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# FONTERRA CO-OPERATIVE GROUP LIMITED

## 2016 ANNUAL MEETING

8 DECEMBER 2016



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# JOHN WILSON

## Chairman



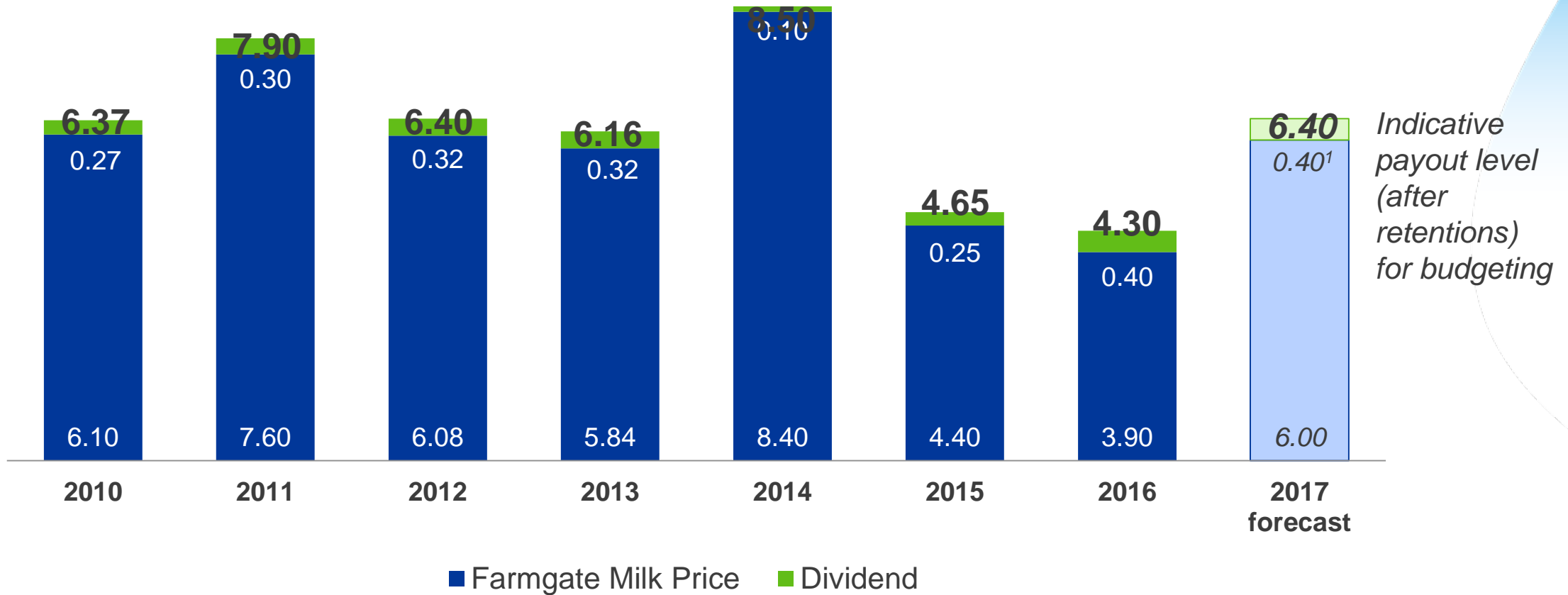
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**Co-operative spirit at work  
during the earthquake response**

# Tough season for farmers

But solid earnings growth and strong Co-operative



1. For farm budgeting purposes a 40 cent dividend is assumed (based on FY17 EPS forecast 50-60 cents) – this is consistent with Fonterra policy of paying out 65-75 per cent of adjusted net profit after tax over time

Note: Farmgate Milk Price: \$ per kgMS; Dividend: \$ per share

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# Benefits from a strong Co-operative



## Competitive Milk Price

### Milk Price model put in place in 2009

- Changes to approaches used since then have resulted in structural increase

### Additional 36c to the Farmgate Milk Price<sup>1</sup>

- 2016 milk price would have been \$3.54 using model assumptions from 2009
  - \$560m additional to milk price

### Reflects improvements by Fonterra and in our operating environment

- Improved manufacturing performance
- Improved supply chain
- Lower manufacturing and capital costs

## Complemented by Co-op Initiatives



### Strong Co-operative balance sheet

- Early dividend & Co-op support loan



### Farm Source™ rewards & benefits

- Around \$30 million in savings for our farmers



### Enhanced digital offering & apps

- Co-op updates and timely milk collection info



### Business support on the ground

- Regional heads and technical reps

# Continued strong business performance



VOLUME

**23.7B LME**

↑ 4%

REVENUE

**\$17.2B**

↓ 9%

NORMALISED EBIT

**\$1,358M**

↑ 39%

RETURN ON CAPITAL<sup>1</sup>

**12.4%**

↑ Up from 8.9%

NET PROFIT AFTER TAX

**\$834M**

↑ 65%

ANNUAL DIVIDEND / YIELD<sup>2</sup>

**40CPS 7.3%**

↑ 60%

## Ingredients

Volume (LME) <sup>3</sup>	↑	22.4B
Gross Margin	↑	14.3%
Normalised EBIT	↑	\$1,204M
Return on Capital <sup>1</sup>	↑	13.4%

