

# CAPILANO HONEY LIMITED

A.C.N.009 686 435

## HALF YEAR REPORT TO SHAREHOLDERS

for the six months ended 31 December 2005

Dear Shareholder

While the financial performance of the holding company for the 6 months has achieved a significant turn-a-round from the prior year, we will recognise in this report the structural changes that have occurred in the marketplace that will affect not only us, but the industry in the future.

### Financial Performance

The table below shows Capilano Honey limited achieved Earnings before Interest & Tax (EBIT) of \$1.9 million, an improvement of \$1.6 million from the prior year, and Net Profit before Tax (NPBT) of \$1.1 million in for the half year.

	2005	2004	2003
<b>Capilano Honey Limited - 6 months</b>	<i>\$million</i>	<i>\$million</i>	<i>\$million</i>
Earnings Before Interest and Tax (EBIT)	\$1.9	\$0.3	\$3.2
Net Operating Profit Before Tax (NPBT)	\$1.1	(\$0.5)	\$2.5

This financial year started with honey-buying prices adjusted to reflect our expectations of the market. While the expected crop remains surplus to Australian requirements, the current estimate of 14,135 tonnes is similar to last year. This equates to a surplus for Capilano of around 3,000-5,000 tonnes. The crop surplus is sold at bulk commodity prices, which are around US\$1350-1500/tonne, or between A\$1.80/kg to A\$2.00/kg before costs of drums, packing and freight. The average honey price of \$2.09/kg is an average determined by the returns of the bulk commodity market and the higher margin retail pack markets. As we receive more surplus under our quota system, the average honey price will move down.

That surplus can also grow through the reduction of retail pack honey we can sell. Although we have achieved a growth in market share, it is of a smaller market. We have advised shareholders previously of the decline of approximately 3,000 tonnes in the Total Honey Category in the Australian supermarket measured by A C Nielsen data over a three year period. This corresponds with a period of higher prices sparked by shortage of honey due to both drought and suppliers leaving the company to pursue export bulk markets; the residue publicity; and lastly the massive growth in chocolate spreads being a new introduction to the category.

	2005	2004	2003
<b>Capilano Honey Limited</b>	<i>tonnes</i>	<i>tonnes</i>	<i>Tonnes</i>
Annual Crop	14,135	14,466	11,949
Honey Price / Kg	\$2.09/kg	\$2.96/kg	\$4.48/kg
Total Honey Category - Supermarkets	9,317	9,338	10,038

The financial result has also been affected not only by the general decline in consumer spending in the last 3 months but also some structural change happening mainly in the domestic market but also in the overseas markets.

### Structural Change

Rather than an improvement in the total honey category in domestic supermarkets, sales have been flat. The total honey category has declined slightly, contrary to our expectation. Despite this, Capilano has again increased its market share as a result of its marketing initiatives.

However, the fragmentation of the industry continues. Initially we had beekeepers exporting direct to chase the high price/low exchange rate, a combination rarely seen in the bulk commodity market. After that 'boom' went 'bust', their attention changed to the domestic market to chase the high prices the shortage of honey produced. New competitor packers emerge and new competition for private label and domestic bulk sales has produced rapid falls in selling prices.

The introduction of electronic auctions over the Internet for private label business and participation by the new competitors has slashed millions of dollars in contributions from these segments. There is no guarantee these electronic competitors can provide the level of supply and quality as noted under the bidding terms. The supplier in these auctions has a reduced contribution and little left to contribute to marketing support to build the category, and support for the products is usually limited to discounting by the retailer.

We have also been affected in this period by the closure of a major customer's factory, permanently moving their manufacturing offshore. This diverts honey back to the bulk commodity market.

In this period we have also observed the replacement by Coles of their 'Farmland' label for 'You'll Love Coles'. Volume estimates supplied by Coles for our supply were down by almost 50% on actual achieved, and honey sales in their private label transferred to the lowest priced tier.

The impact on domestic revenue is seen below. Lower selling prices force profits and supplier honey price down.

<b>Capilano Honey Limited</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
<b>Revenue - 6 months</b>	<i>\$million</i>	<i>\$million</i>	<i>\$million</i>
Domestic	\$27.4	\$29.6	\$32.3
Export	\$8.9	\$10.6	\$9.5
<b>TOTAL</b>	<b>\$36.4</b>	<b>\$40.2</b>	<b>\$41.8</b>

The full impact of the electronic auctions and private label market positioning is yet to be felt by industry as competitor packers adjust honey-buying prices to compete. It makes the product a commodity since the only alternative is the export commodity bulk prices, unless you have overseas retail pack markets.

Our honey-buying price has moved to an average of \$2.09/kg and further adjustment will be required. It means our new product and global strategies become even more important to bring value added products to consumers and markets prepared to pay for them.

#### Associate

<b>Capilano Labonté Inc (CLI)</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
	<i>CAD\$'000s</i>	<i>CAD\$'000s</i>	<i>CAD\$'000s</i>
Revenue	\$5419	\$6030	\$5111
Earnings Before Interest and Tax (EBIT)	(\$22)	(\$402)	\$(157)

Capilano Labonté Inc (CLI), in which we have a 50% share, continues to make gains in the Canadian market. It has been our quality and commitment to growing the honey category in Canada that secures our position in the market. Our exports to Canada of retail tonnage are over 1000 tonnes annually. We have also been successful in exporting Canadian honey in retail packs to SE Asia, to meet certain consumer taste profiles. We hope to successfully use our Canadian position to introduce Canadian, Australian and Argentine honey to the USA. Capilano-Argentina also continues to contribute positively to the Capilano Group.

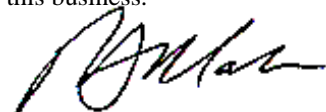
#### Subsidiary

<b>Medihoney Pty Ltd</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
	<i>\$'000s</i>	<i>\$'000s</i>	<i>\$'000s</i>
Revenue	\$1613	\$1016	\$1124
Earnings Before Interest and Tax (EBIT)	\$(790)	\$(573)	\$50

Medihoney is an important initiative in our growth strategy with honey value-added products. The introductory phase has been expensive and time consuming, involving establishing the product's credentials through clinical trials and overcoming the regulatory hurdles to make the product a commercial proposition. While Medihoney results show an EBIT loss of \$790k in line with its budget, it is consolidating its position in the Australian market with success in its distribution through pharmacies. The process has now commenced of distribution of its woundcare products to domiciliary care/hospitals, which requires the education and demonstration of nursing and medical specialists by a small Medihoney clinical team.

Medihoney is making progress in its UK market, building upon the successful completion of regulatory requirements such as the Conformity Assessments and CE Mark Certification of the prior year. These latter achievements took a few years to complete and we have reached a stage where a higher level of investment in the business is necessary to build sales growth.

The environment in which Medihoney competes is changing and much greater interest is developing in using antibacterial honeys as an alternative to existing woundcare products. Our main activities in the initial business stage related to proving its product attributes by case studies, clinical trials and research & development projects. We have recently undertaken a review of our product portfolio and branding strategies to ensure the products are correctly positioned for the growth phase of the business. Further investment is now required to achieve Medihoney's sales potential and the return expected from this business.



R D Masters  
Managing Director