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Operator: Thank you for standing by and welcome to the Billabong Half Year Results conference call. All participants are in a listen only mode. There will be a presentation followed by a question and answer session. We ask that only analysts participate in today's Q&A session. If you wish to ask a question you will need to press the star key, followed by the number one on your telephone key pad.

I would now like to hand the conference over to your speaker today, Mr Neil Fiske, CEO. Please go ahead.

Neil Fiske: Good day everyone and thank you for joining our FY18 Half Year Results call. Also with me today is our Chief Financial Officer, Jim Howell. A short while ago we lodged today's result statement and presentation with the ASX and posted them on our website, www.billabongbiz.com. Unless otherwise stated all the figures are expressed in Australian dollars, excludes significant items and are for continuing businesses only.

Over the course of the first half two important events occurred for Billabong. The first was our AGM in November where we outlined our continuing operational progress in the face of difficult trading conditions. At the same time our Chairman, Ian Pollard, updated shareholders about the Board's continued focus on the balance sheet. We have been reporting for some time on the need to reduce debt and Ian advised how, with the assistance of its advisors, the Board was well advanced in assessing various options related to the Company's term loan with the focus on maximising shareholder value.

One of those options related to the second important development. This was the announcement in December of a proposal from Boardriders Inc to acquire all of the shares in Billabong, other than those already owned by Boardriders related entities. That proposal became a fully funded and committed offer early in January and the Board has unanimously recommended the proposed transaction to shareholders in the absence of a superior proposal.

The Company last week issued a scheme booklet outlining in detail the reasons for the Board's recommendation, the favourable multiples and premium which the offer represents, as well as an independent expert's report that advises shareholders that the proposal of $1 per share is fair and reasonable and therefore in the best interest of shareholders in the absence of a superior proposal. We will come back to the scheme at the end of this presentation but the proposal as well as our results today should be viewed in the context of an industry that continues to undergo swift and far reaching change, including fundamental channel shifts, rapidly changing consumer preferences, challenges in the traditional wholesale base, bankruptcies and company sale processes for a number of industry participants.

It is fair to say that over the past four years Billabong's solid operational progress has been offset by external factors which means that despite all of the improvements we have made our EBITDA has stabilised but now grown materially. Trading conditions remain tough in retail overall in much of the action sport sector. Those trading conditions affected the first half results that we're announcing today and are likely to prevail in the second half and beyond.

In Australia, where we have a large number of stores and high retail exposure, recent reports have weak retail trading and profit downgrades have painted a sober picture of the broader retail landscape. Conditions are expected to become more difficult with the expansion of Amazon into Australia, an important market for us.

With that in mind let's turn to the first half outcome. The results we are reporting today are consistent with the updated guidance given in early January, namely, that we would be down in the first half but up in the second to put EBITDA for the year at or above FY17. A range from $51.1 million to $54 million. This would make it the third consecutive year of relatively flat EBITDA adjusting for the sale of Tigerlily where market conditions have countered the operational progress achieved within the business. This has been a consistent theme of the last few years. For example, improvements in the America's offset by weakness in APAC. Improvements in gross margin offset by revenue declines. CODB reductions limited by the need to invest in revenue generation and supporting platforms. Ecommerce growth offset by a shift away from brick and mortar retail.

Turning to the half year EBITDA was $19.3 million, compared with $23.9 million the prior period, down 19.1% as reported and 15.9% in constant currency. There were some significant shifts between H1 and H2 that we should recoup in the second half, specifically a revenue timing shift in the shipping pattern in Europe between the halves which accounts for about $1.5 million of the H1 EBITDA decline and a shift in the timing of some Billabong global marketing costs from H2 into H1, which represents another $1 million of the H1 EBITDA decline.

Total revenues for the half were $474.5 million, down 3.1% as reported and 1.5% constant currency. Gross margins were up 100 basis points to 52% and were up in every region marking the continued progress in our global sourcing in concept to customer initiatives. CODB was up $5 million in constant currency or 180 basis points which reflects the timing shift in Billabong global marketing mentioned before, as well as investments we made in revenue driving growth areas like ecommerce and RVCA. The results show a small increase in store rent and a non-cash change in long term incentive expenses relating to the use of options as approved by shareholders at the 2016 AGM. Net loss after tax was $18.4 million compared with $13 million in the prior period.

