Fonterra completes reset, announces annual results and long-term growth plan out to 2030

**Annual Results Summary**

- Total pay-out for 2020/21 season: $7.74 per kgMS
  - Final 2020/21 Farmgate Milk Price: $7.54 per kgMS
  - 2020/21 dividend: 20 cents per share, comprised of 5 cent interim dividend and 15 cent final dividend
- Reported Profit After Tax: $599 million, down $60 million*
- Normalised Profit After Tax: $588 million, up $190 million#
- Total Group normalised EBIT: $952 million, up $73 million#
- Net debt1: $3.8 billion, down $872 million
- Debt to EBITDA ratio: 2.7x improved from 3.3x
- Full year normalised earnings per share: 34 cents

* 2020 financial year included the gain from the divestments of DFE Pharma and foodspring®
# Normalised numbers reflect the underlying performance of the business.

Fonterra Co-operative Group Limited today announced a strong set of results for the 2021 financial year, reflected in a final Farmgate Milk Price of $7.54, normalised earnings per share of 34 cents and a final dividend of 15 cents, taking the total dividend for the year to 20 cents per share. The results come as Fonterra moves through its business reset and into a new phase of growing the value of its business.

CEO Miles Hurrell says the last three years have been about resetting the business. “We’ve stuck to our strategy of maximising the value of our New Zealand milk, moved to a customer-led operating model and strengthened our balance sheet.

“The results and total pay-out we’ve announced today show what we can achieve when we focus on quality execution and an aligned Co-op.

“I want to thank our farmer owners and employees for their hard work and commitment over the last few years that has got us to this position. Together, we’ve shored up foundations and done this despite the challenges of operating in a COVID-19 world.

“Although the higher milk price and tightening margins put pressure on earnings in the final quarter, this is a strong overall business performance, allowing us to deliver $11.6 billion to the New Zealand economy through the total pay-out to farmers.

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1 Net debt excludes amounts attributable to disposal groups held for sale.
“The work we’ve done as part of the 2019 strategic reset means we’re well placed to take advantage of favourable industry dynamics. Growing global demand for dairy coupled with constrained supply has resulted in high prices for our milk. Our resilient supply chain has allowed us to get products to market and the healthy demand for our farmers’ New Zealand milk has seen a record shipping year for the Co-op.

“We’ve continued to reshape our business and the sales of our joint venture farms and wholly-owned farming hubs in China. Our continued focus is to get our New Zealand milk to the world.”

Total Group normalised EBIT, which reflects underlying business performance, was up 8% to $952 million, with Total Group normalised operating expenditure down 3% to $2.2 billion.

Mr Hurrell says a focus on financial discipline has paid off. “Net debt is down by $872 million to $3.8 billion, cashflow has improved again and at 2.7x, we are now within our long-term target Debt/EBITDA ratio.

“We are pleased with our $599 million reported profit after tax. While down on last year, the 2020 financial year benefited significantly from the divestments of DFE Pharma and foodspring®. Normalised profit after tax grew by $190 million to $588 million, driven by improved earnings and lower interest expense.

“Our sales book is well balanced across the regions and a number of our markets have performed well. In Asia Pacific, significant improvements in our Foodservice and Consumer channels have pushed normalised EBIT up 28% to $305 million. We’ve expanded our Foodservice footprint in the region and are seeing the benefits of that.

“Here – like in many of our markets – COVID-19 has changed consumer behaviour, with people choosing to cook at home. That’s really benefited our consumer brands and supported upward momentum in our Consumer channel performance, particularly in New Zealand and Australia.

“Greater China continues to be an important market for us, with normalised EBIT up 10% to $403 million. This speaks to the strength of our Foodservice channel, China’s dynamic economy and its love for dairy.

“Africa, Middle East, Europe, North Asia, Americas’ (AMENA) normalised EBIT was down 28% to $336 million, reflecting our strategy of redirecting product into higher-margin markets. However, we have seen improvements in our Foodservice and Consumer channels within the region, including a turnaround for our Chilean business.

“Our total dividend for the year is 20 cents per share, which includes an interim dividend of 5 cents per share and a final dividend of 15 cents per share. Three cents of the 15 cents per share reflects the reversal of previous impairment of our China Farms. For a 100% share backed farm, this means a total pay-out of $7.74 per kgMS.”

Mr Hurrell says that progress isn’t limited to the Co-op’s financial performance. “I’m proud of our efforts to reduce our environmental impact. New Zealand dairy has the lowest carbon footprint in the world, but we also know we need to do much more.

