



INTERIM REPORT 2018





VISION

**GLOBAL EXPERTS
IN FOOD ASSURANCE**

PURPOSE

**TOGETHER WE
BUILD AND PROTECT
CONSUMER CONFIDENCE**

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CHAIR AND CHIEF EXECUTIVE REPORT

RESULTS OVERVIEW

AsureQuality is ahead of budgeted revenue at the end of the first half and forecasting to achieve its budget profit for the year. Increased revenue from the Myrtle Rust and Mycoplasma Bovis biosecurity responses has offset below budget activity in live animal export shipments, albeit at a lower gross margin.

Testing Services revenues are in line with budget but the reduction in demand from infant formula customers has changed the testing mix within the business.

This change in mix combined with the reduced level of higher margin live animal export work has resulted in below budget EBIT for the first half.

SHAREHOLDER DIVIDEND

During the six months ending 31 December 2017, a final dividend of \$2.2 million was paid to the shareholder for the year ended 30 June 2017. This brings the total dividend paid relating to the 2017 financial year to \$3.7 million. In February 2018 an interim dividend of \$1.5 million was paid to the shareholder, which is in line with the dividend policy.

STRATEGIC DIRECTION

Our focus on our strategic priorities continues as we transform AsureQuality toward higher value technology-led analysis, insights and assurance across the supply chain. Our priorities are:

- > **Having highly motivated, performance driven teams.** We are focussed on creating alignment behind a 'one-AQ' approach, which will focus on driving performance with clear accountabilities, open communication and trust.
- > **Doing the basics well, first and foremost.** There will be a continued focus on delivering a consistently high standard of service and customer experience; supported by efficient processes, systems & technology.
- > **Partnering to deliver higher value services.** AsureQuality's strategy is to grow through partnerships. We will invest in opportunities to provide analytics, insights and assurance-based services that deliver more value for customers and AsureQuality; making better use of science & technology and partnerships.

IN CONCLUSION

Despite challenging market conditions, we are forecasting an improvement in profit margins in the second half of the year.

AsureQuality's success is dependent on both the continued support of our customers and the hard work and dedication of our team of food safety experts.

We thank you all for your commitment, and we look forward to continuing to enhance the business performance in the second half of the year.



JANINE SMITH CHAIR



JOHN MCKAY CHIEF EXECUTIVE OFFICER

BUSINESS OVERVIEW



HEALTH & SAFETY

We remain committed to ensuring our employees return home to their families safe and healthy every day. Key highlights for this period include:

- New safety logo and key safety messages developed and launched
- Core Health and Safety manual rewritten and simplified
- Retaining tertiary accreditation in the ACC Partnership Programme
- New Senior Health and Safety Advisor role established



CONTINUOUS IMPROVEMENT

A number of key initiatives have seen pleasing results for the first half of this year. 24 people have been trained in 'Find A Better Way' Foundations. They are now applying these techniques in their business units. The on-going process to standardise and simplify business processes has seen over 400 AsureQuality processes published in 'AQ KnowHow' representing almost 50% of the estimated total. Total benefits of the 'Find A Better Way' programme since inception in January 2015 now exceeds \$6m.



FOOD & CONTAMINANT TESTING

The complex product registration process for AsureQuality clients sending infant formula into China has led to continued volatility in the Testing business. This has contributed to a change in the mix of testing with less nutritional testing within the total testing regime, which has impacted both revenue and EBIT. Indications are that the second half of the financial year will see an improvement, as most manufacturers are well advanced with this process.

The Auckland Laboratory Pathogens team launched a new Polymerase Chain Reaction (PCR) method for pathogen testing. The reduced turnaround time for this method is appreciably beneficial for customers in the New Zealand food industry, and is attracting some significant new business as a result. A faster method for yeast and mould testing was also launched in December delivering a 2-day advantage to customers.

