-
Ms Kerry Ryan	100.0	100.0	-	-	-	-
Mr Russell Shields	100.0	100.0	-	-	-	-
<b>Senior Executive Management</b>						
Mr Richard Hinson	100.0	-	-	-	-	-
Mr Darren Dench	100.0	-	-	-	-	-
Mr Peter McGettigan	84.4	71.9	9.8	21.6	5.8	6.5
Mr Anthony Mark Connors	84.0	68.3	11.9	28.8	4.1	2.8
Mr Michael Gilbert	88.1	98.2	10.9	-	1.0	1.8
<b>Former</b>						
Mr Anthony (Tony) Alford	100.0	77.6	-	22.4	-	-
Mr Gary Alford	100.0	76.6	-	16.3	-	7.2
Mr Andre Nell	91.3	78.2	6.0	14.2	2.6	7.6

# DIRECTORS' REPORT

## (CONTINUED)

### Remuneration report (continued)

#### 4. Remuneration of Directors and Senior Executive Management (continued)

##### Performance Rights Plan

Under the Group's original Performance Rights Plan (refer above), Rights will only vest if performance conditions pertaining to the earnings per share (EPS) growth and relative total shareholder return (TSR) vesting conditions are met and the employee is still employed at the end of the vesting period.

Participating employees do not receive any dividends and are not entitled to vote in relation to the Rights during the vesting period.

Participation in the Performance Rights plan was at the Board's absolute discretion and no individual has a contractual right to participate in the plan. Once vested, a participant will be deemed to have automatically exercised all vested performance rights and the Company will settle its obligation in line with the Performance Rights Plan.

There is no consideration payable by the participant upon exercising of vested performance rights. Upon vesting, the conversion of a performance right to an equity or cash based settlement, is determined using a formula referencing the relevant share prices of the Company, the number of rights exercised, and is at the Board's sole discretion.

Performance Rights granted under the Performance Rights Plan are divided into three (3) equal tranches, with each respective tranche having a 12 month performance period aligned to successive financial years.

Each tranche of Rights is dependent on satisfaction of two discrete performance measures:

1. Earnings per Share (EPS) representing 50% of each tranche (EPS Measure); and
2. Relative Total Shareholder Return (TSR) representing 50% of each tranche (TSR Measure).

The valuation of rights granted is as follows:

Grant date	Vesting & Exercise Date	Base Price	Value per Right at Grant date					
			Tranche 1		Tranche 2		Tranche 3	
			TSR	EPS	TSR	EPS	TSR	EPS
14 July 2016	1 July 2018	\$5.61	-	\$5.06	\$2.54	\$5.06	\$2.77	\$5.06
14 July 2016	1 July 2019	\$5.61	\$2.42	\$4.80	\$2.49	\$4.80	\$2.49	\$4.80
1 December 2016	1 July 2019	\$6.19	\$3.73	\$5.40	\$2.84	\$5.40	\$2.84	\$5.40

The table below shows a reconciliation of options held by each Key Management Personnel from the beginning to the end of FY18. There are no vested options.

Executive	Grant Date	Balance at the start of the year	Number of Rights Forfeited	Forfeited %	Balance of unvested rights at the end of the year
<b>Current Key Management</b>					
Anthony Mark Connors	14 July 2016	17,458	13,963	80%	3,495
Peter McGettigan	14 July 2016	23,879	17,905	75%	5,974
<b>Former Key Management Personnel</b>					
Andre Nell	1 December 2016	44,802	44,802	100%	-
Garry Alford	14 July 2016	22,382	22,382	100%	-
Michael Gilbert	14 July 2016	15,226	15,226	100%	-

The Directors have determined that performance conditions have not been met for the FY16, FY17 and FY18 rights performance periods, and accordingly nil performance rights eligible for vesting on 1 July 2018 will vest.

As noted above, in 1H18 the Directors approved a replacement Rights Plan (Replacement Plan) in connection with future long term incentive remuneration. No Performance Rights have been granted under this plan as at the date of this Report.

##### External Remuneration Consultant Advice

The Company's Remuneration Committee has power under its Charter to consult independent expert advisors as it may consider appropriate for the proper performance of its function and charge the costs to the Company or another appropriate company within the Group.

In FY18 the Directors, via the Remuneration Committee, engaged the services of an external remuneration consultant (RC) to provide key management personnel remuneration recommendations and advice, and advice in connection with the Company's short term incentive (STI) and long term incentive (LTI) remuneration structures.

# DIRECTORS' REPORT

## (CONTINUED)

Remuneration report (continued)

### 4. Remuneration of Directors and Senior Executive Management (continued)

#### External Remuneration Consultant Advice (continued)

*Godfrey Remuneration Group Pty Ltd*

Benchmarking market competitiveness of Group's remuneration practices for certain key management personnel & advice in connection with STI and LTI structures: \$32,000

The Remuneration Consultant submitted its findings and recommendations in relation to benchmarking the market competitiveness of the Group's remuneration practices for key management personnel, together with its recommendations in connection with the Company's STI and LTI structures.

The Directors did not implement the Remuneration Consultant's full recommendations in connection with key management personnel remuneration, instead, taking a more conservative approach to remuneration review than recommended. The Directors otherwise engaged with the Remuneration Consultant in connection with the development of RFG's revised STI and LTI structures (note copies of the Company's Long Term Incentive Policy & Procedure, RFG Rights Plan Rules, and the Rules of the RFG Limited Short Term Incentive Plan are available on the Company's website, [www.rfg.com.au](http://www.rfg.com.au)).

So as to ensure key management personnel remuneration recommendations were free from undue influence from key management personnel to whom they relate, the Company established practices to ensure that:

- Key management personnel remuneration recommendations might only be received from consultants who have been approved by the Remuneration Committee, being a committee of the Board which has functions relating to remuneration of the key management personnel of the Company;
- As required by law, the Remuneration Consultant did not provide its recommendation to an executive director, or a person who is neither a director nor a member of remuneration committee; and
- The Remuneration Committee controls the Company's engagement with the Remuneration Consultant.

The Board is satisfied that the key management personnel remuneration recommendations received were free from undue influence from key management personnel to whom they recommendations related. The reasons the Board is so satisfied include that it is confident that the practices referenced above operated effectively and as intended, the Remuneration Committee and Board has been closely involved in all dealings with the Remuneration Consultant, and the Remuneration Consultant's remuneration recommendation received during the reporting period was accompanied by a legal declaration from the Remuneration Consultant, in accordance with s206M of the Corporations Act 2001 (Cth), that the said recommendation was provided free from undue influence by any key management personnel to whom the recommendation relates.

# DIRECTORS' REPORT

## (CONTINUED)

### Remuneration report (continued)

#### 5. Key Management Personnel equity holdings

Fully paid ordinary shares of Retail Food Group Limited:

FY18	Balance 1 July 2017	Granted as Compensation	Received on Vesting of Rights	Net Other Change	Balance 30 June 2018	Balance Held Nominally
Name	Number	Number	Number	Number	Number	Number
<b>Non-Executive Directors</b>						
Mr Colin Archer	389,377	-	-	1,707	391,084	-
Ms Jessica Buchanan	11,628	-	-	-	11,628	-
Mr Stephen Lonie	52,435	-	-	1,760	54,195	-
Mr Russell Shields	7,500	-	-	252	7,752	-
Ms Kerry Ryan	10,000	-	-	-	10,000	-
<b>Senior Executive Management</b>						
Mr Richard Hinson	-	-	-	-	-	13,000
Mr Darren Dench	-	-	-	-	-	-
Mr Peter McGettigan	31,969	-	-	4,573	36,542	-
Mr Anthony Mark Connors	195,567	-	-	-	195,567	-
Mr Michael Gilbert	1,884	-	-	64	1,948	-
<b>Former</b>						
Mr Anthony (Tony) Alford <sup>(1)</sup>	19,643,078	-	-	(19,643,078)	-	-
Mr Gary Alford <sup>(1)</sup>	836,887	-	-	(836,887)	-	-
Mr Andre Nell <sup>(1)</sup>	12,710	-	-	(12,710)	-	-
	21,193,035	-	-	(20,484,319)	708,716	13,000

(1) Individual was not a KMP as at 30 June 2018

FY17	Balance 1 July 2016	Granted as Compensation	Received on Vesting of Rights	Net Other Change	Balance 30 June 2017	Balance Held Nominally
Name	Number	Number	Number	Number	Number	Number
<b>Non-Executive Directors</b>						
Mr Colin Archer	375,578	-	-	13,799	389,377	-
Ms Jessica Buchanan	23,256	-	-	(11,628)	11,628	-
Mr Stephen Lonie	49,929	-	-	2,506	52,435	-
Ms Kerry Ryan	10,000	-	-	-	10,000	-
Mr Russell Shields	-	-	-	7,500	7,500	-
Mr Anthony (Tony) Alford	19,635,758	-	-	7,320	19,643,078	834,421
<b>Executive Directors</b>						
Mr Andre Nell	12,102	-	-	608	12,710	-
<b>Senior Executive Management</b>						
Mr Gary Alford	829,567	-	-	7,320	836,887	-
Mr Anthony Mark Connors	195,567	-	-	-	195,567	-
Mr Peter McGettigan	30,442	-	-	1,527	31,969	-
Mr Michael Gilbert	1,793	-	-	91	1,884	-
	21,163,992	-	-	29,043	21,193,035	834,421

Nil Rights were exercised by Key Management Personnel during the financial year (FY17: nil).

Details of the Performance Rights Plan are contained in Note 24.

# DIRECTORS' REPORT

## (CONTINUED)

### Remuneration report (continued)

#### 6. Key terms of employment contracts

The employment specifics of the Non-Executive Directors are as follows:

Name	Particulars
Mr Colin Archer	The letter of appointment entered into with the Company requires the Director to give notice of resignation in accordance with the Company's Constitution. The Company may also terminate the Director's appointment in accordance with the Company's Constitution.
Ms Jessica Buchanan	The letter of appointment entered into with the Company requires the Director to give notice of resignation in accordance with the Company's Constitution. The Company may also terminate the Director's appointment in accordance with the Company's Constitution.
Mr Stephen Lonie	The letter of appointment entered into with the Company requires the Director to give notice of resignation in accordance with the Company's Constitution. The Company may also terminate the Director's appointment in accordance with the Company's Constitution.
Ms Kerry Ryan	The letter of appointment entered into with the Company requires the Director to give notice of resignation in accordance with the Company's Constitution. The Company may also terminate the Director's appointment in accordance with the Company's Constitution.
Mr Russell Shields	The letter of appointment entered into with the Company requires the Director to give notice of resignation in accordance with the Company's Constitution. The Company may also terminate the Director's appointment in accordance with the Company's Constitution.
Mr Anthony (Tony) Alford	The letter of appointment entered into with the Company requires the Director to give notice of resignation in accordance with the Company's Constitution. The Company may also terminate the Director's appointment in accordance with the Company's Constitution.

Fees and payments to Non-Executive Directors reflect the demands which are made on, and the responsibilities of, the Directors. Non-Executive Directors' fees and payments are reviewed annually by the Board. Non-Executive Director remuneration takes the form of a set fee plus superannuation entitlements and may comprise other benefits or rewards in certain circumstances.

Fees for the Non-executive Directors were as follows:

Role	FY18	FY17
Chairman	\$210,000	\$210,000
Non-executive Director*	\$110,000	\$110,000
Audit & Risk Management Committee Chairman	\$20,000	\$20,000
Remuneration Committee/Nomination Committee Chairman	\$17,500	\$17,500
Committee Member*	\$10,000	\$10,000

\* Excluding the Chairman or Committee Chairman (as case may be).

# DIRECTORS' REPORT

## (CONTINUED)

### Remuneration report (continued)

#### 6. Key terms of employment contracts (continued)

The maximum aggregate amount of fees that can be paid to Non-Executive Directors is subject to approval by shareholders at the Annual General Meeting. The maximum amount which has been approved by the Company's shareholders for payment to Non-Executive Directors is \$1.1 million. Fees for Non-Executive Directors are not linked to the performance of the Group. However, to align Non-Executive Directors' interests with shareholder interests, the Non-Executive Directors are encouraged to hold shares in the Company.

The employment specifics of the key Executive Directors and Senior Executive management are as follows:

Name	Particulars
Mr Richard Hinson	The contract of employment entered into with RFGA Management Pty Ltd (subsidiary of the Company) requires the employee to give a minimum of six (6) months notice to the employer. RFGA Management Pty Ltd may terminate the employee by giving at least six (6) months notice or payment of equivalent salary of the required notice in lieu.
Mr Darren Dench	The contract of employment entered into with RFGA Management Pty Ltd (subsidiary of the Company) requires the employee to give a minimum of six (6) months notice to the employer. RFGA Management Pty Ltd may terminate the employee by giving at least six (6) months notice or payment of equivalent salary of the required notice in lieu.
Mr Peter McGettigan	The contract of employment entered into with RFGA Management Pty Ltd (subsidiary of the Company) requires the employee to give a minimum of six (6) months notice to the employer. RFGA Management Pty Ltd may terminate the employee by giving at least six (6) months notice or payment of equivalent salary of the required notice in lieu.
Mr Anthony Mark Connors	The contract of employment entered into with RFGA Management Pty Ltd (subsidiary of the Company) requires the employee to give a minimum of six (6) months notice to the employer. RFGA Management Pty Ltd may terminate the employee by giving at least six (6) months notice or payment of equivalent salary of the required notice in lieu.
Mr Michael Gilbert	The contract of employment entered into with RFGA Management Pty Ltd (subsidiary of the Company) required the employee to give a minimum of three (3) months' notice to the employer. RFGA Management Pty Ltd was entitled to terminate the employee by giving at least three (3) months' notice or payment of equivalent salary of the required notice in lieu.
Mr Gary Alford	The contract of employment entered into with RFGA Management Pty Ltd (subsidiary of the Company) required the employee to give a minimum of six (6) months' notice to the employer. RFGA Management Pty Ltd was entitled to terminate the employee by giving at least six (6) months' notice or payment of equivalent salary of the required notice in lieu.
Mr Andre Nell	The contract of employment entered into with RFGA Management Pty Ltd (subsidiary of the Company) required the employee to give a minimum of twelve (12) months' notice to the employer. RFGA Management Pty Ltd was entitled to terminate the employee by giving at least twelve (12) months' notice or payment of equivalent salary of the required notice in lieu.

The Directors consider that the compensation for each Executive is appropriate for the duties allocated to them, the size of the Group's business and the industry in which the Group operates. The service contracts outline the components of compensation paid to the Executives, including Executive Directors, but do not prescribe how compensation levels are modified year to year. Compensation levels are reviewed each year to take into account cost-of-living changes, any changes in the scope of the role performed by the Executive and any changes required to meet the principles of the Remuneration Policy.

# DIRECTORS' REPORT

## (CONTINUED)

### Remuneration report (continued)

#### 7. Loans to Key Management Personnel

There were no loans outstanding at the end of the financial year (FY17: \$nil) to Directors or Senior Executive Management or their related parties.

#### 8. Other transactions with Key Management Personnel and the Directors of the Group

Profit for the year includes the following items of revenue and expense that resulted from transactions, other than compensation, loans or equity holdings, with Key Management Personnel or their related entities:

Consolidated	FY18 \$	FY17 \$
Consolidated revenue includes the following amounts arising from transactions with key management personnel of the Group and their related parties:		
Franchise revenue	40,605	80,504
	<u>40,605</u>	<u>80,504</u>
Consolidated profit includes the following expenses arising from transactions with key management personnel of the Group or their related parties:		
Consulting services	49,000	146,000
	<u>49,000</u>	<u>146,000</u>

The following transactions are made at arm's length terms within the meaning of Section 210 of the *Corporations Act 2001*:

- Harbour Town Investments Pty Ltd, a related party of Mr Anthony (Tony) Alford (ceased as a related party 3 January 2018), owned and operated one Donut King outlet during the year. Included in revenue for the year up to the date he ceased to be a related party is an amount of \$40,605, excluding GST, earned by the Group in respect of royalties and product sales to this store (FY17: \$80,504). As at 30 June 2018, \$867 of trading debt were outstanding (FY17: \$21).
- During FY18, the Group engaged the services of marketing consulting firm, Brands R People 2 Pty Ltd, being related parties of Ms Jessica Buchanan. \$49,000 was billed to the Group during FY18 and \$40,000 was payable as at 30 June 2018 (FY17: nil).
- During FY17, the Group engaged the consulting services of Mr Anthony (Tony) Alford with respect to due diligence activities. Included in acquisition costs for FY17 was an amount of \$146,000 with respect of these services that was due and payable as at 30 June 2017.

# DIRECTORS' DECLARATION

This Directors' report is signed in accordance with a resolution of Directors made pursuant to s.298 (2) of the *Corporations Act 2001*.

RETAIL FOOD GROUP LIMITED

A handwritten signature in blue ink, appearing to read 'Colin Archer', is written over the company name.

Mr Colin Archer  
Chairman and Independent Non-Executive Director

Southport  
31 August 2018

# AUDITOR'S INDEPENDENCE DECLARATION



## *Auditor's Independence Declaration*

As lead auditor for the audit of Retail Food Group Limited for the year ended 30 June 2018, I declare that to the best of my knowledge and belief, there have been:

- (a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and
- (b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Retail Food Group Limited and the entities it controlled during the period.

A handwritten signature in black ink, appearing to read 'Steven Bosiljevac', with a long horizontal stroke extending to the right.

Steven Bosiljevac  
Partner  
PricewaterhouseCoopers

Brisbane  
31 August 2018

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# CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

## FOR THE YEAR ENDED 30 JUNE 2018

Consolidated	Notes	FY18 \$'000	FY17 \$'000
<b>Continuing operations</b>			
Revenue from sale of goods	2	297,719	245,873
Cost of sales	5	(218,832)	(167,772)
<b>Gross profit</b>		<u>78,887</u>	<u>78,101</u>
Other revenue	2	76,315	103,422
Other gains and losses	5	(1,705)	6,102
Selling expenses		(11,095)	(10,167)
Marketing expenses		(6,565)	(2,501)
Occupancy expenses		(32,521)	(7,952)
Administration expenses		(40,645)	(25,680)
Operating expenses		(44,977)	(25,660)
Finance costs	3	(12,877)	(9,560)
Other expenses	5	(385,047)	(18,492)
<b>(Loss)/profit before income tax</b>		<u>(380,230)</u>	<u>87,613</u>
Income tax benefit/(expense)	4	73,537	(25,686)
<b>(Loss)/profit for the year from continuing operations</b>	5	<u>(306,693)</u>	<u>61,927</u>
<b>Other comprehensive (loss), net of tax</b>			
<b>Items that may be reclassified subsequently to profit or loss</b>			
Exchange difference on translation of foreign operations	21	(267)	(241)
Changes in the fair value of cashflow hedges	21	268	(1,762)
Income tax relating to these items	21	(80)	529
<b>Other comprehensive (loss) for the year, net of tax</b>		<u>(79)</u>	<u>(1,474)</u>
<b>Total comprehensive (loss)/income for the year</b>		<u>(306,772)</u>	<u>60,453</u>
<b>(Loss)/profit is attributable to:</b>			
Equity holders of the parent		<u>(306,693)</u>	<u>61,927</u>
<b>Total comprehensive (loss)/income is attributable to:</b>			
Equity holders of the parent		<u>(306,772)</u>	<u>60,453</u>
<b>Earnings per share</b>			
<b>From continuing operations:</b>			
Basic (cents per share)	7	(169.5)	35.7
Diluted (cents per share)	7	(169.5)	35.7

The consolidated statement of profit or loss and other comprehensive income should be read in conjunction with the accompanying notes.

# CONSOLIDATED STATEMENT OF FINANCIAL POSITION

## AS AT 30 JUNE 2018

Consolidated	Notes	FY18 \$'000	FY17 \$'000
<b>Current assets</b>			
Cash and cash equivalents	8	16,498	10,269
Trade and other receivables	9	50,325	83,392
Other financial assets	10	15,639	9,481
Inventories	11	24,568	28,451
Current tax assets	4	7,337	-
Other	12	6,719	3,215
Assets classified as held for sale	13	9,362	-
<b>Total current assets</b>		<b>130,448</b>	<b>134,808</b>
<b>Non-current assets</b>			
Trade and other receivables	9	785	2,423
Other financial assets	10	8,334	14,260
Property, plant and equipment	14	64,625	95,554
Intangible assets	15	364,063	668,926
Deferred tax assets	4	32,255	13,657
<b>Total non-current assets</b>		<b>470,062</b>	<b>794,820</b>
<b>Total assets</b>		<b>600,510</b>	<b>929,628</b>
<b>Current liabilities</b>			
Trade and other payables	16	71,352	69,816
Borrowings	19	264,207	722
Current tax liabilities	4	-	2,546
Provisions	17	18,443	7,422
Other	18	3,980	10,747
Liabilities classified as held for sale	13	3,769	-
<b>Total current liabilities</b>		<b>361,751</b>	<b>91,253</b>
<b>Non-current liabilities</b>			
Borrowings	19	49	249,248
Derivative financial instruments	25	1,547	1,810
Deferred tax liabilities	4	64,187	119,433
Provisions	17	13,245	393
Other	18	1,691	2,319
<b>Total non-current liabilities</b>		<b>80,719</b>	<b>373,203</b>
<b>Total liabilities</b>		<b>442,470</b>	<b>464,456</b>
<b>Net assets</b>		<b>158,040</b>	<b>465,172</b>
<b>Equity</b>			
Issued capital	20	428,640	402,472
Reserves	21	9	106
Retained earnings	22	(270,609)	62,594
<b>Total equity</b>		<b>158,040</b>	<b>465,172</b>

The consolidated statement of financial position should be read in conjunction with the accompanying notes.

