Interim Report

for the six months ended 31 December 2019

The a2 Milk Company Limited

ARBN: 158 331 965

Overview

Financial results for the half year ended 31 December 2019 (NZ$)

Group performance

$806.7m Revenue ↑32%

$263.2m EBITDA ↑21%

$184.9m NPAT ↑21%

25.2c Earnings per share (EPS)

$160.6m Operating cash flow

$618.4m Cash on hand

Product segment revenue

$105.8m Liquid milk ↑27%

$659.2m Infant nutrition ↑33%

$41.7m Other nutrition ↑22%

Regional highlights[1]

Asia Pacific

↑100% Infant nutrition China label

↑58% Infant nutrition cross-border e-commerce

18,300 China store distribution

↑11.3% Australian milk sales

US

↑116% Milk sales growth

17,500 Store distribution

1 Refer to the operating and financial review (from page 2) for source of information.

Photography featured from our recent advertising campaign in Greater China

Contents

Operating and financial review

Financial results for the half year ended 31 December 2019 (NZ$)

Delivered strong financial results
Strategy execution gaining momentum

Summary of Group performance

The a2 Milk Company has made substantial gains in revenue and earnings, and with strong performances in key product segments of infant nutrition and liquid milk, and across core markets.

Our overall result reflects the continued growth in our **infant nutrition** segment with sales totalling $659.2 million for the period – an increase of 33.1% on the prior corresponding period. In-line with our strategy, our strong growth in China label infant nutrition products was particularly pleasing, with sales of $146.7 million, an increase of 100%. We achieved this while also continuing to achieve strong growth in our English label infant nutrition products. During December 2019, distributors requested additional product in advance of Chinese New Year which effectively brought forward approximately $8.0 million of sales from January 2020 to December 2019.

We again achieved strong growth in our **liquid milk** businesses in Australia and the USA, with sales across the Group[1] totalling $104.4 million up 28.7%. Liquid milk sales in Australia were up 11.3% to $74.7 million and sales in the USA more than doubled compared to 1H19, driven by improved sales velocity in established stores as well as an expanded store footprint.

Our **gross margin** percentage[1,2] increased to 57.2%, benefiting from a continued mix shift to infant formula, as well as improved price yield.

We delivered an **EBITDA margin** of 32.6% which was better than expected due to our stronger underlying gross margin.

Net **cash flow** from operating activities for the period was $160.6 million representing a strong cash conversion rate. Our closing **cash** position of $618.4 million reflects growth in revenue and earnings, partially offset by increased working capital.

Our **balance sheet** remains in a strong position with no debt and a significant cash balance. This will continue to be important to provide optionality in the execution of our growth strategy.

1 From continuing operations.
2 Gross margin percentage is calculated as revenue less cost of goods sold, divided by revenue.

Delivering on our strategic priorities and business objectives

We are pleased with the results of our strategy execution and continue to be energised about our key products, core markets and growth outlook.

We are committed to a focused approach to pursuing our strategic growth priorities:

1. Maximise growth from existing products in core markets;
2. Broaden our product portfolio in core markets; and
3. Expand in other targeted markets.

With the benefit of the comprehensive work undertaken during 2019 to enhance our understanding of the consumer and sales channels in our core markets, we have continued the increased levels of investment in marketing and capability to execute our growth plan.

In Australia, we have continued to build on our market leading positions in fresh milk and infant nutrition, whilst leveraging this to launch new products, such as *a2 Smart Nutrition™*, demonstrating our commitment to innovation.

In Greater China, we remain focused on strengthening our infant nutrition position in-market. It is pleasing to see our investments in brand, trade activities and people driving strong sales momentum.

In the USA, we continue to drive towards meaningful scale, with sales more than doubling compared to 1H19. We improved our in-store productivity and further expanded our distribution footprint.

Our targeted exploration of new markets continues – in October we launched infant formula in the city of Hong Kong and in December we launched infant formula in Korea with our partner, YuhanCARE (Yuhan).

Importantly, our strategic priorities translate into four business objectives:

1. Deliver Asia Pacific sales strategy outcomes;
2. Reach meaningful scale in the USA;
3. Build towards sustainable brand leadership; and
4. Deliver the organisation of the future.