Looking at the regional results, in the half we saw continued improvement in our largest market of the Americas as well as continued weakness in APAC. Europe was down for the half but we still expect EBITDA for the region to be up for the full year, although less than we thought a couple of months ago. For comparability we will discuss the regional results in constant currency unless otherwise stated.

In the Americas EBITDA, prior to global allocations, lifted 34.1% to $13.3 million, with total revenue up 3.9% reflecting mostly market share gains in ecommerce. CODB was lower by 40 basis points and gross margins expanded 110 basis points. Ecommerce grew 19.5% and is most developed in this region representing 9.6% of sales. Brick and mortar comparable store sales were up 0.7% on slighter lower margins. Total comparable retail sales with comparable stores and ecommerce combined were up 5.8% and margins were down 60 basis points. Looking at the second half we expect revenue and EBITDA gains in the Americas to level out as we cycle tougher comps and operational improvements.

In Europe EBITDA prior to global allocations for the first half was off 29.4% to $4.9 million, a $2 million decline, reflecting the revenue timing shift I referred to earlier and weaker than expected retail results.

Total revenues declined 6.1% while gross margins were up by 106 basis points. Overhead costs were about flat to prior year but were up 300 basis points as a percentage of the lower sales number.

Brick and mortar comps were down 2.3%. However, ecommerce grew 15.1% and now represents 5.5% of total sales. Total comparable retail sales were down between 3%, with retail gross margins up 140 basis points.

We expect Europe full year revenue to be about flat, with EBITDA improvement driven by higher gross margins.

Asia Pacific still faces tough market conditions, particularly in Australia. However, several of the improvement areas discussed at our AGM have begun to show tangible results.

EBITDA prior to global allocations for the region was off 9.2%, a decline of $2.1 million. This remains our most challenging region.

Total revenues were down 4.5%, up 1.3% on retail, but down 16.6% in wholesale. This reflects ongoing weak market conditions, but also the lag effect of some assortment and execution issues that we have previously reported. Those issues have been addressed, but the market outlook remains weak, limiting the rate of potential EBITDA recovery.

Gross margins improved 120 basis points. CODB was down 0.5% in absolute dollars, but as a percentage of revenue increased 180 basis points on lower sales.

APAC brick and mortar retail comps were up 0.9% for the half. In Australia, where the overall retail climate is more difficult, our first half comp store sales ended down 0.6%. Encouragingly, comps during the key December month were up 2% in Australia on the back of the improvements outlined at the AGM.

Ecommerce was up 28.7% in the region. In Australia ecomm grew 40.2%, including the strong December performance, although still off a small base. Ecomm now represents 2.5% of the region's total sales, still a low penetration overall.

We were pleased with the launch of Surf Dive 'n' Ski on our new ecommerce platform and saw strong sales growth. We've now also launched our New Zealand multi-brand retail, Amazon Surf, on the new platform and are encouraged by what we've seen so far. With the bump in ecommerce growth total comparable retail sales for the APAC region were up 1.8%. Retail margins were up 120 basis points.

Slide 12 gives a summary of the direct consumer comps across all the major geographies.

Turning to the brands, the results varied among our big three brands: Billabong, Element and RVCA, which represent over 90% of our external wholesale sales. Billabong wholesale equivalent revenue - which includes wholesale equivalent sales and our own channels - was down 0.5%, with the Americas at 13.1%, Europe up 4.7% and APAC down 11.5%.

In the US Billabong continued to gain share in the specialty channel, once again ending the calendar year as the number one brand within the core market. In Australia Billabong's wholesale weakness reflected the combination of a soft market, challenges with some of our major accounts, closures and consolidation within the specialty channel and the lag effect of assortment misses and execution issues I mentioned earlier.

The corrective actions we've taken will take time to flow through the wholesale channel, which operates on longer lead times than our retail business. However, within our own retail we've started to see improvements. Comparable sales at Billabong Monogram stores were up 2% in December.

Social media followership for the Billabong brand, its athletes and ambassadors reached $18.4 million. In December the Billabong Pipe Masters - the biggest event on the championship tour - set new viewership records for a world surf league event.