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

## FOR THE YEAR ENDED 30 JUNE 2018

Consolidated	Notes	Fully Paid Ordinary Shares	Other Reserves	Retained Earnings	Total
		\$'000	\$'000	\$'000	\$'000
<b>Balance as at 1 July 2016</b>		324,072	1,495	50,555	376,122
Profit for the year		-	-	61,927	61,927
Other comprehensive income		-	(1,474)	-	(1,474)
<b>Total comprehensive income</b>		-	(1,474)	61,927	60,453
Issue of ordinary shares	20	78,780	-	-	78,780
Share issue costs	20	(543)	-	-	(543)
Related income tax	20	163	-	-	163
Payment of dividends	23	-	-	(49,888)	(49,888)
Recognition of share-based payments		-	85	-	85
<b>Balance at 30 June 2017</b>		<b>402,472</b>	<b>106</b>	<b>62,594</b>	<b>465,172</b>
<b>Balance at 1 July 2017</b>		<b>402,472</b>	<b>106</b>	<b>62,594</b>	<b>465,172</b>
Loss for the year		-	-	(306,693)	(306,693)
Other comprehensive (loss)/income		-	(79)	-	(79)
<b>Total comprehensive (loss)/income</b>		-	(79)	(306,693)	(306,772)
Issue of ordinary shares	20	26,503	-	-	26,503
Share issue costs	20	(477)	-	-	(477)
Related income tax	20	142	-	-	142
Payment of dividends	23	-	-	(26,510)	(26,510)
Recognition of share-based payments	21	-	(18)	-	(18)
<b>Balance at 30 June 2018</b>		<b>428,640</b>	<b>9</b>	<b>(270,609)</b>	<b>158,040</b>

The consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

# CONSOLIDATED STATEMENT OF CASH FLOWS

## FOR THE YEAR ENDED 30 JUNE 2018

Consolidated	Notes	FY18 \$'000	FY17 \$'000
<b>Cash flows from operating activities</b>			
Receipts from customers		565,701	456,000
Payments to suppliers and employees		(535,203)	(361,329)
Interest and other costs of finance paid		(9,603)	(9,416)
Income taxes paid		(10,051)	(21,460)
<b>Net cash provided by operating activities</b>	8	<u>10,844</u>	<u>63,795</u>
<b>Cash flows from investing activities</b>			
Interest received		968	801
Repayment of advances to other entities		2,106	-
Amounts advanced to other entities		(469)	(5,696)
Payments for property, plant and equipment		(22,856)	(30,650)
Proceeds from sale of property, plant and equipment		6,867	163
Payments for intangible assets		(668)	(537)
Payments for business (net of cash acquired)		(7,631)	(67,195)
<b>Net cash used in investing activities</b>		<u>(21,683)</u>	<u>(103,114)</u>
<b>Cash flows from financing activities</b>			
Proceeds from issues of shares and other equity securities	20	21,973	35,600
Proceeds from borrowings		145,500	189,500
Repayment of borrowings		(127,000)	(149,500)
Dividends paid		(21,980)	(42,888)
Payment for share issue costs		(472)	(543)
Payment for debt issue costs		(894)	(223)
<b>Net cash provided by financing activities</b>		<u>17,127</u>	<u>31,946</u>
<b>Net (decrease)/increase in cash and cash equivalents</b>		6,324	(7,336)
Effects of exchange rate changes on cash and cash equivalents		(36)	(37)
Cash and cash equivalents at the beginning of year		9,583	16,956
<b>Cash and cash equivalents at end of year</b>	8	<u>15,871</u>	<u>9,583</u>

The above consolidated statement of cash flows should be read in conjunction with the accompanying notes.

# NOTES TO THE FINANCIAL STATEMENTS

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# NOTES TO THE FINANCIAL STATEMENTS

## Results for the year

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### 1. Segment information

#### 1.1 Description of segments and principal activities

AASB 8 Operating Segments requires operating segments to be identified on the basis of internal reports about components of the Group that are reviewed regularly by the Chief Operating Decision Makers (CODMs), in order to allocate resources to the segments and to assess their performance.

For management purposes, the Group is organised into five major operating divisions. These divisions are the basis upon which the Group reports its primary segment information. The Group's reportable segments under AASB 8 are as follows:

- Bakery/Café Division (incorporating Michel's Patisserie, Donut King and Brumby's Bakery Brand Systems);
- QSR Division (incorporating Crust Gourmet Pizza and Pizza Capers Brand Systems);
- Coffee Retail Division (incorporating Gloria Jean's Coffees, Esquires, Café2U and The Coffee Guy Brand Systems);
- Di Bella Coffee (incorporating wholesale coffee operations); and
- Commercial Food Service (incorporating procurement, warehousing, manufacturing and distribution operations).

#### 1.2 Segment information provided to the Chief Operating Decision Makers

##### Segment Revenue

Revenue from external parties reported to the CODMs is measured in a manner consistent with that in the consolidated statement of comprehensive income. Sales between segments are carried out at arm's length and are eliminated on consolidation, and identified as Inter-segment revenue as presented in Note 1.3.

##### Segment EBITDA

The CODMs assess the performance of the operating segments based on a measure of segment EBITDA.

# NOTES TO THE FINANCIAL STATEMENTS

## 1. Segment information (continued)

### 1.3 Segment revenue

Information related to the Group's operating results per segment is presented in the following table:

Segment	Bakery Cafe		OSR Systems		Coffee Retail Systems		Di Bella Coffee		Commercial Food Services		Total	
	FY18 \$'000	FY17 \$'000	FY18 \$'000	FY17 \$'000	FY18 \$'000	FY17 \$'000	FY18 \$'000	FY17 \$'000	FY18 \$'000	FY17 \$'000	FY18 \$'000	FY17 \$'000
External revenue	54,722	66,608	18,250	19,587	69,482	86,168	53,701	63,726	167,068	100,550	363,224	336,639
External revenue – Corporate stores	6,791	8,175	494	1,345	3,526	3,137	-	-	-	-	10,811	12,657
Inter-segment revenue	765	791	13	31	450	474	-	-	-	-	1,228	1,297
Segment revenue <sup>(1)</sup>	62,279	75,574	18,756	20,963	73,459	89,779	53,701	63,726	167,068	100,550	375,263	350,592
Underlying Segment EBITDA	25,267	43,720	10,927	12,962	17,109	40,786	8,071	14,219	9,983	11,780	71,357	123,467
Depreciation & amortisation												
Finance costs												
Business turnaround & restructuring costs (including acquisition & integration costs)											(13,073)	(9,338)
Impairment & provisions <sup>(2)</sup>											(12,877)	(9,561)
(Loss)/profit before tax											(402,865)	(5,200)
Income tax benefit/(expense)											(380,230)	87,613
(Loss)/profit after tax for the year											73,537	(25,686)
											(306,693)	61,927

(1) Segment revenue reconciles to total revenues from continuing operations as follows:

	FY18 \$'000	FY17 \$'000
Revenue for the period – Statutory	374,034	349,295
Inter-segment revenue: eliminated on consolidation	1,228	1,297
Total segment revenue	375,263	350,592

(2) Refer to Note 6.

For further discussion on Segment Revenues and Underlying Segment EBITDA, refer to the Operating Segment Review in the Directors' Report.

# NOTES TO THE FINANCIAL STATEMENTS

## 1. Segment information (continued)

### 1.4 Geographical information

An insignificant portion of the Group's activities are located outside of Australia, and hence, no geographical information has been disclosed.

## 2. Revenue

Consolidated	FY18 \$'000	FY17 \$'000
Revenue from the sale of goods	297,719	245,873
Revenue from the rendering of services	69,506	96,523
Initial master franchise revenue	4,988	5,188
	<u>372,213</u>	<u>347,584</u>
Interest revenue		
Bank deposits	125	109
Other loans and receivables	843	692
	<u>968</u>	<u>801</u>
Rental revenue	853	910
	<u>374,034</u>	<u>349,295</u>

## 3. Finance costs

Consolidated	FY18 \$'000	FY17 \$'000
Interest on bank overdrafts and loans	12,026	9,184
Total interest expense	<u>12,026</u>	<u>9,184</u>
Other finance costs	851	376
	<u>12,877</u>	<u>9,560</u>

## 4. Income taxes

### 4.1 Income tax recognised in profit or loss

Consolidated	FY18 \$'000	FY17 \$'000
Current tax:		
In respect of current year	246	28,796
	<u>246</u>	<u>28,796</u>
Deferred tax:		
In respect of the current year	(73,783)	(3,110)
	<u>(73,783)</u>	<u>(3,110)</u>
Total Income tax (benefit)/expense recognised in the current year relating to continuing operations	<u>(73,537)</u>	<u>25,686</u>

# NOTES TO THE FINANCIAL STATEMENTS

## 4. Income taxes (continued)

The expense for the year can be reconciled to the accounting profit as follows:

Consolidated	FY18 \$'000	FY17 \$'000
(Loss)/profit from continuing operations before income tax benefit/(expense)	(380,230)	87,613
Income tax benefit/(expense) calculated at 30% (FY17: 30%)	(114,069)	26,284
Effect of:		
Expenses that are not deductible in determining taxable profit	1,416	879
Different tax rates of subsidiaries operating in other jurisdictions <sup>(1)</sup>	(18)	(12)
Non-deductible impairment of goodwill	38,928	-
Capital loss on disposal	429	-
Non-assessable income	(255)	(1,547)
Other	32	82
Income tax (benefit)/expense recognised in profit or loss (relating to continuing operations)	(73,537)	25,686

The tax rate used for the FY18 and FY17 reconciliations is the corporate tax rate of 30% payable by Australian corporate entities on taxable profits under Australian tax law. There has been no change in the corporate tax rate when compared with the previous reporting period.

- (1) A corporate tax rate of 28% (FY17: 28%) is payable by New Zealand corporate entities, and 21% (FY17: 34%) is payable by United States of America corporate entities.

### 4.2 Income tax recognised directly in equity

Consolidated	Notes	FY18 \$'000	FY17 \$'000
Share issue costs	20	143	163
Total income tax recognised directly in equity		143	163

### 4.3 Current tax liabilities

Consolidated	FY18 \$'000	FY17 \$'000
Current tax assets	7,337	-
Current tax liabilities	-	(2,546)
	7,337	(2,546)

# NOTES TO THE FINANCIAL STATEMENTS

## 4. Income taxes (continued)

### 4.4 Deferred tax balances

Consolidated FY18	Opening balance	Recognised in profit or loss	Recognised directly in equity	Recognised in other comprehensive income	Acquisitions/ disposals	Closing balance
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Temporary differences</b>						
Intangible assets	(118,091)	54,803	-	-	-	(63,288)
Unrealised exchange differences	9	(109)	-	-	-	(100)
Employee benefits	1,515	(110)	-	-	-	1,405
Provisions	5,286	4,371	-	-	-	9,657
Doubtful debts	3,027	9,665	-	-	-	12,692
Unearned income	1,130	(309)	-	-	-	821
Share issue costs	451	(277)	143	-	-	317
Other	362	425	-	(81)	-	706
	(106,311)	68,459	143	(81)	-	(37,790)
<b>Unused tax losses and credits</b>						
Tax (losses)/credits	535	5,323	-	-	-	5,858
	535	5,323	-	-	-	5,858
	(105,776)	73,782	143	(81)	-	(31,932)

Consolidated FY17	Opening balance	Recognised in profit or loss	Recognised directly in equity	Recognised in other comprehensive income	Acquisitions/ Disposals	Closing balance
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Temporary differences</b>						
Intangible assets	(114,722)	-	-	-	(3,369)	(118,091)
Unrealised exchange differences	66	(57)	-	-	-	9
Employee benefits	972	543	-	-	-	1,515
Provisions	437	3,154	-	-	1,695	5,286
Doubtful debts	2,184	303	-	-	540	3,027
Unearned income	1,067	63	-	-	-	1,130
Share issue costs	646	(358)	163	-	-	451
Other	99	(336)	-	529	70	362
	(109,251)	3,312	163	529	(1,064)	(106,311)
<b>Unused tax losses and credits</b>						
Tax (losses)/credits	737	(202)	-	-	-	535
	737	(202)	-	-	-	535
	(108,514)	3,110	163	529	(1,064)	(105,776)

# NOTES TO THE FINANCIAL STATEMENTS

## 4. Income taxes (continued)

### 4.4 Deferred tax balances (continued)

Deferred tax balances are presented in the statement of financial position as follows:

Consolidated	FY18 \$'000	FY17 \$'000
Deferred tax assets	32,255	13,657
Deferred tax liabilities	(64,187)	(119,433)
	<u>(31,932)</u>	<u>(105,776)</u>

### 4.5 Tax consolidation

#### *Relevance of tax consolidation to the Group*

The Company and its wholly-owned Australian resident entities are part of a tax-consolidated group under Australian taxation law. The head entity within the tax-consolidated group is Retail Food Group Limited. Tax benefit/expense, deferred tax liabilities and deferred tax assets arising from temporary differences of the members of the tax-consolidated group are recognised in the separate financial statements of the members of the tax-consolidated group using the 'stand alone taxpayer' approach by reference to the carrying amounts in the separate financial statements of each entity and the tax values applying under tax consolidation. Current tax liabilities and assets and deferred tax assets arising from unused tax losses and relevant tax credits of the members of the tax-consolidated group are recognised by the Company, as head entity in the tax-consolidation group.

Due to the existence of a tax funding agreement between the entities in the tax-consolidated group, amounts are recognised as payable to or receivable by the Company and each member of the Group in relation to the tax contribution amounts paid or payable between the parent entity and the other members of the tax-consolidated group, in accordance with the arrangement.

#### *Nature of tax funding arrangements and tax sharing arrangements*

Entities within the tax-consolidation group have entered into both a tax funding agreement and a tax-sharing agreement with the head entity. Under the terms of the tax funding arrangement, Retail Food Group Limited and each of the entities in the tax-consolidated group have agreed to pay a tax equivalent payment to or from the head entity, based on the current tax liability or current tax asset of the entity.

The tax sharing agreement entered into between members of the tax-consolidated group provides for the determination of the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations or if an entity should leave the tax-consolidated group. No amounts have been recognised in the financial statements in respect of this agreement and payment of any such amounts under the tax sharing agreement is considered remote.

# NOTES TO THE FINANCIAL STATEMENTS

## 5. (Loss)/profit for the year from continuing operations

(Loss)/profit for the year from continuing operations has been arrived at after charging (crediting):

Consolidated	FY18 \$'000	FY17 \$'000
Cost of sales	218,832	167,772
Loss/(gain) on disposal of assets <sup>(2)</sup>	545	(1,943)
Write-down of inventory to net realisable value <sup>(1)</sup>	5,991	608
Write-down of property, plant and equipment <sup>(1)</sup>	17,498	189
Loss on sale of QLD properties <sup>(2)</sup>	1,446	-
Write-down of assets held for sale to fair value less costs to sell <sup>(1)</sup>	4,454	-
Impairment loss on intangible assets <sup>(1)</sup>	306,152	-
Impairment loss on trade receivables <sup>(1)</sup>	29,089	2,462
Impairment loss on loans carried at amortised cost <sup>(1)</sup>	8,003	295
Provisions for onerous leases and make good obligations <sup>(3)</sup>	22,837	-
Provisions for obsolete stock with supplier network	2,258	-
Provisions for strategic review and franchisee support costs	4,645	-
De-recognition of Marketing Fund receivables <sup>(1)</sup>	-	5,200
Contingent consideration deemed remuneration	523	462
Adjustments to contingent consideration provision <sup>(2)</sup>	(295)	(3,359)
Business turnaround and restructuring costs (including acquisition and integration costs)	21,318	11,794
Depreciation and amortisation expense:		
Depreciation of property, plant and equipment <sup>(1)</sup>	11,203	7,762
Amortisation of acquired intangible assets - customer contracts <sup>(1)</sup>	1,581	1,376
Amortisation - other <sup>(1)</sup>	289	200
Total depreciation and amortisation expense	13,073	9,338
Employee benefits expenses:		
Post-employment benefits (defined contribution plans)	6,219	5,194
Other employee benefits (wages and salaries)	87,308	72,195
Total employee benefits expense	93,527	77,389

(1) Amounts are included in other expenses in the consolidated statement of profit or loss and other comprehensive income.

(2) Amounts are included in other gains and losses in the consolidated statement of profit or loss and other comprehensive income.

(3) Amounts are included in occupancy expenses in the consolidated statement of profit of loss and other comprehensive income.

# NOTES TO THE FINANCIAL STATEMENTS

## 6. Impairment & provisions

The financial performance of the Group was significantly impacted in FY18 by challenging retail market trading conditions, especially within increasingly competitive shopping centre locations, negative market sentiment towards franchising and RFG in particular, the cumulative impact of 2H17/1H18 outlet closures, and internal challenges in the management of RFG's business model.

Additionally, the market capitalisation of the Group reduced significantly in FY18 to circa \$98.7m, based on the closing share price at 30 June 2018, indicating the carrying value of the net assets of the Group may be impaired as compared to its market capitalisation.

Therefore, the Group has performed an assessment for assets that may be impaired, in accordance with Australian Accounting Standards, which has resulted in the Group recognising a \$402.9 million pre-tax (\$320.9 million post-tax) expense for impairment and provisions as follows:

Consolidated	Impairment and provisions \$'000
Trade and other receivables	(29,089)
Inventory	(5,991)
Other financial assets	(8,003)
Other assets	(116)
Assets held for sale	(4,454)
Property, plant & equipment	(17,498)
Intangible assets	(306,152)
Trade and other payables	(1,711)
Provisions	(29,852)
<b>Pre-tax Total</b>	<b>(402,866)</b>
Current tax benefit	6,652
Increase in deferred tax assets	19,669
Decrease in deferred tax liabilities	55,610
<b>Post-tax Total</b>	<b>(320,935)</b>

### Trade and other receivables

A \$29.1 million pre-tax (\$20.4 million post-tax) provision has been recognised in respect of individually impaired domestic franchise receivables where the Group has determined that the credit quality of the trade receivable has changed. The impairment recognised represents the difference between the carrying amount of these trade receivables and the present value of the estimated recoverable amount.

The remaining \$40.1 million of trade receivables include amounts that are past due at the end of the reporting period but against which the Group has not recognised an allowance for doubtful debtors (refer to Note 9.2) because there has not been a significant change in credit quality and the amounts are still considered recoverable.

### Inventory

An amount of \$6.0 million pre-tax (\$4.2 million post-tax) has been expensed through 'other expenses' in respect of inventory write-downs relating to the following:

- \$4.6 million pre-tax (\$3.2 million post-tax) write-downs of company-owned stores and equipment held for resale considered to no longer be recoverable; and
- \$1.4 million pre-tax (\$1.0 million post-tax) write-downs of slow moving and obsolete stock, and discontinued brand-related stock.

### Other financial assets

A \$8.0 million pre-tax (\$5.6 million post-tax) provision has been recognised in respect of individually impaired loans receivable. The impairment recognised represents the difference between the carrying amount of these loan receivables and the present value of the estimated recoverable amount.

### Assets held for sale

An amount of \$4.5 million pre-tax (\$3.1 million post-tax) impairment has been recognised on properties held for sale located in Yatala and Molendinar, QLD. The impairment recognised represents the difference between the carrying amount of the property and the fair value based on independent valuations.

# NOTES TO THE FINANCIAL STATEMENTS

## 6. Impairment & provisions (continued)

### Property, plant & equipment

An amount of \$17.5 million pre-tax (\$12.3 million post-tax) has been recognised in respect of write-downs of property, plant and equipment relating to discontinued projects and redundant systems and assets (refer to Note 14).

### Intangibles

The Group conducted detailed impairment testing of each of its cash generating units (CGUs).

A \$306.2 million pre-tax (\$253.2 million post-tax) impairment was recognised in respect of the following:

- The Gloria Jean's (\$90.1 million), Michel's Patisserie (\$59.2 million), Brumby's Bakeries (\$22.7 million), Pizza Capers (\$4.5 million) and Cafe2U (\$1.1 million) Brand Networks;
- Goodwill of the Coffee Retail Division (\$46.9 million), Bakery/Cafe Division (\$24.0 million), Food Services Division (\$47.7 million), and Di Bella Division (\$9.6 million); and
- Write-down of customer contracts relating to the Caffitaly distribution agreement (\$0.4 million).

The impairment recognised represents the difference between the carrying values of the CGUs and their recoverable amounts. The key assumptions and methodology behind the assessment of impairment of CGUs is more particularly detailed in Note 15.

### Trade and other payables

A \$1.7 million pre-tax (\$1.2 million post-tax) expense has been recognised for payables in respect of franchisee-focused initiatives.