We are pleased with the progress we have made against each of these business objectives in the first half and are confident that orienting our organisation around these objectives will allow us to capture near-term and longer-term growth opportunities.

1. Deliver Asia Pacific sales strategy outcomes

Our Asia Pacific business revenue was $777.4 million, up 30.0%, with EBITDA of $345.4 million, up 30.2%. This included:

- ANZ segment revenue of $460.2 million, up 10.0%, with EBITDA of $227.9 million, up 18.7%
- China & other Asia segment revenue of $317.2 million, up 76.7%, with EBITDA of $117.5 million, up 60.3%
- Revenue growth benefited from favourable pricing and product mix

Infant nutrition

Our Asia Pacific infant nutrition portfolio encompasses predominantly China and English label products. China label infant nutrition products can be sold in-market in China, via mother and baby stores (MBS), modern supermarkets and China label e-commerce retail channels. English label products can be sold through Australian retailers, Australian-sourced resellers and cross border e-commerce (CBEC) channels. In addition, we supply infant nutrition products into Hong Kong and Korea. Our multichannel approach for our infant formula business gives us the flexibility to meet consumer demands across regions and through multiple distribution pathways.

Infant nutrition – China offline channels

Following a detailed strategic review in 2019, we stepped up investment in our China label infant nutrition business considerably in 2H19 and continued broadly at this level in 1H20. We have also expanded our team in China, reviewed and optimised relationships with distributors and are focusing on the biggest opportunities for growth.

We are pleased our investments to deepen our understanding of consumer and channel trends and the increased levels of investment in marketing and capability development are translating into accelerated growth in our China label business.

For the period, we achieved sales in *a2 Platinum®* China label infant nutrition of $146.7 million, double the sales we achieved in the prior corresponding period. In addition to driving in-store productivity, we also expanded our footprint to 18,300 stores, up from 16,400 stores at the end of 2H19. Furthermore, we achieved our highest market value share in the MBS channel during the period. These indicators give us confidence that our strategy is on track.

We are committed to maximising our growth opportunities, including through product innovation. We launched a China label version of our Stage 4 product in December and recently re-launched our Stages 1, 2 and 3 China label products with a tamper-evident lid for additional product security. Our infant nutrition portfolio is complemented by our other nutritional products as we broaden our appeal to existing consumers and seek to connect with new consumers.

Infant nutrition – Cross-border e-commerce

We delivered *a2 Platinum®* English label infant nutrition sales of $158.7 million, up 57.8%. The results of the 11/11 China e-commerce sales event were very positive. In JD.com, our *a2 Platinum®* Stage 3 was the top selling infant nutrition product, and we were the second best-selling brand overall. In Tmall, we were the number three infant nutrition brand overall (English and China label combined) and we were the number one CBEC flagship store.

Infant nutrition – Australia retailers and resellers

Our infant nutrition sales in Australia grew 9.5% delivering $352.0 million in revenue for the half. We remain the market brand leader in Australian grocery and pharmacy channels and continue to invest strongly behind our brand, with our level of advertising being the highest in the category.

The rate of growth in our English label channels in Australia and China reflects an evolution across channels and in consumer behaviour. In this dynamic environment, it is pleasing to continue to deliver impressive sales growth in CBEC as well as from Australian-sourced resellers.

Infant nutrition – China consumption share

In the latest 12-month data for Key & A, and B, C, D cities in China, our Kantar infant formula consumption value share increased to 6.6%[3] from 5.4%[4] in the prior corresponding period. As previously advised, while Kantar remains the best single metric for consumption, it does not fully capture all consumption. This is due to the structure and definition of the panel, and the fact that it does not have full geographic coverage. Accordingly, our view is that not all of our consumption growth is captured, particularly in Stages 3 and 4.

3 Kantar Infant Formula market tracking of Key & A and BCD cities for 12 months ending 31 December 2019 by value.
4 Kantar Infant Formula market tracking of Key & A and BCD cities for 12 months ending 31 December 2018 by value.