I'd like to congratulate Finn McGill for winning the 2017 Junior World Championship, Griffin Colapinto for winning the 2017 Vans Triple Crown, Josh Moniz for taking out the 2018 Volcom Pipe Pro, and Courtney Conlogue for another excellent year. These results speak to the depth of talent riding for Billabong and the future of our pro surf team and, indeed, for the brand.

For Element wholesale equivalent revenue was down 13% and was most impacted by the timing shift in Europe, which is its largest region. The brand was up 14.1% in the Americas, 11.6% in Europe and 16.2% in APAC. We still expect to see some growth in Element Europe for the year. Nearly all of the Americas decline was due to a shift of distribution strategy in Canada as we chose to exit a large, highly promotional account in that country.

In APAC, and Australia in particular, we see Element performing better in our own retail, although those improvements have yet to translate into wholesale. Element, its athletes and its ambassadors now have a social media followership of 13.2 million.

Nyjah Huston once again proved his immense talent by taking out the 2017 Street League Super Crown World Championship. We're delighted to have Nyjah confirmed as part of the Element team through the Tokyo 2020 Olympics, where skateboarding will feature as a sport for the first time.

RVCA turned in a very good half with 9.6% growth in wholesale equivalent sales, up 8.2% in the Americas, 26.6% in Europe, although still off a small base, and 11.7% in APAC. RVCA ecommerce was up 35.4%.

In the US RVCA continues to gain share in the core specialty channel in both men's and women's categories, with men's ending the calendar year as the number three brand. RVCA Sport recorded strong growth for the half, albeit from a small base, and demonstrates encouraging potential alongside the global growth in popularity of mixed martial arts.

RVCA's unique artist network program again produced a loyal following with a range of artist apparel collections launched in key markets generating good sales. The social media followership of RVCA, its athletes and its ambassadors now stands at 10.3 million.

In summary, the first half result was consistent with the guidance we provided at the AGM and reiterated that the time of announcing the signing of the scheme implementation deed with Boardriders in early January.

Before handing over to Jim to go through the details of the financials it is worth reflecting on what this first half, and the likely outcome for the full year, means in the context of the future of the business. It is now four years since we announced our strategy of global brands and global platforms to position the business for an Omni-Channel future.

We've seen the benefit of those platform initiatives in gross margin expansion, speed to market and operating efficiencies. Through our global sourcing initiatives, by the end of FY18, we will have achieved around $20 million of the $30 million we identified as possible. The remainder we've scheduled to flow in over the course of FY19 and FY20.

There is still much to do to put our brands on competitive platforms. These are strategic investments which we had to make for our brands to be globally competitive. They will take time and require ongoing investment. As we've seen with Omni-Channel systems these large scale platform projects carry inherently high execution risk. Omni is at the core of our strategy.

We're pleased with the first deployment of our new ecommerce system at Surf Dive 'n' Ski in Australia and Amazon Surf in New Zealand. However, there are still 20 websites to be converted to the new system, including all of the brand websites globally, as well as the point of sale roll-out across the regions. While a good deal of expenditure on this project is behind us, there is still significant investment and large scale implementation ahead of us.

Over the four years we've also addressed issues with the balance sheet. We have improved operating cash flow and cash conversion from EBITDA. We have lowered cash restructuring costs and we have sold assets such as Tigerlily and Sector 9 to help pay down debt, but the EBITDA growth needed to improve our credit metrics has not been forthcoming.

In that time we've delivered significant operational improvements, particularly in the Americas and Europe, but we've also confronted tens of millions in adverse currency movements on our product costs, and across multiple geographies we've seen industry bankruptcies, account closures and fundamental shifts away from brick and mortar. These changes are systemic, structural and set to continue. They require us to make fundamental transformative changes to compete and prosper. However, our capital structure has too much debt for the current conditions, the investments we still have ahead of us and our current earnings and risk profile.

To continue with our plan of building global brands and global platforms the Company will need to materially reduce debt. At the same time we're approaching the maturity of our term loan in 2019. The Board has considered a broad range of alternative scenarios in detail. Of those options the Boardriders' proposal is the best and carries the Board's unanimous recommendation. I'll come back to that after Jim has taken us through the financials for the half year.

I'll now hand it over to Jim.

