AGROPUR
Dairy Cooperative

# QUARTERLY REPORT

For the 26-week period ended April 28, 2018

## TO MEMBERS AND EMPLOYEES

**Dear members and colleagues,**

Here are the highlights of the second quarter of fiscal 2018:

- Sales up $60.2 million or 3.8% to $1.6 billion;
- Earnings from operations down $3.6 million (3.8%) to $90.9 million;
- We exceeded the $100-million cost-reduction target we had set for 2016-2018.

Highlights for the six-month period:

- Sales up $10.9 million or 0.3% to $3.2 billion;
- Earnings from operations down $67.7 million (30.3%) to $155.9 million;
- Various projects in our cost-reduction program generated a $17.0-million improvement;
- The acquisition of all shares of Ultima Foods on October 29, 2017 was accretive to earnings from operations;
- A $47.7-million accounting gain on business combination was recognized during the first half of the year.

The slump in cheese and whey markets in the U.S. seems to have eased in the second quarter and some indicators are pointing towards a slightly more favourable environment. However, we cannot predict future market volatility and we are therefore continuing our efforts on the factors under our control. We are pressing ahead with our cost-reduction program and with integration of our acquisitions, including Ultima Foods, in order to capture the anticipated synergies.

**Financial overview**

**Second quarter** sales were up $60.2 million or 3.8%, year over year, to more than $1.6 billion. Additional volume resulting from the acquisition of the assets of Ultima Foods accounted for the bulk of the growth. That factor was partially offset by the appreciation of the Canadian dollar against the U.S. dollar.

Earnings before interest, income taxes, depreciation, amortization, restructuring costs, integration and other non-recurring costs (earnings from operations) decreased $3.6 million or 3.8% year over year to $90.9 million. Despite increased volume, U.S. earnings reflect the negative impact of falling international prices for whey products. In Canada, despite lower net prices, our earnings are improving because of our cost-reduction program and the positive contribution from Ultima Foods' operations.

The depreciation and amortization expense increased $2.1 million to $43.9 million, essentially because of depreciation and amortization of the acquired Ultima Foods assets. Restructuring, integration and other non-recurring costs amounted to $3.0 million. Financial expenses were $11.1 million, an increase from the second quarter of 2017. The income tax expense recorded by our subsidiaries decreased by $3.0 million as a direct result of lower earnings before income taxes.

Net earnings before patronage dividends and the Cooperative's income taxes were therefore $27.8 million in the second quarter of 2018, compared with $39.3 million in the same period of 2017.

**Year-to-date** sales totalled $3.2 billion, a $10.9-million increase from the same period of 2017. Earnings from operations amounted to $155.9 million, a year-over-year decrease of $67.7 million or 30.3%. As a reminder in the first quarter, U.S. earnings were strongly affected by the unfavourable impact of the cheese block price / cost of milk ratio and the significant decrease in world prices for whey products. The depreciation and amortization expense increased by $3.1 million. Restructuring costs, integration and other non-recurring costs were $10.9 million, consisting primarily of expenses related to the business combination and the restructuring of certain activities. Financial expenses were down $0.4 million. The subsidiaries' income tax expense decreased by $26.3 million as a direct result of the lower U.S. earnings.

A $47.7-million accounting gain was recognized in the first half of 2018 in connection with the acquisition of all shares of Ultima Foods. As required by accounting standards, we reassessed the fair value of the interest held in the joint venture prior to the acquisition, giving rise to the gain. By comparison, a $44.0-million net gain was recorded in the first half of 2017 in connection with the acquisition of Sobeys assets, reflecting a purchase price adjustment and impairments of assets. A $4.1-million accounting gain was also recognized in connection with the acquisition of Scotsburn.

Net earnings before patronage dividends and the Cooperative's income taxes decreased $50.9 million or 37.2% year over year.

Cash flows from operating activities were $144.2 million. $6.2 million was used for non-cash items during the first half of the year. This change in working capital was mainly due to a $4.5-million increase in inventories.

Capital expenditures totalled $194.3 million in the first half of 2018. Major expenditures included expansion of our Lake Norden plant in the U.S. and the enterprise resource planning (ERP) system. As well, $68.1 million was spent to acquire Ultima Foods and assume 100% of its debt, which amounted to $81.9 million at the time of the acquisition.

With respect to activities with members, redemption of shares and certificates of indebtedness totalled $40.2 million during the period. Equity rose by $28.1 million in the first half to $2.288 billion.