### Provisions

An amount of \$29.9 million pre-tax (\$20.9 million post-tax) has been recognised in respect of provisions for the following:

- Onerous leases and associated make-goods for stores where the Group is the head on the lease and which have been assessed as high risk of closure (\$22.8 million);
- A provision for strategic review and franchisee support costs (\$4.8 million); and
- A commitment to reimburse the Group's supplier network for slow and obsolete stock (\$2.3 million).

# NOTES TO THE FINANCIAL STATEMENTS

## 7. Earnings per share

Consolidated	FY18 \$'000	FY17 \$'000
<b>Basic earnings per share</b>		
From continuing operations	<u>(169.5)</u>	<u>35.7</u>
	<u>(169.5)</u>	<u>35.7</u>
<b>Diluted earnings per share</b>		
From continuing operations	<u>(169.5)</u>	<u>35.7</u>
	<u>(169.5)</u>	<u>35.7</u>

### 7.1 Basic earnings per share

The earnings and weighted average number of ordinary shares used in the calculation of basic earnings per share are as follows:

Consolidated	FY18 \$'000	FY17 \$'000
(Loss)/profit for the year	<u>(306,693)</u>	<u>61,927</u>
Earnings used in the calculation of basic EPS from continuing operations	<u>(306,693)</u>	<u>61,927</u>

Consolidated	2018 No. '000	2017 No. '000
Weighted average number of ordinary shares for the purpose of basic EPS	<u>180,951</u>	<u>173,441</u>

### 7.2 Diluted earnings per share

The earnings and weighted average number of ordinary shares used in the calculation of diluted earnings per share are as follows:

Consolidated	FY18 \$'000	FY17 \$'000
(Loss)/profit for the year	<u>(306,693)</u>	<u>61,927</u>
Earnings used in the calculation of diluted EPS from continuing operations	<u>(306,693)</u>	<u>61,927</u>

Consolidated	2018 No. '000	2017 No. '000
Weighted average number of ordinary shares for the purpose of basic EPS	180,951	173,441
Adjustments for calculation of diluted EPS:		
Performance rights	-	16
Weighted average number of ordinary shares for purpose of diluted EPS	<u>180,951</u>	<u>173,457</u>

#### Performance rights:

Performance rights granted to employees under the Performance Rights Plan are considered to be potential ordinary shares. These have not been included in the calculation of diluted earnings per share because potential ordinary shares that would reduce a loss per share are not considered to be dilutive.

# NOTES TO THE FINANCIAL STATEMENTS

## Operations

### Assets and liabilities

#### 8. Cash and cash equivalents

##### 8.1 Reconciliation to Consolidated Statement of Cash Flows

For the purposes of the consolidated statement of cash flows, cash and cash equivalents includes cash on hand and in banks and investments in money market instruments, net of outstanding bank overdrafts. Cash and cash equivalents at the end of the reporting year as shown in the consolidated statement of cash flows can be reconciled to the related items in the consolidated statement of financial position as follows:

Consolidated	FY18 \$'000	FY17 \$'000
Cash and bank balances	16,498	10,269
Less: cash not available for use	(627)	(686)
	<u>15,871</u>	<u>9,583</u>

##### 8.2 Cash balances not available for use

Cash balances not available for use relate to unclaimed dividends. As at 30 June 2018, cash balances not available for use totalled \$627 thousand (2017: \$686 thousand). These restricted cash balances have not been included in the period end cash balances for the purposes of the consolidated statement of cash flows.

##### 8.3 Financing facilities

At 30 June 2018, the Group had unused facilities as detailed in the following table. Subsequent to the year end, the Group renegotiated its financing arrangements, resulting in a reduction in the financing facilities. Further details can be found in Notes 19, 25 and 30.

The Group expects to meet its other obligations from operating cash flows and proceeds of maturing financial assets.

Consolidated	FY18 \$'000	FY17 \$'000
Secured bank loan facility:		
Amount used (before deducting debt issue costs)	265,000	246,500
Amount unused	44,000	87,500
	<u>309,000</u>	<u>334,000</u>
Secured ancillary bank facilities (guarantees):		
Amount used	3,407	3,282
Amount unused	593	718
	<u>4,000</u>	<u>4,000</u>
Secured ancillary bank facilities (asset finance):		
Amount used	92	117
Amount unused	2,408	883
	<u>2,500</u>	<u>1,000</u>
Secured ancillary bank facilities (supply chain finance):		
Amount used	788	2,538
Amount unused	3,212	1,462
	<u>4,000</u>	<u>4,000</u>
Secured ancillary bank facilities (overdraft):		
Amount used	-	-
Amount unused	1,000	1,000
	<u>1,000</u>	<u>1,000</u>

# NOTES TO THE FINANCIAL STATEMENTS

## 8. Cash and cash equivalents (continued)

### 8.4 Reconciliation of (loss)/profit for the year to net cash flows from operating activities

Consolidated	FY18 \$'000	FY17 \$'000
(Loss)/profit for the year	(306,693)	61,927
Depreciation of non-current assets	11,203	7,762
Amortisation	1,870	1,576
Amounts invoiced to marketing funds written off	75	-
Impairment loss on loans carried at amortised cost	8,003	5,496
Writedown inventory to net realisable value	5,991	608
Writedown of property, plant and equipment	17,498	189
Impairment loss on intangible assets	306,152	-
Impairment loss on assets held for sale	4,454	-
Non-cash employee benefits expense-share based payments	(18)	85
Net foreign exchange gain	24	(130)
Interest income	(968)	(801)
Loss/(gain) on sale of PPE	545	(1,943)
Loss on sale of QLD properties	1,446	-
Non cash - vendor loan	(324)	(2,446)
Non cash interest expense	3,350	376
Contingent consideration deemed remuneration	523	462
Adjustments to contingent consideration provision	(295)	(3,359)
Increase/(decrease) in Current tax liability	(9,883)	7,107
Increase/(decrease) in Deferred tax balances	(74,003)	(3,117)
Movements in working capital:		
(Increase)/decrease in Trade and other receivables	30,666	(14,286)
(Increase)/decrease in Inventories	(7,849)	(1,489)
(Increase)/decrease in Other assets	(3,504)	(535)
Increase/(decrease) in Trade and other payables	(170)	7,583
Increase/(decrease) in Provisions	23,523	(463)
Increase/(decrease) in Other liabilities	(772)	(807)
Net cash generated by operating activities	10,844	63,795

### 8.5 Non-cash investing and financing activities

Acquisition of property, plant and equipment by means of finance leases was nil (FY17: \$3.8 million).

### 8.6 Debt reconciliation

Changes in Liabilities for which cash flows are classified as financing activities in the statement of cash flows:

Consolidated	Current bank loans \$'000	Current borrowing costs \$'000	Non-current bank loans \$'000	Non-current borrowing costs \$'000
Balance at 1 July 2017	-	-	246,500	(726)
Repayment of borrowings	-	-	(127,000)	-
Proceeds from borrowings	-	-	145,500	-
Payment for debt issue costs	-	-	-	(894)
Amortisation of deferred borrowing costs	-	-	-	807
Other non-cash movements	265,000	(813)	(265,000)	813
Balance at 30 June 2018	265,000	(813)	-	-

# NOTES TO THE FINANCIAL STATEMENTS

## 9. Trade and other receivables

### 9.1 Trade receivables

Consolidated	FY18 \$'000	FY17 \$'000
<b>Current</b>		
Trade receivables	71,248	81,286
Allowance for doubtful debts	(31,101)	(10,094)
	<u>40,147</u>	<u>71,192</u>
Accrued income	5,076	5,897
Sundry debtors	2,714	1,754
Other	1,778	4,549
Goods and services tax (GST) receivable	610	-
	<u>50,325</u>	<u>83,392</u>
<b>Non-Current</b>		
Trade receivables	-	1,582
Sundry debtors	658	280
Other	127	561
	<u>785</u>	<u>2,423</u>
	<u>51,110</u>	<u>85,815</u>

Trade receivables disclosed in this table are classified as loans and receivables and are therefore measured at amortised cost.

The average credit period on sales of goods and rendering of services is 30 days and no interest is charged. The Group has recognised an allowance for the estimated irrecoverable trade receivable amounts arising from the past sale of goods and rendering of services, determined by reference to past default experience.

Trade receivables disclosed in this table include amounts (disclosed in the following table) that are past due at the end of the reporting period but against which the Group has not recognised an allowance for doubtful debtors because there has not been a significant change in credit quality and the amounts are still considered recoverable. The Group holds collateral over the majority of these balances in the form of the franchised outlets.

Trade receivables under formal or contractual payment arrangements have been reclassified to Other financial assets and the comparative period financial statements have been restated.

### 9.2 Ageing of past due but not impaired receivables

Consolidated	FY18 \$'000	FY17 \$'000
31 – 60 days	3,973	3,121
61 – 90 days	1,654	1,729
91 + days	4,170	13,972
	<u>9,797</u>	<u>18,822</u>

# NOTES TO THE FINANCIAL STATEMENTS

## 9. Trade and other receivables (continued)

### 9.3 Movement in the allowance for doubtful debts

Consolidated	FY18 \$'000	FY17 \$'000
Balance at the beginning of the year	10,094	8,001
Reclassification to other receivables	147	43
Amounts acquired through business combinations	-	1,892
Impairment losses recognised on receivables	29,089	2,462
Amounts written off as uncollectable	(8,229)	(2,304)
Balance at the end of the year	<u>31,101</u>	<u>10,094</u>

In determining the recoverability of a trade receivable, the Group considers any change in the credit quality of the trade receivable from the date credit was initially granted up to the end of the reporting period. The concentration of credit risk is limited due to the customer base being large and unrelated. Accordingly, the Directors consider that there is no further credit provision required in excess of the allowance for doubtful debts.

The allowance for doubtful debts includes individually impaired trade receivables amounting to \$31.1 million (FY17: \$10.1 million). The impairment recognised represents the difference between the carrying amount of these trade receivables and the present value of the estimated recoverable amount.

### 9.4 Ageing of impaired trade receivables

Consolidated	FY18 \$'000	FY17 \$'000
0 – 30 days	2,538	479
31 – 60 days	976	873
61 – 90 days	1,107	590
91 + days	26,480	8,152
	<u>31,101</u>	<u>10,094</u>

# NOTES TO THE FINANCIAL STATEMENTS

## 10. Other financial assets

Consolidated	FY18 \$'000	FY17 \$'000
<b>Current</b>		
Loans and receivables carried at amortised cost		
Vendor finance <sup>(1)</sup>	5,206	5,159
Inventory held on behalf of third party <sup>(2)</sup>	8,553	2,232
Other <sup>(3)</sup>	1,880	2,090
	<u>15,639</u>	<u>9,481</u>
<b>Non-Current</b>		
Loans and receivables carried at amortised cost		
Vendor finance <sup>(1)</sup>	5,822	11,458
Other <sup>(3)</sup>	2,512	2,802
	<u>8,334</u>	<u>14,260</u>
	<u>23,973</u>	<u>23,741</u>

(1) Vendor finance represents funding provided to franchisees for the purpose of acquiring a franchised outlet or undertaking refurbishment, and are primarily secured by the franchised outlet, including the business and shop fittings, with guarantors as co-signatories to the loan agreement. These loan receivables are undertaken at arm's length and can be interest bearing. Recoverability of these loan receivables are assessed on the same basis as trade receivables (Note 9). These balances include individually impaired loan receivables amounting to \$11.2 million (FY17: \$2.3 million). The impairment recognised represents the difference between the carrying amount of these loan receivables and the present value of the estimated recoverable amount.

(2) Inventory held on behalf of third party represents inventory processed or manufactured on behalf of a third party.

(3) Other represents all trade receivables under formal or contractual payment arrangements. The receivables under these repayment arrangements have been reclassified from Trade receivables to Other financial assets and the comparative period financial statements have been restated.

# NOTES TO THE FINANCIAL STATEMENTS

## 11. Inventories

Consolidated	FY18 \$'000	FY17 \$'000
Stock held for wholesale supply	24,173	25,144
Equipment held for resale	211	819
Stores held for resale	184	2,488
	<u>24,568</u>	<u>28,451</u>

The cost of inventories recognised as an expense during the period in respect of continuing operations was \$218.8 million (FY17: \$167.8 million). Additionally, an amount of \$6.0 million has been expensed in the year (FY17: \$608 thousand) in respect of write-downs of stores held for resale to their assessed net realisable value.

## 12. Other assets

Consolidated	FY18 \$'000	FY17 \$'000
<b>Current</b>		
Prepayments	<u>6,719</u>	<u>3,215</u>

## 13. Assets classified as held for sale

Consolidated	FY18 \$'000	FY17 \$'000
<b>Assets classified as held for sale</b>		
Land and Buildings <sup>(1)</sup>	8,880	-
Equipment <sup>(2)</sup>	<u>482</u>	<u>-</u>
	<u>9,362</u>	<u>-</u>
<b>Liabilities classified as held for sale</b>		
Finance lease liability <sup>(3)</sup>	<u>(3,769)</u>	<u>-</u>
	<u>5,593</u>	<u>-</u>

(1) In August 2017, the Directors approved the sale of land and buildings located at Yatala, QLD. Subsequent to 30 June 2018, the Group entered into a sale contract with settlement expected to occur in September 2018. A loss of \$1.2 million has been recognised on the measurement of fair value less costs to sell at 30 June 2018. This amount is included in other expenses in the consolidated statement of profit or loss and other comprehensive income.

In February 2018, the Directors approved the sale of lands and buildings located at Molendinar, QLD. The Group expects a sale transaction to be completed by 30 June 2019. A loss of \$3.2 million has been recognised on the measurement of fair value less costs to sell at 30 June 2018. This amount is included in other expenses in the Consolidated Statement of Profit or Loss and Other Comprehensive Income.

(2) The Group approved the sale of coffee roasting machines and related equipment. The Group is actively looking for a buyer and expects a sale transaction to be completed by 30 June 2019.

(3) The Group has a finance lease liability associated with the land and buildings disposal group. The liability will be settled as part of the expected sale transaction. The lease liability has been classified as short term liability associated with assets classified as held for sale.

# NOTES TO THE FINANCIAL STATEMENTS

## 14. Property, plant and equipment

Consolidated	Notes	Land & buildings at cost	Leasehold improvements at cost	Plant & equipment at cost	Motor vehicles at cost	Total
		\$'000	\$'000	\$'000	\$'000	\$'000
<b>Gross carrying amount</b>						
Balance as at 1 July 2016		13,453	1,480	49,173	1,000	65,106
Additions		8,529	117	25,087	834	34,567
Disposals		-	(26)	(2,136)	(129)	(2,291)
Reclassification of inventories		-	-	(1,005)	(146)	(1,151)
Effect of movements in exchange rates		-	(1)	(77)	-	(78)
Acquisitions	28	-	1,484	18,066	982	20,532
<b>Balance as at 1 July 2017</b>		<b>21,982</b>	<b>3,054</b>	<b>89,108</b>	<b>2,541</b>	<b>116,685</b>
Additions		2,038	266	19,553	551	22,408
Disposals		(6,806)	(13)	(4,507)	(158)	(11,484)
Reclassification of inventories		-	-	(543)	-	(543)
Fair value adjustment	28	-	-	(1,293)	-	(1,293)
Assets classified as held for sale	13	(12,978)	-	(837)	-	(13,815)
Effect of movements in exchange rates		-	(4)	111	-	107
<b>Balance as at 30 June 2018</b>		<b>4,236</b>	<b>3,303</b>	<b>101,592</b>	<b>2,934</b>	<b>112,065</b>
<b>Accumulated depreciation</b>						
Balance as at 1 July 2016		(599)	(513)	(12,722)	(166)	(14,000)
Reclassification of inventories		-	-	247	2	249
Disposals		-	7	471	93	571
Depreciation charge		(174)	(192)	(7,105)	(291)	(7,762)
Impairment losses		-	-	(189)	-	(189)
<b>Balance as at 1 July 2017</b>		<b>(773)</b>	<b>(698)</b>	<b>(19,298)</b>	<b>(362)</b>	<b>(21,131)</b>
Reclassification of inventories		-	-	(235)	-	(235)
Disposals		565	6	2,041	15	2,627
Depreciation charge		(29)	(252)	(10,462)	(460)	(11,203)
Impairment losses		(3,999)	-	(13,300)	(199)	(17,498)
<b>Balance as at 30 June 2018</b>		<b>(4,236)</b>	<b>(944)</b>	<b>(41,254)</b>	<b>(1,006)</b>	<b>(47,440)</b>
<b>Net book value</b>						
As at 30 June 2017		21,209	2,356	69,810	2,179	95,554
As at 30 June 2018		-	2,359	60,338	1,928	64,625

# NOTES TO THE FINANCIAL STATEMENTS

## 15. Intangible assets

### 15.1 Intangible assets

Consolidated	Notes	Indefinite Life			Finite Life	Total
		Goodwill	Brand Networks	Intellectual Property Rights	Other	
		\$'000	\$'000	\$'000	\$'000	\$'000
<b>Gross carrying amount</b>						
		207,143	429,188	5,337	3,650	645,318
Balance as at 1 July 2016						
Additions		-	350	-	187	537
Reclassification		-	(218)	-	-	(218)
Acquisitions through business combinations	28	63,404	-	-	11,230	74,634
Exchange differences		(10)	(15)	-	-	(25)
<b>Balance as at 1 July 2017</b>		<b>270,537</b>	<b>429,305</b>	<b>5,337</b>	<b>15,067</b>	<b>720,246</b>
<b>Additions</b>						
		-	200	-	538	738
Acquisitions through business combinations	28	2,603	-	-	-	2,603
Exchange differences		(133)	(38)	-	-	(171)
<b>Balance as at 30 June 2018</b>		<b>273,007</b>	<b>429,467</b>	<b>5,337</b>	<b>15,605</b>	<b>723,416</b>
<b>Accumulated amortisation</b>						
		-	(48,894)	-	(900)	(49,794)
Balance as at 1 July 2016						
Amortisation expense		-	-	-	(1,526)	(1,526)
<b>Balance as at 1 July 2017</b>		<b>-</b>	<b>(48,894)</b>	<b>-</b>	<b>(2,426)</b>	<b>(51,320)</b>
<b>Amortisation expense</b>						
		-	-	-	(1,881)	(1,881)
Impairment losses recognised in profit or loss		(128,256)	(177,418)	-	(478)	(306,152)
<b>Balance as at 30 June 2018</b>		<b>(128,256)</b>	<b>(226,312)</b>	<b>-</b>	<b>(4,785)</b>	<b>(359,353)</b>
<b>Net book value</b>						
As at 30 June 2017		270,537	380,411	5,337	12,641	668,926
As at 30 June 2018		144,751	203,155	5,337	10,820	364,063

### 15.2 Overview

An intangible asset's recoverable value is the greater of its value in use and its fair value less costs of disposal.

For intangible assets with a finite life, if there are indicators that the intangible asset's recoverable value has fallen below its carrying value, an impairment test is performed and a loss is recognised for the amount by which the carrying value exceeds the asset's recoverable value.

Intangible assets that have an indefinite useful life, such as brand systems, intellectual property rights and goodwill, are tested annually for impairment, or more frequently, where there is an indication that the carrying amount may not be recoverable.

The financial performance of the Group was significantly impacted in FY18 by challenging retail market trading conditions, especially within increasingly competitive shopping centre locations, negative market sentiment towards franchising and RFG in particular, the cumulative impact of 2H17/1H18 outlet closures, and internal challenges in the management of RFG's business model.

Additionally, the market capitalisation of the Group reduced significantly in FY18 to circa \$98.7m, based on the closing share price at 30 June 2018, indicating the carrying value of the net assets of the Group may be impaired as compared to its market capitalisation.

In assessing the carrying value of RFG's Brand Systems, the Directors have taken a conservative approach, basing their assessment and subsequent impairment position to reflect both the Group's expected FY19 sustainable earnings and the risk profile inherent in RFG's current challenges. The outcome of this assessment was an impairment charge of \$306.2 million pre-tax.

# NOTES TO THE FINANCIAL STATEMENTS

## 15. Intangible assets (continued)

### 15.3 Assessment of cash-generating units

#### *Indefinite and finite life intangible assets*

There are a total of ten CGU's in existence, with eight CGU's attributable to the operation of the Group's Brand Systems, the ninth CGU attributable to the coffee roasting business, and the tenth CGU attributable to the commercial food services business.

These is also a tenth cash generating unit attributable to the commercial business to which finite intangible assets allocated.

#### *Goodwill*

Goodwill is monitored by management at the level of the five operating segments identified in Note 1.1 and is allocated to cash generating units, or groups of units, expected to benefit from synergies arising from the acquisition giving rise to the goodwill.

