



29 April 2016

Dear Suppliers

I'd like to firstly acknowledge the significance of this week's announcements and apologise for these late changes to milk price settings. I understand the impact this has on farm businesses given the poor seasonal conditions. I would like to extend my thanks to suppliers for the way you have engaged with us in a professional manner despite your disappointment with the result.

Directors and/or staff have spoken to many MG suppliers over the past two days and suppliers have sought clarity on several key administrative matters. Accordingly we have prepared additional information which reflects supplier feedback and seeks to clarify these key questions (see below).

Supplier meetings commence next week in Victoria

Supplier meetings will be held in the western, northern and Gippsland regions next week (Tasmania, South Australia and NSW will follow) at which Chairman Philip Tracy and interim CEO David Mallinson commit to an open and honest dialogue with suppliers about the Board and management's disappointment regarding the financial shortfall in our revised FY16 trading outlook.

I will advise precise supplier meeting details later today but in summary we will visit the western region on Monday, northern region on Tuesday and Gippsland on Wednesday.

We wish to clearly express our determination to resolve the issues associated with this revised outlook and answer any questions you may have at next week's supplier meetings as we aim to continue to implement our strategy and restore any lost confidence.

Sincerely,

Robert Poole
Executive General Manager Supplier Relations

Q&As

What has the Board announced?

The Board has announced that they now expect the final farmgate milk price for FY16 (FY16 FMP) to be in a range of \$4.75 to \$5.00 per kilogram milk solids (kgms). As the opening price was \$5.60 per kgms, this reduction will mean that approximately \$30m less will be paid to suppliers. The final figure will be determined following finalisation of the year end accounts.

In order to balance the impact of this large reduction, the Board has decided that they will reduce the opening price this year as well as announce a Milk Supply Support Package (MSSP) that will recover the remaining amount over a period of three years.

What is the impact on milk price in the current year (2015/16)?

MG has announced a reduction in the opening price to \$5.47 per kilogram milk solids (kgms) for the remainder of FY16. The reduction in the opening price will be implemented via lower fat and protein base prices in May and June 2016.

This allows for a recovery of some of the forecast DMP shortfall in the current financial year. The balance of the forecast DMP shortfall, i.e. the difference between the \$5.47 and the final milk price (to be determined following finalisation of the year end accounts) will be recovered over the coming three years via the MSSP.

By spreading the impact of the forecast DMP shortfall across FY16 and the following three financial years, the Board has sought to minimise the impact of the lower forecast milk price that will be delivered this year.

What is the Milk Supply Support Package?

Following the reduction in opening milk price, MG will now pay a FY16 FMP of \$5.47 per kgms. The balance of the reduced forecast DMP (expected to be between \$0.46 and \$0.72 per kgms) will be funded from MG's balance sheet and paid off over the next three financial years. It is important to note the final value of the MSSP can only be determined once full year accounts for FY16 have been finalised.

Table 1: Indication of how the forecast shortfall will be repaid via opening price reduction in FY16 and the MSSP over the next three years (FY17 to FY19)

	FY16 Reduction in opening price	FY17 MSSP Year 1	FY18 MSSP Year 2	FY19 MSSP Year 3	Total
Scenario A DMP forecast shortfall is at high end of range	\$30m	\$63.3m	\$63.3m	\$63.3m	\$220m
\$ kgms A	\$0.13	\$0.27	\$0.27	\$0.27	\$0.95
Scenario B DMP forecast shortfall is in mid-range	\$30m	\$56.7m	\$56.7m	\$56.7m	\$200m
\$ kgms B	\$0.13	\$0.25	\$0.25	\$0.25	\$0.87
Scenario C DMP forecast shortfall is at low end of range	\$30m	\$46.7m	\$46.7m	\$46.7m	\$170m
\$ kgms C	\$0.13	\$0.20	\$0.20	\$0.20	\$0.74

[Source](#) | Note: \$0.13 per kgms = approximately 1 cent per litre

The Board and management will continue to strive to achieve scenario C to lower the milk payment shortfall in 2015/16 and therefore lower the quantum of the MSSP.

Is the MSSP a loan to suppliers?

No. The MSSP will be managed internally via the MG balance sheet and overall milk payments. MG will not apply a loan against individual suppliers and will not apply terms and conditions retrospectively to suppliers. The MSSP is designed to assist suppliers by spreading the impact of the current milk pricing shortfall across the next three years.

Why is the MSSP necessary?

Given the lateness and scale of the change of forecast it was not feasible to correct the milk price over all of the current year. Therefore the MSSP was designed to assist suppliers by spreading the impact of the current milk pricing shortfall across the next three years.

Does the MSSP start now?

Amounts to recoup the MSSP will be deducted from milk payments over the next three years commencing 1 July 2016. The final quantum will be determined once full year accounts for FY16 are closed. The range of the MSSP is expected to be between \$140 and \$190m.

Is the co-operative in jeopardy?

The company's balance sheet remains strong and the MSSP will return the shortfall from FY16 to the balance sheet over the next three years. The Board is committed to MG's strategy of creating a First Choice Dairy Foods Company. The strength of MG's balance sheet has allowed us to deliver the MSSP to our suppliers.

Does MG have the capital it needs to fund its strategy?

Yes. MG received \$500 million in capital at the time of the capital raising and this sits on MG's balance sheet.

Are incentives such as Flat Milk Incentive and Next Generation payments impacted by recent announcements?

There is no change in this respect and these payments will be administered as per current terms and conditions.

How does the reduction in share price impact suppliers?

Suppliers will be impacted differently depending on how they purchased shares and funded the purchase. The maximum price paid under the Supplier Share Offer (SSO) was \$1.24. Some suppliers may have purchased shares on the market at higher prices.

Have unitholders and shareholders shared in the lower performance in FY16?

Yes, the Profit Sharing Mechanism (PSM) will still be applied to the final Distributable Milk Pool to determine the appropriate FMP to which the dividend applies. There is no change to the PSM. This has led to a forecast reduction in dividend for FY16 from 11.3 cents per share down to a range of 7.1 to 7.8 cents per share. The PSM was designed to lower dividends in line with lower farmgate milk price and vice versa.

What happens if a supplier leaves MG?

If a supplier leaves MG, no MSSP debt will follow them.

Can we pay off our MSSP contribution now instead of over three years from 1 July 2016?

We are reviewing this option and will advise suppliers of an outcome as soon as practicable.

Can MG provide additional support in the circumstances such as a fodder support package?

Yes, given the poor seasonal conditions and lower milk price cycle, MG will provide interest-free finance with extended terms for fodder, pasture re-sowing and stock water management over the next six to 12 months subject to normal terms and conditions.

We encourage suppliers to discuss this further with Field Services.

How did the board not pick up on debt and inventory levels from monthly accounts?

The financial shortfall came primarily as a result of recent lower than expected sales of milk powder sachets, upward movement in the Australian dollar and revaluation of inventory as a consequence of the lower than expected sales of milk powder sachets. As soon as this was identified the Board took decisive and swift action.

MG's current debt levels remain well within management's target range and well within all banking arrangements.

Who can I contact if I or someone I know needs additional support?

We understand developments may have caused both emotional and financial strain in what is a very low rainfall season. The welfare of suppliers, their families and our broader communities is of the utmost importance to MG.

If you feel they would be useful, we encourage you to take the time to review the emotional resilience information from WestVic Dairy, Murray Dairy and GippsDairy that offer important advice on taking care of yourself and one another during challenging periods.