Liquid milk

Our Australian fresh milk business continues to grow. In our most mature category, we achieved double-digit revenue growth of 11.3% totalling $74.7 million. As a consequence, we achieved a record market share of 11.3%. The ***a2 Milk™*** brand continues to be the only fresh milk brand ranged in all major supermarket chains and we are the highest brand advertiser in the fresh milk category, maintaining very high brand awareness and loyalty figures which benefits the portfolio as a whole.

Our liquid milk sales in China and other Asia segment grew 62.0% to $1.8 million for the half year.

Other nutritional products

For other nutritional products, sales grew 21.7% to $41.7 million the majority of which is recorded in our ANZ segment.

a2 Smart Nutrition™ is showing positive signs of developing into a meaningful extension of our infant and children's nutritional portfolio, with early indications of consumer acceptance, and a China label version launched in January 2020.

The re-launch of our nutritional product targeting mothers under the new branding of ***a2 Nutrition for Mothers™*** was successfully completed.

We have continued to experience delays in producing our ***a2 Milk™*** powder blended with Mānuka honey, with this scheduled to be available by 4Q20.

We continue to target growth opportunities for other nutritional products in China.

2. Reach meaningful scale in the USA

USA revenue more than doubled compared to the prior corresponding period, up to $28.0 million and representing growth of 116%. We continue to gain momentum as we execute on our strategy in the USA, building towards an initial milestone of US$100 million of annualised sales.

Given our increased investment in building brand awareness and distribution growth, we recorded an EBITDA loss of $30.0 million.

Our sales performance was driven by improved in-store productivity as well as through expanding our distribution footprint. Distribution grew to 17,500 stores, from 13,100 stores at the end of June 2019.

Increasing sales velocities with our most established retail customers accounted for over a quarter of our sales growth[5] and velocities in key customers were approximately 27% higher than the prior corresponding period.

5 Most established customers defined as customers for >2 years. Based on 52-week period ended December 2019.

Operational highlights in the half included strong performance in Costco, increasing same store velocities in Walmart, increased penetration within Kroger through achieving national coverage; bringing the brand to shelf in Safeway in the Pacific Northwest; and new distribution points in Target, Giant Eagle and Fresh Thymes.

Leveraging the consumer and channel insights obtained through a strategic review completed in 2019, we introduced new packaging and launched a new TV advertising campaign, both of which received positive feedback from the retail trade and is assisting in building brand awareness. We have also improved our in-store presence to convert awareness to trial. All these changes have contributed to increasing consumer offtake.

In July, we launched ***a2 Milk®*** Coffee Creamers which have been received positively and are performing to plan. As consumer demand for our products build, and our distribution footprint strengthens, we expect opportunities to launch additional new products will emerge.

3. Build towards sustainable brand leadership

Building brand value and increasing brand awareness through marketing investment remains an important focus. Our investment in the period was consistent with 2H19 at $84.1 million. The increase from the prior corresponding period was primarily a result of higher advertising spend in China and the USA.

We have leveraged our deepened understanding of consumers and purchasing behaviour in China to continuously improve our marketing mix which includes consumer advertising, in-store activations and the development of a new brand creative platform, which was launched in December 2019.

Similarly, in the USA we have leveraged our consumer insights to launch a new advertising campaign and consumer website and invested in increased in-store activation.

In addition to consumer marketing, our brand value is supported by investment in research and development programmes, an increased focus on sustainability, as well as initiatives to support the communities in which we operate.

Supporting relevant independently managed scientific studies remains important as we build our long-term brand proposition. In September 2019, the results of a clinical trial from 75 Chinese children aged between five and six with mild to moderate milk discomfort or lactose intolerance (confirmed via a urinary galactose test) were published. The study reported that replacing conventional milk with ***a2 Milk™*** "reduced gastrointestinal symptoms associated with milk intolerance" in many subjects and led to "a corresponding improvement in an aspect of cognitive performance" as measured using the Subtle Cognitive Impairment Test (SCIT)[6]. The study was independently peer reviewed and published in the USA based Journal of Pediatric Gastroenterology and Nutrition.