The first shipment of live animal exports did not take place until December, with no serology testing from July to November. This has had a significant negative impact on the speciality testing business in Wellington. The forward forecast shows a recovery in animal exports in the second half, back to levels in line with previous years.

The joint venture ownership with Bureau Veritas of DTS Food Assurance in Australia is now in its second year. As with AsureQuality's New Zealand laboratories, this business has also been impacted by the product registration requirement for China. The issues with Murray Goulburn, a significant customer

in Australia, introduced additional uncertainty and the business moved quickly to restructure. While the first half has failed to meet budget expectations, improvement is already evident and the second half is forecast to achieve targets.



INSPECTION AND CERTIFICATION

A key focus for the first six months has been the development of a transition plan across Inspection & Certification which aligns processes into a standard framework, simplifying the business and programmes within it. The second half of the year will see much of this programme implemented. A further significant area of focus has been supply and demand management, enabling improved alignment (recruitment and staff training) to meet commercial opportunities. The reconfiguration of the Inspection and Certification business that occurred last year is continuing to offer advantages for the business, increasing opportunities for AsureQuality staff to broaden their skills working across a wider range of diverse activities.



BIOSECURITY

Two significant biosecurity responses have been the central focus for the biosecurity business unit over the past six months. Myrtle rust and Mycoplasma bovis responses have seen AsureQuality delivering MPI's operational field requirements utilising staff across AsureQuality as well as from the National Biosecurity Capability Network (NBCN). Ongoing activity is expected from both responses into the second half of the year. The latter part of this reporting period has also seen the response team continuing the work from last year to undertake surveillance programmes to support the eradication and prevent the spread of pea weevil from the Controlled Area.



INTERNATIONAL SERVICES

Our Singapore laboratory has completed its expansion programme in response to growing volume, both from multinational dairy customers and local South East Asian food companies. The laboratory information management system has also been successfully upgraded. The outlook for the rest of the financial year is set to improve as business development activities conducted over the first half of the year are realised along with the on boarding of one large regional entity that required the business to go through a rigorous approvals process before any business could be conducted.

The operational set-up for the joint venture between AsureQuality and Saudi company Motabaqah has been completed. The laboratory has been audited by the Saudi Arabian Accreditation Authority and now has full accreditation.

Our new partnership model is operational with a major project underway for the NZ Meat Industry. Other projects with provincial Governments and private firms are in development. In Qatar, our team of subject-matter-experts have commenced work on the second tranche of work for the Qatar Ministry of Health.



CORPORATE SOCIAL RESPONSIBILITY

AsureQuality's CSR philosophies are embedded in the Company's Vision, Purpose and Values statements and are reflected in how the Company operates across all activities on a day-to-day basis. The Company is focussed on three broad strategic objectives:

- Reducing the Company's environmental impact
- Being a good employer
- Encouraging social and community involvement and support

AsureQuality participates in a number of specific programmes and initiatives aimed at contributing to the achievement of our strategic objectives.

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE SIX MONTHS ENDED 31 DECEMBER 2017

	NOTE	6 MONTHS DECEMBER 2017 UNAUDITED \$000	6 MONTHS DECEMBER 2016 UNAUDITED \$000
REVENUE	6	93,025	83,195
Employee benefit expenditure		(56,563)	(51,861)
Consumables		(8,640)	(7,922)
Contractors and subcontractor testing		(5,515)	(2,160)
Transportation expenses		(5,356)	(4,247)
Rental and operating lease cost		(2,658)	(2,508)
Other expenses	7	(8,449)	(8,137)
OPERATING EXPENSES		(87,181)	(76,835)
Depreciation and amortisation		(2,857)	(2,910)
Finance costs (net)	8	(385)	(538)
Share of loss of associate and joint venture	9	(391)	(435)
Share of acquisition costs of associate		-	(859)
PROFIT BEFORE INCOME TAX		2,211	1,618
Income tax expense		(834)	(748)
PROFIT FOR THE YEAR		1,377	870
OTHER COMPREHENSIVE INCOME			
Items that may be reclassified subsequently to profit or loss:			
Change in foreign currency translation reserve		965	(194)
OTHER COMPREHENSIVE INCOME NET OF TAX		965	(194)
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD, NET OF TAX		2,342	676
Profit for the period attributable to:			
Equity holders of the parent		1,757	1,208
Non-controlling interest		(380)	(338)
		1,377	870
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD ATTRIBUTABLE TO:			
Equity holders of the parent		2,722	1,014
Non-controlling interest		(380)	(338)
		2,342	676