### 15.4 Allocation of goodwill to cash-generating units

A summary of the goodwill allocated to each operating segment is presented below:

Goodwill allocation	FY18 \$'000	FY17 \$'000
Bakery/Café Systems	52,864	76,864
OSR Systems	25,092	25,092
Coffee Retail Systems	18,436	65,367
Di Bella Coffee	30,067	39,810
Commercial Food Services	18,292	63,404
	<u>144,751</u>	<u>270,537</u>

### 15.5 Allocation of indefinite life intangible assets to cash-generating units

A summary of the indefinite life assets allocated to each operating segment is presented below:

Indefinite life intangibles allocation	FY18 \$'000	FY17 \$'000
Donut King Brand System	36,201	36,186
Brumby's Bakeries Brand System	30,797	53,480
Michel's Patisserie Brand System	23,062	82,234
Pizza Capers Gourmet Kitchens Brand System (PC)	8	4,384
Crust Gourmet Pizza Bars Brand System (CGP)	43,097	43,040
The Coffee Guy Brand System	919	957
Café2U Brand System	8,168	9,252
Gloria Jeans Brand System	51,969	141,960
Di Bella Coffee	14,271	14,255
	<u>208,492</u>	<u>385,748</u>

# NOTES TO THE FINANCIAL STATEMENTS

## 15. Intangible assets (continued)

### 15.6 Impairment losses and recoverable amounts

During the year to 30 June 2018, impairment losses totalling \$306.2 million pre-tax (\$253.2 million post tax) have been recognised in respect of the following cash-generating units.

The recoverable amounts of each of these cash-generating units for which an impairment was recognised are also presented below:

Cash-generating unit	Impairment charge	Recoverable amount
<i>Brands</i>		
Brumby's Bakeries	\$22.7m	\$28.7m
Michel's Patisserie	\$59.2m	\$19.5m
Pizza Capers	\$4.5m	\$0.1m
Café 2U	\$1.1m	\$8.1m
Gloria Jeans	\$90.1m	\$58.4m
Di Bella Coffee	\$0.4m	\$52.0m
<i>Goodwill</i>		
Bakery/Café	\$24.0m	\$107.2m
Coffee Retail	\$46.9m	\$67.5m
Di Bella Coffee	\$9.6m	\$51.0m
Commercial Food Services	\$47.7m	\$61.2m

The Group has experienced a decrease in Brand System revenue during the year predominantly attributable to lower planned store commissioning and outlet growth. Additionally, the share price and market capitalisation of the Group declined significantly during the year. Accordingly the Group has performed assessment of the recoverable amount of goodwill and intangible assets and recognised the impairment charges identified above.

### 15.7 Key assumptions used for calculating recoverable amounts

#### *Goodwill*

The recoverable amount of each group of cash generating units (operating segments) to which goodwill is allocated has been determined by reference to a fair value less costs of disposal calculation. The valuation technique adopted was an income based approach by using a discounted cash-flow model. Since the key assumptions and estimates are significant unobservable inputs, this is classified as a level 3 fair value. The discounted cash-flow is based on the following key assumptions and estimates:

#### Year 1 cash-flows

Year 1 cash-flows are based on management's expectations of future performance, specifically incorporating the planned reduction in domestic franchise outlets previously referred to and the cash-flows expected to be incurred associated with these closures.

#### Annual cash-flow growth

The cash-flows in year's two to five are based on management's expectation of cash-flows following the store closure program and the expected normalised, like for like growth in a reduced domestic store network.

#### Terminal growth

An indefinite terminal growth rate of 2% has been applied to all cash-flows to extrapolate these beyond the five year budget period. This rate is consistent with long term industry growth rates.

#### Discount Rates

The following post-tax discount rates have been applied to reflect the specific risks within each operating segment.

Cash-generating unit	Discount rate
Bakery/Café	12.18%
QSR Systems	10.58%
Coffee Retail Systems	12.18%
Di Bella Coffee	11.08%
Commercial Food Services	11.17%

The expected costs of disposal for each segment are deducted from the recoverable amount to determine fair value less costs of disposal.

#### *Identifiable intangible assets*

The recoverable amount of each intangible asset with an indefinite useful life has been determined by reference to a value in use calculation based on the following key assumptions and estimates:

#### Year 1 cash-flows

Year 1 cash-flows are based on management's expectations of future performance, specifically incorporating the planned reduction in domestic franchise outlets previously referred to and the cash-flows expected to be incurred associated with these closures.

# NOTES TO THE FINANCIAL STATEMENTS

## 15. Intangible assets (continued)

### 15.7 Key assumptions used for calculating recoverable amounts (continued)

#### Annual cash-flow growth

The cash-flows in year's two to five are based on management's expectation of cash-flows following the store closure program and the expected normalised, like for like growth in a reduced domestic store network.

#### Terminal growth

An indefinite terminal growth rate of 2% has been applied to all cash-flows to extrapolate these beyond the five year budget period. This rate is consistent with long term industry growth rates.

#### Discount Rates

The following pre-tax discount rates have been applied to reflect the specific risks within each cash-generating unit:

Cash-generating unit	Discount rate
Donut King Brand System	16.89%
Brumby's Bakeries Brand System	16.99%
Michel's Patisserie Brand System	16.88%
Crust Gourmet Pizza Bars Brand System	14.56%
Pizza Capers Brand System	17.03%
The Coffee Guy Brand System	16.16%
Café 2U Brand System	16.68%
Gloria Jeans Brand System	16.68%
Di Bella Coffee Brand System	15.08%

#### Significant estimate: Impact of reasonably possible changes in key assumptions

The recoverable amounts in respect of those cash-generating units against which an impairment loss has been recognised continue to be highly sensitive to a range of assumptions, in particular the growth rates in the cash-flow forecasts.

#### Identifiable intangible assets

With the exception of the Donut King and The Coffee Guy cash-generating unit's, impairment charges have been taken on all other brand systems cash-generating units.

#### Goodwill

With the exception of the OSR cash-generating unit, impairment charges have been taken on all cash-generating units to which goodwill is allocated during the year.

Accordingly, any downwards movement in the growth rate underpinning the calculation of the recoverable amounts of those cash-generating units where an impairment charge has been recognised will result in further impairment. The growth rate assumptions for these cash-generating units were:

Cash-generating unit	Average growth rate years 2 - 5
<i>Brands</i>	
Brumby's Bakeries	1.0%
Michel's Patisserie	0.8%
Pizza Capers	0.0%
Café 2U	1.1%
Gloria Jeans	1.1%
<i>Goodwill</i>	
Bakery/Café	0.9%
Coffee Retail	1.1%
Di Bella Coffee	2.6%
Commercial Food Services	1.1%

The following table outlines the headroom, growth rates and sensitised growth rates which would trigger impairment in the following cash-generating units that are also sensitive to a reasonably possible movement in the growth rate:

Cash-generating unit	Headroom	Average growth rate years 2 - 5	Average growth rate years 2 - 5 to trigger impairment
<i>Brands</i>			
Crust Gourmet Pizza Bars	\$15.4m	1.1%	(3.0%)
<i>Goodwill</i>			
OSR	\$5.1m	1.1%	(3.0%)

# NOTES TO THE FINANCIAL STATEMENTS

## 16. Trade and other payables

Consolidated	FY18 \$'000	FY17 \$'000
<b>Current</b>		
Trade payables <sup>(1)</sup>	51,410	57,629
Accruals and other creditors	19,942	11,469
Goods and services tax (GST) payable	-	718
	<u>71,352</u>	<u>69,816</u>

(1) The average credit period on purchases is 30 days. The Group has financial risk management policies in place to ensure that all payables are paid within the credit time frame.

The carrying amounts of trade and other payables are considered to be the same as their fair values, due to their short-term nature.

## 17. Provisions

Consolidated	FY18 \$'000	FY17 \$'000
<b>Current</b>		
Employee benefits	4,554	6,340
Onerous leases and make-good	7,166	650
Other provisions	6,723	432
	<u>18,443</u>	<u>7,422</u>
<b>Non-Current</b>		
Employee benefits	131	393
Onerous lease and make-good	13,114	-
	<u>13,245</u>	<u>393</u>
	<u>31,688</u>	<u>7,815</u>

Consolidated	Employee benefits	Onerous Leases and Make-Good	Other
	\$'000	\$'000	\$'000
Balance at 1 July 2017	6,733	650	432
Movement in provisions	2,653	22,837	6,723
Payments made	(4,701)	(3,207)	(432)
Balance at 30 June 2018	<u>4,685</u>	<u>20,280</u>	<u>6,723</u>

# NOTES TO THE FINANCIAL STATEMENTS

## 18. Other liabilities

Consolidated	FY18 \$'000	FY17 \$'000
<b>Current</b>		
Retention bonds and deposits	1,662	2,098
Unearned income	2,068	2,016
Other (contingent consideration) <sup>(1)</sup>	250	6,633
	<u>3,980</u>	<u>10,747</u>
<b>Non-Current</b>		
Retention bonds and deposits	55	53
Unearned income	1,542	1,934
Other (contingent consideration) <sup>(1)</sup>	94	332
	<u>1,691</u>	<u>2,319</u>
	<u>5,671</u>	<u>13,066</u>

(1) Other liabilities represent the estimated fair value of the contingent consideration relating to the acquisition of Hudson Pacific Corporation.

### Contingent consideration

The fair value of contingent consideration arising in a business combination is calculated using the income approach based on the expected payment amounts and their associated probabilities. When appropriate, it is discounted to present value.

# NOTES TO THE FINANCIAL STATEMENTS

## Capital

### 19. Borrowings

Consolidated	FY18 \$'000	FY17 \$'000
<b>Secured at amortised cost</b>		
<b>Current</b>		
Finance lease liabilities <sup>(1)</sup>	-	679
Bank loans <sup>(2)</sup>	265,000	-
Equipment loans	20	43
Borrowing costs (deferred)	(813)	-
	<u>264,207</u>	<u>722</u>
<b>Secured at amortised cost</b>		
<b>Non-Current</b>		
Finance lease liabilities <sup>(1)</sup>	-	3,400
Bank loans	-	246,500
Equipment loans	49	74
Borrowing costs (deferred)	-	(726)
	<u>49</u>	<u>249,248</u>
	<u>264,256</u>	<u>249,970</u>

(1) During the period, the Group classified a finance lease liability of \$3.8 million as a short term liability associated with assets held for sale. For further details see Note 13.

(2) As at 30 June 2018, the Group's total gross debt increased to \$273.9 million, including ancillary facilities. The increase in gross debt was predominately due to the timing of working capital cash flows, continued investment in property, plant and equipment and acquisition earn out payments for the Di Bella and Hudson Pacific Corporation acquisitions attended to during FY18.

In December 2017, the Group extended its three-year debt facilities totalling \$150 million, due to mature in December 2018, into longer dated maturities expiring in January 2020 and December 2020. In addition, RFG reduced the existing debt facilities, maturing in December 2020, by \$25 million.

During June 2018, the Group identified a breach of debt covenants for the testing period ended 30 June 2018. The Group received a waiver from its senior debt lenders on 29 June 2018, for testing of financial covenants for the period ended 30 June 2018. The waiver received by the Group from its lenders was subject to a number of conditions and, as a result, the external borrowings of the Group have been classified as current as the Group did not have unconditional right to defer payment for at least 12 months.

Subsequent to 30 June 2018, the Company further negotiated its financial covenants attaching to the Group's debt facilities that support the Group's restructuring plans with its senior debt lenders. Agreement has been reached between the Company and its lenders, subject to formal documentation of amendments to the debt facility agreements, to reset the covenants effective from 31 August 2018 for covenant testing periods commencing 1 July 2018.

The key terms of the covenant reset are:

Financial covenants and conditions	Revised 31 August 2018	Previous covenants
Covenant testing	Quarterly on 31 March, 30 June, 30 September and 31 December	Quarterly on 31 March, 30 June, 30 September and 31 December
Operating Leverage ratio (Secured Net Debt/EBITDA)	5.0x to December 2018; 4.5x to March 2019; 4.0x from 1 April 2019 onwards;	3.0x to December 2018; 2.5x from 1 January 2019;
Interest cover ratio	3.0x	4.0x
Gearing ratio	Covenant removed	Less than 50%
Financial Guarantor EBITDA and Assets ratios	Covenant removed	Greater than 90%
EBITDA performance to budget	Covenant removed	20% variance to budget
Mandatory prepayment – asset sales	100% of net proceeds	60% of net proceeds
Mandatory amortisation	Requirement removed	\$12.5m repayment by 2 March 2019
Total senior debt facilities	\$285 million	\$309 million
Tenor of facilities	31 October 2019	January 2020 and December 2020

In addition, the Group's restructuring program is subject to a review process with the lenders after 31 December 2018.

These revised banking arrangements will also come at an increased cost to the Group, which has been factored into future cash flows.

# NOTES TO THE FINANCIAL STATEMENTS

## 20. Issued capital

Consolidated	FY18 \$'000	FY17 \$'000
182,745,510 fully paid ordinary shares (FY17:176,736,066)	428,640	402,472
	428,640	402,472

Changes to the then Corporations Law abolished the authorised capital and par value concept in relation to share capital from 1 July 1998. Therefore, the Company does not have a limited amount of authorised capital and issued shares do not have a par value.

Consolidated	FY18 No. '000	FY18 \$'000	FY17 No. '000	FY17 \$'000
<b>Fully paid ordinary shares <sup>(1)</sup></b>				
Balance at beginning of period	176,736	402,472	164,968	324,072
Issue of ordinary shares <sup>(2)</sup>	6,009	26,503	11,768	78,780
Share issue costs	-	(477)	-	(543)
Related income tax	-	142	-	163
Balance at end of period	182,745	428,640	176,736	402,472

(1) Fully paid ordinary shares carry one vote per share and carry the right to dividends.

(2) During the period, a total of 6,009,444 ordinary shares were issued as follows:

- a. 1,015,648 shares issued on 17 October 2017 in respect of the Company's Dividend Reinvestment Plan, attributable to the payment of the final dividend for the financial year ended 30 June 2017. The issue price of the shares was \$4.47.
- b. 4,993,796 shares issued on 17 October 2017 in respect of the Company's Dividend Reinvestment Plan shortfall placement. The issue price was \$4.40.

# NOTES TO THE FINANCIAL STATEMENTS

## 21. Reserves

Equity-settled employee benefits reserve	FY18 \$'000	FY17 \$'000
Balance at beginning of year	85	-
Recognition of share-based payments	(18)	85
Balance at end of year	67	85

The equity-settled employee benefits reserve arises on the grant of rights to Directors, executives and senior executive management in accordance with the provisions of RFG's Performance Rights Plan. Amounts are transferred out of the reserve and into issued capital when the rights vest. Further information about share-based payments to employees is set out in Note 24.

Foreign Currency Translation reserve	FY18 \$'000	FY17 \$'000
Balance at beginning of year	1,254	1,495
Exchange difference on translation of foreign operations	(267)	(241)
Balance at end of year	987	1,254

Foreign currency translation reserve represents foreign exchange differences on monetary items receivable from or payable to a foreign operation for which settlement is neither planned or likely to occur.

Hedging reserve	FY18 \$'000	FY17 \$'000
Balance at beginning of year	(1,233)	-
Changes in the fair value of cashflow hedges	268	(1,762)
Deferred tax	(80)	529
Balance at end of year	(1,045)	(1,233)

The hedging reserve is used to record gains or losses on derivatives that are designated and qualify as cash flow hedges and that are recognised in other comprehensive income, as described in Note 35.10. Amounts are reclassified to profit or loss when the associated hedged transaction affects profit or loss.

Total Reserves 9                      106

## 22. Retained earnings

Consolidated	Notes	FY18 \$'000	FY17 \$'000
Balance at beginning of year		62,594	50,555
Net (loss)/profit attributable to members of the parent entity		(306,693)	61,927
Dividends provided for or paid	23	(26,510)	(49,888)
Balance at end of year		(270,609)	62,594

# NOTES TO THE FINANCIAL STATEMENTS

## 23. Dividends

Company	FY18		FY17	
	Cents per share	Total \$'000	Cents per share	Total \$'000
<b>Declared and paid during the financial year</b>				
Fully paid ordinary shares				
Final dividend - fully franked at 30% tax rate <sup>[1]</sup>	15.00	26,510	14.50	23,920
Interim dividend - fully franked at 30% tax rate <sup>[2]</sup>	-	-	14.75	25,968
	<u>15.00</u>	<u>26,510</u>	<u>29.25</u>	<u>49,888</u>
<b>Declared after the end of the financial year</b>				
Fully paid ordinary shares				
Final dividend - fully franked at 30% tax rate <sup>[3]</sup>	-	-	15.00	26,510

(1) In respect of the financial year ended 30 June 2017, as detailed in the Directors' Report for that financial year, a final dividend of 15.00 cents per share, based on 176,736,066 shares on issue at 29 August 2017, franked to 100% at 30% corporate income tax rate, was paid on 17 October 2017. The final dividend was approved by the Directors on 29 August 2017 and, therefore, was not provided for in the Company's financial report. It was resolved that the 2017 final dividend would constitute an eligible dividend for the purpose of the Company's Dividend Reinvestment Plan. The issue price of the shares was \$4.47.

(2) The Directors resolved not to declare an interim dividend in FY18.

(3) The Directors have resolved that no final dividend will be paid in respect of FY18.

Company	FY18 \$'000	FY17 \$'000
Adjusted franking account balance	<u>57,575</u>	<u>61,581</u>

# NOTES TO THE FINANCIAL STATEMENTS

## 24. Share-based payments

### 24.1 Performance Rights Plan

Currently, the Group has a long term incentive scheme under a Performance Rights Plan. The Performance Rights Plan was approved by Directors in August 2015 for commencement in the financial year ending 30 June 2016. Under the Group's Long Term Incentive Plan, the Performance Rights Plan, rights will only vest if performance conditions pertaining to the earnings per share (EPS) growth and relative total shareholder return (TSR) are met and the employee is still employed at the end of the vesting period.

Participation in the plan is at the Board's absolute discretion and no individual has a contractual right to participate in the plan. Once vested, a participant will be deemed to have automatically exercised all vested performance rights and the Company will settle its obligation in line with the Performance Rights Plan.

There is no consideration payable by the participant upon exercising of vested performance rights. Upon vesting, the conversion of a performance right to an equity or cash based settlement is determined using a formula referencing the relevant share price of the Company and the number of rights exercised, and is at the Board's sole discretion.

The Performance Rights are divided into three (3) equal tranches, with each respective tranche having a 12 month performance period aligned to successive financial years.

Each tranche of rights is dependent on satisfaction of two discrete performance measures:

1. Earnings per Share (EPS) representing 50% of each tranche (EPS Measure); and
2. Relative Total Shareholder Return (TSR) representing 50% of each tranche (TSR Measure).

Performance rights granted under the Performance Rights Plan carry no rights to dividends and no voting rights.

The following table summarises the Performance Rights granted under the plan:

	Number of Performance Rights		
	Tranche 1	Tranche 2	Tranche 3
<b>As at 30 June 2016</b>	-	-	-
Granted during the year	65,613	65,613	65,613
Forfeited during the year	(30,247)	(18,584)	(10,684)
<b>As at 30 June 2017</b>	<b>35,366</b>	<b>47,029</b>	<b>54,929</b>
Granted during the year	-	-	-
Forfeited during the year	(35,366)	(47,029)	(42,683)
<b>As at 30 June 2018</b>	<b>-</b>	<b>-</b>	<b>12,246</b>

Performance Rights outstanding at the end of the year have the following expiry dates and base prices:

Grant Date	Expiry Date	Base Price	Performance Rights Issued FY17
14 July 2016	1 July 2018	\$5.61	-
14 July 2016	1 July 2019	\$5.61	12,246
1 December 2016	1 July 2019	\$6.19	-
			<b>12,246</b>

### 24.2 Executive Share Option Plan

In accordance with the provisions of the executive share option plan, as at 30 June 2018, Directors, executives and senior employees have options over nil ordinary shares (FY17: nil).

Share options granted under the executive share option plan carry no rights to dividends and no voting rights.

In FY18 the Directors approved a replacement Rights Plan (Replacement Plan) in connection with future long term incentive remuneration. No Performance Rights have been granted under this plan as at 30 June 2018.

# NOTES TO THE FINANCIAL STATEMENTS

## Risk

### 25. Financial instruments

#### 25.1 Capital risk management

The Group undertakes to manage its capital to ensure that entities in the Group will be able to continue on a going concern basis, while maximising the return to stakeholders through the optimisation of the debt and equity balance.

During June 2018, the Group identified a breach of covenant would arise in respect of the leverage ratio requirements for the testing period ended 30 June 2018. As disclosed in the Directors report under the heading Financial Position, and Notes 19 and 35.1(d), the Group received a waiver from its senior debt lenders on 29 June 2018 for testing financial covenants for the period ended 30 June 2018. As disclosed in note 19, this waiver was conditional upon a number of items, requiring that the Group's debt is classified as current at 30 June 2018.

Subsequent to 30 June 2018, the Group further negotiated its financial covenants attaching to the Group's debt facilities that support the Group's restructuring plans with its senior debt lenders. The Group has clear plans to reduce debt and manage the capital base through a combination of turnaround strategies, including improving the performance of its business operations, consideration of asset sales and a plan for a market recapitalisation when the business performance has stabilised.

The capital structure of the Group consists of net debt (borrowings disclosed in Note 19, offset by cash and cash equivalents) and equity of the Group (comprising issued capital, reserves and retained earnings, as disclosed in Notes 20, 21 and 22).

The Group is not subject to any externally imposed capital requirements.

Operating cash flows are used to maintain and expand the Group's assets, as well as to make the routine outflows of tax and repayment of debt. The Group's policy is to borrow centrally, using a variety of capital market issues and borrowing facilities, to meet anticipated funding requirements.