4. Deliver the organisation of the future

To support the execution of our overall Group strategy, we have continued to build capability within the organisation. In 1H20 we introduced a number of new roles to complement existing capabilities, particularly in-market in China, the USA, and within certain Group functions. We also established several initiatives designed to enhance engagement and launched a revised remuneration framework to align with our strategic direction.

Over the next two years we will be implementing new information technology systems to support the existing organisation and provide for future growth.

We also utilised external resources to accelerate the delivery of certain outcomes and to complement existing internal capabilities. As we improve internal capability, the composition and level of external resourcing should moderate over time.

Group strategic updates

Capital allocation

As part of the Board's ongoing review of the most appropriate use of capital for the business, our intention has been to prioritise investment in growth initiatives ahead of returning capital to shareholders.

Due to the increasing scale of our infant nutrition business, the Board considers it is now appropriate to assess participation in manufacturing capacity and capability to complement our existing supply chain relationships. Accordingly, we are presently evaluating opportunities to address this issue.

Leveraging our strategic partnerships

Key strategic partnerships remain a core element of our business model.

- **China State Farm:** As we continue implementing our infant nutrition strategy, China State Farm Holding Shanghai Co., Ltd's (China State Farm's) strong capabilities in importation services and product traceability as well as local market regulatory insights, will become even more important to our shared success.

6 Xiaoyang S, Zailing L. Effects of Conventional Milk Versus Milk Containing Only A2 ß-Casein on Digestion in Chinese Children. J Pediatr Gastroenterol Nutr. 2019 Jul 9.

"The a2 Milk Company has made substantial gains in revenue and earnings, and with strong performances in key product segments of infant nutrition and liquid milk, and across core markets."

- **Synlait Milk:** We continue to be very well supported by Synlait in meeting increased demand and our teams continue to work closely together to grow our respective businesses. In November 2019, we extended our comprehensive manufacturing and supply arrangements to July 2025. Additionally, in December 2019 Synlait announced it had received the infant formula registration from the General Administration of Customs of the People's Republic of China (GACC) for its Auckland-based blending and canning facility. Synlait is now able to progress seeking infant formula brand registration for China for this site.
- **Fonterra:** We continue to work with Fonterra on the development of milk pools in Australia and New Zealand to build capacity to support future growth. Fonterra is already supplying us with ingredients and our joint teams are working together to commercialise new opportunities. We continue to be encouraged by the potential of this relationship.

Sustainability

In August 2019 we announced our goals as well as our formal commitments to:

- Support the global ambition of the Paris Agreement and a 2050 net zero emissions target;
- Work with our farmers to meet the standards set by the World Organisation for Animal Health and avoid practices that contravene the Five Freedoms[7];
- Continue to improve the very high standards of our animal welfare program;
- Execute on our smarter packaging goals for higher quality and lower environmental impact; and
- Innovate to become even more efficient in product processing.

In addition, we are undertaking a sustainability assessment of our total supply chain. This includes ensuring we are compliant with modern slavery legislation.

7 The Five Freedoms outline five aspects of animal welfare: freedom from hunger or thirst; discomfort; pain, injury or disease; fear and distress; and freedom to express (most) normal behaviour.

We are also working towards implementing the Task Force on Climate-related Finance Disclosures (TCFD) Recommendations within three years, including climate risk scenario planning and embedding climate risk in our governance framework.

We are committed to supporting the communities in which we operate. As such, we recently announced initiatives to support communities in Australia affected by the bushfires. Our donation in Australia was aimed at providing funds to organisations providing front line emergency services. We were moved by the impact of these events on communities, livelihoods and the environment across much of Australia and inspired by those who supported, and continue to support, the recovery effort.

We have developed an assistance and support package valued at NZ$3.0 million in response to the recent coronavirus disease (COVID-19). This includes equal contributions for a product donation being dispatched to frontline medical teams and families, a cash donation to the Shanghai Red Cross to support the areas and people seriously affected, and funding to assist independent research to support the international effort to develop a vaccine for the virus. Research funding has been provided to the University of Queensland's School of Chemistry and Molecular Biosciences and the Peter Doherty Institute for Infection and Immunity (Doherty Institute).

