



'the farmers business'



Executive Summary

Review of the Year 2016/2017

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Executive Summary

The financial and operational performance of the business continued to improve in the year to 31 March 2017 – the second year of the turnaround plan that started in 2015.

The financial highlights were:

- **Operating profit (before exceptional items) was £11.7m** (2016: £6.0m)
- **Net profit for the year was £6.0m** (2016: loss £5.1m)
- **Group turnover was £206.5m** (2016: £294.2m)
- **Net bank borrowings increased to £37.6m** (2016: £32.1m)
- **Capital investment of £3.8m across all our sites in the year** (2016: £4.8m)
- **Total group capital and reserves increased to £22m** (2016: £17.4m)
- **9ppl average increase in member milk price**
(including payment of 2ppl Business Performance Supplement)





Clive Sharpe

The Chairman's review

Over the last two years, First Milk has transformed. We have put in place a new business strategy, divested loss making subsidiaries, improved our operational performance and implemented an effective co-operative governance structure.

Rapid surgery was required over this period and it is a testament to our farmer members that they recognised and supported us through particularly difficult market conditions.

First Milk today is now a more focused and financially secure business. This is demonstrated through these significantly improved financial results and most importantly through our ability to increase milk prices to our farmer members ahead of the market during the last financial year.

Milk Price

The year to 31 March 2017 was a year of two halves for the dairy industry in terms of the cycle of milk price movements. After an extended period of low market prices, the nine pence improvement in members' milk price which was paid out during the year was much needed by our farmer members.

Seven pence of this increase came from improved market returns, with the other two pence reflecting the benefits of our restructuring initiatives. This additional sum was paid in the form of a Business Performance Supplement which was delivered to members by October 2016, quicker than originally expected.

Strategic

Following a strategic review in early 2015, we exited Glenfield Dairy and our Westbury joint venture in the previous financial year. The structural elements of the turnaround plan were completed with the sale of our CNP sports nutrition business in December 2016, leaving a profitable core business based around hard cheese and liquid milk contracts.

Partnerships

The long term relationship with Ornuva Foods is working well, and we continue to collaborate on new retail business with the UK multiple retailers. During the year we agreed a long term cheese supply partnership with Tesco, with the supply group being established after year end. Tesco has a long track record of working with British dairy farmers and we were delighted to work with them and Ornuva to create a strategic supply chain for British cheddar.

Having supplied fresh British milk to Nestlé UK and Ireland since 2003, we were pleased to agree a new long term contract with them during the financial year. Nestlé has consistently supported British dairy farmers and are at the forefront of driving best practice on responsible sourcing and sustainability. In March we were delighted to win two awards at The Nestlé Supplier Awards 2017 – Supplier of the Year and Best Quality Award.

Capital investment

Through the turnaround we have continued to invest in the capital assets of the business. The major projects in the financial year were the renewal of the CIP (Cleaning in Place) equipment at both Haverfordwest and Lake District Creameries.

Member Council

Dr Séan Rickard was appointed as the independent chairman of our Member Council in June 2016. He has had a successful career as a professional economist spanning 40 years and latterly has been at Cranfield School of Management where he was director of their MBA programme. He has also been a government academic adviser on food and rural policy.

Séan's appointment follows 2015's governance review, which led to member approval and implementation of a leaner and more commercial Board structure and strong Member Council. He works with our seven Member Council members who oversee the strategy of the business and represent our farmer owners.

Refinancing, Pensions and Capital

We successfully refinanced our debt facilities, and signed a new 4-year facility with Wells Fargo in January 2017. These facilities are significantly more flexible and lower cost than the ones they replaced, and, crucially, allowed us to reverse the payment deferral of member milk payments that had been implemented in January 2015. Our payment terms to members are now back to industry norms.

Our pension liabilities rose modestly, largely as a consequence of the reduction in long term interest rates following the Brexit vote in June 2016. However our total pension liabilities remain in the range expected when we agreed the long term funding levels with the Trustees of both schemes. Total pension liabilities (net of deferred tax assets) increased from £6.4m to £11.2m during the year.

The capital structure of the group was revised in August 2016, with the creation of a new class of shares and the conversion of member loan accounts, B preference shares and debentures into the new C preference shares.

Change of CEO

I would like to place on record the Board's appreciation for the work done by Mike Gallacher as Chief Executive during the turnaround phase, and wish him well for the future.

