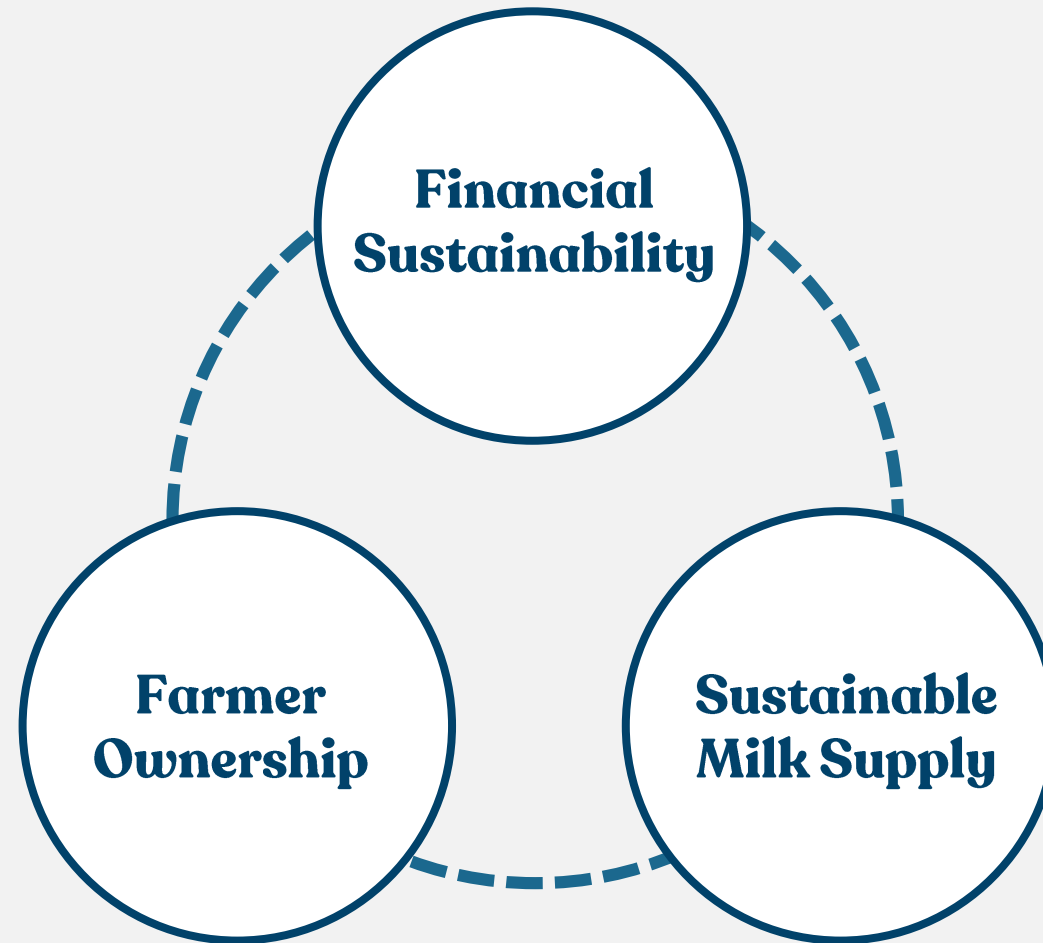


# Capital structure review update

July 2021

# A recap on the fundamentals of our review

- A strong farmer-owned Co-operative is good for farmers and good for New Zealand.
- We have choices to make to protect our Co-op for generations to come.



# First phase of consultation now completed

- Our focus shifts to reflecting farmer feedback in a more detailed proposal for further consultation.
- While we mark the end of phase one, this is an ongoing conversation. If farmers still have questions, views or ideas, they can reach out to Directors, Area Managers and Co-op Councillors, or email us via [CSfeedback@fonterra.com](mailto:CSfeedback@fonterra.com).



# High level of participation shows farmers' commitment to our Co-op



**90** Director-led farmer meetings held across the country

**7** farmer webinars with an average of around **200** attendees at each

**100s** of written responses received from farmers

Over **5,000** farmers have directly engaged through feedback channels to date



Dairy for life

# **This is a tough conversation, but it's important we have it now**



We thank farmers for approaching consultation with open minds, while managing uncertainty.

As an intergenerational Co-op, it's important we have this conversation now.

The Board maintains its belief that, in a flat or potentially declining milk environment, making changes early will put us in the best position to provide farmers more flexibility while protecting farmer ownership and strengthening the Co-op's financial sustainability.

Delaying the conversation may limit our options and increase the cost of addressing the challenges we face.

# Ongoing engagement with other stakeholders throughout consultation is also a key focus



**FONTERRA CO-OPERATIVE COUNCIL:** We are working closely with the Council as a sounding board. The approval of at least 50% of Council members is required to implement capital structure changes to the Co-op's Constitution.