Jim Howell: Thank you Neil. This has been an exciting and busy time for our Company. While there has been a significant amount of effort on the scheme we organised ourselves to ensure this effort did not impact the broader organisation and our focus on serving our customers in running the business.

We continue to forecast a full year EBITDA in the range of $51.1 million to $54 million, albeit with the first half down on the prior corresponding period. This is consistent with our expectations for FY18 that we first shared with you in August of 2017. As a result, the financial outcome for the first half is in line with expectations.

My portion of the prepared remarks will focus on our cash flow, balance sheet, liquidity, debt and, lastly, how we are planning the business for the remainder of 2018. I will keep my remarks short to allow for any questions you may have.

First, I need to address some housekeeping so we are clear on the basis of comparability. We are again providing a bridge between our statutory loss of $18.4 million and the EBITDA of $19.3 million, which as expected, is lower than the comparable as reported number for last year of $23.9 million.

We consider - and I am sure everyone would agree - that the continuing operations numbers are the most important, namely the performance of the brands we have in the portfolio today. Following that principle requires that we (1) exclude significant items which are not part of the continuing businesses and secondly, are consistent with our disclosure at last year end by treating Tigerlily as a discontinued operation. That sale, which was effective on 1 April 2017, was a continuation of our efforts to simplify the business and reduce our debt.

Neil has already covered the regional results so I don't have much to add other than to point out that global costs which get allocated to the regions are not just corporate costs. They include operating functions like central marketing and sourcing operating functions. Our global costs were up $2.9 million on the prior period. Of that $1 million is the timing shift of Billabong global marketing into Half 1, $900,000 is a decrease in sourcing commissions now being picked up by the regions, and another $900,000 relates to the treatment of our LTI expense.

We have also disclosed both the as reported change, which represents the difference using actual FX rates and the constant currency comparison, to provide a more accurate measure of operational performance.

Pre-tax significant items totalled $8.5 million and are roughly $1 million higher than the prior year. They are primarily related to restructuring our logistics platform, which we previously foreshadowed, and that will continue into Half 2, as well as costs related to the scheme. These costs are partially offset by a net gain related to the settlement of a legal dispute and more detail is provided in the notes to our financial statements.

Our operating cash flow is $33 million in the current period compared with operating cash flow of $27.3 million in the prior period. Unlike the continuing business treatment for the income statement, Tigerlily was included last year and EBITDA is down this year. So from a trading perspective it was a good result.

Additionally, financing costs were lower as last year included ABL establishment costs and fees for the covenant amendments on the term loan. Capital expenditures are up year-over-year from spend in 2018 related to the Omni project which Neil mentioned earlier.

Working capital is $158.5 million which is down 2.7% compared with the same point last year. However, as I look at our inventory position at the end of the half, we are higher than we would like to be, particularly in Australia, and are already hard at work addressing this.

Net debt is down 6.7% from $148.6 million at 30 June 2017 to $138.6 million at 31 December 2017. Net debt is up over the proforma debt of $130 million at December 2016, which was adjusted for the Tigerlily sale.

Net interest expense is down $3 million as the term loan was reduced last year using the proceeds from the sale of Tigerlily.

Our liquidity includes cash from the balance sheet of $84 million which is lower than last year by $16 million. It is important to again mention that a significant portion of that cash is needed in the business to meet our peak seasonal working capital need or is otherwise spoken for. There is no material ability to use the cash in the balance sheet to permanently reduce gross debt.

The ABL, which has undrawn availability of $66 million at 31 December 2017, is the source of standby liquidity if our come and go cash balance is fully utilised. In recent years we have made progress in our management of working capital, ensuring sufficient liquidity, improving EBITDA to cash flow conversion and lowering cash significant items, but we need to acknowledge the fact that our EBITDA has essentially been flat for three years on a like-for-like basis. It cannot support our current strategy at current debt levels with a maturing term loan in under two years.

The term loan was approximately $228 million at the end of Half 1. The Board considers that in order to fund the further investment required for the Company to continue with its current strategy, it will become necessary to materially reduce debt to a level where Billabong can fund that investment out of earnings after servicing the interest on debt.

The debt needs to be reduced and refinanced prior to the September 2019 maturity. If the scheme proceeds, we avoid the risk and uncertainty represented by the upcoming maturity of the term loan at a time when we see negative sentiment in the debt markets for retailers.