Mike led First Milk through a period of huge change, with enormous levels of energy and focus. In addition to delivering a real transformation in our business performance he also built an effective team and put in place the modern governance processes that will underpin our future success.

At the same time we welcome Shelagh Hancock who started at the beginning of April as our new Chief Executive and brings a wealth of experience to the role that will be key to unlocking the next stage of improvements in the performance of the business.

Brexit

While the Brexit vote in June 2016 has created considerable political and economic uncertainty, our focus on the UK market and the British provenance of our milk puts us in a strong position. We are actively working with our customers on their scenario planning, where they are particularly focused on how they source dairy products from the UK rather than through imports in the future. We believe that the role for a scale British Dairy Co-operative is even more compelling post Brexit and we aim to demonstrate this in the years ahead.

Summary

First Milk's business is now well placed to play a leading role in the industry, and now that the structural elements of the turnaround plan have been delivered, we are concentrating on improving efficiencies and returns in our core business.

Finally may I take this opportunity to thank all of the staff of First Milk, my fellow Board directors and above all our members for their hard work and commitment during the last year.



Shelagh Hancock

The CEO's statement

Having joined the business right at the end of the financial year being reported, I am delighted to be working again for a farmer co-operative, as I am a firm believer in the principle of farmers working together for the benefit of each other.

It is clear that, following the transformation process that was completed before I joined; we have a focused and financially stable foundation to build from.

We have a robust governance structure, a clear strategy and good customer relationships. We also have a good balance between customer demand and milk supply and importantly we have a hard-working and committed team. All these things provide us with a solid platform for progress.

So now we must look to the future and exploit these advantages to grow the business and enable us to deliver competitive total returns to our members. Working as one team, we will develop a relentless focus on efficiency and quality. We will put customers at the heart of our business, creating value through strong, long-term partnerships.

Our strategy will see us achieve this by:

- Investing further in the processing capacity and capabilities at our manufacturing sites;
- Improving our productivity by tirelessly driving out cost and streamlining our business processes and systems throughout our supply chain to leverage smarter ways of working;
- Strengthening our customer relationships through working closely in partnership to deliver their needs in a flexible, agile way for mutual benefit;
- Growing our total milk pool, primarily by encouraging our existing members to expand their milk production to meet growing customer demand;
- Continuing to develop the capabilities and expertise of our people and management teams.

Finally

I strongly believe that First Milk has a bright future and as a British farmer owned co-op we have great credentials to build on, particularly against the backdrop of the ongoing Brexit process.

I am confident that we can build on our solid relationships to create a strong and vibrant business capable of delivering competitive returns to our members and providing opportunities for those that want to grow their own businesses.

Profit and Loss Accounts:

for the year ended 31 March 2017

	2017	2016
	Group £'000	Group £'000
Turnover - continuing operations	206,468	294,232
Less: share of joint ventures' turnover	(3,878)	(2,781)
Total turnover	202,590	291,451
Cost of sales	(181,437)	(274,669)
Gross profit	21,153	16,782
Administrative expenses		
- <i>Recurring</i>	(9,426)	(10,748)
- <i>Exceptional items</i>	(2,309)	(5,104)
	(11,735)	(15,852)
Operating profit		
- <i>Continuing operations</i>	9,418	930
Share of operating profit / (loss) in joint ventures		
- <i>Continuing operations</i>	470	(501)
- <i>Discontinued operations</i>	-	150
Profit before interest	9,888	579
Finance income	21	26
Finance costs	(3,439)	(4,044)
Profit / (loss) on ordinary activities before taxation	6,470	(3,439)
Tax on profit / (loss) on ordinary activities	(425)	(1,687)
Profit/(Loss) for the financial year	6,045	(5,126)

Balance Sheet:

for the year ended 31 March 2017

	2017	2016
	Group £'000	Group £'000
Fixed Assets		
Intangible fixed assets	-	-
Property, plant and equipment	32,717	33,078
Investments in subsidiary undertakings	-	-
Investments in joint ventures	554	83
Total fixed assets	33,271	33,161
Current assets		
Inventories	43,462	37,296
Trade and other receivables	27,940	28,447
Cash and cash equivalents	4,607	350
	76,009	66,093
Trade and other payables amounts falling due within one year	(32,086)	(70,325)
Net current assets / (liabilities)	43,923	(4,232)
Total assets less current liabilities	77,194	28,929
Trade and other payables amounts falling due after more than one year	(41,599)	(2,928)
Provisions for liabilities and charges	-	(833)
Total net assets employed excluding pension liability	35,595	25,168
Pension liability	(13,554)	(7,802)
Net assets	22,041	17,366
Capital and reserves		
Share capital	73,886	8,616
Profit and loss reserve	(51,845)	(52,555)
Members' funds	22,041	(43,939)
Loan Capital	-	61,305
Total capital and reserves	22,041	17,366