The accompanying notes form part of these condensed consolidated interim financial statements

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE SIX MONTHS ENDED 31 DECEMBER 2017

		SHARE CAPITAL	REVALUATION RESERVE	TRANSLATION RESERVE	RETAINED EARNINGS	ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT	NON- CONTROLLING INTEREST	TOTAL EQUITY
	NOTE	\$000	\$000	\$000	\$000	\$000	\$000	\$000
BALANCE AT 30 JUNE 2016 (AUDITED)		22,100	9,614	(1,892)	18,816	48,638	440	49,078
Total comprehensive income for the period		-	-	(194)	1,208	1,014	(338)	676
TRANSACTIONS WITH OWNERS RECORDED DIRECTLY IN EQUITY								
Dividend to equity holders	5	-	-	-	(3,400)	(3,400)	-	(3,400)
BALANCE AT 31 DECEMBER 2016 (UNAUDITED)		22,100	9,614	(2,086)	16,624	46,252	102	46,354
Total comprehensive income for the period		-	-	1,206	4,973	6,179	81	6,260
TRANSACTIONS WITH OWNERS RECORDED DIRECTLY IN EQUITY								
Dividend to equity holders		-	-	-	(1,500)	(1,500)	-	(1,500)
BALANCE AT 30 JUNE 2017 (AUDITED)		22,100	9,614	(880)	20,097	50,931	183	51,114
Total comprehensive income for the period		-	-	965	1,757	2,722	(380)	2,342
TRANSACTIONS WITH OWNERS RECORDED DIRECTLY IN EQUITY								
Dividend to equity holders	5	-	-	-	(2,200)	(2,200)	-	(2,200)
BALANCE AT 31 DECEMBER 2017 (UNAUDITED)		22,100	9,614	85	19,654	51,453	(197)	51,256

The accompanying notes and accounting policies form part of these financial statements.

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2017

	NOTE	DECEMBER 2017 UNAUDITED \$000	JUNE 2017 AUDITED \$000
CURRENT ASSETS			
Cash and cash equivalents		7,788	4,402
Trade and other receivables		26,359	30,642
Inventories		5,430	4,799
Current income tax assets		220	-
Contract work in progress		799	1,052
TOTAL CURRENT ASSETS		40,596	40,895
NON-CURRENT ASSETS			
Property, plant and equipment		31,953	32,209
Intangible assets		6,212	6,601
Investment in associate and joint venture		31,364	30,343
Deferred income tax assets		2,748	2,370
TOTAL NON-CURRENT ASSETS		72,277	71,523
TOTAL ASSETS		112,873	112,418
CURRENT LIABILITIES			
Trade and other payables		26,119	26,466
Borrowings		3,500	5,000
Derivative financial instruments	14	176	226
Current income tax liabilities		-	372
TOTAL CURRENT LIABILITIES		29,795	32,064
NON-CURRENT LIABILITIES			
Borrowings		26,531	24,056
Loan from non-controlling interest		1,583	1,535
Payables		3,708	3,649
TOTAL NON-CURRENT LIABILITIES		31,822	29,240
TOTAL LIABILITIES		61,617	61,304
EQUITY			
Equity attributable to equity holders of the parent		51,453	50,931
Non-controlling interest		(197)	183
TOTAL EQUITY		51,256	51,114
TOTAL LIABILITIES AND EQUITY		112,873	112,418

The Board of Directors of AsureQuality Limited authorised these financial statements for issue on 13 February 2018.