Withdrawal from fresh milk operations in the UK

Further to our announcement in August 2019, we progressed with our withdrawal from fresh milk operations in the UK to focus on the Group's position in core regions. There have been no material financial impacts.

From 1 July 2019, UK infant nutrition customers were transferred to our China and other Asia segment.

Board and management

Pip Greenwood was appointed as an independent non-executive director of the Company with effect from 1 July 2019 and elected by shareholders at the Annual Meeting in November 2019. Pip succeeded Peter Hinton who retired on 30 June 2019.

In December 2019, former Managing Director and CEO, Geoffrey Babidge returned to the role of CEO on an interim basis following the departure of Jayne Hrdlicka. A global search for a new CEO is underway and an update will be provided at the appropriate time.

Race Strauss recently joined the business as our Chief Financial Officer.

Susan Massasso has elected to continue employment with the Company in the recently expanded role of Chief Growth and Brand Officer.

Outlook

FY20

Overall for FY20, we anticipate continued strong revenue growth across our key regions supported by increased marketing investment in China and the USA as well as the ongoing development of organisational capability to support the execution of our strategy.

Globally, there is uncertainty around the potential impact to supply chains and consumer demand in China resulting from COVID-19 and we continue to monitor the situation closely.

The health and wellbeing of our people is our primary focus and we have taken all measures to ensure our staff in China are as safe as possible. We remain vigilant to the advice of relevant authorities.

Given the essential nature of our products for many Chinese families, demand is strong, particularly through online and reseller channels, with revenue for the first two months of 2H20 above expectations. However, this is a dynamic situation and at this stage we are unable to quantify the impact, either positively or negatively, for the full year.

Notwithstanding this uncertainty, full year EBITDA margin is still anticipated to be in the range of 29-30%. 2H20 EBITDA margin is therefore expected to be lower than 1H20. The improved price yield in 1H20 is expected to be offset by:

- Increased COGS (including lactoferrin, milk price, and tamper-evident infant nutrition packaging)
- Planned increased levels of strategically important trade marketing activation in China
- Potential for increased supply chain costs resulting from COVID-19
- Phasing of marketing and capability investment weighted to 2H20; full year marketing investment expected to be approximately $200 million, as previously communicated
- Potential impact from unfavourable foreign exchange movements (weaker AUD:NZD)

Given the COVID-19 situation, we are assessing the level of discretionary marketing investment and trade marketing activation that can be effectively deployed in China for the remainder of the fiscal year.

Medium-term target

The Board considers it appropriate that the Company target an EBITDA margin in the order of 30% in the medium-term. This assumes the market performance and mix of our products remains broadly consistent and the competitive environment evolves as anticipated. We will keep the balance between growth and investment under constant review.

Reconciliation of EBITDA to net profit after tax

Earnings before interest, tax, depreciation and amortisation (EBITDA) is a non-GAAP measure. The Company believes that it provides investors with a comprehensive understanding of the underlying performance of the business.

	Half year ended 31-Dec-19 $'000	**Half year ended 31-Dec-18 $'000**
Group EBITDA	263,229	218,407
Depreciation and amortisation	(1,769)	(965)
EBIT	261,460	217,442
Interest income	3,055	1,615
Interest expense	(174)	–
Income tax expense	(79,415)	(66,362)
Net profit after tax	**184,926**	**152,695**

Financial statements

Directors’ declaration for the six months ended 31 December 2019

The directors of The a2 Milk Company Limited are pleased to present the interim report for the six months ended 31 December 2019. The interim report is unaudited and was authorised for issue by the directors on 26 February 2020.

Signed on behalf of the Board by:

David Hearn
Chair

Julia Hoare
Deputy Chair and Chair of the Audit & Risk Management Committee

26 February 2020

Auditor’s review report for the six months ended 31 December 2019

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Review Report to the Shareholders of The a2 Milk Company Limited (“the company”) and its subsidiaries (together “the group”)

We have reviewed the interim financial statements on pages 10 to 23, which comprise the statement of financial position of the group as at 31 December 2019, and the statement of comprehensive income, statement of changes in equity and statement of cash flows of the group for the period ended on that date, and a summary of significant accounting policies and other explanatory information.

