Fonterra
Dairy for life

Market Announcement

12 August 2019

FONTERRA PROVIDES UPDATE ON EARNINGS, DIVIDEND, AND ONE-OFF ACCOUNTING ADJUSTMENTS

Fonterra Co-operative Group Limited today reconfirmed its underlying earnings guidance for the 2019 financial year that ended on 31 July 2019 (FY19), announced a final decision on its full-year dividend for FY19, and provided further information on some significant adverse one-off accounting adjustments.

Chief Executive Officer, Miles Hurrell said that as a result of the full review of the business which has taken place across the year, as well as the work done so far to prepare its financial statements for FY19, it has become clear that Fonterra needs to reduce the carrying value of several of its assets and take account of other one-off accounting adjustments, which total approximately $820-860 million.

"Since September 2018 we've been re-evaluating all investments, major assets and partnerships to ensure they still meet the Co-operative's needs. We are leaving no stone unturned in the work to turn our performance around. We have taken a hard look at our end-to-end business, including selling and reviewing the future of a number of assets that are no longer core to our strategy. The review process has also identified a small number of assets that we believe are overvalued, based on the outlook for their expected future returns.

"While the Co-op's FY19 underlying earnings range is within the current guidance of 10-15 cents per share, when you take into consideration these likely write-downs, we expect to make a reported loss of $590-675 million this year, which is a 37 to 42 cent loss per share.

"We made a commitment to provide information to update farmers and unit holders as it comes available. The numbers still need to be finalised and audited but we now have enough certainty overall to come out in advance of our annual results announcement in September."

Mr Hurrell said that the majority of the one-off accounting adjustments related to non-cash impairment charges on four specific assets and the divestments that the Co-op has made this year as part of the portfolio review.

"DPA Brazil, the New Zealand consumer business, China Farms and Australian Ingredients' performance have been improving, but slower than expected and not at the level we had based our previous carrying values on."

Commenting on the one-off financial accounting adjustments, Mr Hurrell said:

- "Our accounting valuation for **DPA Brazil** will be impaired by approximately $200 million. This change is mainly due to the economic conditions in Brazil. While they are improving, consumer confidence and employment rates are not at the level required to support the sales volumes and price points our forecast cashflows were based on.

- "As a result of the previously announced sale of our **Venezuelan consumer** business, and the closing of our small **Venezuelan Ingredients business,** due to the country's economic and political instability, we have made an accounting adjustment of approximately $135 million relating primarily to the release of the adverse accumulated foreign currency translation reserve.

- "Our carrying value for **China Farms** will be impaired by approximately $200 million due to the slower than expected operating performance. While the extent in which we participate is under strategic review, the fresh milk category in China continues to look promising and is growing.

- "In our **New Zealand consumer business**, the compounding effect of operational challenges, along with a slower than planned recovery in our market share has resulted in us reassessing its future earnings. We are now rebuilding this business and, as part of this, have sold Tip Top which allows the team to focus on its core business. The combined impact is a write-down of approximately $200 million.

- "Our **Australian Ingredients business** is adapting to the new norm of continued drought, reduced domestic milk supply and aggressive competition in the Australian dairy industry. This includes closing our Dennington factory, which combined with writing off the goodwill in Australia Ingredients, results in a one-off impact of approximately $70 million (this includes the $50 million previously announced as part of the Dennington announcement).

"These are tough but necessary decisions we need to make to reflect today's realities.

"We're in no doubt that farmers and unit holders will be rightly frustrated by these write-downs. I want to reassure them that they do not, in any way, impact our ability to continue to operate. Our cashflow remains strong, our debt has reduced and the underlying performance of the business for FY19 is in-line with our latest earnings guidance of 10-15 cents per share. We remain on track with our other targets relating to reducing capital expenditure and operating expenses."

Chairman John Monaghan said that in-light of the significant write-downs that reflect important accounting adjustments Fonterra needed to make, the Board had brought forward its decision on the full year dividend for FY19.

"We have made the call not to pay a dividend for FY19. Our owners' livelihoods were front of mind when making this decision and we are well aware of the challenging environment farmers are operating in at the moment.

"Ultimately, we are charged with acting in the best long-term interests of the Co-op. The underlying performance of the business is in-line with the latest earnings guidance, but we cannot ignore the reported loss of $590 - $675 million once you look at the overall picture.

"Not paying a dividend for the FY19 financial year is part of our stated intention to reduce the Co-op's debt, which is in everybody's long-term interests.

"Our Co-op remains strong at its core. Over the last 12 months we have improved our cashflow, reduced our debt and removed significant cost from within the business, but there is still more to do. The business units that are at the heart of our new strategy are delivering for us and we look forward to discussing our new strategy and our performance with our owners in September.

"It's important that we now implement our new strategy and deliver value back to them," says Mr Monaghan.

Notes:

All numbers remain subject to the Board reviewing the full financial statements and are subject to audit adjustments and reflect the values attributable to equity holders.

ENDS

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