Janine Smith
Chair



Bruce Scott
Chair Audit Committee

The accompanying notes form part of these condensed consolidated interim financial statements

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE SIX MONTHS ENDED 31 DECEMBER 2017

	NOTE	6 MONTHS DECEMBER 2017 UNAUDITED \$000	6 MONTHS DECEMBER 2016 UNAUDITED \$000
CASH FLOWS FROM OPERATING ACTIVITIES			
Receipts from customers		98,413	84,995
Payments to suppliers and employees		(89,398)	(80,950)
Interest paid net of interest and dividends received		(619)	(609)
Income tax paid		(1,805)	(3,017)
NET CASH GENERATED FROM OPERATING ACTIVITIES		6,591	419
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property, plant and equipment		(1,664)	(1,392)
Purchase of intangibles		(316)	(617)
NET CASH USED IN INVESTING ACTIVITIES		(1,980)	(2,009)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from borrowings		975	6,316
Dividend paid to shareholder		(2,200)	(3,400)
NET CASH USED IN FINANCING ACTIVITIES		(1,225)	2,916
NET INCREASE IN CASH		3,386	1,326
Cash and cash equivalents at beginning of six month period		4,402	2,722
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD		7,788	4,048
RECONCILIATION OF THE PROFIT FOR THE YEAR WITH CASH FLOWS FROM OPERATING ACTIVITIES			
PROFIT FOR THE PERIOD		1,377	870
ADJUSTMENTS FOR:			
Depreciation and amortisation		2,857	2,910
Share of loss of associate and joint venture		391	435
Share of acquisition costs of associate		-	859
Other non-cash movements		(1,000)	48
IMPACT OF CHANGES IN WORKING CAPITAL			
Trade and other receivables		4,283	(885)
Income tax		(592)	(2,650)
Trade and other payables		(347)	(1,104)
Other non-cash movements		(378)	(64)
NET CASH GENERATED FROM OPERATING ACTIVITIES		6,591	419

The accompanying notes and accounting policies form part of these financial statements.

CONSOLIDATED NOTES TO AND FORMING PART OF THE INTERIM FINANCIAL STATEMENTS FOR THE SIX MONTHS ENDED 31 DECEMBER 2017

I. REPORTING ENTITY

AsureQuality Limited is a company registered under the Companies Act 1993 and is a company incorporated and domiciled in New Zealand. The Company provides food quality assurance and biosecurity services and manufactures and sells animal diagnostic products.

Condensed consolidated interim financial statements are presented, comprising AsureQuality Limited and its subsidiaries (the "Group"). The Group is designated as a profit-oriented entity for financial reporting purposes.

2. STATEMENT OF COMPLIANCE

The condensed consolidated interim financial statements have been prepared in accordance with the State-Owned Enterprises Act 1986 and generally accepted accounting practice in New Zealand ("NZ GAAP") as appropriate for profit-orientated entities.

The condensed consolidated interim financial statements have been prepared in accordance with NZ IAS 34 and IAS 34 Interim Financial Reporting.

The condensed consolidated interim financial statements do not include all of the information required for full annual financial statements. Accordingly, these financial statements should be read in conjunction with the annual report for year ending 30 June 2017. The Condensed consolidated interim financial statements have been prepared in accordance with the accounting policies set out in the 2017 Annual Report, except for the application of the following standards as of 1 July 2017:

- Amendments to NZ IAS 12 – Recognition of Deferred Tax Assets for Unrealised Losses
- Amendments to NZ IAS 7 – Disclosure Initiative

There was no material impact on these financial statements from applying these standards.

The financial information contained in this report has not been audited by AsureQuality's auditors.