“This year, we reduced our carbon emissions from coal by more than 11%, as Te Awamutu completed its first season using renewable wood pellets. We also recently announced our Stirling site will move to renewable energy from August next year. Our farmer owners are also doing their bit, with record numbers achieving the top level of our Co-operative Difference framework and 53% of supplying farms now having a Farm Environment Plan. That’s good for the environment and it’s also what our customers expect.”

Looking to the current season, Fonterra has announced a 2021/22 earnings guidance range of 25-40 cents per share and has also reaffirmed its 2021/22 forecast Farmgate Milk Price range of $7.25 - $8.75 per kgMS, with a midpoint of $8 per kgMS.

Mr Hurrell says the strong milk price is likely to continue. “A high milk price is good for farmers and good for the New Zealand economy. However, this does have the potential to squeeze our sales margins and impact earnings.”

Mr Hurrell says the impact of COVID-19 continues to be felt, particularly across the supply chain. “We expect competitive tension in the global shipping market to continue this financial year. We have largely been able
to mitigate this thanks to the strength of our Kotahi partnership which has allowed us to keep our product moving through the supply chain.”

**Long-term strategy**

Fonterra is now turning its mind to the next phase of its strategy, as it completes its reset and focuses on value growth. Mr Hurrell says as the Co-op looks out to 2030, the fundamentals of dairy – in particular, New Zealand dairy – look strong.

“Put simply, the world wants what we’ve got – sustainably produced, high-quality, nutritious milk. This comes at a time when we see total milk supply in New Zealand as likely to decline, and flat at best.

“On one hand, this requires the right capital structure to help ensure we don’t lose the benefits of what generations of farmers have built – a New Zealand dairy co-operative of scale.

“But on the other hand, it gives us more options to be selective about what we do with our Co-op’s milk. In doing so, we can increase the value we generate for farmers and New Zealand over the next decade.

“To make this happen we have made three strategic choices – continue to focus on New Zealand milk, be a leader in sustainability and be a leader in dairy innovation and science.”

**Refine our asset portfolio to focus on New Zealand milk**

Fonterra believes it has an opportunity to differentiate New Zealand milk further on the world stage, with the aim of getting more value from the Co-op’s milk.

Mr Hurrell says this requires Fonterra to focus its capital and people on enhancing New Zealand milk and for these reasons the Co-op has reviewed the ownership of its two other milk pools – in Australia and Chile.

“Soprole is a leading Chilean dairy brand, and Prolesur is a subsidiary of Soprole focused on sourcing milk and manufacturing products in Southern Chile. The operations do not require any New Zealand-sourced milk or expertise, and in this context, we are starting the process to divest our integrated investment in Chile.

“Fonterra Australia is on strategy for the Co-op and remains an important export market for our New Zealand milk, especially for Foodservice products and advanced ingredients. We are considering the most appropriate ownership structure for this business, one option is an IPO, with the intention that we retain a significant stake.

“We see both these moves as critical to enabling greater focus on our New Zealand milk and, importantly, allowing us to free up capital, much of which is intended to be returned to shareholders.”

**Invest in sustainability and dairy innovation and science**

Mr Hurrell says to strengthen the value proposition of its New Zealand milk, the Co-op will increase investment in sustainability and R&D.

“New Zealand has the unique position of being the lowest carbon producing dairy nation on the planet and when you combine this with our pasture-based model, animal welfare standards and scale efficiency, we have something that can’t be replicated.

“But we can’t slow down now. Customers want to know where their food comes from and the environmental impact it leaves, and a farmer’s livelihood relies on a stable climate and healthy ecosystems.

“This is why we have an aspiration for our Co-op to be Net Zero carbon by 2050. Over the next decade we intend to invest around $1 billion in reducing carbon emissions and improving water efficiency and treatment at our manufacturing sites.

“We also know that to maintain our relative carbon footprint advantage against the northern hemisphere farming system we must solve the methane challenge.

“We are aiming to increase our current total annual R&D investment by over 50% to around $160 million per annum in 2030, with about $60 million per annum specifically targeted at growth in Active Living, as
we continue to look for solutions for the methane challenge and develop new innovative products to support our value growth plans.

“Our investment in sustainability initiatives across our supply chain, will support our investment in our brands to showcase our New Zealand sustainable nutrition story. This will put us in a position to further grow our Foodservice and Consumer channels across our markets in the Asia Pacific region and gain more value through our Ingredients channel by helping customers meet their own sustainability goals.