#### 25.2 Gearing ratio

The Group's Board and management review the capital structure on an annual basis. As a part of this review, the Board and management consider the cost of capital and the risks associated with each class of capital. The Group previously held a target gearing ratio of 40% to 60% as the proportion of net debt to equity.

The gearing ratio of 159.6% at the end of the reporting period, is well outside the target gearing ratio range, attributable to the significant decline in earnings experienced in FY18, and significant asset impairments recognised in the financial year.

The Group has clear plans to reduce debt and manage the capital base through a combination of turnaround strategies, including improving the performance of its business operations, consideration of asset sales and a plan for a market recapitalisation when the business performance has stabilised. The Group will advise a revised gearing ratio target at completion of the planned debt reduction and market recapitalisation activities.

The gearing ratio at the end of the reporting period is presented in the following table:

Consolidated	FY18 \$'000	FY17 \$'000
Debt <sup>(1)</sup>	268,025	249,970
Cash and bank balances	(15,871)	(9,583)
Net debt	252,154	240,387
Equity <sup>(2)</sup>	158,040	465,170
Gearing ratio	159.6%	51.7%

(1) Debt is defined as long and short term borrowings, net of deferred borrowing costs (excluding derivatives and financial guarantee contracts), as described in Note 19.

(2) Equity includes all capital and reserves of the Group that are managed as capital.

# NOTES TO THE FINANCIAL STATEMENTS

## 25. Financial instruments (continued)

### 25.3 Categories of financial instruments

Consolidated	FY18 \$'000	FY17 \$'000
<b>Financial assets</b>		
Loans and receivables		
Trade and other receivables	51,110	85,815
Other financial assets	23,973	23,741
Cash and cash equivalents	16,498	10,269
<b>Financial liabilities</b>		
Trade payables	51,410	57,629
Other payables	19,942	12,187
Retention bonds and deposits	1,717	2,151
Contingent consideration	344	6,965
Loans (at amortised cost)	264,256	249,970
Derivative financial instruments	1,547	1,810
Liabilities classified as held for sale	3,769	-

### 25.4 Financial risk management objectives

The Group's finance department co-ordinates access to domestic and international financial markets, monitors and manages the financial risks relating to the operations of the Group in line with the Group's policies. These risks include market risk (including currency risk, fair value interest rate risk and price risk), credit risk, liquidity risk and cash flow interest rate risk.

The Group's senior executive management team reports to the Board on a monthly basis in relation to the risks and policies implemented to mitigate risk exposure.

### 25.5 Derivatives

Derivatives are only used for economic hedging purposes and not as speculative investments. However, where derivatives do not meet the hedging criteria, they are classified as 'held for trading' for accounting purposes. The Group has the following derivative financial instruments:

	FY18 \$'000	FY17 \$'000
<b>Non-current liabilities</b>		
Interest rate swap contracts - cash flow hedges	1,547	1,810
Total non-current derivative financial instrument liabilities	1,547	1,810

### 25.6 Market risk

The Group's activities expose it primarily to the financial risk of changes in foreign currency exchange rates (refer Note 25.8) and interest rates (refer Note 25.7).

At a Group level, market risk exposures are measured using sensitivity analysis.

### 25.7 Interest rate risk management

The Group is exposed to interest rate risk as it borrows funds at variable (floating) interest rates. Hedging activities are evaluated regularly to align with interest rate views and defined risk appetite ensuring optimal hedging strategies are applied, by either positioning the balance sheet or protecting interest rate expense through different interest rate cycles.

During FY17, the Group enhanced its interest rate risk management measures via entering into fixed interest rate contracts covering an additional \$150 million of gross debt with a 3.0 - 4.0 year maturity profile. The fixed interest rate contracts were taken out to hedge the interest rate risk of associated movements in the Bank Bill Swap Benchmark (BBSW), and the Group considers these derivatives to be effective hedges in accordance with AASB 139 *Financial Instruments: Recognition and Measurement*. The hedged interest payment transactions are expected to impact profit monthly between 1 and 3 years from the reporting date. The swaps are expected to be highly effective and therefore no hedge ineffectiveness has been recognised in the profit or loss in the year ended 30 June 2018.

At 30 June 2018, the Group's weighted average interest rate is 5.67% and total debt at fixed interest rates is \$150 million.

# NOTES TO THE FINANCIAL STATEMENTS

## 25. Financial instruments (continued)

### 25.7 Interest rate risk management (continued)

#### Interest rate sensitivity analysis

The following sensitivity analysis has been determined based on the exposure to interest rates for both derivative and non-derivative instruments at the end of the reporting period. For floating rate liabilities, the analysis is prepared assuming the amount of the liability outstanding at the end of the reporting period was outstanding for the whole year. A 100 basis point increase or decrease is used when reporting interest rate risk internally to Key Management Personnel and represents Management's assessment of the possible change in interest rates.

Sensitivity	Impact on post-tax profit		Impact on other components of equity	
	2018 \$'000	2017 \$'000	2018 \$'000	2017 \$'000
Interest rates - increase by 100 basis points (1%)	(805)	(965)	2,384	3,274
Interest rates - decrease by 100 basis points (1%)	805	965	(2,384)	(3,274)

### 25.8 Foreign exchange risk

The Group undertakes transactions denominated in foreign currencies; consequently, exposures to exchange rate fluctuations arise.

The carrying amounts of the Group's foreign currency denominated monetary assets and monetary liabilities at the end of the reporting period are as follows:

Exposure	Assets		Liabilities	
	FY18 \$'000	FY17 \$'000	FY18 \$'000	FY17 \$'000
US Dollar	16,497	14,764	1,744	3,652
Euro	723	1,648	343	2,472
New Zealand Dollar	2,817	4,462	614	451

#### Foreign currency sensitivity analysis

The following table summarises the Group's sensitivity to a 10% increase and decrease in the Australian Dollar against the relevant foreign currencies. 10% is the sensitivity rate used when reporting foreign currency risk internally to Key Management Personnel and represents management's assessment of the reasonably possible change in foreign exchange rates.

Impact of Sensitivity to Profit or Loss	FY18		FY17	
	10%	-10%	10%	-10%
US Dollar	(939)	1,147	(707)	864
Euro	(24)	30	52	(65)
New Zealand Dollar	(140)	171	(255)	312
Total increase/(decrease)	(1,103)	1,348	(910)	1,111

# NOTES TO THE FINANCIAL STATEMENTS

## 25. Financial instruments (continued)

### 25.9 Credit risk management

Credit risk refers to the risk that the counterparty will default on its contractual obligations resulting in financial loss to the Group. The Group has adopted a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral, where appropriate, as a measure of mitigating the risk of financial loss from defaults. Credit exposure is reviewed continually.

Trade receivables consist of a large number of unrelated customers. Ongoing credit evaluation is performed on the financial conditions of accounts receivable and, where appropriate, additional collateral is obtained for balances identified as "at risk". Often this collateral is in the form of franchised outlets.

The credit risk on liquid funds and derivative financial instruments is limited because the counterparties are banks with high credit ratings, assigned by international credit rating agencies.

Except as detailed in the following table, the carrying amount of financial assets recognised in the financial statements, which is net of any allowances for losses, represents the Group's maximum exposure to credit risk without taking account of the value of any collateral obtained:

Financial assets and other credit exposures	FY18 \$'000	FY17 \$'000
<b>Contingent liabilities</b>		
Financial guarantees	814	814
Rental guarantees	3,407	3,282
Letters of credit	788	2,538
	<u>5,009</u>	<u>6,634</u>

### 25.10 Liquidity risk management

Ultimate responsibility for liquidity risk management rests with the Board, which has established an appropriate liquidity risk management framework for the management of the Group's short, medium and long-term funding and liquidity management requirements. The Group manages liquidity risk by maintaining adequate cash reserves, banking facilities and undrawn borrowing facilities, by continuously monitoring forecast and actual cash flows, and matching the maturity profiles of financial assets and liabilities. Note 8.3 sets out details of additional undrawn facilities that the Group had at 30 June 2018. Note 19 sets out details of the Group's borrowings at 30 June 2018, and also revised facilities and covenants with respect to these borrowings, agreed with the lenders subsequent to year end. The reduction in undrawn facilities subsequent to year end increases liquidity risk of the Group.

# NOTES TO THE FINANCIAL STATEMENTS

## 25. Financial instruments (continued)

### 25.10 Liquidity risk management (continued)

#### Liquidity and interest rate risk tables

The following table details the Group's remaining contractual maturity for its financial liabilities with agreed repayment periods. The information has been presented based on the non-discounted cash flows of financial liabilities, using the earliest date on which the Group can be required to pay. The table includes both interest and principal cash flows. To the extent that interest cash flows are at floating rates, the non-discounted amount is derived from forward interest rate curves at the end of the reporting period.

Consolidated	Weighted	Less than 1 year	1 – 5 years	Over 5 years	Total
	average effective interest rate				
	%	\$'000	\$'000	\$'000	\$'000
<b>FY18</b>					
<b>Non-derivatives</b>					
Trade payables	-	51,409	-	-	51,409
Other payables	-	19,942	-	-	19,942
Retention bonds and deposits	-	3,980	1,691	-	5,671
Bank loans	5.7	298,217	-	-	298,217
Equipment loans	6.0	20	49	-	69
Contingent consideration	-	250	94	-	344
Finance lease liabilities <sup>(1)</sup>	6.8	540	2,699	1,620	4,859
Rental guarantee contracts	0.3	3,407	-	-	3,407
Financial guarantee contracts	-	814	-	-	814
Letters of credit	0.3	788	-	-	788
		<u>379,367</u>	<u>4,533</u>	<u>1,620</u>	<u>385,520</u>
<b>Derivatives</b>					
<b>Interest rate swaps</b>					
- (inflow)	1.9	(2,899)	(4,045)	-	(6,944)
- outflow	2.5	3,618	5,126	-	8,744
		<u>719</u>	<u>1,081</u>	<u>-</u>	<u>1,800</u>
<b>FY17</b>					
<b>Non-derivatives</b>					
Trade payables	-	57,629	-	-	57,629
Other payables	-	12,187	-	-	12,187
Retention bonds and deposits	-	2,098	53	-	2,151
Bank loans	3.7	9,117	257,715	-	266,832
Equipment loans	6.0	43	74	-	117
Contingent consideration	-	6,633	332	-	6,965
Finance lease liabilities	7.0	702	3,049	1,460	5,211
Rental guarantee contracts	0.3	3,282	-	-	3,282
Financial guarantee contracts	-	814	-	-	814
Letters of credit	0.3	2,538	-	-	2,538
		<u>95,043</u>	<u>261,223</u>	<u>1,460</u>	<u>357,726</u>
<b>Derivatives</b>					
<b>Interest rate swaps</b>					
- (inflow)	1.7	(2,505)	(6,001)	-	(8,506)
- outflow	2.5	3,680	8,925	-	12,605
		<u>1,175</u>	<u>2,924</u>	<u>-</u>	<u>4,099</u>

(1) Finance lease liability is expected to be settled within a year together with assets classified as held for sale.

The maximum amount the Group could be forced to settle under the rental and financial guarantee contracts, if the fully guaranteed amount is claimed by the counterparty to the guarantee, is \$4.2 million (FY17: \$4.1 million).

# NOTES TO THE FINANCIAL STATEMENTS

## 25. Financial instruments (continued)

### 25.10 Liquidity risk management (continued)

#### Liquidity and interest rate risk tables (continued)

The following table details the Group's expected maturity for its non-derivative financial assets. The information has been presented based on the non-discounted contractual maturities of the financial assets, including interest that will be earned on those assets. The inclusion of information on non-derivative financial assets is necessary in order to understand the Group's liquidity risk management, as the liquidity is managed on a net asset and liability basis.

Consolidated	Weighted	Less than 1 year	1 – 5 years	Total
	average effective interest rate			
	%	\$'000	\$'000	\$'000
<b>FY18</b>				
Cash and cash equivalents	-	16,498	-	16,498
Loans and receivables	-	66,146	9,346	75,492
		<u>82,644</u>	<u>9,346</u>	<u>91,990</u>
<b>FY17</b>				
Cash and cash equivalents	-	10,269	-	10,269
Loans and receivables	-	92,710	18,038	110,748
		<u>102,979</u>	<u>18,038</u>	<u>121,017</u>

The Group has access to financing facilities, as described in Note 8.3, of which \$51.2 million was unused at the end of the reporting period (FY17: \$91.6 million). Note 19 sets out details of the Group's borrowings at 30 June 2018, and also revised facilities and covenants with respect to these borrowings, agreed with the lenders subsequent to year end, resulting in a reduction of unused facilities available to the Group. The Group expects to meet its other obligations from operating cash flows and proceeds of maturing financial assets.

# NOTES TO THE FINANCIAL STATEMENTS

## 25. Financial instruments (continued)

### 25.11 Fair value of financial instruments

The Directors consider that the carrying amount of financial assets and financial liabilities recorded in the financial statements approximate to their fair values.

Financial instruments that are measured subsequent to initial recognition at fair value are grouped into Levels 1 to 3, based on the degree to which the fair value is observable.

#### Recognised fair value measurements

The Group did not measure any financial assets or financial liabilities at fair value on a non-recurring basis as at 30 June 2018.

**Level 1:** The fair value of financial instruments traded in active markets (such as publicly traded derivatives, and trading and available-for-sale securities) is based on quoted market prices at the end of the reporting period. The quoted market price used for financial assets held by the group is the current bid price. These instruments are included in level 1.

**Level 2:** The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined using valuation techniques which maximise the use of observable market data and rely as little as possible on entity-specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in level 2.

**Level 3:** If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3. This is the case for unlisted equity securities.

<i>Recurring fair value measurements</i> At 30 June 2018	Notes	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
<b>Financial Liabilities</b>					
Derivatives used for hedging - interest rates swaps	25.5	-	1,547	-	1,547
Contingent consideration	25.3	-	-	344	344
<b>Total financial liabilities</b>		-	1,547	344	1,891

<i>Recurring fair value measurements</i> At 30 June 2017	Notes	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
<b>Financial Liabilities</b>					
Derivatives used for hedging - interest rates swaps	25.5	-	1,810	-	1,810
Contingent consideration	25.3	-	-	6,965	6,965
<b>Total financial liabilities</b>		-	1,810	6,965	8,775

Specific valuation techniques used to value financial instruments include:

- The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows based on observable yield curves; and
- The fair value of the remaining financial instruments is determined using discounted cash flow analysis.

Consolidated	Contingent consideration payable \$'000
<b>Opening balance 1 July 2017</b>	6,965
(Gains)/losses recognised in other income	(294)
Finance costs	77
Cash payments	(6,404)
<b>Closing balance 30 June 2018</b>	344

# NOTES TO THE FINANCIAL STATEMENTS

## Group structure

### 26. Subsidiaries

Significant subsidiaries of the Group, which are those subsidiaries with contribution to the Group's net profit or net assets, are as follows:

Entity	FY18 %	FY17 %	Entity	FY18 %	FY17 %
Addiction Holdings Pty Ltd <sup>(2)</sup>	100	100	Gloria Jean's Coffees International China*	100	100
Adonai International Unit Trust <sup>(2)</sup>	100	100	Gloria Jean's Coffees International Pty Limited*	100	100
Associated Foodservice Distributors Pty Ltd <sup>(2)</sup>	100	100	Gloria Jeans's Coffees International (UK) Pty Ltd*	100	100
Associated Smallgoods Distributors Pty. Ltd. <sup>(2)</sup>	100	100	Gloria Jeans's Coffees UK Limited*	100	100
Bakery Fresh Pty Ltd <sup>(2)</sup>	100	100	Gloria Jeans's Gourmet Coffees Corp. (GJ Stores, GJ Ecommerce)*	100	100
BB's Cafe System Pty Ltd <sup>(2)</sup>	100	100	Gloria Jean's Gourmet Coffees Franchising Corp (GJ Franchising, GJ Ad Fund, GJ Gift Card)*	100	100
bb's New Zealand Limited <sup>Δ</sup>	100	100	Gourmet Foods Australia Pty Limited <sup>(2)</sup>	100	100
BDP Franchise Pty Ltd <sup>(2)</sup>	100	100	HDCZ (NZ) Limited <sup>Δ</sup>	100	100
BDP System Pty Ltd <sup>(2)</sup>	100	100	Hot Dog Construction Zone (Aust) Pty Ltd <sup>(2)</sup>	100	100
Booming Pty Ltd <sup>(2)</sup>	100	100	Hudson Pacific Corporation Pty Ltd <sup>(2)</sup>	100	100
Brumby's Bakeries Corporate Retail Division Pty Ltd <sup>(2)</sup>	100	100	International Franchisor Pty Ltd <sup>(2)</sup>	100	100
Brumby's Bakeries Holdings Pty Ltd <sup>(2)</sup>	100	100	Jireh Group Pty Limited <sup>(2)</sup>	100	100
Brumby's Bakeries Pty Ltd <sup>(2)</sup>	100	100	Jireh International Retail Pty Limited <sup>(2)</sup>	100	100
Brumby's Bakeries System (NZ) Limited <sup>Δ</sup>	100	100	Jireh International Unit Trust <sup>(2)</sup>	100	100
Brumby's Bakeries System Pty Ltd <sup>(2)</sup>	100	100	Jonamill Pty. Limited <sup>(2)</sup>	100	100
Cafe2U (NZ) Limited <sup>Δ</sup>	100	100	Maranatha Import Export India Private Limited*	100	100
Cafe2U International Pty. Ltd. <sup>(2)</sup>	100	100	MEMGMT Pty Ltd <sup>(2)</sup>	100	100
Cafe2U Pty Limited <sup>(2)</sup>	100	100	Michel's Patisserie (S.A.) Pty. Limited <sup>(2)</sup>	100	100
Caffe Coffee (NZ) Limited <sup>Δ</sup>	100	100	Michel's Patisserie (VO) Pty Ltd <sup>(2)</sup>	100	100
Caper Construction Pty Ltd <sup>(2)</sup>	100	100	Michel's Patisserie (VOL) Pty Ltd <sup>(2)</sup>	100	100
Capercorp Pty Ltd <sup>(2)</sup>	100	100	Michel's Patisserie (W.A.) Pty. Limited <sup>(2)</sup>	100	100
Capers Gourmet Kitchen Pty Ltd <sup>(2)</sup>	100	100	Michel's Patisserie Corporate Retail Division Pty Ltd <sup>(2)</sup>	100	100
CGP (NZ) Limited <sup>Δ</sup>	100	100	Michel's Patisserie Management Pty Ltd <sup>(2)</sup>	100	100
CGP Systems Pty Ltd <sup>(2)</sup>	100	100	Michel's Patisserie Operations Pty Ltd <sup>(2)</sup>	100	100
Coffee Houses CRD Pty Ltd <sup>(2)</sup>	100	100	Michel's Patisserie System Pty Ltd <sup>(2)</sup>	100	100
Dairy Country Pty Ltd <sup>(2)</sup>	100	100	Michel's Patisserie Systems (NZ) Limited <sup>Δ</sup>	100	100
DBC Services Pty Ltd <sup>(2)</sup>	100	100	Mules Enterprises Pty Ltd <sup>(2)</sup>	100	100
DCM System Pty Ltd <sup>(2)</sup>	100	100	Patisserie Delights Pty Ltd <sup>(2)</sup>	100	100
Di Bella Coffee Domestic GJC Supply Pty Ltd previously Jireh International and Warehouse Distribution Pty. Limited <sup>(2)</sup>	100	100	Pizza Capers Franchise Pty Ltd (formally PCGK Holdings Pty Ltd) <sup>(2)</sup>	100	100
Di Bella Coffee International Network Supply Pty Ltd previously Gloria Jean's Coffees Supply Pty Limited <sup>(2)</sup>	100	100	Pizza Corporate Retail Division Pty Ltd <sup>(2)</sup>	100	100
Di Bella Coffee Network Supply Pty Ltd previously Caffe Coffee Pty Ltd <sup>(2)</sup>	100	100	Praise IAG Franchisor, LLC (IAG Franchising, IAG Ad Fund, IAG Ecommerce)*	100	100
Di Bella Coffee Retail and Wholesale Pty Ltd previously Espresso Enterprises Pty Ltd <sup>(2)</sup>	100	100	Praise IAG Stores, LLC*	100	100
Di Bella Coffee Supply Holdings Pty Ltd previously Roasting Australia Holdings Pty. Limited <sup>(2)</sup>	100	100	Praise Operations Company, LLC*	100	100
Di Bella Coffee, LLC (previously Maranatha Import Export, LLC)*	100	100	PRCH Holdings Pty Ltd <sup>(2)</sup>	100	100
DK China Pty Ltd <sup>(2)</sup>	100	100	Regional Franchising Systems Pty Ltd <sup>(2)</sup>	100	100

# NOTES TO THE FINANCIAL STATEMENTS

## 26. Subsidiaries (continued)

Entity	FY18 %	FY17 %	Entity	FY18 %	FY17 %
Donquay Pty Limited <sup>(2)</sup>	100	100	Retail Food Group Limited <sup>(1)</sup>	100	100
Donut King (NZ) Limited <sup>Δ</sup>	100	100	Retail Food Group USA, Inc (previously Praise International North America Inc)*	100	100
Donut King Corporate Retail Division Pty Ltd <sup>(2)</sup>	100	100	RFG (NZ) Limited <sup>Δ</sup>	100	100
Donut King Franchise Pty Ltd <sup>(2)</sup>	100	100	RFG Finance Pty Ltd <sup>(2)</sup>	100	100
Donut King System Pty Ltd <sup>(2)</sup>	100	100	RFGA Equitech Pty Ltd <sup>(2)</sup>	100	100
ECH System (NZ) Limited <sup>Δ</sup>	100	100	RFGA Holdings (Aust) Pty Ltd <sup>(2)</sup>	100	100
Espresso Concepts Pty Ltd <sup>(2)</sup>	100	100	RFGA Holdings Pty Ltd <sup>(2)</sup>	100	100
Espresso Kick Pty Ltd <sup>(2)</sup>	100	100	RFGA Management Pty Ltd <sup>(2)</sup>	100	100
Esquires Coffee Houses System Pty Ltd <sup>(2)</sup>	100	100	Roasted Addiqtion Pty Ltd <sup>(2)</sup>	100	100
Freezer Rental Pty Ltd <sup>(2)</sup>	100	100	Systems Franchisor Pty Ltd <sup>(2)</sup>	100	100
GJCI Malaysia SDN BHD*	100	100	TCG Franchising Limited <sup>Δ</sup>	100	100
Gloria Jean's Coffees Australasia Pty Limited <sup>(2)</sup>	100	100	TCG IProp Pty Ltd <sup>(2)</sup>	100	100
Gloria Jean's Coffees Holdings Pty Ltd <sup>(2)</sup>	100	100	WDM Holdings Pty Ltd <sup>(2)</sup>	100	100

All entities utilise the functional currency of the country of incorporation.