## Consumer and Foodservice

Volume (LME) <sup>3</sup>	↑	4.9B
Gross Margin	↑	28.7%
Normalised EBIT	↑	\$580M
Return on Capital <sup>1</sup>	↑	41.7%

## China Farms

Volume (LME) <sup>3</sup>	↑	0.2B
Gross Margin	↑	(22.4%)
Normalised EBIT	↓	(\$59M)

1. Return on Capital (ROC) excludes goodwill, brands and equity accounted investments; Group ROC including these items was 9.2% in FY16 (FY15: 6.9%)

2. FY16 dividend over volume weighted average closing FCG share price (\$5.50) across the year; 3. Includes sales to other strategic platforms

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# Investing for growth in Canterbury

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**Investments support efficiency  
and flexibility**

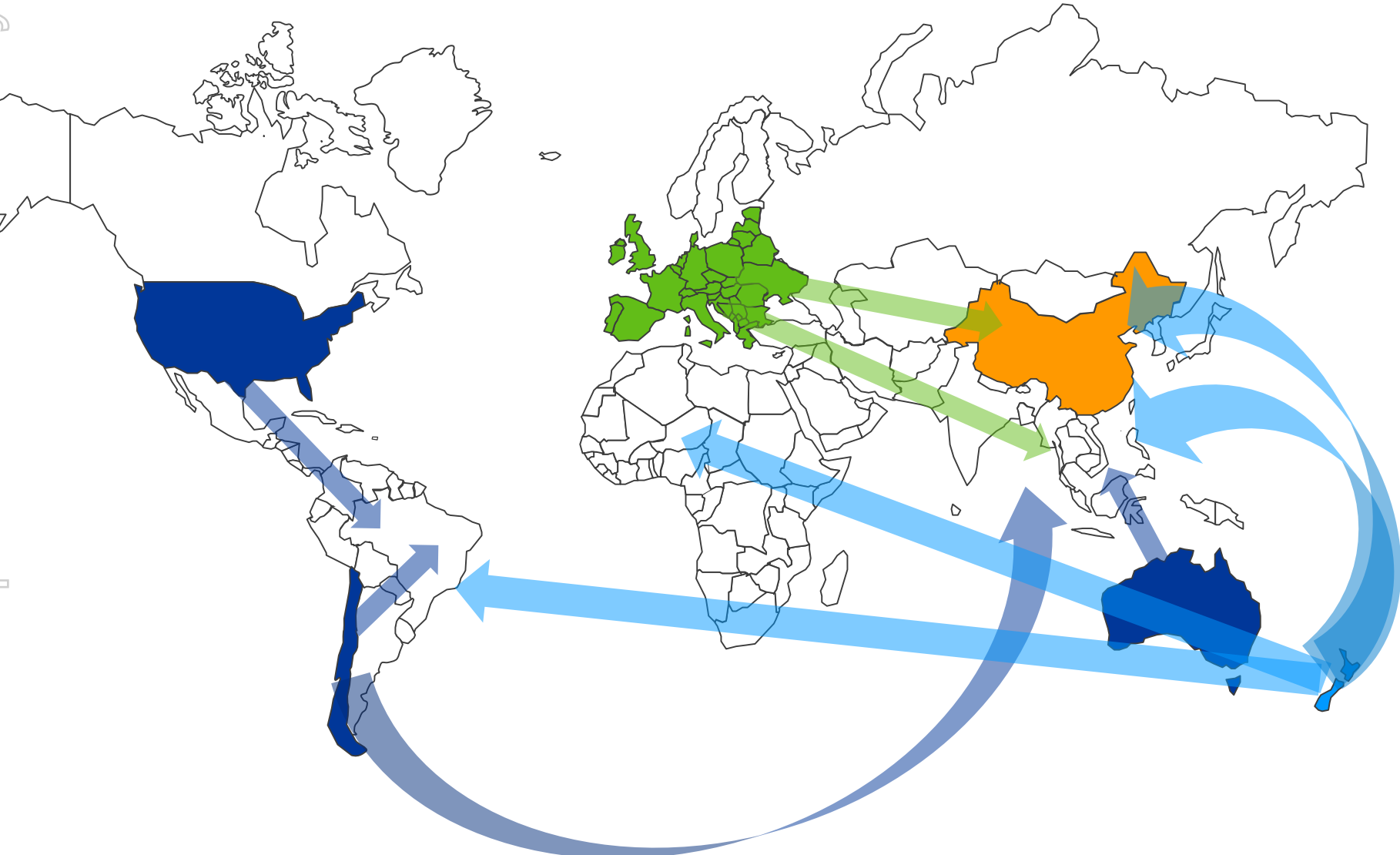




# Other sources keep access secure, support growth and increase returns



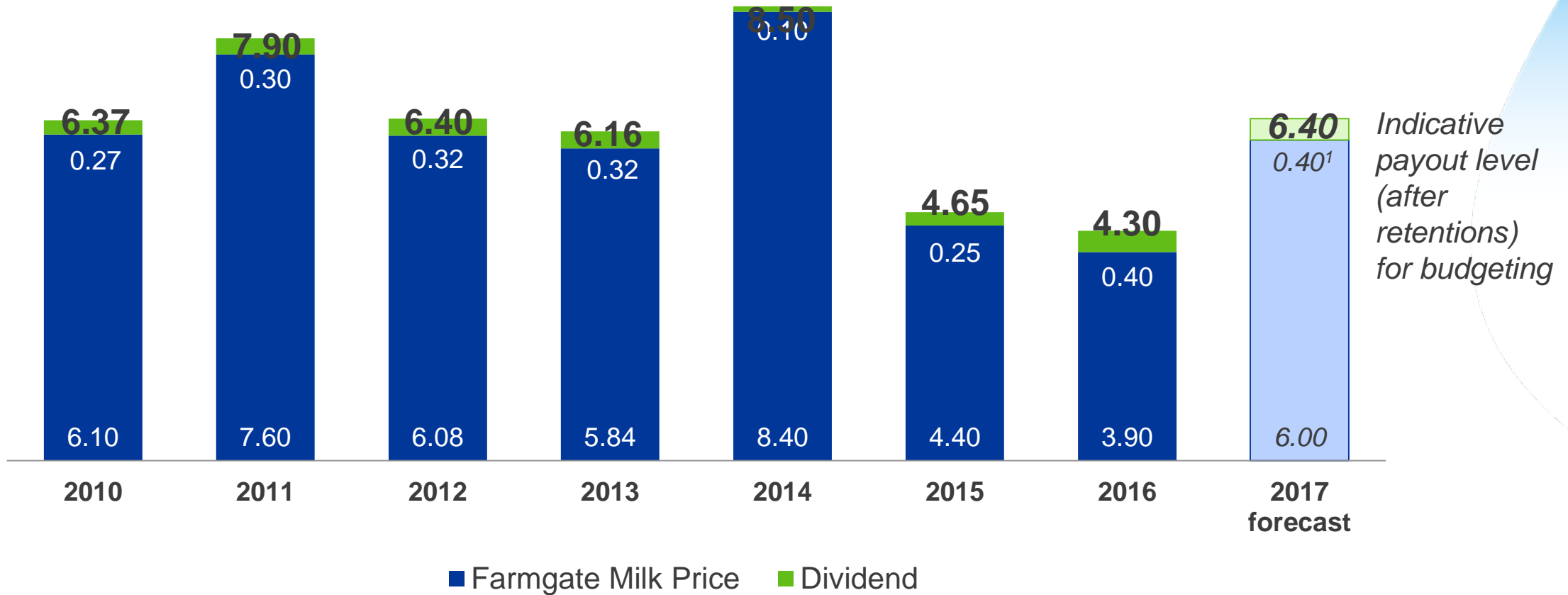
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- Primary Investment**
- WMP / SMP
  - Whey
  - Cheese / Whey / Nutritional
  - Fresh milk / UHT