“As we move more milk into Foodservice and Consumer, we will direct less through our Ingredients channel and aim to shift more towards higher value ingredients such as in our Active Living business. This will see us focus more of our Ingredients business on solutions for physical, patient, digestive and mental wellness plus immunity where we can make the most of our expertise in dairy innovation,” says Mr Hurrell.

Future growth opportunity – nutrition science solutions

Mr Hurrell says the Co-op’s focus on value creation also opens up choices for investing in new, high value growth opportunities in future.

“We have an ambition to play more boldly in nutrition science solutions, which underpins a $500 billion slice of the global health and wellness category.

“We have set up a dedicated team to explore what the future of Nutrition Science Solutions looks likes for our Co-op, and over the next year we’ll narrow down and prioritise the areas where we can build a competitive advantage,” says Mr Hurrell.

2030 financial targets

“Our focus on New Zealand milk, sustainability, and innovation and science will see us shift every aspect of our business to create more value. In doing so we aim to continue to improve our financial performance and, as a result, strengthen our ability to repeatedly generate cash and create value for our shareholders and New Zealand,” says Mr Hurrell.

There are four key value targets we’re aiming to achieve by FY30:

1. **An average Farmgate Milk Price range for the decade of $6.50-$7.50 per kgMS**
2. **A 40-50% increase in operating profit** from FY21 and, with the reduced interest from having less debt, this should translate into an approximately 75% increase in earnings, giving us the ability to steadily increase dividends to around 40-45 cents per share by FY30
3. **A Group Return on Capital of 9-10%**, up from 6.6% in FY21
4. Through planned divestments and improved earnings, **an intended return of about $1 billion to shareholders by FY24, and around $2 billion of additional capital available** for a mix of investment in further growth and return to shareholders. This is in addition to the approximately $2 billion expected to be invested in sustainability and moving milk into higher value products.

“We have an incredible natural product made on the pastures of New Zealand farms, a business supported by a talented and committed team, and an exciting opportunity to create value. It’s up to us as a Co-op to work together, make the necessary changes and ensure we’re creating goodness for generations,” says Mr Hurrell.

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Non-GAAP measures

Fonterra uses several non-GAAP measures when discussing financial performance. These measures include normalised profit after tax, normalised EBIT, EBIT, normalised earnings per share, normalisation adjustments and total Group measures. Total Group measures present the combined financial performance of the Group’s continuing and discontinued operations. Non-GAAP financial measures are not defined or specified by NZ IFRS.

Management believes that these measures provide useful information as they provide valuable insight on the underlying performance of the business. They are used internally to evaluate the underlying performance of business units and to analyse trends.

These measures are not uniformly defined or utilised by all companies. Accordingly, these measures may not be comparable with similarly titled measures used by other companies. Non-GAAP financial measures should not be viewed in isolation nor considered as a substitute for measures reported in accordance with NZ IFRS. Non-GAAP measures are not subject to audit unless they are included in Fonterra’s audited Financial Statements.

Please refer to the Non-GAAP Measures section in Fonterra’s 2021 Annual Review for further information about non-GAAP measures used by Fonterra, including reconciliations back to NZ IFRS measures. Definitions of non-GAAP measures used by Fonterra can be found in the Glossary.

Further detail of key assumptions, risks and uncertainties

This announcement refers to, and provides a high-level summary of, matters that are described in more detail in the booklet titled Our Plans to 2030. That booklet should be read in full. The booklet also identifies relevant assumptions, known and unknown risks, uncertainties and other important factors that could materially affect the actual outcomes achieved by Fonterra.

Any forward-looking statements, financial targets and ambitions (“Forward Statements”) in this announcement or the booklet are based on a range of assumptions, including the assumptions noted in the Appendix of the booklet. None of the Forward Statements is intended as a forecast, estimate or projection of the outcome that will, or is likely to, eventuate. They should not be taken as forecasts or a guarantee of returns to shareholders. The Forward Statements were prepared by Fonterra and have not been audited or independently reviewed.

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About Fonterra

We're an Aotearoa, New Zealand dairy co-operative owned by 10,000 farming whānau (families). Through the spirit of co-operation and a can-do attitude, Fonterra’s farmers, along with 20,000 employees around the world, share the goodness of our milk through innovative consumer, foodservice and ingredient brands. Sustainability is at the heart of everything we do, and we’re committed to leaving things in a better way than we found them. Everyday people working hard to be Good Together in the community.

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