- (1) Retail Food Group Limited is the head entity within the tax consolidated group.
- (2) These companies are members of the tax consolidated Group.
- (3) All entities are incorporated in Australia unless identified with one of the following symbols:  
  - Δ New Zealand.
  - \* Other international tax jurisdictions

# NOTES TO THE FINANCIAL STATEMENTS

## 27. Parent entity disclosures

### 27.1 Financial position

Parent entity	FY18 \$'000	FY17 \$'000
<b>Assets</b>		
Current assets	7,338	41
Non-current assets	534,008	676,807
Total assets	<u>541,346</u>	<u>676,848</u>
<b>Liabilities</b>		
Current liabilities	267,077	3,266
Non-current liabilities	1,054	247,592
Total Liabilities	<u>268,131</u>	<u>250,858</u>
<b>Equity</b>		
Issued capital	428,640	402,472
Retained earnings	(154,446)	24,666
Reserves	(1,045)	(1,233)
Equity-settled employee benefits	67	85
Total equity	<u>273,216</u>	<u>425,990</u>

### 27.2 Financial performance

Parent entity	FY18 \$'000	FY17 \$'000
Profit for the year	(152,602)	30,987
Other comprehensive income	(1,045)	(1,233)
Total comprehensive income	<u>(153,647)</u>	<u>29,754</u>

### 27.3 Other Commitments

The parent entity has no contingent liabilities or expenditure commitments as at 30 June 2018 (2017: nil).

# NOTES TO THE FINANCIAL STATEMENTS

## 28. Acquisitions

### 28.1 FY17 Acquisitions

Name of businesses / intellectual property acquired	Principal activity	Date of acquisition	Total cost of acquisition	Cash cost of acquisition	Scrip cost of acquisition	Contingent cost of acquisition
			\$'000	\$'000	\$'000	\$'000
Hudson Pacific Corporation	Procurement, warehousing, manufacturing and distribution business	22 September 2016	86,394	49,493	36,178	723
Associated Foodservice Distribution Pty Ltd	Procurement, warehousing and distribution business	12 May 2017	6,252	6,252	-	-
	Total consideration:		92,646	55,745	36,178	723

#### Hudson Pacific Corporation

On 22 September 2016, the Group acquired 100% of the issued share capital of Hudson Pacific Corporation through a Sales and Purchase Agreement (SPA). The acquisition has offered significant integration opportunities and substantially increased the scale of food service activities undertaken by the Group in support of its franchise community.

This transaction was accounted for on a provisional basis using the acquisition method of accounting as at 30 June 2017, pending further assessment of identifiable intangible assets and deferred tax liabilities. These valuations have since been completed and accordingly the acquisition accounting has been finalised, resulting in a decrease in the valuation of Property, plant and equipment by \$1.3 million, a \$0.2 million increase to deferred tax liabilities and a \$0.1 million increase in intangible assets at 30 June 2018.

Details of the purchase consideration are as follows:

Consideration	\$'000
Cash	49,493
Scrip consideration	36,178
Contingent consideration	723
Total	86,394

Shares issued as scrip consideration relates to 5,379,747 shares which are held in escrow and will be released in tranches from 2017 - 2019. The fair value of these shares is based on the share price as at settlement date, discounted for the impact of the escrow terms.

Additional amounts payable contingent on key persons remaining associated with Hudson Pacific Corporation for periods of 12, 24 and 36 months have not been included in contingent consideration of the business. In accordance with the Group's accounting policy on acquisitions, the contingent payments will be recognised in profit or loss as incurred. The potential undiscounted amount payable at 30 June 2018 is \$1.0 million.

The acquired businesses' contribution of gross revenues and earnings before interest, tax, depreciation and amortisation (EBITDA) to the Group for the period from 1 July 2017 to 30 June 2018 are included in the Commercial Food Services segment note (Note 1.3) of this report.

# NOTES TO THE FINANCIAL STATEMENTS

## 28. Acquisitions (continued)

### 28.1 FY17 Acquisitions (continued)

#### Hudson Pacific Corporation (continued)

The assessment of the net assets acquired in the business combination are as follows:

Net assets acquired	Fair value on acquisition \$'000
<b>Current assets</b>	
Cash and cash equivalents	577
Trade and other receivables	25,004
Inventories	11,500
Other current assets	470
Current tax assets	106
<b>Total current assets</b>	<u>37,657</u>
<b>Non-current assets</b>	
Property, plant and equipment	18,808
Deferred tax asset	2,197
Intangible assets	11,300
<b>Total non-current assets</b>	<u>32,305</u>
<b>Total assets</b>	<u>69,962</u>
<b>Current liabilities</b>	
Trade and other payables	36,085
Provisions	4,453
<b>Total current liabilities</b>	<u>40,538</u>
<b>Non-current liabilities</b>	
Deferred tax liability	3,589
<b>Total non-current liabilities</b>	<u>3,589</u>
<b>Total liabilities</b>	<u>44,127</u>
<b>Net Assets</b>	25,835
Goodwill on acquisition of business	60,559
<b>Acquisition price</b>	<u>86,394</u>
<b>Net cash flow on acquisition</b>	<b>FY17 \$'000</b>
Total purchase consideration	86,394
Less: non-cash consideration	<u>(36,901)</u>
Consideration paid in cash	49,493
Less: Cash and cash equivalent balances acquired	<u>(577)</u>
<b>Total</b>	<u>48,916</u>

The goodwill is attributable to the profitability of the acquired business and the vertical integration synergies expected to arise from the acquisition. The goodwill will not be deductible for tax purposes.

# NOTES TO THE FINANCIAL STATEMENTS

## 28. Acquisitions (continued)

### 28.1 FY17 Acquisitions (continued)

#### Associated Foodservice

On 12 May 2017, the Group acquired 100% of the issued share capital of Associated Foodservice through a Sales and Purchase Agreement (SPA). The acquisition also offers significant integration opportunities and further increased the scale of food service activities undertaken by the Group in support of its franchise community.

This transaction was accounted for on a provisional basis using the acquisition method of accounting as at 30 June 2017, pending further assessment of identifiable intangible assets, acquisition liabilities and deferred tax liabilities. These valuations have since been completed and accordingly the acquisition accounting has been finalised, resulting in the recognition of an additional \$0.2 million of inventory provisions and \$0.4 million of make good provisions in the acquired net assets at 30 June 2018. A \$0.6 million retention payment was paid to the vendor during FY18.

Details of the purchase consideration are as follows:

Consideration	FY17 \$'000
Cash	6,252
Total	<u>6,252</u>

The acquired businesses' contribution of gross revenues and earnings before interest, tax, depreciation and amortisation (EBITDA) to the Group for the period from 1 July 2017 to 30 June 2018 are included within the Commercial Food Services segment in Note 1.3 of this report.

The net assets acquired in the business combination are as follows:

Net assets acquired	Fair value on acquisition \$'000
<b>Current assets</b>	
Cash and cash equivalents	61
Trade and other receivables	3,180
Inventories	1,116
Total current assets	<u>4,357</u>
<b>Non-current assets</b>	
Property, plant and equipment	431
Deferred tax asset	109
Total non-current assets	<u>540</u>
<b>Total assets</b>	<u>4,897</u>
<b>Current liabilities</b>	
Trade and other payables	3,743
Provisions	350
Total current liabilities	<u>4,093</u>
<b>Total liabilities</b>	<u>4,093</u>
<b>Net Assets</b>	804
Goodwill on acquisition of business	<u>5,448</u>
Acquisition price	<u>6,252</u>

# NOTES TO THE FINANCIAL STATEMENTS

## 28. Acquisitions (continued)

### 28.1 FY17 Acquisitions (continued)

#### Associated Foodservice (continued)

Net cash flow on acquisition	FY18 \$'000
Total purchase consideration	6,252
Consideration paid in cash	6,252
Less: Cash and cash equivalent balances acquired	(61)
Total	6,191

## 29. Related party transactions

Balances and transactions between the Company and its subsidiaries, which are related parties of the Company, have been eliminated on consolidation and are not disclosed in this note. Details of transactions between the Group and other related parties are disclosed in the following sections.

### 29.1 Equity interests in related parties

#### Equity interests in subsidiaries

Details of the percentage of ordinary shares held in subsidiaries are disclosed in Note 26 to the financial statements.

#### Equity interests in associates and joint ventures

There are no equity interests in associates or joint ventures.

#### Equity interests in other related parties

There are no equity interests in other related parties.

### 29.2 Transactions with Key Management Personnel

Details of all transactions with Key Management Personnel are disclosed in the Directors' Report to the financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

## Other

### 30. Events after the reporting period

Except for the subsequent agreement with its senior debt lenders to reset financial covenants, refer Borrowings, Note 19, there has not been any other matter or circumstance occurring, in the reasonable opinion of the Directors, that may significantly affect the operations of the Group, the results of those operations, or the state of affairs of the Group in future financial years.

#### Final dividend

The Directors have resolved that no final dividend will be paid in respect of FY18.

### 31. Contingent liabilities

Consolidated	FY18 \$'000	FY17 \$'000
<b>Contingent liabilities</b>		
Financial guarantee contracts <sup>(1)</sup>	814	814
Rental guarantee contracts <sup>(2)</sup>	3,407	3,282
Letters of credit	788	2,538
	<u>5,009</u>	<u>6,634</u>

(1) During FY08, RFGA Management Pty Ltd, a subsidiary of Retail Food Group Limited, guaranteed the repayment of borrowings in the amount of \$814 thousand made by the Australia and New Zealand Banking group (ANZ Bank) to selective Franchisees. The guarantees had been given as security in respect of loans made by the ANZ Bank to enable certain franchisees to commission their outlets. Each guarantee is expected to be extinguished without cost to the Group in future financial periods.

(2) The Group, through various subsidiaries, is guarantor to a number of leases occupied and licensed to franchisees. No liabilities have been recognised in relation to these rental guarantees.

#### 31.1 Other - franchisee disputation

The Group is currently in dispute with certain franchisees over minor matters. No liability has been recognised in relation to these matters as the Directors are confident that these matters will be successfully resolved.

### 32. Commitments for expenditure

Consolidated	FY18 \$'000	FY17 \$'000
Plant and equipment	<u>698</u>	<u>3,280</u>

# NOTES TO THE FINANCIAL STATEMENTS

## 33. Operating leases

### 33.1 Leasing arrangements

Operating leases relate to property leases (company stores and office premises) with lease terms of mainly five years, motor vehicle leases with lease terms of three years and office equipment leases with lease terms between two and four years. The Group does not have an option to purchase the leased asset at the expiry of the lease period.

The Group has a large number of back-to-back leases with Franchise Partners, which are contracted at substantially offsetting terms. The Group has not recognised these leases as commitments.

Future lease payment relating to back-to-back leases are \$161.7 million, of which \$147.2 million are expected to be paid by Franchise Partners. The Group has recognised a provision for onerous leases for the amount that is not expected to be recovered.

### 33.2 Amounts recognised in profit or loss

Consolidated	FY18 \$'000	FY17 \$'000
Lease expense	9,300	8,044
	<u>9,300</u>	<u>8,044</u>

### 33.3 Future minimum lease payments

Consolidated	FY18 \$'000	FY17 \$'000
Less than one year	8,806	8,066
Between one and five years	16,407	18,299
More than five years	1,822	1,252
	<u>27,035</u>	<u>27,617</u>

### 33.4 Liabilities recognised in respect of non-cancellable operating leases

Consolidated	FY18 \$'000	FY17 \$'000
Onerous leases and make-good (Note: 17)	20,280	650
	<u>20,280</u>	<u>650</u>

## 34. Remuneration of auditors

Consolidated	FY18 \$	FY17 \$
<b>Audit and other assurance services:</b>		
Audit and review of financial statements	972,050	485,000
<b>Other assurance services:</b>		
Consulting services on acquisition	-	363,187
IT review	-	36,220
<b>Taxation services:</b>		
Tax advice on acquisition	-	20,305
	<u>972,050</u>	<u>904,712</u>
<b>Other auditors</b>		
Audit and review of financial statements	39,312	20,000
	<u>39,312</u>	<u>20,000</u>

The auditor of Retail Food Group Limited in FY18 is PricewaterhouseCoopers.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies

This note provides a list of the significant accounting policies adopted in the preparation of these consolidated financial statements to the extent they have not already been disclosed in the other notes above.

### 35.1 Basis of preparation

The financial statements comprise the consolidated financial statements of the Group. For the purpose of preparing the consolidated financial statements, the Group is a for-profit entity.

These financial statements are general purpose financial statements which have been prepared in accordance with the *Corporations Act 2001*, Australian Accounting Standards and other authoritative pronouncements of the Australian Accounting Standards Board.

The nature of the operations and principal activities of the Group are described in the Directors' Report.

#### (a) Statement of compliance

The financial statements comply with Australian Accounting Standards. The financial statements also comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

The financial statements were authorised for issue by the Directors on the 31 August 2018.

#### (b) Basis of measurement

The financial statements have been prepared on the basis of historical cost, except for the revaluation of certain financial instruments. Cost is based on the fair values of the consideration given in exchange for assets. All amounts are presented in Australian Dollars, unless otherwise noted.

The Company is a company of the kind referred to in ASIC Corporations Instrument 2016/191, and, in accordance with that Corporations Instrument, amounts in the financial report are rounded off to the nearest thousand dollars, unless otherwise indicated.

#### (c) Early adoption of Accounting Standards

The Directors have elected not to early adopt Accounting Standards that are not applicable to the reporting period ended 30 June 2018.

#### (d) Going concern

These financial statements have been prepared on the basis that RFG is a going concern, able to realise assets in the ordinary course of business and settle liabilities as and when they are due.

The Group has experienced challenging operating conditions over the year and as announced with the release of its operating results for the half-year ended 31 December 2017, has instituted a restructure of its franchise brand systems networks to right-size the operation base of its respective businesses and set a course for growth in both domestic and international franchise activities. During the year ended 30 June 2018, the Group incurred a loss after income tax of \$306.7 million, which included business turnaround, restructuring costs and impairment losses of \$427.3 million as a result of the provisioning for the closure of circa 250 franchise stores and the impairment impacts arising from the revised profitability forecasts associated with the reset franchise networks going forward. The Group has a net current liability position of \$231.3 million at balance date. Despite these challenges, the Group generated a positive cashflow from operating activities of \$10.8 million and a positive Underlying EBITDA of \$71.4 million. Management and the Board are focussed on implementing the restructuring plan through FY19 and continuing to execute initiatives which are expected to boost operating earnings and reduce costs in future periods.

As referred to in Note 19 of the Financial Statements, the Group's secured syndicated loans totalling \$265 million are classified as current liabilities at the balance date. The Group had breached one of its lending covenants under its syndicated lending facility agreement at 30 June 2018. However, the Group has received a conditional waiver from the syndicate lenders. In addition, subsequent to the year end, agreement has been reached between the Company and its lenders to reset the covenants effective from 31 August 2018 for covenant testing periods commencing 1 July 2018. The Group's syndicated loan facility reduced from \$309 million to \$285 million and the maturity date was brought forward to 31 October 2019.

Despite the program to restructure the franchise businesses and build confidence in the franchise brands by consumers and potential franchise investors, there remains significant risk that the Group may breach financial covenant thresholds under its financing agreements within the next twelve months. A breach of one or more of these financial covenants may result in all the syndicated debt becoming due and payable. The continuing viability of the Group and its ability to continue as a going concern is dependent upon the Group maintaining the continuing support of the syndicated lenders, and managing the covenants and the terms of the renegotiated facility.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.1 Basis of preparation (continued)

#### (d) Going concern (continued)

Achieving this outcome also depends upon:

- (1) The Group's ability to implement successfully an asset sales program over the next twelve months to realise funds to assist in paying down the syndicated debt;
- (2) The Group's ability to obtain additional funding (by way, for example, of a capital raising or accessing alternative sources of finance);
- (3) The Group's ability to execute successfully the restructuring initiatives previously referred to.

As a result, there is a material uncertainty that may cast significant doubt on whether the Group will continue as a going concern and, therefore, whether it will realise its assets and settle its liabilities and commitments in the normal course of business and at the amounts stated in the financial report. However, the Directors, after taking into account all relevant factors, have concluded that there are reasonable grounds to believe both that the secured syndicate financiers will continue to support the Group and that the business will remain a going concern for the next twelve months.

Accordingly, the Directors have prepared the financial report on a going concern basis. As a consequence, no further adjustments have been made to the financial report relating to the recoverability and classification of the assets carrying amounts or the amounts and classifications of liabilities that might be necessary should the Group not continue as a going concern.

RFG's auditor continues to work with the Board and management through these issues and has included an emphasis of matter paragraph in its audit opinion on the financial statements as at 30 June 2018 on the basis of material uncertainty associated with the syndicated debt facility and the various recapitalisation initiatives. Your Directors understand and accept the position taken by the auditor at this date, as RFG's relationship bankers are still considering the impacts of RFG's turnaround strategies that are currently in progress.

#### (e) Foreign currencies

The individual financial statements of each group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each group entity are expressed in Australian Dollars ('\$'), which is the functional currency of the Company and the presentation currency for the consolidated financial statements.

In preparing the financial statements of the individual entities, transactions in currencies other than the entities functional currency (foreign currencies) are recognised at the rates of exchange prevailing at the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences are recognised in profit or loss in the period in which they arise, except for:

- Exchange differences on foreign currency borrowings relating to assets under construction for future productive use. These are included in the cost of the assets only when they are regarded as an adjustment to interest costs on the related foreign currency borrowings;
- Exchange differences on transactions entered into, in order to hedge certain foreign currency risks; and
- Exchange differences on monetary items receivable from or payable to a foreign operation for which settlement is neither planned nor likely to occur (therefore forming part of the net investment in the foreign operation), and which are recognised initially in other comprehensive income and reclassified from equity to profit or loss on disposal or partial disposal of the net investment.

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are expressed in Australian Dollars using exchange rates prevailing at the end of the reporting period. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuated significantly during that period in which case the exchange rates at the dates of the transactions are used. Exchange differences arising, if any, are recognised in other comprehensive income and accumulated in equity.

Goodwill and fair value adjustments on identifiable assets and liabilities acquired arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and translated at the rate of exchange prevailing at the end of each reporting period. Exchange differences arising are recognised in equity.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.1 Basis of preparation (continued)

#### (f) Use of estimates and judgements

The preparation of the consolidated financial statements requires Management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is amended and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on amounts recognised in the consolidated financial statements are included in the following notes:

Note 9 - Recoverability of debtors

Note 18 - Fair value of assets and liabilities acquired in a business combination

Note 35.2 - Revenue recognition

Note 35.3 - Deferred tax assets

Note 35.6 - Impairment of non-financial assets other than goodwill and indefinite life intangible assets

Note 35.7 - Impairment of goodwill and indefinite life intangible assets

Note 35.7 - Determination as indefinite life intangible assets

#### (g) Goods and services tax

Revenues, expenses and assets are recognised net of the amount of goods and services tax (GST), except:

- Where the amount of GST incurred is not recoverable from the taxation authority, it is recognised as part of the cost of acquisition of an asset or as part of an item of expense; or
- For receivables and payables which are recognised inclusive of GST.

The net amount of GST recoverable from, or payable to, the taxation authority is included within receivables or payables.

Cash flows are included in the consolidated statement of cash flows on a gross basis. The GST component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified within operating cash flows.

#### (h) Adoption of new and revised Accounting Standards

##### Standards and Interpretations adopted in the current period

The Group has adopted all of the new and revised Standards and Interpretations issued by the AASB that are relevant to its operations and are effective for the current reporting period.

The adoption of new Standards and Interpretations during the current reporting period did not have any material effect on the reported results or financial position of the Group, or the presentation and disclosure of amounts in these financial statements.