# Tough season for farmers

But solid earnings growth and strong Co-operative



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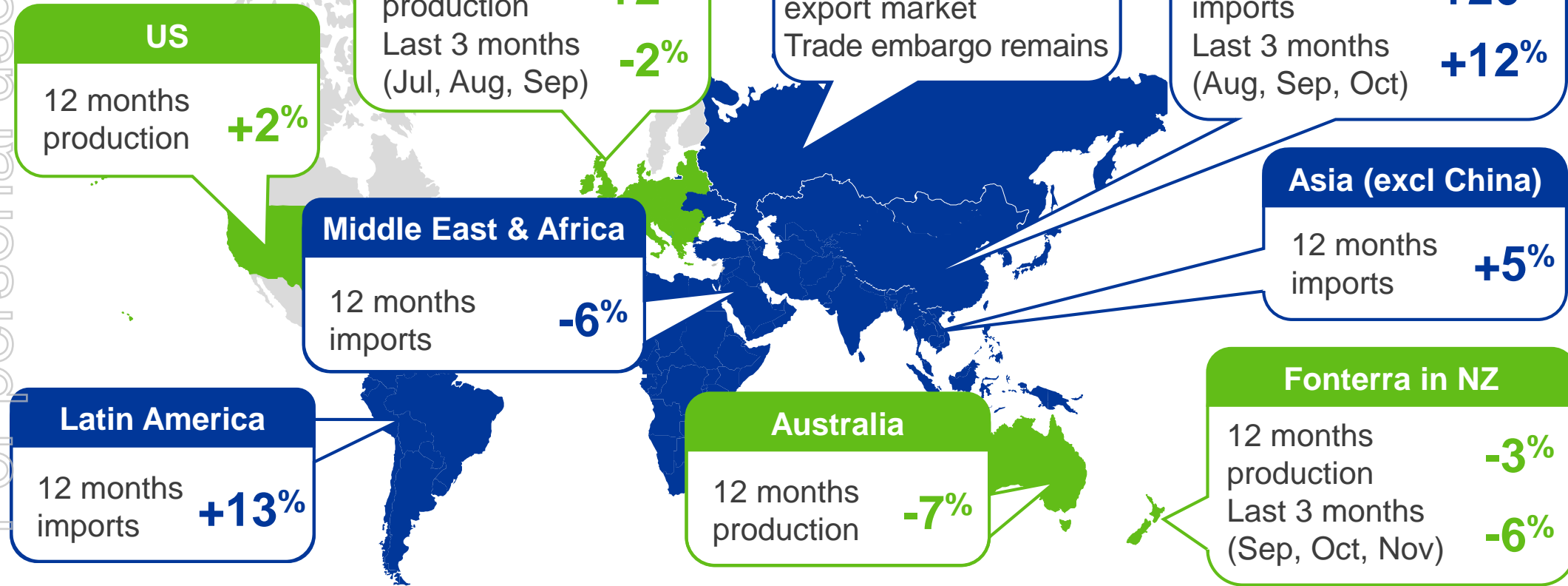
Note: Farmgate Milk Price: \$ per kgMS; Dividend: \$ per share

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# Global dairy update – supply driven rebalancing



Supply  
Demand



Note: All 12 month figures are rolling 12 months compared to previous comparable period: Australia (October), EU (September), United States (October), China (October), Asia (August), Middle East & Africa (August), Latin America (August), New Zealand (Fonterra only) (November)

Source: Government milk production statistics; GTIS trade data; Fonterra analysis

# Priorities for the coming year

1. Continued commitment to most sustainable returns
2. More momentum in strategy delivering to support higher returns
3. Expansion of Farm Source support to farmers

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# THEO SPIERINGS

## Chief Executive Officer



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# FINANCIAL PERFORMANCE



## Global Context

- Future for dairy remains strong
- Low global commodity prices
- Unstable world

## Value Creation

- Transforming our business leads to strong results
- Strategy is working – more milk into higher value products
- Paying off – higher earnings and a stronger Co-op

## Trust

- Doing what we said we would do
- Investing in our communities and our future
- Very focused on future delivery