That is not to say we have not been focused on the term loan maturity. We have consistently commented on the need for building blocks such as the sale of non-core assets like Tigerlily, the simplification of our business and improving cash flow; all things that would improve our credit quality. We have completed many initiatives over the last couple of years, but still face balance sheet challenges and risks which are removed by the certainty of the scheme.

Regarding our outlook, the Company confirms the guidance provided in early January, that it expects the Group's FY18 EBITDA, excluding significant items, to exceed the prior year; to be in a range between $51.1 million and $54 million, subject to reasonable trading conditions and currency markets remaining relatively stable.

The Group continues to have a significant bias of second half earnings to the Americas, with a high concentration of sales in the month of June. Trading in that month remains key to achieving the Group's full year expectations.

That concludes my prepared remarks and I will turn it back over to Neil to close.

Neil Fiske: Thanks Jim. As I announced at the start of this call, we want to make sure the call today is also an opportunity for investors to hear from us about the proposal from Boardriders.

The Directors unanimously recommend that shareholders vote in favour of the scheme and nothing in the results announced today or the expectations for the full year in any way impact that recommendation other than to affirm it.

Based on Billabong's current circumstances, difficult conditions existing in much of this [R] sector, and the work still ahead of us to complete the strategy of transforming Billabong to a global brand-led business, operating on strong global platforms, the Board and the Company's two largest shareholders, apart from Oaktree, are in favour of the proposal.

Both Centerbridge and Gordon have had deep insight into the progress we have made and the difficulties we have encountered, and have been represented on the Board for more than four years, and have confirmed that they will be voting in favour of the scheme.

The independent expert considers the proposal fair and reasonable and in the best interests of shareholders in the absence of a superior proposal. The valuation represents a 16.6 times enterprise value to EBIT multiple, well ahead of peers and precedents and also the significant premium to the undisturbed trading valuation; 28% to the undisturbed price and 69% to the average price over the previous three months.

Despite the proposal being public for three months, there has been no other superior proposal emerge. The scheme provides certainty as to value and provides certainly against an otherwise significant number of risks and uncertainty.

There is a combination of factors that has led to the Directors' recommendations to vote in favour of this scheme. These factors include difficult external conditions that continue to offset the progress we've making, the fact that EBITDA is not growing which makes our balance sheet and high debt levels an issue, and the certainty of the proposal from Boardriders, which in addition to a fair price, removes the uncertainty created by these circumstances including refinancing risk.

We have already discussed how the operational progress in recent years has been countered by the difficult market conditions and conditions are not expected to improve. Guidance for FY18 implies a third year of relatively flat EBITDA adjusting for Tigerlily, and the term loan is now less than two years from maturity.

Despite initiatives to address the balance sheet, such as key asset sales and improved cash flows, credit metrics are not materially improving. Debt market conditions for borrowers with retail operations are difficult.

At the AGM we advised that with the assistance of its advisors the Board was well advanced in assessing various options related to the Company's term loan with the focus on maximising shareholder value. The scheme booklet makes it clear that the alternatives being considered to address these circumstances in addition to the scheme included asset sales and raising equity and refinancing the remaining term loan.

An equity raising would need to be substantial, at least $100 million, to get the gross debt to EBITDA ratio to not more than two times EBITDA, noting that it is currently 4.8 times.

Jim has commented on the fact that we can't use the cash on the balance sheet to permanently reduce gross debt, since it is required to fund seasonal working capital peaks where is otherwise spoken for.

Achieving an equity raising would be problematic since raising equity would be highly reliant on support from Oaktree, Centerbridge and Gordon Merchant, who each agree the scheme is their preferred option to deal with the situation.

Asset sales are the other alternative, but this would not necessarily repay the term loan in full. So contemporaneously refinancing the remaining balance would be required and we would need a new strategy for what's left, the viability of which is uncertain.

It is important to appreciate that this is not an offer that can be accepted at any time. If the scheme does not proceed there is no reason to expect Boardriders will revisit the proposal.

Finally, the scheme booklet highlights that Oaktree, who own a controlling stake in Boardriders and Centerbridge, are the lenders to Billabong under Billabong's term loan. If the scheme does not proceed, Centerbridge and Oaktree will presumably continue to be both major shareholders in the Company as well as senior secured lenders.

