



Supplier Meetings – Northern Region & Tasmania

Post-session Q&A summary

The following is a summary of key questions asked by MG suppliers at recent Supplier Meetings in Corryong, Kiewa, Milawa, Cobram, Finley, Rochester, Echuca, Cohuna, Smithton and Deloraine.

1. Is there any update on MG factories rumoured to be at risk of closing as a result of the business review?

As announced at our AGM in October, MG is undertaking an extensive review of all aspects of the business including our footprint, assets and distribution network, which will deliver further efficiencies into the milk pool in the future. The review is focussed on ensuring that we run our business as effectively as possible. We will continue to provide updates on review outcomes as appropriate.

2. Given the loss of milk intake, is it inevitable that we will need to downsize?

We remain Australia's largest milk processor by some margin and the business review is focused on rightsizing our overall operations relative to milk intake and general market conditions, to ensure optimum efficiency and that we provide a competitive milk price for our suppliers into the future. In October 2016 we said our milk intake would be down approximately 20% due to the combined impact of very wet weather at the start of the season and supplier departures and retirements. Our forecast for the year remains broadly in line with that guidance. About a quarter of this reduced milk supply has been caused by climactic conditions and also a deterioration in terms of trade impacting on how suppliers manage their dairy businesses with consideration of herd size and production output.

3. Are you going to cancel the MSSP?

We understand that the Milk Supply Support Package (MSSP) is still a source of continuing concern among suppliers. It has become increasingly clear that although the intention and structure of the MSSP was right, the interpretation and outcome for suppliers was not. We are currently looking closely at all aspects of MG's business including the MSSP to ensure we have a competitive milk price in FY18 and we will continue to listen to feedback from suppliers on this issue.

4. How many suppliers have we lost this season? Are we still losing suppliers?

MG has lost approximately 350 suppliers to date this season and has gained approximately 30 suppliers. We currently have a total of approximately 2,000 suppliers. The number of supplier departures has slowed, but competition for milk supply remains intense, particularly due to the reduced milk intake across the industry caused by very wet weather earlier this season.

5. How are you going to get the farmgate milk price up and stop suppliers leaving?

Since joining MG on 13 February, Ari Mervis has extended the business review announced at the AGM to include a review of MG's entire asset and cost bases, with the primary objective of providing a competitive farmgate milk price for suppliers now and in the future. Following the supplier meetings in the Northern Region and Tasmania during the past weeks, he is fully aware of the urgency in addressing these issues as MG looks to set its opening price for next season.

6. Why are we paying a dividend for the first half when MG made a loss?

Our financial loss of \$31.9 million reported for the first half to 31 December was due to the deviation to the profit sharing mechanism announced in October, comprised of an impairment of the Milk Supply Support Package and step-up payments to suppliers. Without the impact of these one-off items, our Normalised Net Profit After Tax (NPAT) for the first half was \$9.4 million. We have paid a dividend in

accordance with our obligations under MG's profit sharing mechanism and it is based on this Normalised NPAT figure.

7. Why is the Board considering the appointment of a non-supplier Chairman? Doesn't this require constitutional change or approval of suppliers?

As a large and complex international business, the MG Chair role requires knowledge across areas including agricultural production, manufacturing, supply chain and fast moving consumer goods, as well as the ability to engage with a large range of external stakeholders. It is vital that we get the right person to chair the Board so that the co-operative has the strength and depth of governance expertise that is required. Under MG's Board Charter the appointment of the Chairman is a matter for the Board to decide. Traditionally the Chairman is chosen from among the Supplier Directors, but there is no requirement in MG's constitution for the Chairman to be a Supplier Director.

8. What is the latest with the review of the Board's structure and composition?

MG's Board is large relative to comparable companies and current best practice. We are considering a structure which could result in 5-6 Supplier Directors, 3 Special Directors and the Managing Director. This ensures majority farmer representation will be maintained and if endorsed, the proposal will require a vote for constitutional change by suppliers.