# Value creation

Higher return on capital from gains on all business drivers

## RETURN ON CAPITAL

# 12.4%

**↑** Up from 8.9%

GROSS MARGIN

## 21.1%

**↑** Up from 17.4%

CAPEX

## \$944M

**↓** 38%

OPEX

## \$2,528M

**↓** 8%

WORKING CAPITAL

## 77 DAYS

**↓** Down 10 days

NORMALISED EBIT

## \$1,358M

**↑** 39%

DIVESTMENTS

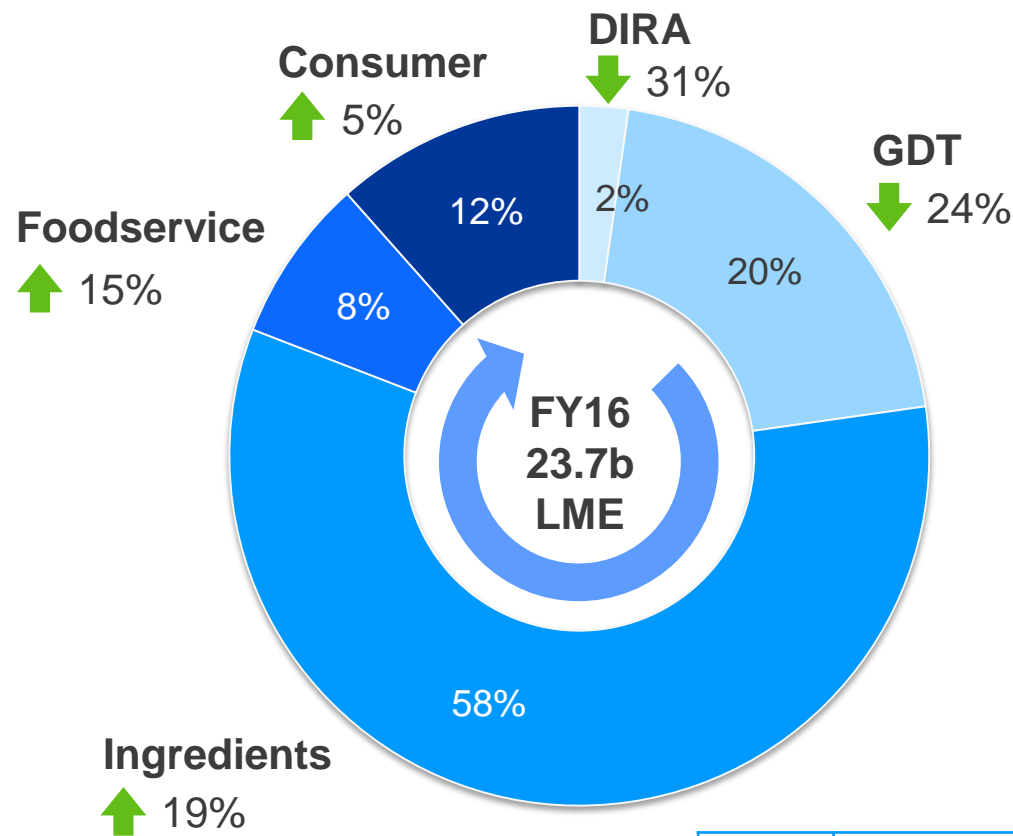
## \$308M

Note: Return on Capital (ROC) excludes goodwill, brands and equity accounted investments; Group ROC including these items was 9.2% (2015: 6.9%)

# Delivering our strategy

## Volume to higher Value at Velocity

- 1 **Optimise**  
NZ milk
- 2 **Build and grow**  
beyond our current consumer positions
- 3 **Deliver**  
on Foodservice potential
- 4 **Grow**  
our Anlene™ business
- 5 **Develop**  
leading positions in paed & maternal nutrition
- 6 **Selectively invest**  
in milk pools
- 7 **Align**  
our business and organisation



- GDT volume lower
- Ingredients
  - Optionality improved mix
  - Ingredients solutions for customers adding value
  - Lower operating costs
  - Return on capital of 13.4%
- Consumer and Foodservice
  - Added 380m more LMEs
  - 1 billion added in 2 years
  - Return on capital of 41.7%

↑ %	<i>FY16 sales volume growth over FY15</i>
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Note: Return on Capital (ROC) excludes goodwill, brands and equity accounted investments

Source: Wheel shows percentage of total FY16 external sales (LME) by strategic platform; Growth rates include intercompany sales to other strategic platforms

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# Transformation is unlocking value



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- ✓ Owner's mindset
- ✓ Business-led
- ✓ Relentless execution

**>4,000** *employees involved*

Initiatives<sup>1</sup>

**4,000**



Capex<sup>1</sup>

**\$944M**



Free Cash Flow<sup>1</sup>

**\$2.2B**



Debt

**-\$1.6B**



Working Capital

**-10 days**



Closing Inventory

**-21%**



1. Actual figures shown – not movements

Note: Free Cash Flow is net operating cash flows less net investing cash flows; Debt is economic net interesting bearing debt

# Doing what we said we will in FY17

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Optimisation & Price Achievement

Fonterra story

Accelerate growth in our 8 strategic and leadership markets

Brazil transformation

Maximise Beingmate partnership

China Farms – Downstream Value

Australian endgame

Disrupt

Velocity / Engagement

- Optimising for lower volumes
- Launched 'Trusted Goodness'
- Volumes and margins up on last year
- Gross margin increased due to strategic pricing in anticipation of higher milk prices
- New structure delivering but tough market
- Darnum JV operational
- Annum volumes up 78%
- Integrating China businesses
- Turnaround delivering
- Two new start-ups established
- Additional Velocity benefits identified

# FY17 Q1 performance summary

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VOLUME (LME)	REVENUE	GROSS MARGIN	OPEX	CAPEX
<b>4.9B</b>	<b>\$3.8B</b>	<b>21.9%</b>	<b>\$621M</b>	<b>\$116M</b>
2.0%	5.9%	FROM 22.6%	1.7%	55%

## Ingredients

Volume	4.5B UP 2%
Gross Margin	12% FROM 15%

## Consumer & Foodservice

Volume	1.3B UP 11%
Gross Margin	31% FROM 28%

## China Farms

Volume	0.1B UP 62%
Gross Margin <sup>1</sup>	-12% FROM -8%

1. Impacted by one-off sale of inventory below cost – gross margin excluding this impact was 4%

Note: Volume is in billion LME; All changes are expressed relative to first quarter of FY16



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# FUTURE OF FOOD



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# MAKING A DIFFERENCE TO THE LIVES OF TWO BILLION PEOPLE



# Food has a massive global economic, social and environmental footprint...

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# The productivity and climate challenge

Dairying is 20% of all global agricultural land

Today farmers grow 5 - 6 times the amount of produce from the same hectare of land as 100 years ago BUT...

Post-war era  
3 - 4%

Today  
<1%

Tomorrow  
2 - 3% ?

