MEDIA RELEASE

Fonterra
Dairy for life

27 March 2013

FONTERRA POSTS STRONG HALF YEAR RESULT: VOLUME AND PROFIT GROWTH
$459 MILLION HALF YEAR NET PROFIT AFTER TAX
2013 MILK PRICE FORECAST REVISED

Click here to review the Interim Results presentation and Interim Report

Forecast

Fonterra Co-operative Group Limited today lifted its current forecast cash Payout for the 2012/13 season to $6.12 for a fully shared-up farmer, based on a higher forecast Farmgate Milk Price of $5.80 per kgMS and a forecast dividend of 32 cents per share.

The Co-operative also narrowed its earnings per share guidance to 45-50 cents per share.

The higher forecast was on the back of a strong first half performance by Fonterra, which saw Net Profit After Tax increase by 33 per cent to $459 million, following a particularly robust performance by NZ Milk Products and significant lifts in sales volumes in Fonterra's Asian and Latin American brands. These achievements were partly offset by continuing challenges affecting the performance of the Australian business.

"The new forecast reflects a recovery in global dairy commodity prices over the past two months," said Chairman John Wilson.

"Prices have increased in seven of the last fortnightly auctions on the online trading platform GlobalDairyTrade (GDT). The GDT-Trade Weighted Index is now 26.7 per cent above where it stood in February when the Board issued its last forecast.

"World dairy trade growth is being led by powders (combined whole milk and skim), reflecting strong demand at a time when global supply is constrained."

Interim Result

Commenting on the Co-operative's half year performance, Mr Wilson said: "We had excellent spring and early summer growing conditions across most of the country leading to strong growth in New Zealand dairy production and record volumes in the first half.

"However, the dry conditions in the North Island since January have created real challenges for our farmers, with many turning to supplementary feeds and shifting to once a day milking to maintain the condition of their herds.

"The drought in the third quarter has been more severe and lasted longer than anyone might have predicted, and means we are currently forecasting total milk collection volumes for the full season to finish in line with last season.

"Coping with the climate is part of farming. But there is no denying the stress that a drought causes and at times like these, farmer shareholders are looking for support from their Co-operative.

“Backed by our strong balance sheet and operating cash flows, we were able to increase the advance rate paid to farmers for their milk. The faster advance rate together with the higher forecast Milk Price means on average farmer shareholders will receive $100,000[1] earlier in the season.

“This is particularly important to our farmers. It means we are getting cash to them faster, as they begin to dry off their herds for the winter earlier because of the drought and no longer have milk flowing,” said Mr Wilson.

With the strong first half performance, the Board has lifted the interim dividend from 12 to 16 cents, 33 per cent higher than the comparable period. Sixteen cents represents 50 per cent of Fonterra’s forecast dividend for the current financial year, and the maximum available under the 40-50 per cent range in its dividend policy.

The interim dividend will be paid on 19 April 2013.

The Co-operative’s strong growth contributed to a Normalised Earnings Before Interest and Tax (EBIT) of $693 million, up 26 per cent. Revenue, however, was 7 per cent lower at $9.3 billion, reflecting lower dairy commodity prices and the strength of the New Zealand dollar against the US, more than offsetting the higher volumes sold.

Highlights compared to the same period last year include:

- Record milk volumes collected up 6 per cent;
- Total external sales volume growth of 8 per cent to 2.1 million metric tonnes;
- Normalised EBIT of $693 million was up 26 per cent (Normalised EBIT has been adjusted for the $24 million cost associated with the planned closure of the Cororooke plant);
- Net Profit After Tax of $459 million, up 33 per cent;
- Economic Debt to equity of 40 per cent, an improvement from 47 per cent last year;
- Earnings per share up 21 per cent;
- An interim dividend of 16 cents per share, up 4 cents per share.

CEO Theo Spierings said NZ Milk Products’ strong first half reflected the drive to achieve increased Volume and Value – two core elements of Fonterra’s business strategy.