This report is made solely to the company's shareholders, as a body. Our review has been undertaken so that we might state to the company's shareholders those matters we are required to state to them in a review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's shareholders as a body, for our review work, for this report, or for our findings.

Directors’ Responsibilities

The directors are responsible for the preparation and fair presentation of interim financial statements which comply with New Zealand Equivalent to International Accounting Standard 34: *Interim Financial Reporting* and for such internal control as the directors determine is necessary to enable the preparation and fair presentation of the interim financial statements that are free from material misstatement, whether due to fraud or error.

Reviewer’s Responsibilities

Our responsibility is to express a conclusion on the interim financial statements based on our review. We conducted our review in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity*. NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects, in accordance with New Zealand Equivalent to International Accounting Standard 34: *Interim Financial Reporting*. As the auditor of the group, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements.

Basis of Statement

A review of interim financial statements in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand). Accordingly we do not express an audit opinion on those financial statements.

Other than in our capacity as auditor we have no relationship with, or interests in, the group.

Conclusion

Based on our review nothing has come to our attention that causes us to believe that the accompanying interim financial statements, set out on pages 10 to 23, do not present fairly, in all material respects, the financial position of the group as at 31 December 2019 and its financial performance and cash flows for the six month period ended on that date in accordance with New Zealand Equivalent to International Accounting Standard 34: *Interim Financial Reporting*.

Our review was completed on 26 February 2020 and our findings are expressed as at that date.

Ernst & Young
Sydney

Consolidated statement of comprehensive income (Unaudited) for the six months ended 31 December 2019

	Notes	31 Dec 19 $'000	31 Dec 18 $'000
Continuing operations			
Sales		804,946	610,629
Cost of sales		(344,282)	(270,634)
Gross margin		460,664	339,995
Other revenue		374	235
Distribution expenses		(19,811)	(14,548)
Administrative expenses	5	(44,189)	(35,120)
Marketing expenses		(83,861)	(44,721)
Other expenses	5	(48,421)	(26,186)
Operating profit		264,756	219,655
Finance income		3,048	1,592
Finance costs		(195)	(74)
Net finance income		2,853	1,518
Profit before tax		267,609	221,173
Income tax expense		(79,415)	(66,190)
Profit from continuing operations		**188,194**	**154,983**
Discontinued operation			
Loss from discontinued operation, net of tax	4	(3,268)	(2,288)
Profit for the period		**184,926**	**152,695**
Other comprehensive income			
Items that may be reclassified to profit or loss:			
Foreign currency translation loss		(973)	(3,491)
Items not to be reclassified to profit or loss:			
Listed investment fair value loss	8	(9,664)	(68,625)
Total comprehensive income		**174,289**	**80,579**
Earnings per share			
Basic (cents per share)		25.15	20.85
Diluted (cents per share)		24.90	20.52
Earnings per share – continuing operations			
Basic (cents per share)		25.59	21.16
Diluted (cents per share)		25.34	20.83

The accompanying notes form part of these financial statements.

Consolidated statement of changes in equity (Unaudited) for the six months ended 31 December 2019

Six months ended 31 December 2019	Foreign currency translation reserve $'000	Fair value revaluation reserve $'000	Employee equity settled payments reserve $'000	Total reserves $'000	Retained earnings $'000	Share capital $'000	Total equity $'000
Balance 1 July 2019	(15,341)	59,723	20,535	64,917	578,442	144,495	787,854
Profit after tax for the period	–	–	–	–	184,926	–	184,926
Foreign currency translation differences – foreign operations	(973)	–	–	(973)	–	–	(973)
Listed investment – fair value movement	–	(9,664)	–	(9,664)	–	–	(9,664)
Total comprehensive income for the period	(973)	(9,664)	–	(10,637)	184,926	–	174,289
Transactions with owners in their capacity as owners:							
Issue of ordinary shares	–	–	–	–	–	525	525
Share issue costs	–	–	–	–	–	(32)	(32)
Share-based payments	–	–	2,404	2,404	–	–	2,404
Income tax	–	–	9,546	9,546	–	–	9,546
Total transactions with owners	–	–	11,950	11,950	–	493	12,443
Balance 31 December 2019	(16,314)	50,059	32,485	66,230	763,368	144,988	974,586

