AGROPUR
Dairy Cooperative

QUARTERLY REPORT

For the 39-week period ended July 28, 2018

TO MEMBERS AND EMPLOYEES

Dear members and colleagues,

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

- Sales up $84.6 million (5.3%) to $1.7 billion;
- Earnings from operations down $5.6 million (5.4%) to $97.1 million;
- Capital expenditures of $134.8 million, including the Lake Norden plant expansion, which is within budget and on schedule.

2018 nine-month highlights:

- Sales up $95.6 million (2.0%) to $4.9 billion;
- Earnings from operations down $73.3 million (22.5%) to $252.9 million;
- We have exceeded our $100-million cost-reduction target for 2016-2018;
- The acquisition of all outstanding 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 in the first quarter.

Our financial results continue to be impacted by slumping cheese and whey markets. We are therefore continuing to implement our plan for sound cost management and our organic growth projects. The expansion of our plant in Lake Norden, South Dakota is proceeding according to schedule and commissioning is slated to begin in 2019. The US$255-million investment approved last year will eventually triple the plant's processing capacity and enable us to step up our development in the U.S. We are confident that the project will let us fully capitalize on the upcoming recovery and strengthen our position as a key player in the dairy processing industry.

Financial overview

Third quarter sales were up $84.6 million or 5.3%, year over year, to more than $1.7 billion. Additional revenues resulting from the acquisition of the assets of Ultima Foods and increased cheese sale volume accounted for the bulk of the growth.

Earnings before interest, income taxes, depreciation and amortization, restructuring costs, integration and other non-recurring costs (earnings from operations) decreased $5.6 million or 5.4% year over year to $97.1 million. Despite increased volume, U.S. earnings reflect the negative impact of lower world prices for whey products. In Canada, our earnings are improving in spite of lower net prices because of our cost-reduction program and the contribution from Ultima Foods' operations.

The depreciation and amortization expense increased $2.7 million to $45.1 million, essentially because of depreciation of the acquired Ultima Foods assets. Restructuring, integration and other non-recurring costs amounted to $7.9 million. Financial expenses were $13.0 million, higher than in the third quarter of 2017 due to rising interest rates. The subsidiaries' income tax expense declined by $8.6 million because of lower earnings before income taxes and the cut in the tax rate in December 2017 under the U.S. tax reform.

Net earnings before patronage dividends and the Cooperative's income taxes were therefore $27.6 million in the third quarter of 2018, compared with $44.1 million in the same period of 2017.

Year-to-date sales totalled $4.9 billion, a $95.6-million year-over-year increase. Earnings from operations amounted to $252.9 million, a decrease of $73.3 million or 22.5% from the same period of 2017 due mainly to 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 $5.8 million. Restructuring, integration and other non-recurring costs were $18.8 million, consisting primarily of expenses related to the business combination and the restructuring of some operations. Financial expenses rose by $4.3 million. The subsidiaries' income tax expense decreased by $35.0 million because of lower U.S. earnings and the cut in the tax rate.

A $47.7-million accounting gain was recognized in the first quarter of 2018 in connection with the acquisition of all outstanding shares of Ultima Foods. As required by accounting standards, we remeasured the fair value of the interest held in the joint venture prior to the acquisition, giving rise to the gain. By comparison, a $44.6-million net gain was recorded in the first nine months of 2017 in connection with a previous acquisition, reflecting a purchase price adjustment and impairment of assets. As well, a $14.0-million accounting gain was recognized in connection with the acquisition of Scotsburn.

Net earnings before patronage dividends and the Cooperative's income taxes decreased $67.4 million or 37.3%, year over year.

Cash flows from operating activities were $312.2 million in the first nine months of the year, including $96.0 million from active management of working capital.

Capital expenditures totalled $330.1 million. 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 debt securities totalled $40.2 million during the period. Equity rose by $78.6 million in the first nine months to $2.339 billion.

We are all aware of the significant volatility to which our U.S. operations are exposed. Under the circumstances, we are pressing ahead with our efforts in the areas that are under our control, such as our cost-reduction program, integration of our acquisitions, and organic 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	39 WEEKS 2018	39 WEEKS 2017
Sales	**1,670,894**	1,586,260	**4,916,808**	4,821,238
Operating expenses excluding depreciation and amortization	**1,573,839**	1,483,618	**4,663,896**	4,495,039
Earnings before interest, income taxes, depreciation, amortization, restructuring costs, integration and other non-recurring costs	**97,055**	102,642	**252,912**	326,199
Depreciation and amortization	**45,117**	42,399	**131,775**	125,960
Restructuring costs, integration and other non-recurring costs[1]	**7,882**	5,768	**18,770**	9,681
Operating earnings	**44,056**	54,475	**102,367**	190,558
Net financial expenses	**13,039**	8,318	**30,917**	26,590
Loss (gain) on disposal of assets and impairment of assets	**173**	28	**(274)**	6,375
Purchase price adjustment	**-**	-	**-**	(50 220)
Accounting gains as a result of business combinations	**-**	(9,845)	**(47,660)**	(13,971)
Income taxes of subsidiaries	**3,278**	11,903	**5,789**	40,756
Net earnings[2]	**27,566**	44,071	**113,595**	181,028

CONSOLIDATED CASH FLOWS

(IN THOUSANDS OF CANADIAN DOLLARS) (unaudited)	39 WEEKS 2018	39 WEEKS 2017
Operating activities		
Net earnings[2]	**113,595**	181,028
Net financial expenses	**30,917**	26,590
Items not involving use of funds	**87,904**	162,071
	232,416	369,689
Patronage dividends paid	**(16,178)**	(14,946)
Change in non-cash items	**95,980**	(94,663)
	312,218	260,080
Financing and share capital activities		
Long-term debt and interest paid	**136,801**	(25,783)
Dividends on first preferred shares	**(26,577)**	(23,690)
Issuance and redemption of members' shares and certificates of indebtedness	**(40,070)**	(40,124)
	70,154	(89,597)
Investing activities		
Business combinations	**(68,059)**	(54,815)
Proceeds from disposal of assets	**1,209**	13,883
Property, plant and equipment, intangible assets and others	**(330,059)**	(98,733)
	(396,909)	(139,665)
Effect of exchange rate fluctuations on cash position	**(423)**	(685)
Net change in cash position	**(14,960)**	30,133

CONSOLIDATED BALANCE SHEETS

(IN THOUSANDS OF CANADIAN DOLLARS)	July 28 2018 (unaudited)	October 28 2017 (audited)
Assets		
Current assets	**1,243,753**	1,373,100
Investments and loan	**1,224**	17,280
Property, plant and equipment and other long-term assets	**3,307,235**	2,825,778
	4,552,212	4,216,158
Liabilities		
Current liabilities	**819,367**	840,513
Long-term debt	**1,289,480**	1,022,906
Deferred income taxes	**84,682**	65,230
Employee future benefits obligation	**16,070**	23,427
Other long-term liabilities	**4,063**	4,127
	2,213,662	1,956,203
Equity		
Members' capital	**755,636**	795,706
First preferred shares	**770,000**	770,000
Reserve and others	**812,914**	694,249
	2,338,550	2,259,955
	4,552,212	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.