##### New Standards and Interpretations issued but not yet effective

At the date of authorisation of the financial statements, the following Standards and Interpretations have been issued but were not yet effective.

Standard/Interpretation	Effective for annual reporting periods beginning on or after	Expected to be initially applied in the financial year ending
AASB 9 'Financial Instruments', and the relevant amending standards	1 January 2018	30 June 2019
AASB 15 'Revenue from Contracts with Customers', and the relevant amending standards	1 January 2018	30 June 2019
AASB 16 'Leases'	1 January 2019	30 June 2020

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.1 Basis of preparation (continued)

#### (h) Adoption of new and revised Accounting Standards (continued)

##### New Standards and Interpretations issued but not yet effective (continued)

The Group has yet to fully assess the impact the following accounting standards and amendments will have on the financial statements when applied in future periods:

##### AASB 16 *Leases*

AASB 16 will result in the leases where the Group is the lessee being recognised on the balance sheet, as the distinction between operating and finance leases is removed. Under the new standard, a depreciating non-financial asset (the right to use the leased item) and the associated payable, under the lease, are recognised. For leases in which the Group is the lessor, changes are not required for any adjustments on transition however additional requirements have been introduced for subleases and lease modifications, and lessor disclosure requirements have been expanded.

In addition, the nature of expenses related to those leases will now change as AASB 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. The only exceptions will be short-term and low-value leases.

The new leasing Standard will have a material impact on the Group's financial statements, particularly with the inclusion of new assets and liabilities associated with lease recognition. In addition, there may be a significant impact on the way that the revenues and expenses associated with lease accounting will be reported in the consolidated statement of profit or loss and other comprehensive income.

Initial assessment activities have been undertaken on the Group's current leases to determine the impact AASB 16 Leases. As at the reporting date, the Group has operating lease commitments of \$188.7 million of which \$147.2 million have a corresponding future lease receivable under back-to-back lease arrangements (refer to Note 33).

A detailed review of contracts, financial reporting impacts and system requirements will continue. The Group does not intend to adopt the standard before its effective date 1 July 2019 (the date of initial application of the standard).

Further information on the Group's operating lease commitments are disclosed in Note 33.

##### AASB 9 *Financial Instruments*

AASB 9 replaces AASB 139 Financial Instruments: Recognition and Measurement. AASB 9 contains revised guidance for the classification and measurement of financial instruments, a new impairment model for most debt instruments and new hedge accounting requirements.

There is no change to the financial assets falling under the scope of AASB 139 and subsequently under AASB 9. These assets are classified as amortised cost under both standards, therefore there is an insignificant impact on the classification and measurement of the Group's financial assets.

The new impairment model requires the recognition of impairment losses based on expected credit losses (ECL) rather than incurred credit losses, as is the case under AASB 139. It applies to financial assets classified at amortised cost, debt instruments measured at FVOCI, contract assets under AASB 15 Revenue from Contracts with Customers, lease receivables, loan commitments and certain financial guarantee contracts. The Group has not yet undertaken a detailed assessment of how its impairment provision would be affected by the new model. It is however expected that the impairment loss provision as at the date of initial application of the standard will increase.

The new hedge accounting rules will align the accounting for hedging instruments more closely with the Group's risk management practices. Whilst the Group is yet to undertake a detailed assessment, it would appear that the Group's current hedge relationships would qualify as continuing hedges upon the adoption of AASB 9. Accordingly, the Group does not expect a significant impact on the accounting for its hedging relationships.

The Group intends to apply the standard commencing on 1 July 2018 without providing comparative information, adjusting retained earning balances and other equity components as at 1 July 2018 (the date of initial application of the standard) if there is any such impact.

##### AASB 15 *Revenue from Contracts with Customers*

AASB 15 replaces the current guidance regarding recognition of revenues and presents a new model for recognising revenue from contracts with customers. The standard requires revenue to be recognised when control of a good or service is passed to the customer. This may be at a single point in time or over time. The new standard also provides new guidance on the identification and separation of obligations to a customer. The implementation of the new guidance will have no impact on the amount or timing of cash flows.

Under the current guidance, the Group recognises initial franchise fees when it has performed all material obligations and services which generally occurs when a franchise opens for initial fees and when renewal options become effective for renewal fees. Under the new guidance, the initial obligations do not contain separate and distinct performance obligations from the franchise right and therefore the Group will defer the initial and renewal fees and recognise revenue over the term of the related franchise agreement.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.1 Basis of preparation (continued)

#### (h) Adoption of new and revised Accounting Standards (continued)

##### New Standards and Interpretations issued but not yet effective (continued)

The Group has completed an initial quantification of the impact of AASB 15 however estimates may be subject to change as we progress with the analysis which ongoing, including detailed contract verification as well as the estimated period over which the initial franchise fees will be deferred.

The Group intends to apply the standard commencing on 1 July 2018 using the modified retrospective method, adjusting retained earning balances as at 1 July 2018 for contracts that are not completed as at the transition date.

#### (i) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) (referred to as 'the Group' in these financial statements). Control is achieved where the Company has power over an entity, is exposed or has rights to variable returns from the entity and has the ability to use its power to affect its returns.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated statement of profit or loss and other comprehensive income from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the Subsidiaries' financial statements to make their accounting policies consistent with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

### 35.2 Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable.

#### *Revenue from the sale of goods*

Revenue from the sale of goods is recognised when all of the following conditions are satisfied:

- The Group has transferred to the buyer the significant risks and rewards of ownership of the goods;
- The Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- The amount of revenue can be measured reliably;
- It is probable that the economic benefits associated with the transaction will flow to the entity; and
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

#### *Revenue from processing of dairy products on behalf of third parties*

Revenue is recognised when the terms of the relevant agreement have been met and the processed goods are delivered to the customer.

#### *Revenue from the rendering of services*

Revenue from the rendering of services comprises franchisor income and royalty revenue.

Franchisor income is recognised on an accrual basis, in accordance with the terms of the relevant franchise agreement.

Royalty revenue and revenue from suppliers (supplier licence fees) are recognised on an accrual basis in accordance with the terms of the relevant agreement, provided that it is probable that the economic benefits will flow to the Group and the amount of revenue can be measured reliably.

#### *Initial network access fee revenue*

Initial network access fees are received on execution of certain contracts with approved suppliers to the Group's Brand Systems. This class of revenue is recognised over the corresponding term of the contract period.

#### *Interest revenue*

Interest revenue is recognised when it is probable that the economic benefits will flow to the Group and the amount of revenue can be measured reliably. Interest revenue is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable. This is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

### 35.3 Income taxes

Income tax expense represents the sum of current tax expense and deferred tax expense.

#### *Current tax*

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated statement of profit or loss and other comprehensive income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.3 Income taxes (continued)

#### *Current and deferred tax for the year*

Current and deferred taxes are recognised as an expense or income in profit or loss, except when they relate to items that are recognised outside profit or loss (whether in other comprehensive income or directly in equity). In this case the tax is also recognised outside profit or loss, or where it arises from the initial accounting for a business combination. In the case of a business combination, the tax effect is included in the accounting for the business combination.

#### *Deferred tax balances*

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax base used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised for all deductible temporary differences, to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such deferred tax assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets, arising from deductible temporary differences associated with such investments and interests, are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences, and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would flow in the manner the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to do so set off current tax assets against current tax liabilities or when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

#### **Critical accounting judgements and key sources of estimation uncertainty**

The Group's accounting policy for taxation requires Management's judgement as to the types of arrangements considered to be a tax on income in contrast to an operating cost. Judgement is also required in assessing whether deferred tax assets and certain deferred tax liabilities are recognised on the balance sheet. Deferred tax assets, including those deferred tax assets arising from non-recovered tax losses, capital losses and temporary differences, are recognised only where it is considered more likely than not that they will be recovered, which is dependent on the generation of sufficient future taxable profits. Deferred tax liabilities arising from temporary differences in investments, caused principally by retained earnings held in foreign tax jurisdictions, are recognised unless repatriation of retained earnings can be controlled and are not expected to occur in the foreseeable future.

Assumptions about the generation of future taxable profits, and repatriation of retained earnings, depend on Management's estimates of future cash flows which, in turn, depend on estimates of future production and sales volumes, operating costs, restoration costs, capital expenditure, dividends and other capital management transactions. Judgements are also required in relation to the application of income tax legislation.

#### *Deferred tax assets*

Deferred tax assets are recognised for deductible temporary differences as Management considers that it is probable that future taxable profits will be available to utilise those temporary differences.

These judgements and assumptions are subject to risk and uncertainty, hence there is a possibility that changes in circumstances will alter expectations, which may impact the amounts of deferred tax assets and deferred tax liabilities recognised on the balance sheet and the amount of other tax losses and temporary differences not yet recognised. In such circumstances, some or all of the carrying amounts of recognised deferred tax assets and liabilities may require adjustment, resulting in a corresponding credit or charge to the consolidated statement of profit or loss and other comprehensive income.

### 35.4 Cash and cash equivalents

Cash comprises cash on hand and demand deposits. Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash, which are subject to an insignificant risk of changes in value and have a maturity of three months or less at the date of acquisition or at reporting date. Bank overdrafts are shown within borrowings in current liabilities in the balance sheet.

### 35.5 Inventories

Inventories are stated at the lower of cost and net realisable value. Cost, including an appropriate portion of fixed and variable overhead expenses, are assigned to inventories by the method most appropriate to each particular class of inventory, with categories being valued on a weighted average cost basis as determined by the inventory's nature and use.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.6 Property, plant and equipment

Land and buildings held for use in the production or supply of goods or services, or for administrative purposes, are stated in the consolidated statement of financial position at cost, less any subsequent accumulated depreciation and accumulated impairment losses.

Properties in the course of construction for production, supply or administrative purposes, or for purposes not yet determined, are carried at cost less any recognised impairment loss. Cost includes professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policy. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Freehold land is not depreciated.

Fixtures and equipment are stated at cost less accumulated depreciation and accumulated impairment losses.

Depreciation is recognised to write off the cost or valuation of assets (other than freehold land and properties under construction) less their residual values over their useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at each year-end, with the effect of any changes in estimate accounted for on a prospective basis.

The gain or loss arising on the disposal or retirement of an item of property, plant or equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit or loss.

Voluntary company stores (VCS), including leasehold improvements and fixtures and equipment, are included as items of property, plant and equipment until such time as the VCS becomes held for sale and is, thereafter, reclassified to inventories.

The following useful lives are used in the calculation of depreciation:

- buildings 40 years;
- leasehold improvements 5 - 25 years; and
- plant and equipment 2 - 25 years.

#### Estimation of useful lives of assets

The estimation of the useful lives of assets has been based on historical experience as well as manufacturers' warranties (for plant and equipment), lease terms (for leased equipment) and turnover policies (for motor vehicles). In addition, the condition of the assets is assessed at least once per year and considered against the remaining useful life. Adjustments to useful lives are made when considered necessary.

#### Impairment of non-financial assets other than goodwill and indefinite life intangible assets

The Group assesses impairment of all assets at the end of each reporting period by evaluating conditions specific to the Group and to the particular asset that may lead to impairment. These assessments include product and manufacturing performance, technology, economic and political environments and future product expectations. If an impairment trigger exists, the recoverable amount of the asset is determined.

Management does not consider that there have been any indicators of impairment and, as such, these assets have not been tested for impairment in this financial period.

### 35.7 Intangible assets

#### *Intangible assets acquired separately*

Intangible assets with finite lives that are acquired separately are carried at cost less accumulated amortisation and accumulated impairment losses. Amortisation is recognised on a straight-line basis over their estimated useful lives (which are estimated to be between 2 - 10 years). The estimated useful life and amortisation method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives that are acquired separately are carried at cost less accumulated impairment losses.

#### *Intangible assets acquired in a business combination*

Intangible assets acquired in a business combination, and recognised separately from goodwill, are initially recognised at their fair value at the acquisition date (which is regarded as their cost).

Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets that are acquired separately.

#### Franchise networks and intellectual property

Intangible assets include franchise networks (consisting of identifiable franchise systems and brand names) and intellectual property (consisting of trademarks, recipes, manuals and systems).

Franchise networks are identified and recognised at the time of a business combination and recorded at their fair value, if their fair value can be measured reliably. Franchise networks acquired separately and intellectual property are recorded at cost.

Franchise networks and intellectual property are not amortised on the basis that they have an indefinite life and are reviewed annually.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.7 Intangible assets (continued)

#### Franchise networks and intellectual property (continued)

Expenditure incurred in maintaining intangible assets is expensed in the period in which it is occurred.

#### Goodwill

Goodwill arising in a business combination is recognised as an asset at the date that control is acquired (the acquisition date). Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the acquisition date amounts of the identifiable assets acquired and the liabilities assumed.

If, after reassessment, the Group's interest in the fair value of the acquiree's identifiable net assets exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held equity interest in the acquiree (if any), so the excess is recognised immediately in profit or loss as a bargain purchase gain.

#### Impairment of goodwill and indefinite life intangible assets

Goodwill is not amortised but is reviewed for impairment at least annually. For the purpose of impairment testing, goodwill is allocated to each of the Group's operating segments expected to benefit from the synergies of the combination. Operating segments, to which goodwill, has been allocated are tested for impairment annually or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the operating segments is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit on a pro-rata basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period. On disposal of a subsidiary, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

At the end of each reporting period, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units. Otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount. Hence the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior financial years. A reversal of an impairment loss is recognised immediately in profit or loss.

#### Determination as indefinite life

No amortisation is provided against the carrying value of franchise networks and intellectual property rights on the basis that these assets are considered to have an indefinite life.

Key factors taken into account in assessing the useful life of franchise networks and intellectual property rights are:

- These assets are all well established and have experienced strong sales and profit growth over time;
- None of the assets have a foreseeable limit to when they will stop generating future net cash inflows to the Group; and
- There are currently no legal, technical or commercial obsolescence factors applying to the assets or related products which indicate that the life should be considered limited.

Specifically, in respect of the intellectual property rights, the Group holds a significant number of registered trademarks for each franchise network. Since inception, all of the trademarks have demonstrated significant growth and this growth is forecasted to continue. It is noted that the trademark registrations have a finite legal life, however renewal of the registrations is simple with little cost involved. Management oversees the registration of the trademarks, as well as the protection of these trademarks. The Group intends to renew all trademarks as they expire and has the infrastructure and allocated resources to ensure this renewal occurs.

Therefore, consistent with AASB 138 *Intangible Assets* the Group treats each of its franchise networks and intellectual property rights as having an indefinite life. All such assets are tested for impairment annually.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.7 Intangible assets (continued)

#### Internally Generated Intangible Assets, Including Research and Development Expenditure

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally generated intangible asset arising from the development phase of internal projects is recognised if all of the following requirements have been demonstrated:

- The technical feasibility of completing the intangible asset so that it will be available for use or sale;
- The intention to complete the intangible asset for use or sale;
- The ability to use or sell the intangible asset;
- How the intangible asset will generate probable future economic benefits;
- The availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and
- The ability to measure reliably the expenditure attributable to the intangible asset during its development.

The amount initially recognised for internally generated intangible assets is the total of expenditure incurred from the date when the intangible asset first meets the recognition criteria. Where no internally generated intangible asset can be recognised, development expenditure is recognised in the consolidated statement of profit or loss and other comprehensive income in the period incurred.

### 35.8 Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, and if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably, a receivable is recognised as an asset.

#### *Employee Benefits*

A liability is recognised for benefits accruing to employees in respect of wages and salaries, annual leave and long service leave when it is probable that settlement will be required and they are capable of being measured reliably.

Liabilities recognised in respect of short-term employee benefits are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Liabilities recognised in respect of long-term employee benefits are measured as the present value of the estimated future cash outflows to be made by the Group in respect of services provided by employees up to the reporting date.

Contributions to defined contribution retirement benefit plans are recognised as an expense when employees have rendered service entitling them to the contributions.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.8 Provisions (continued)

#### *Onerous leases and make-good*

A provision has been made for the present value of future lease payments where the Group is presently obliged to make payments under non-cancellable onerous lease contracts relating to certain loss-making non-voluntary company stores. A provision has been made for the present value of the Directors' best estimate of the future sacrifice of economic benefits that will be required to restore the site occupied by the loss-making non-voluntary company stores that existed at the end of the reporting period, to a condition specified in the relevant lease agreement. The estimate has been made on the basis of quotes obtained from restoration specialists or past experience.

The calculation of both provisions requires assumptions such as the likelihood of sale of the non-voluntary company store, the estimated lease termination costs and the expected costs of making-good the premises. These uncertainties may result in future actual expenditure differing from the amounts currently provided. The provision recognised for each site is periodically reviewed and updated based on the facts and circumstances available at the time. The exit from onerous leases and make-good activities are expected to be completed by the Group within twelve months.

#### *Warranties*

The provision for warranties represents repairs on coffee machines. Management has estimated the provision based on historical warranty trends which may vary as a result of new materials, altered manufacturing processes or other events affecting product quality.

### 35.9 Share-based payments

Equity-settled share-based payments to employees, and others providing similar services, are measured at the fair value of the equity instrument at the grant date.

The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Group's estimate of equity instruments that will eventually vest. At the end of each reporting period, the Group revises its estimate of the number of equity instruments expected to vest. The impact of the revision of the original estimates, if any, is recognised in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the equity-settled employee benefits reserve.

Equity-settled share-based payment transactions, with parties other than employees, are measured at the fair value of the goods or services received, except where the fair value cannot be estimated reliably. In which case they are measured at the fair value of the equity instruments granted, measured at the date the entity obtains the goods or the counterparty renders the service.

#### **Measurement of equity-settled share-based payments**

The Group measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. Rights subject to marketing conditions have been valued using the Monte Carlo simulation (using the Black-Scholes framework) and rights subject to non-market conditions have been valued using the Black-Scholes option pricing model. The accounting estimates and assumptions relating to equity-settled share-based payments would have no impact on the carrying amounts of assets and liabilities within the next annual reporting period but may impact expenses and equity.

### 35.10 Financial instruments

#### *Financial Assets*

Trade receivables, loans and other receivables that have fixed or determinable payments, that are not quoted in an active market, are classified as loans and receivables. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

#### *Financial liabilities and equity instruments issued by the Group*

#### *Classification as debt or equity*

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

#### *Equity instruments*

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Group are recognised as the proceeds received, net of direct issue costs.

#### *Financial liabilities*

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.10 Financial instruments (continued)

#### *Financial liabilities and equity instruments issued by the Group (continued)*

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

#### *Derecognition of financial liabilities*

The Group derecognises financial liabilities only when the Group's obligations are discharged, cancelled or they expire.

#### *Financial guarantee contract liabilities*

Financial guarantee contract liabilities are measured initially at their fair values, and, if not designated as at FVTPL, are subsequently measured at the higher of:

- The amount of the obligation under the contract, as determined in accordance with AASB 137 *Provisions, Contingent Liabilities and Contingent Assets*, or
- The amount initially recognised less, where appropriate, cumulative amortisation, recognised in accordance with the revenue recognition policies set out in Note 35.2.

#### *Derivatives and hedging activities*

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value at the end of each reporting period. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged.

The Group designates certain derivatives as either:

- Hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedges);
- Hedges of a particular risk associated with the cash flows of recognised assets and liabilities and highly probable forecast transactions (cash flow hedges); or
- Hedges of a net investment in a foreign operation (net investment hedges).

At the inception of the hedging transaction, the Group documents the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions have been and will continue to be highly effective in offsetting changes in fair values or cash flows of hedged items.

The fair values of various derivative financial instruments used for hedging purposes are disclosed in Note 25.10. Movements in the hedging reserve in shareholders' equity are shown in Note 21. The full fair value of a hedging derivative is classified as a non-current asset or liability when the remaining maturity of the hedged item is more than 12 months and it is classified as a current asset or liability when the remaining maturity of the hedged item is less than 12 months. Trading derivatives are classified as a current asset or liability.

#### *(i) Cash flow hedge*

The effective portion of the changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income and accumulated in reserves in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss within other income or other expense.

Amounts accumulated in equity are reclassified to profit or loss in the periods when the hedged item affects profit or loss. The gain or loss relating to the effective portion of interest rate swaps hedging variable rate borrowings is recognised in profit or loss within finance costs. The gain or loss relating to the effective portion of forward foreign exchange contracts hedging export sales is recognised in profit or loss within 'sales'. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset (for example inventory or fixed assets) the gains and losses previously deferred in equity are reclassified from equity and included in the initial measurement of the cost of the asset. The deferred amounts are ultimately recognised in profit or loss as cost of goods sold in the case of inventory or as depreciation or impairment in the case of fixed assets.

When a hedging instrument expires and is sold or terminated, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity until the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately reclassified to profit or loss.

#### *(ii) Net investment hedges*

Hedges of net investments in foreign operations are accounted for on a similar basis to cash flow hedges.

Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in other comprehensive income and accumulated in reserves in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss within other income or other expenses. Gains and losses accumulated in equity are reclassified to profit or loss when the foreign operation is partially disposed of or sold.

# NOTES TO THE FINANCIAL STATEMENTS

## 35. Summary of significant accounting policies (continued)

### 35.10 Financial instruments (continued)

#### (iii) Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in profit or loss and are included in other income or other expenses.