Six months ended 31 December 2018	Foreign currency translation reserve $'000	Fair value revaluation reserve $'000	Employee equity settled payments reserve $'000	Total reserves $'000	Retained earnings $'000	Share capital $'000	Total equity $'000
Balance 1 July 2018	(11,022)	122,113	12,351	123,442	290,701	141,566	555,709
Profit after tax for the period	–	–	–	–	152,695	–	152,695
Foreign currency translation differences – foreign operations	(3,491)	–	–	(3,491)	–	–	(3,491)
Listed investment – fair value movement	–	(68,625)	–	(68,625)	–	–	(68,625)
Total comprehensive income for the period	(3,491)	(68,625)	–	(72,116)	152,695	–	80,579
Transactions with owners in their capacity as owners:							
Issue of ordinary shares	–	–	–	–	–	1,828	1,828
Share issue costs	–	–	–	–	–	(42)	(42)
Share-based payments	–	–	5,904	5,904	–	–	5,904
Total transactions with owners	–	–	5,904	5,904	–	1,786	7,690
Balance 31 December 2018	(14,513)	53,488	18,255	57,230	443,396	143,352	643,978

The accompanying notes form part of these financial statements.

Consolidated statement of financial position (Unaudited) as at 31 December 2019

	Notes	31 Dec 19 $'000	30 Jun 19 $'000
Assets			
Current assets			
Cash and short-term deposits		618,420	464,805
Trade and other receivables		71,794	66,248
Prepayments		55,883	49,693
Inventories	7	118,162	108,453
Total current assets		**864,259**	**689,199**
Non-current assets			
Property, plant and equipment		18,207	10,296
Intangible assets		12,986	12,985
Other financial assets	8	277,143	286,807
Deferred tax assets		16,910	7,683
Total non-current assets		**325,246**	**317,771**
Total assets		**1,189,505**	**1,006,970**
Liabilities			
Current liabilities			
Trade and other payables		189,120	173,748
Customer contract liabilities		5,864	1,431
Lease liabilities		1,374	–
Income tax payable		12,186	43,710
Total current liabilities		**208,544**	**218,889**
Non-current liabilities			
Trade and other payables		267	227
Lease liabilities		6,108	–
Total non-current liabilities		**6,375**	**227**
Total liabilities		**214,919**	**219,116**
Net assets		**974,586**	**787,854**
Equity attributable to owners of the Company			
Share capital	6	144,988	144,495
Retained earnings		763,368	578,442
Reserves		66,230	64,917
Total equity		**974,586**	**787,854**

The accompanying notes form part of these financial statements.

Consolidated statement of cash flows (Unaudited) for the six months ended 31 December 2019

	Notes	31 Dec 19 $'000	31 Dec 18 $'000
Cash flows from operating activities			
Receipts from customers		810,788	614,674
Payments to suppliers and employees		(543,169)	(424,049)
Interest received		3,055	1,615
Interest paid		(174)	–
Taxes paid		(109,945)	(79,943)
Net cash inflow from operating activities	9	**160,555**	**112,297**
Cash flows from investing activities			
Payments for property, plant and equipment		(1,655)	(1,755)
Payments for intangible assets		(216)	(640)
Payment for listed investment		–	(162,335)
Net cash outflow from investing activities		**(1,871)**	**(164,730)**
Cash flows from financing activities			
Payments of lease principal		(677)	–
Proceeds from issue of equity shares	6	493	1,786
Net cash (outflow)/ inflow from financing activities		**(184)**	**1,786**
Net increase/(decrease) in cash and short-term deposits		158,500	(50,647)
Cash and short-term deposits at the beginning of the period		464,805	340,455
Effect of exchange rate changes on cash		(4,885)	(1,876)
Cash and short-term deposits at the end of the period		**618,420**	**287,932**

The accompanying notes form part of these financial statements.

Notes to the interim financial statements for the six months ended 31 December 2019

1. Basis of preparation

The a2 Milk Company Limited (the Company) and its subsidiaries (together the Group) is a for-profit entity incorporated and domiciled in New Zealand.