Cash Flow:

for the year ended 31 March 2017

	2017	2016
	Group £'000	Group £'000
Net cash from operating activities	(2,494)	21,662
Taxation paid	-	-
Net cash generated from/(used in) operating activities	(2,494)	21,662
Cash flow from investing activities		
Finance income	21	26
Purchase of property, plant and equipment	(3,772)	(4,827)
Movement in investment in joint ventures	-	1,693
Proceeds from sale of investment	242	-
Proceeds from sale of property, plant and equipment	202	1,357
Net cash generated from / (used in) investing activities	(3,307)	(1,751)
Cash from financing activities		
Finance costs	(2,588)	(2,737)
Net proceeds from members	2,899	10,101
Repayment / (drawdown) of loans	9,747	(28,316)
Movement in loans with joint ventures	-	982
(Decrease) / increase in debt facilities	-	19
Net cash generated (used in) / from financing activities	10,058	(19,951)
Net increase (decrease) / in cash and cash equivalents	4,257	(40)
Cash and cash equivalents at the beginning of the year	350	390
Cash and cash equivalents at the end of the year	4,607	350

The Board



Clive Sharpe
Chairman

Clive joined First Milk as chairman in February 2016.

He is also currently chairman of Peters Foods and Janan Meats. In a food manufacturing career spanning 37 years, he is former chairman of Quorn Foods and Burtons Biscuits and former CEO of WT Foods, Golden Wonder and Homepride Foods.



Shelagh Hancock
Chief Executive

Shelagh joined First Milk as chief executive in April 2017.

She has over 25 years' experience in the food and agricultural supply sectors. She held a number of senior executive positions including managing director at Medina Dairy and milk business unit director at farmer-owned co-operative Milk Link .



Brian Mackie
Non-Executive Director

Brian has held a range of international chief financial officer roles in a number of large businesses; Starbev/ Molson Coors Europe, Maxxium Worldwide and Cott Corporation. He has also had international responsibility for IT, Legal, Human Resources, and Commercial Operations during his career.



Carl Ravenhall
Non-Executive Director

Carl was latterly managing director of Muller Wiseman Dairies.

Prior to that in a dairy career that spans more than 25 years, he held a number of senior executive roles including managing director of Milk Link's cheese business, and MD of Adams Foods.



Nigel Evans
Farmer Director

Nigel farms with his family in Pembrokeshire and has studied dairying in the US, South America and New Zealand.

He has also been instrumental in establishing a number of other property investment businesses and holds directorships in 17 UK and Swedish property investment companies and partnerships.



Jim Baird
Farmer Director

Jim farms in Lanarkshire as part of a family partnership. He has undertaken a Nuffield scholarship, visiting countries including USA, China, Australia and New Zealand to research the key attributes of enterprising rural businesses. Jim also sits on the Scottish Advisory Board of the NFU Mutual.



Greg Jardine
Chief Financial Officer

Greg joined First Milk in 2010 and held several senior management and executive roles in finance and commercial before being appointed as chief financial officer and joining the Board in September 2017. Greg has 12 years' dairy experience, having previously worked for Lactalis McLelland as Industrial finance director.

Member Council



Séan Rickard
Independent Chairman



Di Clements
Council Member



Mike Smith
Council Member



Scott Calderwood
Council Member



Christine Kelsall
Council Member



Willie Campbell
Council Member



Willie Purdie
Council Member



Robert Craig
Council Member

Role of the Member Council

The powers of the Council include:

- Holding the Board to account on behalf of the Members
- Approving the annual budget, business plan and company strategy
- In consultation with the Board, recommending candidates for the role of the chair and vice chair for election by Members at AGM
- In consultation with the Board, approving the nomination process for Independent Non-Executive Directors and Farmer Non-executive Directors
- Communicating with Members and approving processes for groups of Members to raise matters of concern with the Council
- Having the power to remove any Director from office
- Setting the remuneration of the Non-Executive Directors



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