Climate change working against future of food

Food production contributes 30% of global greenhouse gas emissions

Serious land degradation affects 20% of world's arable land

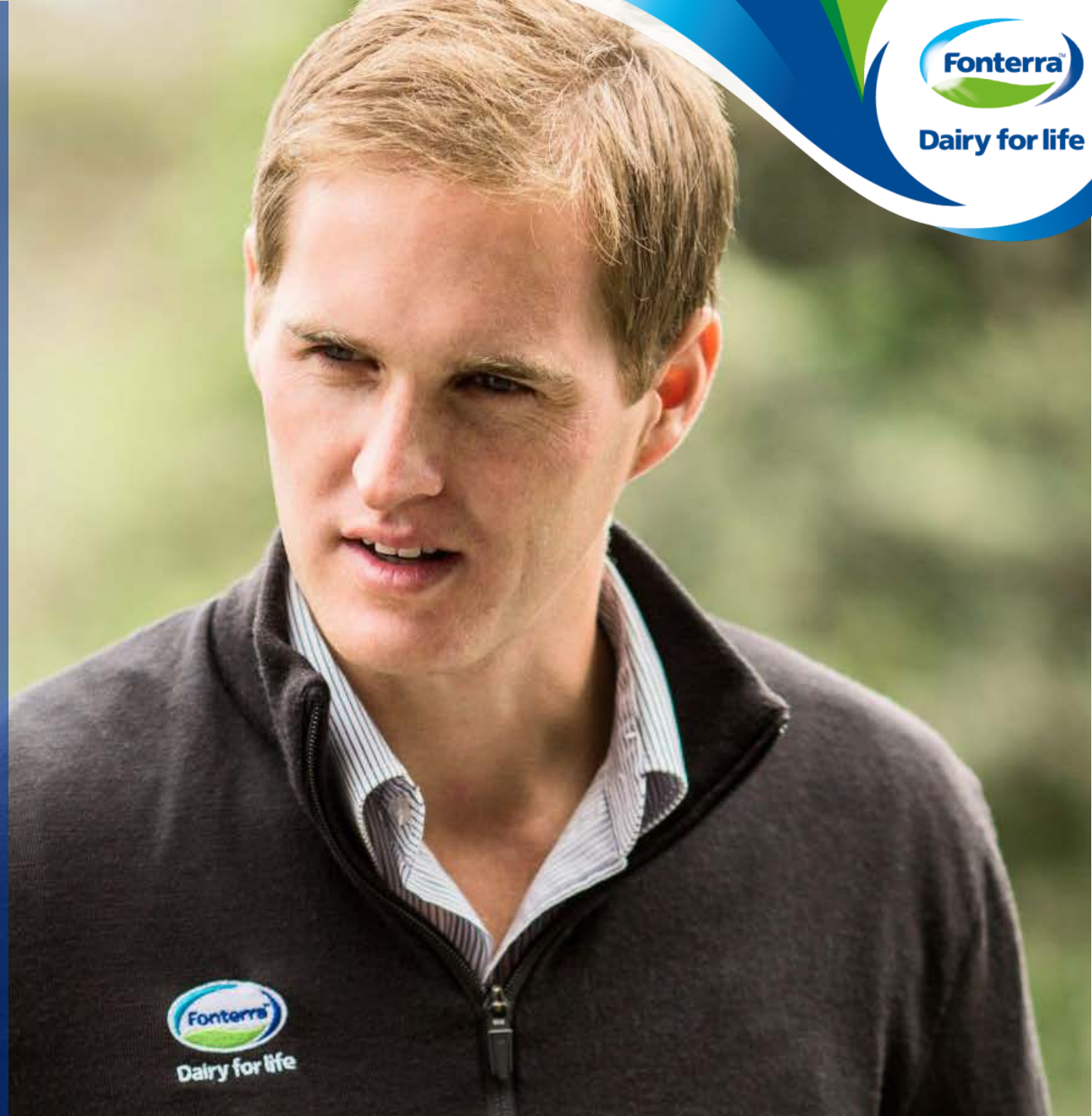
# We recognise the challenge

Step change over last 12 months:

- Productivity up 8%
- Emissions down 3.1%
- \$1BN on-farm environment initiatives
- \$20M community partnerships
- 97% of waterways on our farms fenced
- UN 2020 Sustainable Development agenda

- Our farmers are responding and seeking to be at the forefront of precision agriculture

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# Feeding the world challenge

6 billion people rely on dairy as one of most important sources of protein and energy

800 million people don't get enough to live a healthy life

3 billion new consumers will enter middle class by 2030

100% increase in food demand by 2050

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# Fonterra Strategy – Nutrition focused

Everyday nutrition

Out of home nutrition

Advanced nutrition

Affordable nutrition

Social responsibility:

- Milk for Schools - two thirds of NZ's primary schools (140,000 children)
- KickStart Breakfasts - 125,000 breakfasts per week (28,000 children)
- Dairy Development - work with approx. 6,500 farming families

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Dairy for life



# The innovation opportunity

Smart precision farming to revolutionise on-farm productivity

3D printing to transform the foodservice supply chain

Genetic mapping to enable individually tailored medical nutrition

Block chain to revolutionise food traceability

Digital / e-commerce



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# The trust opportunity

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# TRACE THE GOODNESS IN EVERY DROP