9. What advantage is there in having a smaller Board?

The "ideal" size for a Company's Board will depend on a range of factors, including the complexity of the company's structure and operations, the need to have Directors representing different skills and expertise present on the Board, and succession planning. Consistent with advice provided by an independent corporate governance expert and review of comparable companies, the Board's view is that 12 Directors is too large. A smaller Board would allow greater agility in decision making and also support the business wide focus on cost reduction. Farmer representation would continue to be provided via majority representation by Supplier Directors on the Board. Given the significant expertise in agricultural production provided through the Supplier Directors, the review is also looking at how other expertise and experience can be brought into the Board and balanced alongside the skills of Supplier Directors.

10. If farmers don't want the change the Board proposes, will you listen?

Any changes to the structure and composition of the Board proposed by the review and endorsed by MG Directors and which require constitutional change will also need the approval of shareholders. This would require a vote to be taken either at the AGM or an EGM. The appointment of the Chairman is a matter for the Board to decide and the appointment of a non-supplier Chairman does not require constitutional change or supplier approval.

11. How is MG proposing to gather supplier feedback for the milk payment system review?

As announced at the AGM and in response to supplier feedback, MG is undertaking a farmgate milk payment review to ensure MG sends the right market signals, in a timely manner, while also balancing farmers' business management needs. All suppliers will have the opportunity to provide feedback via an online survey which has just been launched via MG's website (it is also possible to complete a hard copy survey which can be requested via Field Services staff). 300 suppliers will also be selected randomly to participate in telephone surveys, which will be arranged by an independent research company at a time convenient to the selected participants. In line with its co-operative principles MG regularly reviews its milk payment system, the last occasion being in 2013. MG's underlying view – which is consistent with the views of suppliers – is that our milk payment system is currently too complicated and needs to be simplified.

12. Is MG intending to retain the Flat Milk Incentive?

The Flat Milk Incentive (FMI) is included in the overall review of MG's milk payment system. The FMI was designed to implement the value of committed milk during the off-peak period and the current evidence is that the FMI isn't providing the intended outcome. We will have to await the views expressed by suppliers in the survey before any changes are made and MG is mindful of providing suppliers with adequate time to be able to adjust to any changes that may be made as a part of the review.

13. What are the new CEO's priorities?

Ari Mervis has prioritised the need to engage with the maximum number of suppliers as practicable. This is being organised via an extensive schedule of 24 supplier meetings over the next few weeks, one of the largest ever organised by the co-op. During this time he will also visit MG operations and will meet with employees as well as other key stakeholders. This will inform his thinking about the actions required to be taken to strengthen MG's position.

14. Is MG's value-add strategy still correct and delivering value?

Ari Mervis believes that MG's previously articulated strategy for consumer goods remains correct. He believes the best way to maximise profitability is to move up the value chain with quality products that are relevant to evolving consumer demand. The new consumer cheese facility at Cobram shows what is possible for future product innovation.

15. Is there any update on China and how the new CEO is looking at our operations there given his experience in this region?

Ari Mervis spoke to suppliers about his extensive knowledge of the business environment in China, gained through his previous role as Managing Director of SAB Miller in the Asia-Pacific and as Chairman of a local brewing joint venture with China Resources. Ari's view is that overnight success is very unusual in China and that MG needs a sustainable and deliberate business model. Ari also spoke of the need to find the correct route to market for MG via distributors and other channels. He also spoke of the high regard in China for Australian agricultural produce and the long term opportunities there for the co-operative.

16. What has Ari Mervis learnt about dairy farmers in his first three weeks in the job?

Ari has been impressed by the open and honest feedback he has received in all interactions with MG suppliers since starting in his new role. The feedback has been constructive even if not always positive and the sincerity has been very evident. He has also noted the resilience of suppliers as well as the high degree of emotional connectivity that exists between suppliers and the co-operative and with the dairy business generally.

17. What happens to the shares of suppliers who are leaving or have left the co-op?

All supplier shareholders who leave MG lose their voting rights. Retiring shareholders may retain their shares and if they wish to sell down, may do so over a 3 year period. The Share Standard policy requires suppliers who commence supplying a competitor to sell their shares over 3 years and MG has the right to force these sales if not completed within the required timeframe. The Board will continue to monitor and assess the enforcement of this right.