3. ACCOUNTING JUDGEMENTS AND ESTIMATES

The preparation of financial statements in conformity with NZ IFRS requires judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The judgements and estimates used in the preparation of these interim financial statements are consistent with those used in the annual report for the year ended 30 June 2017.

4. SEASONALITY OF OPERATIONS

AsureQuality's revenues are seasonal and largely follow the primary production industry cycle.

5. DIVIDENDS

During the six months ended 31 December 2017, a dividend of \$2,200,000 representing 9.24 cents per share, relating to the 12 months period ended 30 June 2017, was paid by AsureQuality Limited to the shareholder (six months ending 31 December 2016: \$3,400,000 representing 14.29 cents relating to the 12 months period ended 30 June 2016).

CONSOLIDATED NOTES TO AND FORMING PART OF THE INTERIM FINANCIAL STATEMENTS FOR THE SIX MONTHS ENDED 31 DECEMBER 2017

	6 MONTHS DECEMBER 2017 UNAUDITED	6 MONTHS DECEMBER 2016 UNAUDITED
	\$000	\$000
6. REVENUE		
Revenue from operations comprises:		
Revenue from the rendering of services	90,725	80,527
Revenue from the sale of goods	2,295	2,659
Other income	5	9
	93,025	83,195

7. OTHER OPERATING EXPENSES

Other operating expenses include donations of \$2,000 (December 2016: \$11,000).

8. FINANCE COSTS (NET)

Interest expense on borrowings	(619)	(617)
Interest income on short-term bank deposits	5	1
Movement of derivatives held at fair value through profit or loss	50	74
Net foreign exchange gains	179	4
	(385)	(538)

9. SHARE OF LOSS OF ASSOCIATE AND JOINT VENTURE

Share of trading profit 49% (December 2016: 49%)	1,192	1,288
Management fees received	(414)	(1,077)
	778	211
Amortisation of intangibles	(1,169)	(646)
	(391)	(435)

NAME	COUNTRY OF INCORPORATION	PRINCIPAL ACTIVITIES	BALANCE DATE	OWNERSHIP AND VOTING INTEREST DECEMBER 2017	OWNERSHIP AND VOTING INTEREST DECEMBER 2016
Bureau Veritas AsureQuality Holdings Limited (BVAQ)	Australia	Independent food testing laboratories	31-December	49%	49%

The Group's share of Bureau Veritas AsureQuality Holdings Limited's loss has been recognised in profit.

10. CONTINGENT LIABILITIES

There are no material contingent liabilities as at 31 December 2017 (December 2016: Nil).

CONSOLIDATED NOTES TO AND FORMING PART OF THE INTERIM FINANCIAL STATEMENTS FOR THE SIX MONTHS ENDED 31 DECEMBER 2017

11. RELATED PARTY TRANSACTIONS

The ultimate shareholder of the Company is the Crown. The Company undertakes many transactions with other State-Owned Enterprises and Government entities and departments in the normal course of business. These transactions are carried out on a commercial and arm's length basis. The Company made significant sales of biosecurity services to the Government, Ministry of Primary Industries, during the six month period. The remaining transactions were not significant and are exempt from related parties disclosures (under NZ IAS 24 (Revised) Related Party Disclosures). The following represents the major ongoing transaction types but should not be taken as a complete list: product and environmental testing services, animal health services, accident compensation levies, air travel services, energy products, postal and courier services, specific scientific advisory services and rental and leasing services.

The Group made sales to and purchases from its associate, Bureau VeritasASUREQuality Holdings Limited during the period.

The following transactions were carried out with related parties:

	6 MONTHS DECEMBER 2017 UNAUDITED	6 MONTHS DECEMBER 2016 UNAUDITED
	\$000	\$000
SALES OF SERVICES:		
Sales of biosecurity services to Government	13,755	4,224
Services provided to associate	1,221	2,398
EXPENSES:		
Purchase of services from associate	550	751

12. SIGNIFICANT EVENTS AFTER INTERIM BALANCE DATE

On 13 February 2018, the Board of Directors declared an interim dividend of \$1,500,000 relating to the 12 months ending 30 June 2018, representing 6.30 cents per share. As the dividends were declared after balance date the financial effect has not been recognised in these financial statements.

