Media release

Fonterra 2015/16 Annual Results Show Stronger Returns

Highlights

- Sales volume increased 4% to 23.7 billion Liquid Milk Equivalents (LME)
- Revenue $17.2 billion, down 9%
- Normalised EBIT $1.4 billion, up 39%
- Net profit after tax $834 million, up 65%
- Return on capital 12.4%, up from 8.9%
- Ingredients inventories down 25%
- Gearing ratio reduced to 44.3% from 49.7%
- Debt reduced by $1.6 billion to $5.5 billion
- Earnings per share 51 cents
- Cash Payout $4.30
  - Farmgate Milk Price $3.90 per kgMS
  - Dividend of 40 cents per share

Annual results

Fonterra Co-operative Group has announced a 65 per cent increase in net profit after tax to $834 million for the financial year ended 31 July 2016 – reflecting a stronger business despite ongoing challenges in global dairy markets.

The Co-operative is paying a Cash Payout of $4.30 for the 2016 season for a 100 per cent share-backed farmer, comprising a Farmgate Milk Price of $3.90 per kgMS and a dividend of 40 cents per share, on a total available for payout of $4.41.

Chairman John Wilson said that the 2015/16 season had been incredibly difficult for farmers, their families and rural communities, with global dairy prices at unsustainable levels.

“Our Co-operative has responded. We continued with the significant and necessary changes we began in the business over three years ago to support our strategy and its priorities, and worked hard to return every possible cent of value back to our farmers.

“Our business strategy is serving us well. We are moving more milk into higher-returning consumer and foodservice products while securing sustainable ingredients margins over the GlobalDairyTrade benchmarks, especially through speciality ingredients and service offerings.

“Through increased earnings and continuing financial discipline we have increased the return on capital and strengthened our balance sheet by significantly reducing debt.

“We have done what we can to support our farmers with the Co-operative Support Loan, and early payment of dividends.

“After a period of deliberate and disciplined attention to the business, we have become a stronger Co-operative operationally, financially and in our mindset with a clear sense of direction and a structure which will support real momentum in our strategy going forward,” said Mr Wilson.

Mr Wilson said farmers' decisions to reduce stocking rates and supplementary feeding to help lower costs resulted in milk collection across New Zealand for the 2015/16 season declining to 1,566 million kgMS, down three per cent on the previous season.

Strong volume and value growth

Chief Executive Theo Spierings said more volumes of milk sold at higher value is at the heart of Fonterra's strategy.

"For our farmers, the promise is that we will make the most of their milk. We're keeping that promise.

"We've seen the real strength of our ingredients business this year. The money our farmers have invested in stainless steel is giving us more choice, and we have matched production to the highest value customer demand. In a difficult market, we increased ingredients normalised EBIT this year by 24 per cent to $1,204 million.

"In consumer and foodservice, we converted an additional 380 million litres of liquid milk equivalents (LME) into higher returning products, bringing our total volumes in this business up from 4.5 billion LME to 4.9 billion. Increasing our consumer and foodservice volumes, and especially our foodservice growth, meant we increased our normalised EBIT in this business by 42 per cent to $580 million.

"Our results show that we continue to do what we said we would do right across the Co-op. We are single-minded about transforming our business to get the best results. We have cut our operating expenses, increased our free cash flow, reduced our working capital days, driven debt down, and reduced our capex and our gearing.

"All of this effort, combined with higher earnings and margins meant our measure of return on capital has increased from 8.9 per cent to 12.4 per cent.

"Our results show how our strategy is creating value for our shareholders. We are driving more volume into higher value products, and we are achieving results with increasing efficiency. We will continue to build on this strong platform to keep improving and delivering results to our farmers.

Investing in our communities and future

"At the same time, we have kept our promise to share great dairy nutrition with our communities through Fonterra Milk for Schools, and through our Grass Roots Fund and Living Water partnership, we are looking after local communities and the environment.

"We can only do all of this with the support and commitment of our farmers, investors and employees. Throughout the year we have challenged our people to adapt how we work to better manage the shifts in the global market. It has been a real team effort and I want to thank all of our people in New Zealand and around the world," said Mr Spierings.

Future outlook

With a forecast Farmgate Milk Price of $5.25 per kilogram of milksolids (kgMS), the forecast total payout available to farmers in the 2016/17 season is $5.75 to $5.85 before retentions. This includes a forecast earnings per share range of 50 to 60 cents.

Mr Wilson said over the past three years the Co-operative had worked hard to align its structure to its strategy with a focus on achieving more value for the volumes of milk produced by its farmers.

"The higher forecast earnings per share range reflects the performance improvements the business will continue making.

"It is still early in the season, and we expect continuing volatility as reflected in price improvements in recent GDT auctions.

"Current global milk prices remain at unrealistically low levels, but as the signs in the market improve, we are very strongly positioned to build on a good result in the year to come," said Mr Wilson.

NB: All dollars quoted are New Zealand dollars.

- ENDS -

For further information contact:
Connie Buchanan
Fonterra Communications
Phone: +64 22 698 5602

24-hour media line
Phone: +64 21 507 072

Non-GAAP measures

Fonterra uses several non-GAAP measures when discussing financial performance. For further details and definitions of non-GAAP measures used by Fonterra, refer to the Glossary in Fonterra's 2016 Annual Review. These are non-GAAP measures and are not prepared in accordance with NZ IFRS.

Management believes that these measures provide useful information as they provide valuable insight on the underlying performance of the business. They may be 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.

- Fonterra calculates normalised earnings by adding back 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 on-going 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.
- Debt – Debt is economic net interest-bearing debt. This reflects total borrowings less cash and cash equivalents and non-current interest-bearing advances adjusted for derivatives used to manage changes in hedged risks.
- Gearing ratio – Gearing ratio is economic net interest bearing debt divided by economic net interest bearing debt plus equity, excluding cash flow hedge reserve
- Return on capital – return on capital is calculated as normalised EBIT less equity accounted investee earnings, less a notional tax charge divided by capital employed. Capital employed excludes intangible assets, goodwill and equity accounted investments.

Reconciliation of normalised earnings to reported profit

	GROUP $ MILLION	
	31 JULY 2016	31 JULY 2015
Profit for the period	**834**	506
Add: Net finance costs	**499**	518
Add / (Less): Taxation expense / (credit)	**98**	(82)
Total EBIT	**1,431**	942
Add: Disposal and impairment of the Australian yoghurt and dairy desserts business	**23**	108
Less: Gain on sale of DairiConcepts investment	**(68)**	-
Add: Restructuring and redundancy provisions	**-**	33
(Less) / Add: Time value of options	**(28)**	20
Less: Net gain on Latin America strategic realignment	**-**	(129)
Total normalised EBIT	**1,358**	974

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. It is also a market leader with its own consumer dairy brands in New Zealand and Australia, Asia, Africa, the Middle East and Latin America. Fonterra is a farmer-owned co-operative and the largest processor of milk in the world. It is one of the world's largest investors in dairy research and innovation drawing on generations of dairy expertise to produce more than two million tonnes of dairy ingredients, value added dairy ingredients, specialty ingredients and consumer products for 140 markets.