“NZ Milk Products’ performance was achieved through increased volumes, effective management of our product mix and a focused effort by the sales team to achieve higher price premiums compared to dairy commodity prices.

“Despite the drought taking effect in the North Island in January, it was a different story for those in the South Island where the rainfall was higher than last summer. Fonterra’s milk collections for the season to the end of January were up 6 per cent on the same period in 2012 – which in turn flowed into record production, and another new export volume record achieved in December 2012.

“The commissioning last year of the Co-operative’s new Darfield site – where the Darfield Drier 1 can process 2.2 million litres of milk at peak in one day and produce 15 metric tonnes of milk powder per hour – was one of the factors that enabled NZ Milk Products to process the higher peak milk flows and deliver a strong performance.

“The business reacted swiftly to higher price signals for cheese, casein and Milk Protein Concentrate compared with Whole Milk Powder and other powder prices for most of the first half of the financial year. By moving our discretionary manufacturing, we were able to take advantage of this pricing differential. This flexibility at an operational level was a significant contributor to NZ Milk Products’ 9 per cent rise in sales volumes to 1,474,000 MT.

“At the same time, the sales team kept its focus on adding value for customers and attaining prices for products above GlobalDairyTrade (GDT).

“Despite the average USD commodity price being 16 per cent lower than the same period last year, NZ Milk Products’ focus on performance was reflected in a 65 per cent increase in Normalised EBIT to $422 million.

“The Australia-New Zealand business’ earnings declined, with Normalised EBIT down 32 percent. While our consumer business performance in New Zealand was slightly better than last year, Australia’s consumer business had to contend with a very competitive retail environment. Meanwhile, the ingredients business experienced a significant margin squeeze as the competition for milk supply in Australia intensified. This was compounded by an adverse product mix due to lower demand in the export sales of value-added nutritional powders, and more milk being channelled into lower value milk powder sales.

“A recovery plan is now in place, with the planned closure of our Cororooke site, continuing rationalisation of the brands portfolio, and cost reductions following a recent restructure of the business.

“In Asia/AME higher volume growth in the Foodservice and consumer brands business across China, Indonesia, Malaysia, Middle East and Vietnam, contributed to a 13 per cent increase in sales volume to 186,000 MT, which helped underpin a strong first half performance with Normalised EBIT up 27 per cent.

“Latam did well with Normalised EBIT up 5 per cent driven by solid earnings growth from Soprole, which was offset to some extent by a weaker result from Dairy Partners Americas (DPA). In particular, product innovation in the Chilean market with the successful launches of new dairy desserts and yoghurts has supported earnings growth,” said Mr Spierings.

Outlook

Looking ahead, Mr Spierings said Fonterra’s strong first half earnings were unlikely to be repeated in the second half.

“For the full year, we expect to see total milk volumes for the current season to be in line with last season.

“The ongoing volatility in commodity markets could have a negative impact on product mix profitability.

“In many of our consumer markets, we are expecting intensified competition in the second half – particularly in Australia – and in Asia we are seeing signs of demand slowing,” said Mr Spierings.

(Further detail on Fonterra’s half year financial highlights follows in Appendix One.)

[1] As at June 2013, compared to the opening advance rate schedule

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About Fonterra

Fonterra *is a global leader in dairy nutrition – the preferred supplier of* ***dairy ingredients*** *to many of the world’s leading food companies. Fonterra is also a market leader with our own* ***consumer dairy brands*** *in Australia/New Zealand, Asia/Africa, Middle East and Latin America.*

The ***farmer-owned*** *New Zealand co-operative is the largest processor of milk in the world, producing more than two million tonnes of dairy ingredients, value added dairy ingredients, specialty ingredients and consumer products every year. Drawing on* ***generations of dairy expertise****, Fonterra is one of the largest investors in dairy based* ***research and innovation*** *in the world. Our more than* ***16,000 staff*** *work across the dairy spectrum from advising farmers on sustainable farming and milk production, to ensuring we live up to exacting quality standards and delivering every day on our customer promise in more than 100 markets around the world.*

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APPENDIX ONE

Half Year Financial Highlights

Volumes up – with record New Zealand milk flows in the first half, up 6 per cent, matched by strong growth in sales volume, up 8 percent across our business globally.