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DUNCAN COULL

Chairman

Fonterra Shareholders' Council



# Representation Review Recommendations



<p>The Shareholders' Council's role is refocused on the delivery of its constitutional duties alone.</p> <p>– <b>Underway</b></p>	<p>The number of Shareholders' Council Committees is reduced from four to three.</p> <p>– <b>Completed</b></p>	<p>Shareholders' Council will lead an oversight committee to refresh the Fonterra Network programme.</p> <p>– <b>Underway</b></p>
<p>The interface document between the Shareholders' Council and Board is updated and made available to Farmers.</p> <p>– <b>Completed</b></p>	<p>Shareholders' Council's communications with Farmers will be written in a distinctive "owner's voice" and make better use of the Co-operative's modern communication tools.</p> <p>– <b>Underway</b></p>	<p>Over the next 12 months, the number of Shareholders' Council Wards is reviewed to establish how they can be reduced within the range that is permitted under the current Constitution.</p> <p>– <b>Underway</b></p>
<p>A regional Young Farmers Forum is established to improve the connection with our young Farmers.</p> <p>– <b>Underway</b></p>	<p>The Council will introduce a set of attributes and capabilities for Councillors, to help Farmers assess candidates during Shareholders' Council elections.</p> <p>– <b>Completed</b></p>	<p>The Council will introduce a maximum term for Councillors of nine years.</p> <p>– <b>Completed</b></p>

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## Statement of Intentions (SOIs) for the year ending 31 July 2016

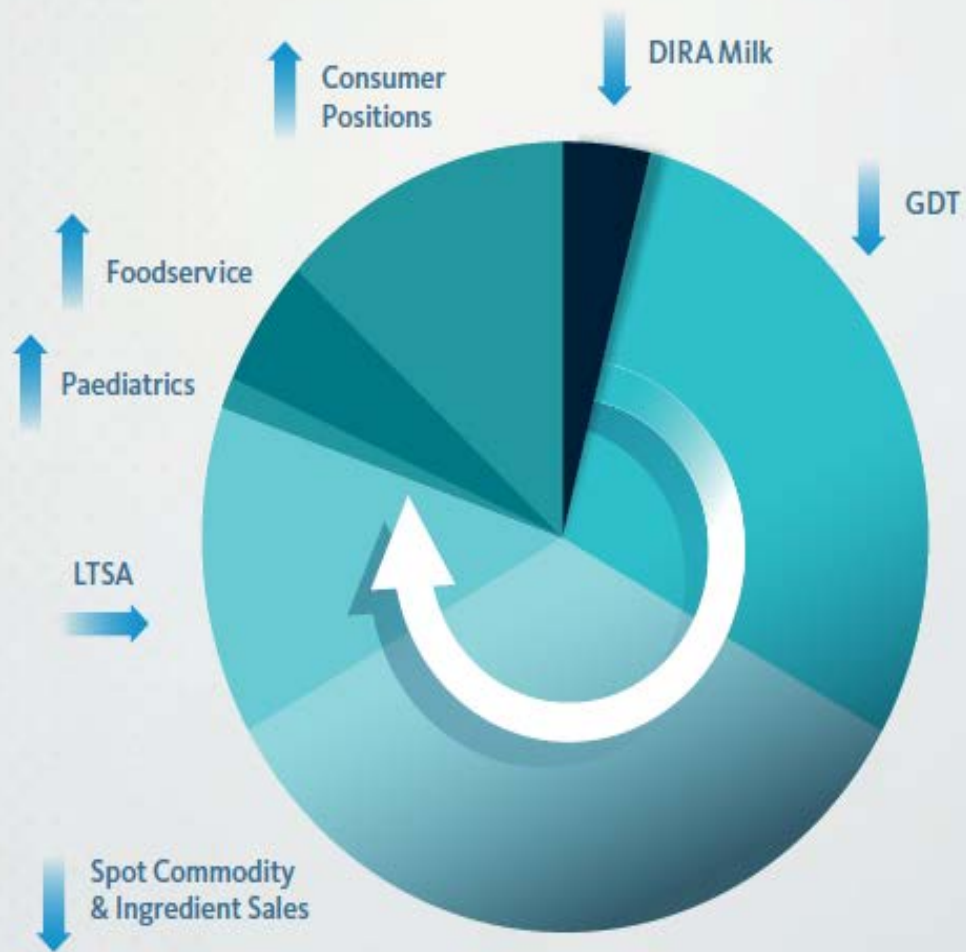
Key Performance Indicator (KPI)	Description	2016 Actual	2016 SOI Target	2015 Actual	Achieved
Total Available for Payout	Total available for Payout per Kilogram of Milksolids (kg/MS) Supplied before Retentions	4.41	4.25 - 4.35	4.65	✓
Volume	Sales Volume (Metric Tonnes 000)	4,526	4,648	4,303	
Farmgate Milk Price	The Farmgate Milk Price delivered to Farmers per kg/MS Supplied	3.90	3.85	4.40	✓
Earnings per Share	Net Profit after Tax divided by the Weighted Average Number of Shares on Issue.	0.51	0.40 - 0.50	0.29	✓
Gearing Ratio	Economic Net Interest Bearing Debt to Net Economic Net Interest Bearing Debt plus Equity	44.3%	44.0%	49.7%	
Return on Capital Employed	ROCE is EBIT Divided by Capital Employed	12.4%*	10.9%	8.9%	✓
Milk Solids (Retain and Grow)	% kg/MS of NZ Milk Collected	82.2%*	84.1%	85.4%	✗
Total Recordable Injury Frequency Rate	Total Recordable Injury	6.4	7.3	370	✓

