11th Annual General Meeting (AGM) of Saudee Group Berhad ("Saudee" or the Company") to be held on 20 December 2019

Strategy & Financial Matters

1) During the financial year (FY) 2019, the Company has changed its business model to "Distributorship" from "Direct Retail Selling" previously. The transition has lowered the expenses spent on administrative works, selling and distribution activities. Cashflow from operating activities has also improved as distributors are more disciplined in fulfilling their commitment (page 17 of AR2019). Nevertheless, the Company is still making losses at pre-tax level in FY2019.

   a) To what extent is the Management confident that the new "Distributorship" model as well as the strategy to grow the Hotel, Restaurant and Café (HORECA) and Original Equipment Manufacturer (OEM) segment will improve the Company's financial performance?

   Our response:

   Barring any unforeseen circumstances, the Management is of the opinion that the new "Distributorship" model as well as HORECA and OEM segment will improve the Company's financial performance gradually. Even though, the Company still record a loss at the pre-tax level in FY2019, but the results has also shown the following positive indicators:

   i) The changed of business model from "Direct Retail Selling" (DRS) to "Distributorship" has reduced the expenses spent on administrative works, selling and distribution activities;
   ii) The number of customers in thousands under DRS has been consolidated to a few Distributors which are more organised and experience in the FPP distribution network;
   iii) The appointed Distributors are better equipped financially and resourceful in managing the distribution cost. Thus, they are more disciplined in fulfilling their commitment;
   iv) HORECA and OEM segment require more time and commitment to materialise the potentials into sales. However, once the potential customers are satisfied with the proposed products, the Company will be able to develop a long term relationship as long as the products cost and quality are not compromised. Further, the HORECA and OEM segment contribute higher margin to the Company.

b) Given the improvement and benefits brought by the new business model and direction, why was it not implemented earlier but only now after five-year of losses?

<u>Our response:</u>

We wish to highlight that the Management under the new leadership has started to take its form in FY2018. Under the new guidance, the Management has since, focused on the potential of HORECA and OEM segment. As explained earlier, these segments require time, effort and commitment to convince the potential customers that the Customers has the capability and capacity to deliver in such segment.

Further, the Company was facing more critical issues such as tight cashflow position, high gearing ratio and slow collection issues, low staff morale, just to name a few, of which, the Management must focus and turnaround the unfavourable financial positioning before the Company can embark on any new business direction.

Moreover, the change of business model from DRS to Distributorship requires more time to study and evaluate its benefits and risks before the Management could make a decision. The Management did not have the privilege of any excess fund to rollout new ideas and gauge the market feedback later.

c) Please explain how different is the "Distributorship Model" from the "Direct Retail Selling Model" in terms of processes and modus operandi.

<u>Our response:</u>

In "Direct Selling Model" the Company need to maintain internal sales teams to service all customers in the regions and this incurred high selling and administrative cost such as promotion expenses, listing of products cost, sales commissions, salary and etc. With the implementation of "Distributorship Model" the Company is able to pass over all this administrative and selling costs to the Distributor as all marketing and logistic matters are handled by the Distributors.

Besides that, the Company is able to get more accurate market feedback from the Distributors, as such, the Company will be able to give timely respond to the needs of the market.

2) Gross profit margin of Saudee has declined to 9.2% in FY19 from 20.3% in FY18 (page 17 of AR2010) due to a RM1.5 million write-down of inventory value (page 79 of AR2019).

a) Does the Company foresee another write-down on inventory value in FY2020?

<u>Our response:</u>

Barring any unforeseen circumstances, the Company does not foresee drastic write-down on inventory in FY2020. However the business environment remain challenging. If the situation on rework of slow moving Further Processed Products (FPP) occur, it will leave the Management with no choice but to rework on the slow moving FPP in which might affect the value of inventories. Nevertheless, the Management will continue to push for the sales of potentially slow-moving FPP to avoid the repeat of such circumstances.

b) What lessons has the Management learned from this incident?

Our response:

The Company will improve on the inventory management system i.e. control of the finished goods of FPP in term of volume produced, delivered and the turnover period, volume of raw material purchased in order to achieve optimal level of inventories on hand without putting burden on cash flow. More market feedback and market research to be performed in order to understand the market need.

Ultimately, the Management must be prudent in its decision making process. The Management need to understand the difference between fantasy and reality.