**RURAL PROFESSIONALS, BANKS, ANALYSTS:** A dozen Director-led meetings, a webinar and calls were organised for rural professionals (accountants, farm consultants etc.), plus meetings and calls with banks and research analysts.



**FONTERRA SHAREHOLDERS' FUND:** We have been engaging with the manager of the Fund who has been communicating with unit holders directly.



**OTHER STAKEHOLDERS:** We have been talking with Government and other groups to keep them updated and will continue to do so.

# A summary of farmer feedback



- We've heard good levels of support for addressing the issues we have identified through our capital structure review.
- We've heard how much farmers value a strong Co-op and how important intergenerational succession is to them.
- Many farmers have told us that to form a clearer view on capital structure they would like more information on where the Co-op is heading in terms of strategy and performance.
- There have been some common themes when it comes to farmer views on the preferred option.
- Some farmers have shared new ideas, or innovations on the other options outlined in the Consultation Booklet.

# The common themes

The Board is focusing on the common themes that have come through. These have been grouped into three areas, with further details on the next slides.



**1. Farmer-only market and share price impacts**



**2. Balancing flexibility and Co-op alignment**



**3. Managing transition**



## Theme 1: Farmer-only market and share price impacts

- There's a lot of discussion around the challenge of protecting farmer ownership and impacts on the share price.
- There's support for a market where the share price is ultimately determined by the Co-op's performance and farmers' assessment of that. But there are also concerns about the share price impacts of a farmer-only market, including whether there's enough depth in the market when it comes to buyers and sellers of shares.
- There's a clear call for more information on business strategy and future performance.
- Farmers are also keen for more information around how a permanent farmer-only market would operate.
- There's no clear preference from farmers on the future of the Fund. There have been suggestions that instead of buying back the Fund, Fonterra should consider buying back shares to reduce the overall shares on issue.

## Theme 2: Balancing flexibility and Co-op alignment

- We have heard support for the concept of giving all farmers some level of flexibility with their shareholding at any point of their farming career.
- There are a range of views on how to strike the right balance between flexibility and ensuring farmers still maintain a strong capital commitment to the Co-op.
- Many farmers have shared that moving from a 1:1 to a 1:4 Share Standard may be a step too far, with a lot wanting to retain a 1:1 Share Standard. Farmers proposed other ways of making it easier for new farmers to join the Co-op, including increasing the time to share-up and making loans available.
- Questions were raised about potential misalignment within the farmer-base between those who would choose to sell down some of their shareholding and be less exposed to earnings, and those who would want to invest more in the Co-op. Some farmers would like to see more detail around how we make sure the Co-op stays aligned if we reduced the minimum shareholding requirements.
- We've had some feedback around voting, including whether voting should be based on share-backed supply or milk solids.

## Theme 3: Managing transition

- We've heard a lot from farmers about the need to recognise the loyalty of Co-op members.

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- This has led to many conversations about the appropriate length of time we could allow farmers to share-down when they retire or leave the Co-op. Related to this, there has been feedback from some farmers that we need to make sure that the proposals cater for retiring farmers who have been part of the Co-op for many years.

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- We've also had some feedback on making sure that any new structure works for sharemilkers and contract milkers. We've heard from farmers who would like to see opportunities for them to participate in the farmer-only market.

# Some farmers have shared new ideas or innovations on the other options

- We received ideas for multiple variations within the different options presented, including a number of alternative proposals provided as written submissions.
- A huge amount of time and effort has gone into developing some of these proposals, and we really appreciate these ideas.
- All the proposals have been worked through in detail and there are some aspects that we are considering as we work towards a final proposal.
- High-level summaries are provided [here](#), with similar proposals grouped together for simplicity.



# A summary of the changes to the preferred option that we're considering



## Preferred option presented in May

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Minimum shareholding requirement of 1 share per 4 kgMS or 25% of supply

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Maximum shareholding of 4 x supply

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5 years to enter

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5 years to exit

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Farmer-only market

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Voting based on share-backed supply

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## Changes we are considering

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Minimum shareholding requirement 1 share per 3 kgMS or 33% of supply

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Maximum shareholding of 4 x supply *(no change from May)*

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6 years to enter

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10 - 15 years for current shareholders

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Sharemilkers and contract milkers can also buy, hold and sell shares in the farmer-only market

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Possible share buy-back options

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Voting based on share-backed supply *(no change from May)*

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## Some further detail on the changes we're considering

