

„BANJALUČKA PIVARA“ AD  
BANJA LUKA  
- Management Board -  
Ref: 02-189-1/2016  
Date: April 26, 2016

## **Report on Business Operations in 2015**

### **Introduction**

2015 was one of the best beer seasons for a number of years. Summer started early and stayed warm well into the autumn. This helped to reverse the market decline of recent years and our assessment is that the total beer market grew by around 2% in 2015. Banja Luka Brewery outperformed the market, with strong sales growth of 7.5% in volume and value. These gains came primarily from increasing market share of Nektar Pivo against our key competitor Jelen. Nektar Pivo is now the clear beer market leader on the BiH market with a total share of 21%.

Net profit of 6.2 million KM is a small drop of 0.2 million versus 2014. However it should be noted that the 2014 result was boosted by a one-off revenue item of 2.8 million KM due to a reversal of previous years' expenses related to provisions for preferential dividend. Consequently, shareholders will be pleased to note that this result is an increase of 2.6 million KM on a like-for-like basis, when this is excluded.

### **The Beer Market in 2015**

The competitive landscape on the BiH beer market continues to become more intensive. Our key competitor Molson Coors (Jelen) focused a large portion of its investment on Banja Luka in 2015. In particular, they attempted to drive Nektar out of distribution in leading bars and restaurants in the region by offering inflated sales incentives and capital investments. To a very large degree, thanks to the loyalty of Nektar consumers, they have not been successful in this endeavour. Nonetheless, we were obliged to increase our level of spend in HoReCa and leading retailers to maintain our presence.

Carlsberg (Lav, Tuborg), on the other hand has, to a large extent, scaled back its investment in Banja Luka, in order to focus on Semberija and Middle Bosnia. They have closed their Banja Luka distribution centre and significantly reduced their regional sales team. This can be seen as a clear endorsement and victory for the strength of Nektar Pivo and Banja Luka Brewery as an independent player able to compete with major multinationals.

Unfortunately, where one player fades a new one inevitably comes to take its place. This new threat appears to be from Heineken, who have taken a number of big steps to strengthen their regional position in the beer market. In Serbia Zaječarsko Pivo has very successfully challenged Jelen, taking their volume and share. This brand will inevitably be heavily promoted in BiH and is already starting to be present,

especially in the Eastern Republic of Srpska. Heineken also completed the purchase of Laško group breweries in 2015. Their brands sell around 130,000 hectolitres in Bosnia and Herzegovina, which will give important additional weight to their portfolio here.

Among the local breweries, Sarajevo brewery was notable for a strong re-launch of their core brand Sarajevsko. This was quite successful, particularly in Sarajevo itself and resulted in some loss of volume for our Kaltenberg Pils sales, which are mostly centred in Sarajevo region.

### **Investments in Production**

The main focus of investment and management resource in 2015 was on our utilities. This included completing the installation of water and energy measurement throughout the Brewery, separation and replacement of our waste water pipes throughout the Brewery, and installation of a new 10 bar compressor.

This work is yielding important benefits both directly and indirectly. We have achieved a 30% reduction in water consumption in the last few years, as well as discovered that we were being overcharged by the water company. Energy consumption is now much better understood and consequently we know where future projects should be focused.

Another important investment was made in installation of fixed piping in the 'old' fermenters block as well as re-sealing the internal surfaces of a number of unused fermenters. This effectively means that we have increased our fermentation capacity and made a very valuable step via the fixed network to increase quality control, reduce losses, improve the process management, and eliminate possible microbe infections.

### **Sales and Marketing**

This year proved to be an exhausting year for the event team, who covered over 100 events directly and countless more indirectly. Our ability to be always present at local events and gatherings is an important part of our total marketing activity which we plan to spread geographically in the coming years. Two new activities were the Nektar Fresh Wave Music Festival, which took place in August, and the Banja Luka Winter Ice rink, which we set up and financed through the winter season. Both helped us to project the brand and build strong local relations. It is our intention to continue to expand these events in the coming years.

The impossible task of meeting the ever growing demands of café and bar owners for investments and equipment, was a big theme in 2015. This was largely thanks to a sustained campaign by Molson to drive Nektar out of distribution through big investments. The Company reacted to this pressure by increasing investments, but we try at all times to maintain a balanced long term view and spend intelligently. Certainly this problem will dominate our budget discussion over the coming years.

Advertising and promotion for Nektar was energised by the launch of a new image TVC in April and a major consumer promotion for cans in May and June. Both were well received and our research tells us that Nektar continues to score particularly highly among younger consumers, which we find especially positive.

We would also like to highlight the great success of our cans sales which increased by 41% in 2015. A combination of promotion, improved listings and strong merchandising yielded dramatic results.

### **Prices and Margins**

The main driver of the big improvement in 2015 financial results was excellent management of costs. This comes from the cumulative focus of the last few years on efficiency and strong relationships with suppliers, which has resulted in dramatic cost savings throughout production. In addition to this we saw the benefit of our investment in the canning facility in 2014, which has resulted in direct cost savings compared to using a 3<sup>rd</sup> party filler of more than half a million KM. We should also mention that we have benefited from the lower rate of excise that we were paying in 2015. On 1<sup>st</sup> January 2016 the Company started to pay excise at the rate of 'big' breweries.

### **Human resources**

The process of improving management processes has continued, with a focus upon clearer responsibilities throughout the business, with greater accountability. A number of changes were made to structure and a reduction of complexity in some of our processes, particularly in the logistics department. Our management aim is to build strength in depth throughout the Company. The Company is committed to its employees, and in particular the long term stability of the workforce, recruiting and maintaining good skills and experienced employees. The Company also seeks and supports young, dedicated and ambitious talents in all areas of its operations, and is fully supportive of continuous development of its employees' skills.

### **Corporate Governance - Application of Standards**

Commitment of the Brewery management to transparency of its operations and application of recognised Standards of corporate governance (adopted by the Republic of Srpska Securities Commission) is unchanged. The Standards Governing Joint Stock Companies (applying to companies enlisted on the official stock exchange) are applied in daily practices of the Company. In March 2011, Banjalučka pivara adopted its own Code of Conduct and Management, and Banjalučka pivara continues to further develop its corporate website, to include all relevant, timely available investor information - company financials, the most important information on business operations, its governing bodies and members of the management team, etc.

In addition to this, Banjalučka pivara is fully implementing various imperative norms, regulated and sanctioned by various laws (Law on Enterprises, Law on Securities Market, Law on Accounting and Audit, etc.) and acts of the Commission for Securities and Stock Exchange Rules, incorporated in the Brewery's Articles of Association, Rulebook on Procedures of the Assembly and other acts of the Company.

### **Conclusion**

The Company achieved an excellent set of results in 2015, thanks to our approach of focusing on building a vibrant and well managed portfolio of brands. Our various improvement programmes, the falling oil price and well-judged investments have all helped us to another year of improved results. As a result, on many levels, this Company is in a stronger and more stable position than four years ago. We will continue to build on our strengths and develop our position on the market. Nonetheless the general state of the BiH economy is not improving and competitors are constantly finding new ways to undermine our position. Furthermore, in many respects the greatest threat to the future success of the Company is the unpredictable and increasingly aggressive approach of government and government institutions towards business in any form of revenue generation and tax collection. Our hope is that this attitude will change and instead manufacturers and employers of any kind will be more highly appreciated in future.

CHAIRMAN of  
MANAGEMENT BOARD  
Ragnar Tryggvason

GENERAL MANAGER

Nicholas Penny