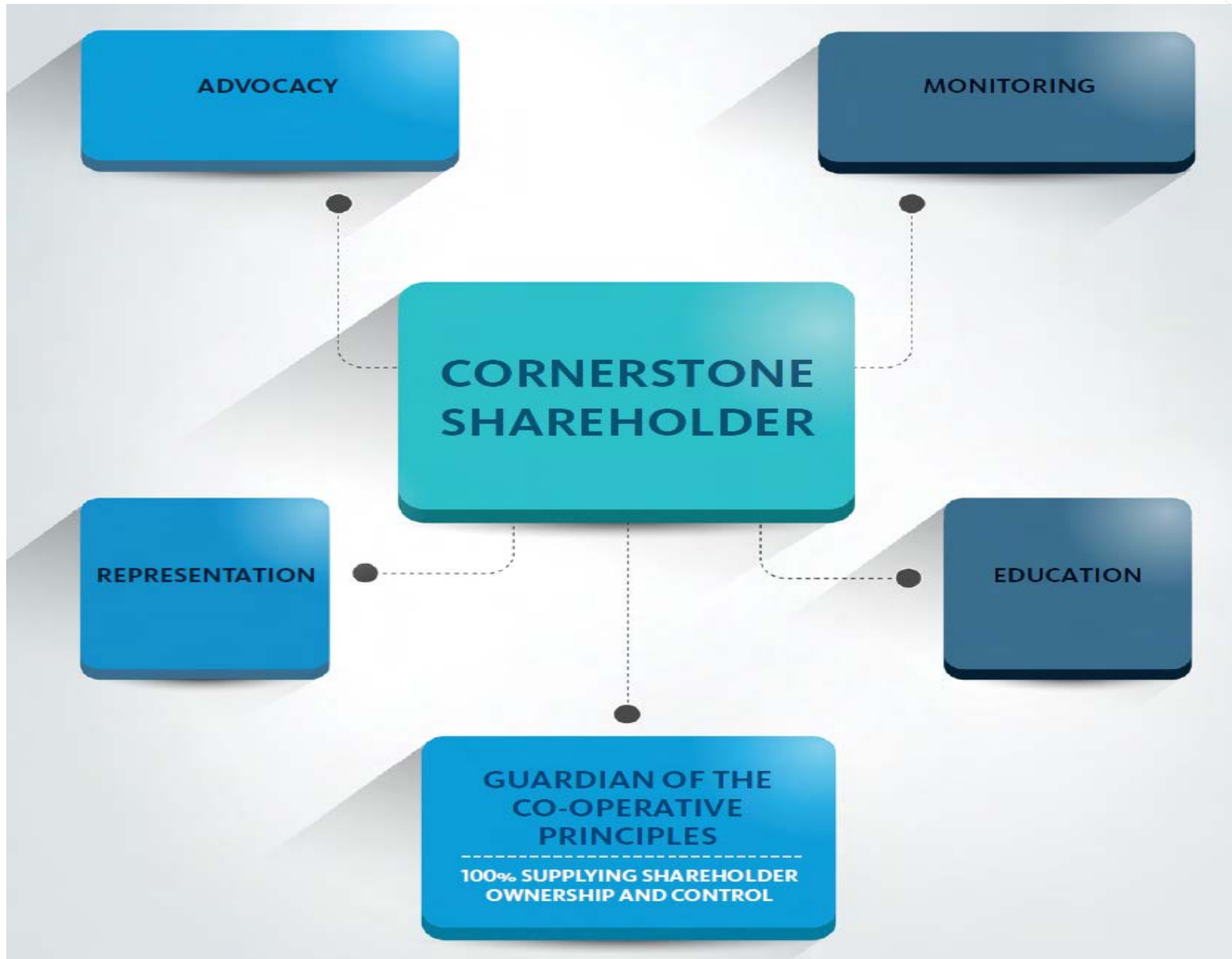
\*Fonterra mgmt. Methodology to Measure ROCE. Using standard Methodology ROCE would show as 9.2%.

\* 82.2% = 2017 Season Market Share Estimate, the result for the 2016 Season was 84.1%

## Turning the Wheel

Intention of Volume Change





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