	DECEMBER 2017 UNAUDITED	DECEMBER 2016 UNAUDITED
	\$000	\$000

13. COMMITMENTS

CAPITAL COMMITMENTS

Capital expenditure contracted for at reporting date but not provided for	1,033	1,080
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CONSOLIDATED NOTES TO AND FORMING PART OF THE INTERIM FINANCIAL STATEMENTS FOR THE SIX MONTHS ENDED 31 DECEMBER 2017

14. FAIR VALUE MEASUREMENT OF FINANCIAL INSTRUMENTS

The Group is party to financial instruments as part of the normal course of operations. These financial instruments include bank accounts, short-term deposits, borrowings, derivatives, trade receivables and payables.

Cash, trade receivables, payables and non-current liabilities are disclosed in the condensed statement of financial position at their amortised cost which is equivalent to their fair value.

The fair value of financial instruments that are not traded in an active market (for example, over the counter derivatives) is determined by using valuation techniques such as discounted cashflows.

Derivative financial instruments

The Group enters into various financial instruments to either eliminate or manage its exposure to interest rate and foreign currencies movements. Interest rate swaps are used to economically convert the Group's exposure to floating interest rates to fixed rates.

Forward exchange rate contracts are used to economically convert material exposures to foreign exchange. Other financial instruments may be used from time to time to reduce risk.

The Group holds the following instruments:

	NOTIONAL PRINCIPAL		FAIR VALUE		MOVEMENT OF DERIVATIVES HELD AT FAIR VALUE THROUGH PROFIT OR LOSS	
	DECEMBER 2017	JUNE 2017	DECEMBER 2017	JUNE 2017	DECEMBER 2017	DECEMBER 2016
	\$000	\$000	\$000	\$000	\$000	\$000
Interest rate swaps	17,825	19,476	(176)	(384)	50	74
Foreign exchange contracts	-	8	-	104	-	-
	17,825	19,484	(176)	(280)	50	74

COMPARISON WITH PERFORMANCE TARGETS INCLUDED IN THE STATEMENT OF CORPORATE INTENT FOR THE SIX MONTHS ENDED 31 DECEMBER 2017

	6 MONTHS DECEMBER 2017 TARGET	6 MONTHS DECEMBER 2017 ACTUAL	12 MONTHS JUNE 2018 TARGET
FINANCIAL PERFORMANCE TARGETS			
Revenue	\$84.8m	\$93.0m	\$176.6m
Earnings before interest and tax	\$3.8m	\$2.6m	\$10.1m
Net profit after tax	\$2.0m	\$1.4m	\$5.9m
Net cash flow from operating activities	\$2.6m	\$6.6m	\$9.5m
ANNUAL KEY RATIOS			
Operating margin ¹	8.1%	5.9%	9.0%
Solvency ²	1.4	1.4	1.4
NON-FINANCIAL PERFORMANCE TARGETS			
Critical programme audit failures	Nil	Nil	Nil
Critical facility audit failures	Nil	Nil	Nil
Staff turnover rate ³	<12%	11%	<12%
Total recordable injury frequency rate (TRIFR) ⁴	<5.4	6.0	<5.0

1. Operating margin is calculated as Earnings before interest, tax, depreciation and amortisation divided by Revenue
2. Solvency is calculated as total current assets divided by total current liabilities.
3. Staff turnover rate is calculated as a rolling average of permanent staff (excluding redundancy) who have left the business in the last twelve months.
4. This measure has been updated to align with New Zealand best practice of using a frequency rate per 200,000 hours (previously used per 1,000,000 hours, which is most commonly used internationally).

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