

CAVALIER CORPORATION

MANAGING DIRECTOR'S ADDRESS

19 NOVEMBER 2013 ANNUAL MEETING OF SHAREHOLDERS

Today, I will cover the following key items:

- Overview of the financial year just gone
- Carpet business
- Wool business
- Yarn business
- Earnings outlook
- The future

Overview of the 2012/13 year

I am happy to report that 2013 was a better year than 2012. However, it must be acknowledged that 2012 was an extremely tough year, with operating conditions the worst the Group has ever experienced.

For the first half of 2013, the carpet business was adversely affected by the high carrying value of finished goods stock caused by the almost doubling in wool price in the 2010/11 season. The second half of the year saw a return to better trading, and profits lifted accordingly.

2013 was a year where the focus was on further restructuring the cost base to align production with demand, introducing new products and ranges and strengthening the balance sheet by reducing debt. Now that these have been achieved, our objective is to lift profits and shareholder returns.

Results

As was the case last year, reported profit has been reduced substantially by the on-going costs of restructuring our broadloom carpet operations.

Reported profit after tax was \$3.0 million, compared with a loss of \$1.6 million in the previous year. Operating profit after tax but before restructuring costs was \$6.6 million, 55% up on the \$4.3 million in the previous year.

We are pleased to report that restructuring is now largely complete, and all likely associated costs have been accounted for.

Financial position

With the benefit of strong cash flows from the business, and careful attention to inventory and capital expenditure, we were able to materially strengthen the balance sheet over the course of the year. Net debt was reduced by \$13.3 million or 20% to \$53.3 million at year end, and the gearing ratio reduced to a more conservative 57%, compared with 73% at the end of the previous year.

Total assets for the Group at year end were \$197 million, a decrease of \$5 million from the previous year, mainly attributable to reduction in inventories.

Shareholders' equity was up \$3.1 million to \$93.9 million.

Cash flows

Net cash flows from operating activities were \$11.7 million, which is a \$3.6 million or 44% improvement on 2012.

Carpet business

The carpet business comprises our broadloom carpet operations, Cavalier Bremworth and Norman Ellison Carpets, and our carpet tile division, Ontera Modular Carpets.

The difficulties we encountered in 2012 and part of 2013, including, amongst other things, increased wool price in finished goods, depressed residential and contract building activity and a shift from wool-rich products to synthetics, have been well documented and largely behind us now as we move into the 2014 financial year.

We have been compelled to look very closely at the way we were operating the business with the changing landscape, and we have reengineered ourselves in order to prosper in the long term.

We announced our business improvement plan at the last Annual Meeting. While most initiatives have been implemented, some are still in progress. The main areas of improvement are:

- Reduction of debt and inventory – the targets have been met, and we are at debt and stock levels that we are much more comfortable with.
- Closure of one of three spinning plants to reduce the cost base – this has been completed.
- The consolidation of the New Zealand-based warehousing and distribution operations has been completed.

- In March 2013 in New Zealand and June 2013 in Australia, we introduced a synthetic range of carpet under the Cavalier Bremworth brand, called the Habitat Collection, featuring the premium Solarmax yarn system. This has been well received in the market, and while the programme is still in its infancy, we have already exceeded our sales targets for these products and demand is strong.
- In June 2013, we announced the consolidation of tufting with the transfer of the NEC Tufting operation in Onehunga to the Cavalier facility at Papatoetoe making us more efficient and cost effective. This project is all but completed.
- We have combined the sales and administration functions of NEC and Cavalier, further reducing costs while arming our sales force with a complete range of products to offer the market
- We have simplified our brands to avoid confusion and duplication by dropping the Knightsbridge and Kimberley offerings, reducing poor performing SKU's in the process. We now have products that span all segments of the market, from the high-end Bremworth Collection and Cavalier Bremworth to mid to lower-end NEC offerings, in both synthetic and wool products. The commercial sector is also covered with Ontera tiles and Cavalier Commercial products.

Other future initiatives

We will be introducing new products in both synthetic and wool in the upcoming months.

We have demand for high-end felted yarn products in Australia and further offshore, and we have recently had positive dialogue with, and orders from, customers in the US, Asia and Europe. While current volumes are low, this is an area we are looking to expand in 2014, as new products currently under development come on stream.

Carpet tiles, once almost exclusively destined for CBD commercial office applications, are now a common feature in education, health and aged care, hospitality and “soft commercial” multi-level apartments. We will be looking to increase our volumes in these areas, also with some exciting new products.

Wool business

Our wool business comprises the Elco Direct wool acquisition operation and our 50% interest in commission woolscourer, Cavalier Wool Holdings.

Wool acquisition

I am happy to report that 2013 was a much better year for our wool buying business, with operating profit significantly up on 2012 as a result of stronger margins.

Volumes were higher – although revenue did drop 15%, which is a function of lower wool prices in the market.

Wool scouring

Our 50% owned wool scouring business, Cavalier Wool Holdings or CWH, had a stunning year, with Cavalier's share of tax paid earnings of \$5 million from this business a record.

This is a well-managed business that has benefited from high wool grease prices. Wool grease is a by-product of the scouring process that is sought after for a variety of compounds including lanolin that is used in pharmaceutical and skincare products.

Yarn business

Radford Yarn or RYT is our specialist felted yarn manufacturer, which is now 100% owned following the purchase of the remaining 25% owned by minorities in December 2012.

The 2013 year started slowly for RYT. However, towards the latter part of the year, demand and volume increased, and these have continued strongly into the 2014 financial year.

The specialist yarn produced by RYT is a critical element for our expansion into luxury carpets for premium-end markets offshore with the products' unique look and feel.

Earnings outlook

At this early stage of the 2014 financial year, it is difficult to predict the year end position as there are many factors that can influence results.

We have had a slower start to the year than we would have liked. However, we are still significantly ahead of the corresponding period last year.

The main shortfall has been in the carpet business where margins and volumes have been below expectations. However, confidence does appear to be improving in both New Zealand and Australia, so at this stage, we are reasonably comfortable that we will meet targets for the remainder of the year.

It is unlikely that the wool scouring business can match last year's record result as wool grease prices have dropped substantially, and wool grease revenue is a significant component of bottom line profit.

The volume of wool in the market has reduced due mainly to the drought early in the year and a lack of supply. This is driving up wool prices, and while they are not at the levels experienced in the 2010/11 season, we are monitoring developments very carefully.

The yarn and wool acquisition businesses have exceeded expectations for the first quarter of the financial year.

We have had a close look at the performance of all divisions to date and considered the impact of the key variables going forward and the best earnings guidance we can give at this stage is normalised earnings between \$8 million and \$10 million tax-paid.

The future

While we have been through two difficult years, and profits have fallen well below traditional levels, they have forced the company to take a close look at itself and change many aspects of the business so that we are better-placed to improve Cavalier's performance.

We have reduced the cost base to more appropriate levels, streamlined the business, developed and introduced new products and channels and formalised strategic plans for the main businesses.

I am confident that we have laid a platform for growth that will increase future company profitability.

Staff

On a final note, there has been significant change over the last 24 months and these changes would not have been possible without the support and dedication of all our staff. I would like to take this opportunity to acknowledge and thank them all for their commitment, hard work and energy – without good people we will not succeed.

Ladies and gentlemen, that concludes my presentation.

Thank you.

Colin McKenzie
Managing Director