Media release

13 September 2018

FONTERRA ANNOUNCES FY18 ANNUAL RESULTS AND OUTLOOK FOR FY19

- Total Cash Payout for 2017/18 season: $6.79
  - Farmgate Milk Price $6.69 per kgMS
  - Dividend of 10 cents per share
- New Zealand milk collections: 1,505 million kgMS, down 1%
- Sales volumes: 22.2 billion Liquid Milk Equivalents (LME), down 3%
- Normalised sales revenue: $20.4 billion, up 6%
- Net loss after tax: $196 million
- Normalised EBIT: $902 million, down 22%
- Normalised gross margin: 15.4%, down from 16.9%
- Return on capital: 6.3%, down from 8.3%
- Normalised earnings per share: 24 cents
- Gearing ratio: 48.4%, up from 44.3%
- FY19 forecast Farmgate Milk Price: $6.75 per kgMS
- FY19 forecast earnings per share range: 25-35 cents

** Non-GAAP measures. Information on the non-GAAP financial information used by Fonterra are found at the end of this document.*

Today Fonterra announces its FY18 annual results, the plan to improve its business performance and the outlook for FY19.

The Co-operative reports a Net Loss After Tax of $196 million. Normalised EBIT was $902 million, down 22%, the Co-operative's gearing ratio was up from 44.3% last year to 48.4% and return on capital was 6.3%, down from 8.3%.

Fonterra CEO Miles Hurrell says the Co-operative's business performance must improve.

"There's no two ways about it, these results don't meet the standards we need to live up to. In FY18, we did not meet the promises we made to farmers and unitholders," says Mr Hurrell.

"At our interim results, we expected our performance to be weighted to the second half of the year. We needed to deliver an outstanding third and fourth quarter, after an extremely strong second quarter for sales and earnings – but that didn't happen."

Mr Hurrell says that in addition to the previously reported $232 million payment to Danone relating to the arbitration, and $439 million write down on Fonterra's Beingmate investment, there were four main reasons for the Co-operative's poor earnings performance.

"First, forecasting is never easy but ours proved to be too optimistic. Second, butter prices didn't come down as we anticipated, which impacted our sales volumes and margins. Third, the increase in the forecast Farmgate Milk Price late in the season, while good for farmers, put pressure on our

margins. And fourth, operating expenses were up in some parts of the business and, while this was planned, it was also based on delivering higher earnings than we achieved.
"Even allowing for the payment to Danone and the write down on Beingmate, which collectively account for 3.2% of the increase in the gearing ratio, our performance is still down on last year."

Mr Hurrell says when looking at the underlying performance of the business, which you can see in the normalised EBIT of $902 million, progress has been made in moving more milk into higher value products.

"While sales volumes were down 3% in FY18, a larger proportion of milk was sold through Consumer and Foodservice and Advanced Ingredients. In fact, 45% of our sales volumes were through these businesses and this is up from 42% in FY17, despite the higher input-price environment.

"Our Consumer and Foodservice business grew in all regions, except Oceania, with our strongest growth in Greater China. Of particular note, our Consumer business in China broke even this year, two years ahead of schedule. A big contributor to this success is the popularity of Anchor, which is now the number one brand of imported UHT milk in both online and offline sales in China.

"Despite this progress, performance across the Co-operative was below our expectations. Based on this, the Board has decided to limit our dividend to just the 10 cents paid in April and has confirmed the final Farmgate Milk Price for the 2017/18 season at $6.69 per kgMS," added Mr Hurrell.

Plan to lift Fonterra's business performance

Mr Hurrell says these results are not just numbers – they're the livelihoods of the Co-operative's farmers and their families and the investment of unitholders.

"There are people depending on us – farmers, unitholders and employees who want to be part of a successful Co-operative. We are putting in place a clear plan for how we are going to lift Fonterra's performance. It relies on us doing a number of things differently.

Fonterra's Board and Management has outlined a plan based on three immediate actions:

1. **Taking stock of the business** – Fonterra will re-evaluate all investments, major assets and partnerships to ensure they still meet the Co-operative's needs today. This will involve a thorough analysis of whether they directly support the strategy, are hitting their target return on capital and whether it can scale them up and grow more value over the next two-three years. This will start with a strategic review of the Co-operative's investment in Beingmate.

2. **Getting the basics right** – Fonterra has already begun taking action and fixing the businesses that are not performing. The level of financial discipline will be lifted throughout the Co-operative so debt can be reduced and return on capital improved.

3. **Ensuring more accurate forecasting** – the business will be run on more realistic forecasts with a clear line of sight on potential opportunities as well as the risks. It will also be clear on its assumptions, so farmers and unitholders know exactly where they stand and can make the decisions that are right for them and their businesses.

Outlook for 2019

The forecast Farmgate Milk Price for the 2018/19 season is held at the $6.75 per kgMS Fonterra announced at the end of August and the Co-operative's forecast earnings per share range for FY19 is 25-35 cents.

At $6.75 per kgMS the forecast Farmgate Milk Price for the 2018/19 season is the third consecutive year of strong milk prices. That's good for farmers and for rural economies where farmers spend 46 cents of every dollar they earn.

Chairman John Monaghan says the Co-operative is being clear with farmers and unitholders on what it will take for the Co-operative to achieve the forecast earnings guidance.

"For the first time we are sharing some business unit specific forecasts. Among others, these see the Ingredients and Consumer and Foodservice businesses achieving an EBIT of between $850 million and $950 million, and between $540 million and $590 million, respectively."

"FY19 is about lifting the performance of our Co-operative.

"We are taking a close look at the Co-operative's current portfolio and direction to see where change is needed to do things faster, reduce costs and deliver higher returns on our capital investments.

"This includes an assessment of all of the Co-operative's investments, major assets and partnerships against our strategy and target return on capital. You can expect to see strict discipline around cost control and respect for farmers' and unitholders' invested capital. That's our priority."

Click here to view Fonterra's Annual Results presentation and Annual Report.

Visit the Annual Results multimedia page to access B-roll and five short, downloadable audio grabs of Chairman John Monaghan, CEO Miles Hurrell and CFO Marc Rivers talking about aspects of this announcement.

Non-GAAP financial information

Fonterra uses several non-GAAP measures when discussing financial performance. These measures include normalised segment earnings, normalised EBIT, EBIT, normalisation adjustments and payout. These are non-GAAP financial measures and are not defined 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. These non-GAAP measures are not subject to audit unless they are included in Fonterra's annual financial statements.

Definitions of the non-GAAP measures used by Fonterra, and reconciliations of the NZ IFRS measures to the non-GAAP measures can be found on page 106 and 107 of Fonterra's Annual Report that is available on Fonterra's website.

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About Fonterra

We're a global dairy nutrition company owned by 10,000 farmers and their families. We've built our expertise on the legacy of the thousands of farmers who've made New Zealand a world leader in dairy. With a can-do attitude and a collaborative spirit, we're a world leading dairy exporter. Our 22,000 people share the goodness of dairy nutrition with the world through our innovative consumer, foodservice and ingredient solutions brands, and our farming and processing operations across four continents.