3) Going forward, the Company expects its finance cost and bank borrowings to decrease gradually (page 23 of AR2019).

a) Why does the Company expect the financing cost and bank borrowings to decrease gradually?

Our response:

The changes in business model enable the Company to generate positive operation cash flow. With the better cash flow management, the excess fund from operation can be used to reduce bank borrowings thus reduce the finance cost in coming financial years.

b) With Saudee's strategy to grow the HORECA and OEM segment, does it not require additional financing to expand the manufacturing facilities to cater for the new products?

Since additional financing may be required for the HORECA and OEM segment, will the Company continue still gradually reduce bank borrowings?

Our response:

As of FY2019, the manufacturing facilities is able to cope with the gradual growth of HORECA and OEM segment. However, the Company will continue to monitor and assess on the need to expand the manufacturing facilities as and when the need arises. The Company has been approached by a few potential parties in the OEM segment and the Management is still evaluating its potentials and the estimated CAPEX required.

4) The Company put RM6.37 million of receivables which is past due more than 90 days under the Expected Credit Loss (ECL) category when analysing the ageing profile of receivables (page 123 of AR2019).

   a) The ECL made up 35% of Saudee's total gross receivables of RM18.25 million in FY19, Why are the receivables facing such high non-collection risk?

      Our response:

      This is the inevitable business risk associated with the "Direct Retail Selling model" as the Company had to deal with thousands of customers. Lots of resources such as manpower need to be allocated to credit control under this business model. Unfortunately the Company is unable to manage this in the past, thus, straining the working capital and cashflow of the Company.

   b) What has been done to recover the outstanding receivables before they are classified as ECL?

      Our response:

      The Company will continue its effort to recover the overdue debts. Legal action will be taken against those with large amount of debts coupled with potential recoverability. However, for small amount of debts, the Company is unable to take legal action against such debtors as the legal cost is not justifiable.

   c) What are the suggestions provided by the Risk Management Committee to better assess future customers and thus reduce the risk of ECL?

      Our response:

      Stricter credit control procedures have been implemented e.g. more checking on customer historical and financial background via CITOS search, etc.

Corporate Governance Matters

1) Ordinary Resolution 4 is to seek approval in advance for the payment of Directors' fees for a sum not exceeding RM250for the financial year ending 31 July 2020 (page 2 of AR2019).

   Why does the Company seek shareholders' approval in advance for the payment of Directors' fee when the overall performance of the Company and the directors in FY2020 is yet to be seen?

   Our response:

   The Company is of the view that it is equitable to pay the Directors' fees on monthly basis and/or as and when incurred, particularly after the directors have discharged their responsibilities and rendered their services to the Company.

   The Management will monitor the approved amount to ensure no overpayment of fees.

2) The executive directors of Saudee namely Mr. Khoo Lay Tatt, Mr Tan Khang Khim and Ms. Low Ai Choo received RM256,400, RM206,400 and RM81,400 worth of bonuses in FY19 (page 32 of CG Report 2019), representing 9.5 months, 7.6 months and 4.28 months of their salaries.

   As the Company is making losses, what is the justification for EDs (ESPECIALLY Mr. Khoo and Mr. Tan) receiving such substantial bonuses?

   Our response:

   Previously the Company assess the bonus entitlement based on the financial year result and individual performance and payment was made in 2 to 3 months after the financial year. However with the Company's financial year in July, the Management has decided to change the bonus assessment from financial year to calendar year and the payment of bonus is to be made either in January or February of the following year. This also follow the norm that bonus payment is made before the festive season. For FY2019 bonus payment which is in relation to a period of 17 months with assessment from 1 August 2017 to 31 December 2018.

   Although the Company has recorded a pre-tax losses in FY2019, the financial position has gradually improved as follows:

i) The Company has recorded a net cash of operating activities of RM6.2 million in FY2019 as compare to RM5.5 million in FY2018;
ii) The Company's Current Ratio has improved from 1.4 times in FY2018 to 1.5 times in FY2019;
iii) The Company's Debts to Equity Ratio has been reduced further from 0.56 in FY2018 to 0.41 in FY2019. The Company's bank borrowings has reduced from RM37.6 million in FY2018 to RM29.3 million in FY2019.

   The Company reckoned the heavy responsibilities and time commitment of the Executive Directors in their tireless efforts to turnaround the Company with their knowledge, skills and experience to produce improving financial results. Thus, rewarding them with bonuses for the improved financial position of the Company.