Net Profit After Tax of $459 million, 33 per cent higher than the corresponding period in FY 2012 driven primarily by sales volume growth in NZ Milk Products and Asian and Latin American brands.

Gearing ratio improved to 40 per cent from 47 per cent in the prior period. Although the gearing ratio at 31 July 2012 was lower at 39 per cent, the seasonal nature of our business means the more meaningful comparison is with the position at the previous half year.

NZ Milk Products delivered a robust performance with total sales volumes up 9 per cent to 1,474,000 MT. Gross margin in NZ Milk Products was up 29 per cent to $797 million, mainly because of favourable relative cheese and protein pricing, effective management of our product mix and higher price premiums compared to dairy commodity prices. Normalised EBIT was up 65 per cent to $422 million, compared to $255 million in the previous period.

Asia/Africa, Middle East (Asia/AME) delivered growth in the Foodservice and consumer brands business across China, Indonesia, Malaysia, Middle East and Vietnam, which contributed to a 13 per cent increase in sales volume to 186,000 MT. The growth was partly offset by lower volumes in Sri Lanka. Normalised EBIT was $100 million which was 27 per cent higher than the previous period. (On a constant currency basis, EBIT was up 34 per cent, due to the Asia/AME basket of currencies weakening against the NZD.)

Australia/New Zealand's total sales volume of 471,000 MT was down 4 per cent compared to last year, primarily because of the sale of the Norco liquid distribution business and lower volumes in private label in our Australian business. After adjusting for the sale of Norco, which was sold in November 2012, external sales volumes were up 1 per cent to 391,000 MT. Despite the challenging environment in Australia, volume in our branded products increased, particularly spreads and cheese. The result reflected a challenging retail environment and aggressive competition for milk supply in Australia, and an adverse Ingredients product mix due to lower demand in export sales of value-added nutritional powders, and more milk being channelled into lower value milk powder sales. After adjusting for the costs of $24 million associated with the planned Cororooke plant closure in Australia, Normalised EBIT was 32 per cent lower than last period at $98 million.

Latin America (Latam) had volume growth of 11 per cent for the first half, mainly because of Soprole's volume growth across all key categories in consumer and fresh products, particularly in liquid milk and mature cheese. Balancing this, however, the trading environment for DPA continues to be challenging. Fonterra's share of profit from DPA was down 21 per cent primarily due to operational issues leading to lower volumes and margins in Venezuela. Normalised EBIT for Latam was $67 million, up 5 per cent from the same period last year.

Non-GAAP financial information

Fonterra refers to Normalised Earnings/Normalised EBIT, EBIT, constant currency variances, Normalisation Adjustments and payout when discussing financial performance. These are non-GAAP financial measures and are not prepared in accordance with IFRS. Fonterra 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 IFRS.

- Fonterra calculates Normalised Earnings by adding back depreciation, amortisation, net finance costs, taxation expense and Normalisation Adjustments to net profit for the period.
- Normalisation Adjustments are transactions that are unusual by nature or size so that they materially reduce the ability of users of the financial results to understand the ongoing performance of the Group or operating segment to which they relate.
- Unusual transactions by nature are the result of a specific event or set of circumstances that are outside the control of the business, or relate to the major acquisitions or disposals of an asset/group of assets or business.
- Unusual transactions by size are those that are unusually large in a particular accounting period, that is not expected to repeat regularly to the same extent in future periods.
- Normalisation adjustments are determined on a consistent basis each year.

Reconciliation of Normalised Earnings to Reported Profit before Tax

($M)	31 Jan 2013	31 Jan 2012
Normalised EBIT	693	552
Normalisation Adjustments:		
- Cororooke	(24)	-
- Impairment losses recorded in equity accounted investees	-	(20)
- Other Items	-	(2)
Reported EBIT	669	530
Next Financing Costs	(152)	(153)
Reported Profit Before Tax	517	377