In this circumstance their interest may not always align with those of other shareholders. In particular, there's a risk that in any discussions between Billabong on the one hand and Centerbridge or Oaktree on the other about the refinancing of the loan, Centerbridge and Oaktree may favour their interest as lenders over their interest as shareholders in the Company.

If the scheme does not proceed Billabong will not be in a position to continue on a business as usual basis. Changes will be necessary to our capital structure, strategy and operations.

That is the end of our formal presentation, so I will now open it up for analyst questions.

Operator: Thank you. If you wish to ask a question please press star one on your telephone and wait for your name to be announced. If you wish to cancel your request please press star two. If you are on a speaker phone, please pick up the handset to ask your question. Your first question comes from Craig Woolford from Citi Group. Please go ahead.

Craig Woolford: (Citi Group, Analyst) Hi Neil and Jim. Just wanted to ask about the operating performance of the business, particularly on Australia. You said the number of accounts had shrunk or the wholesale sales had shrunk 16%. A lot of it was accounts reducing. Can you just break that down or like how much came from the accounts versus the ordering which may have reflected a weaker summer season for you?

Neil Fiske: Yeah, so I think there are a number of factors in the wholesale market Craig. Closed accounts is one. There's also been some consolidation of accounts in this market where competitors of ours have bought previously independent retailers and we've lost volume there. There has been pressure from some of the major accounts. You're well aware of what's going on with Surf Stitch and the risks that we have around that and you see in some of the bigger accounts the continued trend of the substitution of vertical private label product for branded product. All of those things for us sort of go into a thematic of structural change and contraction in the wholesale market.

It's significant, it's pronounced. We expect it to continue. We've acknowledged that not all of our decline in Australia is due to market factors. Some of it was our own execution and we have taken the steps to correct that but I think it would be safe to say that while we will get some benefit from those initiatives and are seeing some early signs, the wholesale market outlook is going to remain bleak for a while.

Craig Woolford: (Citi Group, Analyst) Okay and it's obviously been a tough season for the Australian business but in the slide deck I'm pretty sure you said gross margins were up. I'm just trying to square how all that works given it was a - you said it wasn't a great season. Comps were virtually flat or low single digit and gross margins were up. What was the driver of better gross margin in Australia?

Neil Fiske: Really I think, Craig, the benefits are global platform initiatives, global sourcing and concept to customer which are now flowing through in higher initial product margins and we've been able to maintain those higher mark ups into final margins.

Craig Woolford: (Citi Group, Analyst) Alright, because in the US gross margins were down in retail.

Neil Fiske: Yeah, a little bit. I think probably the US had already seen the flow through of some of those global platform initiatives in the prior year and was cycling up against those improvements in this half. By the way, I think you should expect to see that as a thematic in the second year where we're going to be cycling tougher comps from last year and that the operational improvements run better than the second half results from last year. You've got a glimpse of that in the retail numbers in this half.

Craig Woolford: (Citi Group, Analyst) Okay. You mentioned you set up a business called Amazon, but how significant has the third party platforms online been for surf and are you supplying Amazon in Australia?

Neil Fiske: Yeah, so third party platforms I think across the globe have been a significant factor of growth, factoring in of themselves in surf. Clearly Amazon and the Americas which we've been dealing with for years and the third party market place around that, Europe with a number of the large pure play ecomm players, we're seeing both - we're seeing third party market places emerge there as well. I would say that Australia is wide open. We are going to have to see how Amazon plays out in this market. We know that it's going to have a big impact. They are both a customer of ours and in some ways a competitor and so we have to work with them very carefully.

I think the lessons that we've learned in the other regions we're going to apply to this region as well. Even though that's an incremental source of revenue, the growth we've seen in other markets is it's not that additive. It's actually cannibalistic and it puts pressure on industry margins as the ecommerce players get bigger.

Craig Woolford: (Citi Group, Analyst) Yeah. That's great. Thanks Neil. Thanks Jim.

Operator: Thank you. There are no further questions at this time. I will now hand back to Mr Fiske for closing remarks.

Neil Fiske: Thank you for joining us this morning everyone. We have shared a lot of information with you today. We are happy for anyone on the call or any shareholder to reach out to us through the contacts on our ASX release. Thank you.

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