- **Share Standard and Minimum Shareholding Requirement:** We are reconsidering the proposed reduction to the Share Standard. Instead, the Share Standard could stay at 1 share for every kgMS supplied, and the minimum shareholding requirement could be set at 33% of that Share Standard (or around 1 share / 3 kgMS). This better respects the principle of shareholder alignment, but still provides flexibility for those who need it at different points in their farming career. The 33% also reflects the feedback from many of you that 1:4 (25%) is too far too fast.
- **Maximum Shareholding:** We are not looking to lower the cap of 4 x supply to support liquidity in the market.
- **Entry:** We are considering extending the entry timeframe from five years to six years, with no obligation to purchase more than 1,000 shares in the first year.
- **Exit:** We are also looking at extending exit timeframes for all farmer owners on the date of the vote to up to 10 or 15 years, including those who have already ceased in the past few seasons but who still hold shares.
- **Farmer-only Market:**
  - We are looking at allowing sharemilkers and contract milkers to participate in the farmer-only market and hold shares in the Co-op.
  - We are also reviewing the market maker role and looking further at how potential share buy-back options might support liquidity in a farmer-only market.
- **Voting Rights:** We have reconsidered voting rights in light of feedback from some of you and at this stage our preference is for voting to continue to follow share-backed supply as it currently does under the Constitution.

# We're also going to share more on strategy & performance

- In August and September, we will provide further information on our long-term strategy, including the types of activities we will invest in, the returns we are targeting and the measures against which we will track our progress.
- It's clear that farmers would value this to help inform their decisions on capital structure.

## Innovation

To create superior value for our customers and our Co-operative

## Sustainability

To do what is right for the long term good and meet consumer and community needs

## Efficiency

Unlock greater value from our scale efficiency and focus on execution



# We are aiming for a farmer vote before the end of the year



We're committed to moving as quickly as we can through this review, while ensuring that all views are heard and considered so that we get a quality outcome. Our highest priority is to get it right.

Over the next couple of months, we plan to do surveys and run focus groups with farmers, while recognising it's a busy time of year on farm with calving.

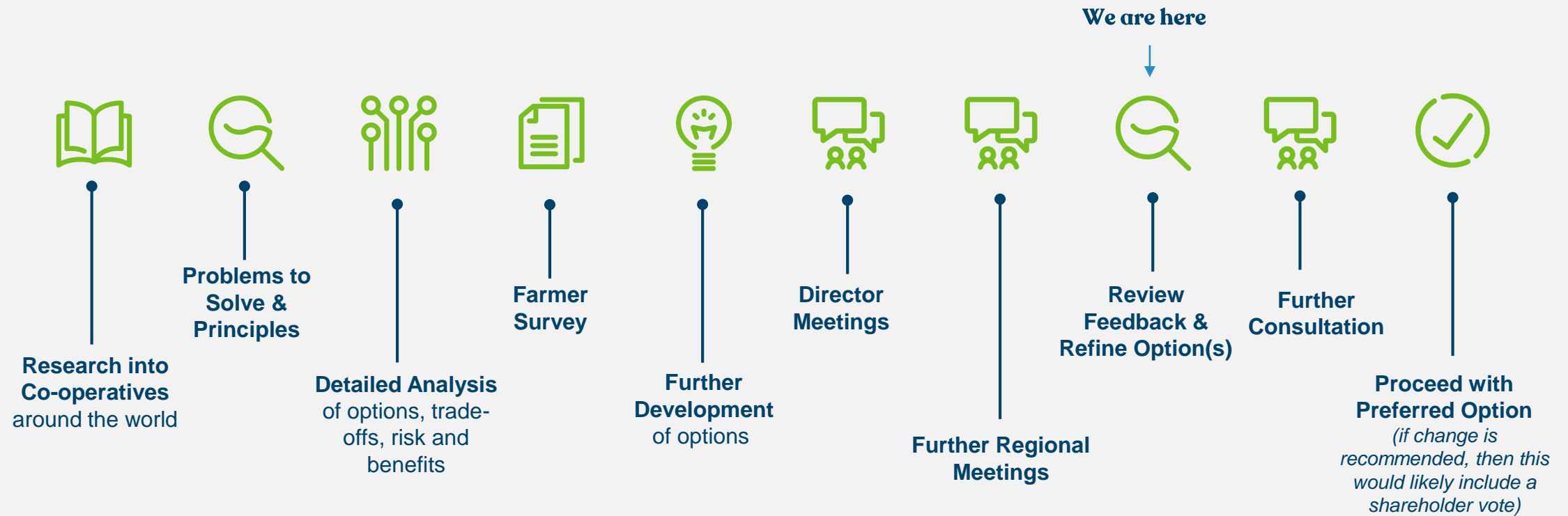
This will help us as we continue to develop a more detailed proposal to present to farmers around the time of our annual results in late September for further consultation.

At this stage, we are still aiming for a farmer vote at our Annual Meeting, which will be held in December.



# We look forward to continuing the conversation

If farmers still have questions, views or ideas, they can contact Directors, Area Managers and Co-op Councillors. Or you can submit your views via [Fonterra.com/CSFeedback](https://Fonterra.com/CSFeedback) or email [CSfeedback@fonterra.com](mailto:CSfeedback@fonterra.com).



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**Thank You**