### 35.11 Acquisitions

Acquisitions of subsidiaries and businesses are accounted for using the acquisition method. The consideration for each acquisition is measured at the aggregate of the fair values (at the date of exchange) of assets given, liabilities incurred or assumed and equity instruments issued by the Group in exchange for control of the acquiree. Acquisition-related costs are recognised in profit or loss as incurred.

Where applicable the consideration for the acquisition includes any asset or liability resulting from a contingent consideration arrangement measured at its acquisition-date fair value. Subsequent changes in such fair values are adjusted against the cost of the acquisition where they qualify as measurement period adjustments. All other subsequent changes in the fair value of contingent consideration classified as an asset or liability are accounted for in accordance with relevant standards. Changes in the fair value of contingent consideration classified as equity are not recognised.

Where a business combination is achieved in stages, the Group's previously held interests in the acquired entity are remeasured to fair value at the acquisition date (i.e. the date the Group attains control) and the resulting gain or loss, if any, is recognised in profit or loss. Amounts arising from interests in the acquiree prior to the acquisition date that have been recognised in other comprehensive income are reclassified to profit or loss, where such treatment would be appropriate if that interest was sold.

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognised at their fair value at the acquisition date, except that:

- Deferred tax assets or liabilities and liabilities or assets related to employee benefit arrangements are recognised and measured in accordance with AASB 112 *Income Taxes* and AASB 119 *Employee Benefits* respectively;
- Liabilities or equity instruments related to the replacement by the Group of an acquiree's share-based payment awards are measured in accordance with AASB 2 *Share-based Payment*; and
- Assets (or disposal groups) that are classified as held for sale in accordance with AASB 5 *Non-current Assets Held for Sale and Discontinued Operations* are measured in accordance with that standard.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Group reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period, or additional assets or liabilities are recognised, to reflect new information obtained about facts and circumstances that existed as of the acquisition date that, if known, would have affected the amounts recognised as at that date.

The measurement period is the period from the date of acquisition to the date the Group obtains complete information about facts and circumstances that existed as of the acquisition date and is subject to a maximum time of one year.

Business combinations that took place prior to 1 July 2009 were accounted for in accordance with the previous version of AASB 3.

### 35.12 Operating leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

#### *Group as lessor*

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease.

#### *Group as lessee*

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred. In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

# NOTES TO THE FINANCIAL STATEMENTS

## DIRECTORS' DECLARATION

The Directors declare that:

- (a) In the Directors' opinion, the financial statements and notes set out on pages 28 to 88 are in accordance with the Corporations Act 2001, including:
  - (i) complying with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and
  - (ii) giving a true and fair view of the consolidated Group's financial position as at 30 June 2018 and of its performance for the financial year ended on that date; and
- (b) In the Directors' opinion, there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable;
- (c) In the Directors' opinion, the financial statements are in compliance with International Financial Reporting Standards, as disclosed in the notes to the financial statements of the 2018 Annual Report;
- (d) The Directors have been given the declarations required by s.295A of the *Corporations Act 2001*.

Signed in accordance with a resolution of the Directors made pursuant to s.295 (5) of the *Corporations Act 2001*.

On behalf of the Directors

**RETAIL FOOD GROUP LIMITED**



Mr Colin Archer  
Chairman and Independent Non-Executive Director  
Southport  
31 August 2018

# INDEPENDENT AUDITOR'S REPORT



## *Independent auditor's report*

To the members of Retail Food Group Limited

### *Report on the audit of the financial report*

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#### *Our opinion*

In our opinion:

The accompanying financial report of Retail Food Group Limited (the Company) and its controlled entities (together the Group) is in accordance with the *Corporations Act 2001*, including:

- (a) giving a true and fair view of the Group's financial position as at 30 June 2018 and of its financial performance for the year then ended
- (b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

#### ***What we have audited***

The Group financial report comprises:

- the consolidated statement of financial position as at 30 June 2018
- the consolidated statement of profit or loss and other comprehensive income for the year then ended
- the consolidated statement of changes in equity for the year then ended
- the consolidated statement of cash flows for the year then ended
- the notes to the consolidated financial statements, which include a summary of significant accounting policies
- the directors' declaration.

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#### *Basis for opinion*

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial report* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### ***Independence***

We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

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# INDEPENDENT AUDITOR'S REPORT

## (CONTINUED)



### *Material uncertainty related to going concern*

We draw attention to Note 35(d) in the financial report, which indicates that the Group incurred a net loss before tax of \$380m for the year ended 30 June 2018 and, as of that date, the Group's current liabilities exceeded its current assets by \$231m, inclusive of syndicated secured borrowings of \$265m.

The Group's ability to continue as a going concern is dependent on the Group having a continued appropriate level of funding from its existing lenders and/or other sources for at least the next twelve months from the date of this report. These conditions, as well as successfully executing the assets sales program and other Group restructuring initiatives as set forth in Note 35(d), indicate that a material uncertainty exists that may cast significant doubt on the Group's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

### *Our audit approach*

An audit is designed to provide reasonable assurance about whether the financial report is free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report.

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial report as a whole, taking into account the geographic and management structure of the Group, its accounting processes and controls and the industry in which it operates.



### **Materiality**

- For the purpose of our audit we used overall Group materiality of \$2.4 million, which represents approximately 5% of the Group's loss before tax adjusted for unusual or infrequently occurring items impacting profit and loss, such as asset impairments and onerous lease provisions.
- We applied this threshold, together with qualitative considerations, to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements on the financial report as a whole.
- We chose Group loss before tax because, in our view, it is the benchmark against which the performance of the Group is most commonly measured.
- We utilised a 5% threshold based on our professional judgement, noting it is within the range of commonly acceptable thresholds.

# INDEPENDENT AUDITOR'S REPORT

## (CONTINUED)



### Audit Scope

- Our audit focused on where the Group made subjective judgements; for example, significant accounting estimates involving assumptions and inherently uncertain future events.
- The Group is structured across 5 operating segments, being Bakery Cafe, QSR Systems, Coffee Retail Systems, Coffee and Allied Beverage and Commercial Food Services. Its head office is based in Brisbane, Queensland.

### Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report for the current year. The key audit matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. Further, any commentary on the outcomes of a particular audit procedure is made in that context. We communicated the key audit matters to the Audit and Risk Committee.

In addition to the matter described in the *Material uncertainty related to going concern* section, we have determined the matters described below to be the key audit matters to be communicated in our report.

#### Key audit matter

#### How our audit addressed the key audit matter

#### Restructuring of domestic franchising business

(Refer to note 6) \$403m

The Group's comprehensive review of the outlook for the Australian franchise business operations has resulted in the planned closure of a number of stores throughout FY19 and FY20.

As a result, significant asset impairments and provisions have been recognised in the 30 June 2018 financial report.

This was a key audit matter because in recognising asset impairments and provisions, a number of significant judgements were made by the Group. The most significant judgements included the estimation of:

- the recoverable amount of corporate stores assets classified as either inventory or property, plant and equipment based on the store closure plan.
- the recoverability of trade receivables and

For corporate store asset impairments recorded, we performed the following audit procedures, amongst others:

- considered available information regarding the planned store closures where these included corporate stores.
- assessed the appropriateness of the impairment of corporate store assets related to the store closures plan and checked that corporate stores planned for closure have been fully impaired at 30 June 2018.

For the impairment of amounts due from franchisees (including master franchisees) we performed the following procedures, amongst others:

- developed an understanding of the Group's policies and procedures in relation to the

# INDEPENDENT AUDITOR'S REPORT

## (CONTINUED)



### Key audit matter

### How our audit addressed the key audit matter

#### **Restructuring of domestic franchising business**

*(Refer to note 6) \$403m (cont'd)*

- vendor finance amounts due from franchisees (including master franchisees), based on the store closure plan and other specific indicators of impairment.
- the recoverable amount and associated impairment of property, plant and equipment based on the store closure plan and the restructuring review of the Group.
- the recognition of provisions for onerous lease contracts at corporate store locations,
- the provision for costs and other expenses directly linked to the restructuring the Group is committed to incur.
- the expected financial impact of potential legal claims and regulatory reviews against the Group
- the recoverable amounts of intangible assets (including goodwill) attributed to franchise brand systems. This has been addressed in a separate key audit matter.

- recognition of provisions for doubtful debts in light of the store closure plan.
- made enquiries of management in respect of past due debtors and assessed the risk of impairment.
- considered selected correspondence between the Group and franchisees in respect of balances past due or on payment plans.
- tested the accuracy of the aged receivables listing through tracing a sample to the underlying invoices to assess the dates included in the listing.
- tested a sample of trade receivables and vendor finance amounts due from franchisees to subsequent receipts in the bank including testing if they were in line with the agreed payment plans for those franchisees and tested the allocation of these receipts against outstanding debtor balances.
- considered appropriateness of provisions raised in respect of the sample of amounts due from franchisees who had not paid and had overdue amounts.

For impairments in respect of property, plant and equipment, we performed the following audit procedures, amongst others:

- developed an understanding of the Group's policy in respect of assessing the net realisable value of property, plant and equipment.
- made enquiries of management in respect of the nature of property, plant and equipment and assessed the risk of the net realisable value being lower than the carrying value.
- considered whether impairments of property, plant and equipment were appropriate in light of the Group's planned store closure plan and business restructure.

# INDEPENDENT AUDITOR'S REPORT

## (CONTINUED)



### *Key audit matter*

### *How our audit addressed the key audit matter*

#### ***Restructuring of domestic franchising business***

*(Refer to note 6) \$403m (cont'd)*

For onerous lease contract provisions, we performed the following audit procedures, amongst others:

assessed the Group's assumptions relating to onerous contracts by comparing them to supporting documentation, including current trading performance of stores, planned store closure dates and correspondence with landlords.

- evaluated whether the onerous contract provisions met the criteria in Australian Accounting Standards for recognition as liabilities at 30 June 2018.
- for those onerous contract provisions recognised, assessed whether the measurement of the provision was in accordance with criteria outlined in Australian Accounting Standards.

For the provision of costs and other expenses we performed the following procedures, amongst others:

- obtained an understanding and assessed the Group's assumptions relating to expected costs and other expenses associated with the restructuring of the domestic franchise business.

For the expected impact of the potential legal claims and regulatory reviews we performed the following procedures, amongst others:

- obtained an understanding from the Group's inhouse legal advisers of the current and potential legal claims and actions against the Group.
- considered board minutes and correspondence between the Group and external legal advisers.
- obtained legal confirmations from the Group's external legal advisers.

# INDEPENDENT AUDITOR'S REPORT

## (CONTINUED)



### *Key audit matter*

### *How our audit addressed the key audit matter*

#### **Assessment of recoverability of goodwill and intangible assets** *(Refer to note 15) \$364m*

The Group recognises goodwill and indefinite life intangible assets which relate to brand networks and intellectual property rights.

As required by Australian Accounting Standards, these non-amortising assets are tested each year end for impairment.

The Group performed impairment assessments over each of their cash generating units (CGUs) by calculating the recoverable amount of each CGU. The recoverable amount was determined by either a value in use calculation or fair value less cost of disposal methodology using discounted cash flow models (the models). The Group have recorded impairments charges on goodwill and brand networks totaling \$306m for the year ended 30 June 2018.

The key judgements in the models are the budgeted brand system cash flows, the expected average percentage growth rate, discount rates and terminal growth rates.

The assessment of impairment was a key audit matter due to the size of goodwill and indefinite life intangible assets in the balance sheet, the impairments taken during the year and the key judgements and assumptions incorporated in the impairment models prepared to assess the recoverable amount of the goodwill and indefinite life intangible assets.

In assessing the recoverable amount of goodwill and intangible assets, we performed the following procedures, amongst others:

- assessed whether the Group's identification of CGUs was consistent with our knowledge of the operations, internal reporting lines and the level of largely independent cash-flows.
- tested the mathematical accuracy of the calculations in the models and compared the future cash flow forecasts in the models to the Board approved budgets.
- assessed the 2019 year cash flow forecasts in each of the models by developing an understanding of the underlying drivers for the budget in the context of the Group's future operational plans.
- compared the discount rates used by the Group and benchmarked implied multiples to external market data and trends that were obtained with the assistance of PwC valuation experts.
- compared the recoverable amount to the market capitalisation of the Group at 30 June 2018.
- checked that the impairments to intangible assets and goodwill identified in the impairment models were consistent with the Group's financial records at balance date.
- assessed if the presentation and disclosures made in the financial report in respect of impairment were compliant with the relevant Australian Accounting Standard.

# INDEPENDENT AUDITOR'S REPORT

## (CONTINUED)



### **Key audit matter**

### **How our audit addressed the key audit matter**

#### **Classification of external borrowings**

(Refer to note 19) \$264m

The Group's current liabilities includes syndicated secured borrowings of \$265m at balance date.

Expecting to breach one of the financial covenants for the 30 June 2018 covenant testing period, the Group sought and received a waiver from its lenders to forego covenant testing for 30 June 2018. The waiver was subject to a number of conditions and additional information being supplied by the Group to the lenders after balance date, as outlined in note 19 to the financial statements.

Given the size and importance of the syndicated secured borrowings to the Group's funding structure and the Group's ongoing dialogue with its lenders regarding structuring and debt covenant compliance requirements, the accounting, presentation and disclosure of the Group's borrowings arrangements was considered a key audit matter.

We obtained confirmations directly from the Group's lenders to confirm borrowings, including amounts, tenure and conditions.

We read the most up-to date agreements and correspondence between the Group and its lenders to obtain an understanding of the terms and conditions associated with the facilities, the amount of facilities available for future redraw and any covenants contained in the facilities.

Where debt was classified as current we tested the Group's assessment that they did not have the unconditional right to defer payment for at least 12 months from 30 June 2018.

We evaluated whether the disclosures were consistent with the requirements of Australian Accounting Standards.

#### **Revenue recognition**

(Refer to note 2) \$374m

The Group's revenue is based on a very high volume of transactions across a number of different businesses, which each have several streams of revenue being revenue from the sale of goods, food processing revenue, revenue from the rendering of services (including master franchise fees (both domestic and international), franchisor income, franchise service fees, supplier license fees) and initial network access fees, some of which can be complex.

Complexity arises from the judgements employed by the Group in the recognition and measurement of each source of revenue and the timing of its recognition based on the terms of the relevant agreements.

We performed the following procedures, amongst others:

- developed an understanding of each significant revenue stream, being revenue from the sale of goods, food processing revenue, revenue from the rendering of services (including master franchise fees (both domestic and international), franchisor income, franchise service fees, supplier license fees) and initial network access fees and the policies used to recognise revenue.
- tested a sample of Master Franchise Agreements to evaluate if the Master Franchise Fees were recorded in the correct accounting period. This included testing of amounts recorded to the underlying agreement and payment receipts.

# INDEPENDENT AUDITOR'S REPORT

## (CONTINUED)



### Key audit matter

### How our audit addressed the key audit matter

#### Revenue recognition

(Refer to note 2) \$374m (cont'd)

The particular revenue streams that involve complexity include:

- Master Franchise Fees - For Master Franchise Agreements entered into (both International and Domestic) the Group receives Master Franchise Fees at the commencement of the agreement in addition to other franchise service fees over the term of the agreement.
- Supplier License Fees - Supplier arrangements, where the Group grants exclusive supply rights to the Group's franchisees, resulting in the Group receiving amounts upfront (Supplier License Fees) from the supplier at the commencement of the arrangements.

Each of these revenue streams is underpinned by different systems, processes and controls meaning our focus was whether revenue was being correctly recorded (accuracy) and also recognised in the appropriate period (cut-off).

Due to the opportunity for manual intervention, the high volume of transactions and the interfaces of multiple systems with the general ledger there is potential for these transactions to be recorded incorrectly.

Revenue recognition was a key audit matter because of this complexity, the quantum of the Group's revenue and the number of different revenue streams, systems and processes involved.

- where individually material Supplier License Fees were identified, we tested amounts recognised by the Group to the terms of the supplier agreement to determine whether the revenue and related costs were recorded accurately and within the correct accounting period.
- for Supplier License Fees that had previously been deferred, we checked whether the amounts recognised in the current year were consistent with the terms of the supplier agreement and the recognition profile for each agreement.

In relation to revenue from the sale of goods, food processing revenue, franchisor income and franchise service fees we performed detailed testing of a sample of revenue transactions, which included the following:

- Assessing the consistent application of the Group's revenue recognition policies with the underlying terms and conditions of the sale of goods and services performed.
- Developing an understanding of the processes and key controls in place for each revenue stream.
- For all major revenue streams, agreeing a sample of transactions from the general ledger listing to supporting documentation, including bank statements. This included checking whether a sample of transactions either side of the Group year end date were recorded in the appropriate period.

# INDEPENDENT AUDITOR'S REPORT

## (CONTINUED)



### *Other information*

The directors are responsible for the other information. The other information comprises the information included in the annual report for the year ended 30 June 2018, but does not include the financial report and our auditor's report thereon. Prior to the date of this auditor's report, the other information we obtained included the Director's report, Summary Financial Information, Corporate Directory and Additional Stock Exchange Information. We expect the remaining other information to be made available to use after the date of this auditor's report, including Chairman's Letter and CEO's Report.

Our opinion on the financial report does not cover the other information and we do not and will not express an opinion or any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

When we read the other information not yet received as identified above, if we conclude that there is a material misstatement therein, we are required to communicate the matter to the directors and use our professional judgement to determine the appropriate action to take.

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### *Responsibilities of the directors for the financial report*

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the ability of the Group to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

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### *Auditor's responsibilities for the audit of the financial report*

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report.

# INDEPENDENT AUDITOR'S REPORT

## (CONTINUED)



A further description of our responsibilities for the audit of the financial report is located at the Auditing and Assurance Standards Board website at: [http://www.auasb.gov.au/auditors\\_responsibilities/ar1.pdf](http://www.auasb.gov.au/auditors_responsibilities/ar1.pdf). This description forms part of our auditor's report.

### *Report on the remuneration report*

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#### *Our opinion on the remuneration report*

We have audited the remuneration report included in pages 14 to 25 of the directors' report for the year ended 30 June 2018.

In our opinion, the remuneration report of Retail Food Group Limited for the year ended 30 June 2018 complies with section 300A of the *Corporations Act 2001*.

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#### *Responsibilities*

The directors of the Company are responsible for the preparation and presentation of the remuneration report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with Australian Auditing Standards.

*PricewaterhouseCoopers*

PricewaterhouseCoopers

*Steven Bosiljevac*

Steven Bosiljevac  
Partner

Brisbane  
31 August 2018

# ADDITIONAL STOCK EXCHANGE INFORMATION

Number of holders of equity securities as at 22 August 2018

## Ordinary share capital

- 182,745,510 fully paid ordinary shares are held by 18,964 individual shareholders.

All issued ordinary shares carry one vote per share.

## Distribution of holders of equity securities

	Total holders fully paid ordinary shares	Fully paid ordinary shares	% Issued capital	Total holders options	Options
1 - 1000	7,054	3,522,840	1.93%	-	-
1,001 - 5,000	7,811	20,049,842	10.97%	-	-
5,001 - 10,000	2,072	15,835,440	8.67%	-	-
10,001 - 100,000	1,881	46,892,994	25.66%	-	-
100,001 and over	146	96,444,394	52.77%	-	-
	18,964	182,745,510	100.00%	-	-

The number of shareholders holding less than a marketable parcel of ordinary shares is 5,543.

## Substantial shareholders

Ordinary shareholders	Fully paid		Partly paid	
	Number held	Percentage	Number held	Percentage
Invesco Australia Limited	22,475,278	12.30%	-	-

## Twenty largest holders of quoted equity instruments

Ordinary shareholders	Fully paid		Partly paid	
	Number	Percentage	Number	Percentage
HSBC Custody Nominees (Australia) Limited	30,146,190	16.50%	-	-
Citicorp Nominees Pty Limited	8,407,419	4.60%	-	-
Alford s Holdings (Qld) Pty Ltd	6,637,309	3.63%	-	-
AXNA Pty Ltd	5,999,177	3.28%	-	-
J P Morgan Nominees Australia Limited	3,031,380	1.66%	-	-
Antra Pty Ltd	2,138,717	1.17%	-	-
Molves Pty Ltd	2,000,000	1.09%	-	-
BNP Paribas Nominees Pty Ltd	1,801,528	0.99%	-	-
AMA Holdings (Qld) Pty Ltd	1,294,042	0.71%	-	-
Archerfield Airport Corporation	1,200,000	0.66%	-	-
CSF Investments (Qld) Pty Ltd	1,115,142	0.61%	-	-
Mrs Christine Ann D'souza	1,095,000	0.60%	-	-
Comsec Nominees Pty Limited	1,071,780	0.59%	-	-
VeHlanga Pty Ltd	1,000,000	0.55%	-	-
WSS Holdings (Aust) Pty Ltd	927,217	0.51%	-	-
Tea & Coffee Traders Pty Ltd	841,912	0.46%	-	-
Mr Noel Diago Lawrence Francis D'souza + Mrs Christine Ann D'souza	807,000	0.44%	-	-
Mr Garry Michael Heffernan	670,000	0.37%	-	-
Mr Jisi Liu	630,000	0.34%	-	-
Hishenk Pty Ltd	600,000	0.33%	-	-
	71,413,813	39.09%	-	-



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