In short, while we have exceeded our 3-year, $100-million cost-reduction target, we are continuing our cost-out initiatives, which remain vital to earnings growth in a competitive environment. We are also continuing work on integrating Ultima Foods in order to realize the anticipated synergies and support earnings growth.


**Robert Coallier**
Chief Executive Officer

**Émile Cordeau**
Senior Vice-President and Chief Financial Officer


## CONSOLIDATED EARNINGS

| (IN THOUSANDS OF CANADIAN DOLLARS) (unaudited) | 13 WEEKS 2018 | 13 WEEKS 2017 | 26 WEEKS 2018 | 26 WEEKS 2017 |
|---|---|---|---|---|
| Sales | **1,643,024** | 1,582,804 | **3,245,914** | 3,234,978 |
| Operating expenses excluding depreciation and amortization | **1,552,123** | 1,488,278 | **3,090,057** | 3,011,421 |
| Earnings before interest, income taxes, depreciation, amortization, restructuring costs, integration and other non-recurring costs | **90,901** | 94,526 | **155,857** | 223,557 |
| Depreciation and amortization | **43,905** | 41,839 | **86,658** | 83,561 |
| Restructuring costs, integration and other non-recurring costs[1] | **3,016** | 375 | **10,888** | 3,913 |
| Operating earnings | **43,980** | 52,312 | **58,311** | 136,083 |
| Net financial expenses | **11,098** | 9,098 | **17,878** | 18,272 |
| Loss (gain) on disposal of assets and impairment of assets | **(294)** | (420) | **(447)** | 6,347 |
| Purchase price adjustment | **-** | - | **-** | (50,220) |
| Accounting gains as a result of business combinations | **-** | (4,126) | **(47,660)** | (4,126) |
| Income taxes of subsidiaries | **5,409** | 8,451 | **2,511** | 28,853 |
| Net earnings[2] | **27,767** | 39,309 | **86,029** | 136,957 |

## CONSOLIDATED CASH FLOWS

| (IN THOUSANDS OF CANADIAN DOLLARS) (unaudited) | 26 WEEKS 2018 | 26 WEEKS 2017 |
|---|---|---|
| **Operating activities** | | |
| Net earnings[2] | **86,029** | 136,957 |
| Net financial expenses | **17,878** | 18,272 |
| Items not involving use of funds | **40,264** | 119,118 |
| | **144,171** | 274,347 |
| Patronage dividends paid | **(16,178)** | (14,946) |
| Change in non-cash items | **(6,217)** | (71,553) |
| | **121,776** | 187,848 |
| **Financing and share capital activities** | | |
| Long-term debt and interest paid | **122,283** | (38,931) |
| Dividends on first preferred shares | **(26,577)** | (23,690) |
| Issuance and redemption of members' shares and certificates of indebtedness | **(40,083)** | (40,120) |
| | **55,623** | (102,741) |
| **Investing activities** | | |
| Business combinations | **(68,059)** | (62,287) |
| Proceeds from disposal of assets | **1,120** | 13,493 |
| Property, plant and equipment, intangible assets and others | **(195,267)** | (46,016) |
| | **(262,206)** | (94,810) |
| Effect of exchange rate fluctuations on cash position | **531** | 1,675 |
| Net change in cash position | **(84,276)** | (8,028) |

## CONSOLIDATED BALANCE SHEETS

| (IN THOUSANDS OF CANADIAN DOLLARS) | April 28 2018 (unaudited) | October 28 2017 (audited) |
|---|---|---|
| **Assets** | | |
| Current assets | **1,242,230** | 1,373,100 |
| Investments and loan | **1,208** | 17,280 |
| Property, plant and equipment and other long-term assets | **3,197,325** | 2,825,778 |
| | **4,440,763** | 4,216,158 |
| **Liabilities** | | |
| Current liabilities | **794,413** | 840,513 |
| Long-term debt | **1,248,012** | 1,022,906 |
| Deferred income taxes | **80,716** | 65,230 |
| Employee future benefits obligation | **25,553** | 23,427 |
| Other long-term liabilities | **4,040** | 4,127 |
| | **2,152,734** | 1,956,203 |
| **Equity** | | |
| Members' capital | **755,623** | 795,706 |
| First preferred shares | **770,000** | 770,000 |
| Reserve and others | **762,406** | 694,249 |
| | **2,288,029** | 2,259,955 |
| | **4,440,763** | 4,216,158 |

[1] Restructuring costs, integration and other non-recurring costs include costs for the business combination and the restructuring of certain activities.
[2] Net earnings presented before patronage dividends and the Cooperative's income taxes which are accounted for only at year end.