18. Is it true suppliers seeking to leave MG have been threatened with legal action?

MG expects that milk supply agreements with suppliers will be honoured. Suppliers have entered fixed term contracts on the basis of clearly expressed terms and conditions, including those disclosed in the Supplier Share Offer prospectus. Fixed term contracts are entered by MG in exchange for the provision of financial benefits to relevant suppliers, with the length of the fixed term varying based on the type and size of the financial benefit received.

19. What can you do to improve the information provided to suppliers and its clarity?

MG communicates regularly with suppliers and we have sent over 40 letters to suppliers providing updates since April 2016. When the current schedule of supplier meetings finishes, we will have arranged almost 100 supplier meetings in the past year. We have also created a Supplier Information Centre on MG's website where information can be readily accessed.

MG has a Market Disclosure and Communications Policy which sets out our commitment to effective communication with all stakeholders, so as to give them ready access to balanced and clear information. This includes continuous disclosure obligations related to our ASX listing, which require that material price or value sensitive information is not communicated to any external party prior to that information being disclosed to all shareholders and unitholders. We do receive feedback from suppliers that some communication is complicated and hard to read. We are committed to simplifying our supplier communication and making it shorter and sharper.

20. Is MG buying milk to try to cover the lost intake?

Like many processors MG engages in milk swaps, which provide a cost effective and efficient system for moving milk around the co-operative's areas of operation. Although commercial swaps deliver benefits, we are assessing whether MG will continue to participate in these arrangements to the extent that the co-op has in the past. In general we are net sellers of milk rather than net buyers.

21. What caused the debt increase in the first half – is it sustainable?

Debt in the first half rose in line with expectation due to the final spend on our consumer cheese plant investment, the implementation of a new integrated SAP technology system across MG's business (driving efficiency gains, improved data accuracy and reporting capabilities) and funding of the MSSP. Debt also increased in the first half due to the seasonal milk supply curve – whereby most milk is paid for in the first half before being sold in the second half. We expect our closing net debt level for full year 2017 to be broadly similar to closing net debt for full year 2016.

22. A series of small supplier meetings were held in January - why were only select groups invited?

A few small supplier meetings were organised in the Northern Region in January. This was to facilitate open dialogue with suppliers, particularly given strong competition for milk supply at the time and false information circulating about MG in the area. We organised these meetings as we believed smaller group settings allowed for a more open and detailed discussion, as well as to provide reassurance for our suppliers. Supplier Relations intends to organise more of these smaller discussion group format meetings in the future, involving local Directors, Field Services and senior management.

23. Is there any update on our planned Nutritionals investment now that Mead Johnson Nutrition has announced it will acquiring its own production assets?

As we announced in December following the termination of our alliance with Mead Johnson Nutrition, MG remains committed to a B2B nutritionals strategy. We are reviewing our strategy for this investment to ensure we maximise value for suppliers and owners, whilst exercising capital discipline. Our supply agreement with Indonesia's Kalbe Nutritionals remains in place and we continue to look at potential offtake opportunities with other parties.

24. Is there any update on the new consumer cheese facility at Cobram? When will suppliers be allowed to visit the site?

The consumer cheese plant is now in commercial production and completing normal commissioning. Ramp up to full production and transition to Devondale branded products will continue over coming months. Our priority has been getting the plant ready. However, we are planning to organise some tours for suppliers once full commissioning has been completed.

25. Heavy discounting of cheese by retailers is being reported in the media – is MG being impacted? How can we differentiate our products from cheap imports?

Retailers control retail pricing and MG supplies private label cheese to Coles and Devondale branded cheese to all retailers at acceptable margins. As expected there is a swing to private label on the lower private label prices in total market, however Devondale is holding volume in the market. Ari Mervis has toured the new Cobram facility and was greatly impressed by the maturity of our standard cheese products and believes there is an opportunity to highlight this more clearly in our marketing.

26. With respect to the growing use of Tasmania branding in the marketing of local products, why doesn't MG use the Tasmanian origin of some production in its marketing?

Devondale is an Australian brand and does not have a specific origin. The brand is something the business has invested in over a long period of time to ensure it is recognised and trusted by consumers. We aim to sell our branded products both nationally and internationally and believe a single brand aligns best to the retail landscape and universal needs from a consumer perspective.