The Company is registered in New Zealand under the Companies Act 1993, and is an FMC reporting entity under the Financial Markets Conduct Act 2013. The Company is also registered as a foreign company in Australia under the *Corporations Act 2001* (Cth, Australia). The shares of The a2 Milk Company Limited are publicly traded on the New Zealand Stock Exchange (NZX), the Australian Securities Exchange (ASX) and Chi-X Australia (Chi-X). The financial report is presented in New Zealand dollars, and all values are rounded to the nearest thousand ($'000), unless otherwise indicated.

The principal activity of the Company is the sale of branded products in targeted markets made with milk from cows that produce milk naturally containing only the A2 protein type.

These consolidated financial statements were authorised for issue by the directors on 26 February 2020.

Statement of compliance

These interim financial statements have not been audited. The interim financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand, comply with NZ IAS 34 *Interim Financial Reporting* and IAS 34 *Interim Financial Reporting*, and have been the subject of a review by the auditors.

This interim report should be read in conjunction with the Group's annual report for the year ended 30 June 2019, available at www.thea2milkcompany.com/investor-centre/results.

The same accounting policies and methods of computation are followed in this interim report as were applied in the preparation of the Group's financial statements for the year ended 30 June 2019, other than the changes arising from the adoption of NZ IFRS 16: *Leases*, noted below.

Certain comparative amounts have been restated to conform with the current period's presentation.

Changes in significant accounting policies

The Group has applied all of the new and revised Standards and Interpretations issued by the New Zealand External Reporting Board that are relevant to the Group's operations and effective for the current accounting period. Other than the adoption of NZ IFRS 16: *Leases*, their application has not had any material impact on the Group's assets, profits or earnings per share for the half-year ended 31 December 2019.

Adoption of NZ IFRS 16: *Leases*

The Group has adopted this standard from 1 July 2019, using the modified retrospective transition method, under which the cumulative effect of initial application, if any, is recognised in retained earnings at 1 July 2019, with no restatement of prior periods.

The standard introduces a single, on-balance sheet accounting model for lessees. Right-of-use assets are recognised representing the lessee's right to use the underlying leased assets, together with lease liabilities representing the obligation to make lease payments.

The Group previously recognised operating leases for office and industrial premises, motor vehicles and equipment. On transition to NZ IFRS 16 the Group recognises right-of-use assets and lease liabilities on balance sheet for most of these leases, but has elected not to recognise on balance sheet leases of low-value assets and those leases with a remaining life on transition of less than 12 months.

Carrying amounts of right-of-use assets in property, plant and equipment:

$'000	Leased property	Plant and equipment	Office and computer	Total
Recognised 1 July 2019	7,499	314	56	7,869
Balance 31 December 2019	6,849	313	46	7,208

1. Basis of preparation (cont.)

Adoption of NZ IFRS 16: *Leases* (cont.)

Accounting policy

A right-of-use asset and a lease liability are recognised at the lease commencement date.

The right-of-use asset is initially measured at cost, and subsequently at cost less accumulated depreciation as the asset is written off over the term of the lease, and impairment losses, and any adjustments for remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments payable from the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's incremental borrowing rate. Generally, the Group uses its incremental borrowing rate as the discount rate.

The lease liability is subsequently increased by the interest cost on the lease liability and decreased by lease payments made. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, a change in the estimate of the amount expected to be payable, or changes in the assessment of whether a purchase or extension option is reasonably certain to be exercised.

The Group has applied judgement to determine the lease term for some lease contracts that include renewal options. This assessment impacts the lease term, which may significantly affect the amount of lease liabilities and right-of-use assets recognised.

Transition

On transition lease liabilities were measured at the present value of the remaining lease payments, discounted at the Group's incremental borrowing rate as at 1 July 2019. Right-of-use assets were measured at an amount equal to the lease liability, less accrued lease payments as at 30 June 2019.

The Group used the following practical expedients when applying NZ IFRS 16:

- Applied the exemption not to recognise right-of-use assets and liabilities for leases with less than 12 months of lease term remaining.
- Used hindsight when determining the lease term if the contract contains options to extend or terminate the lease.

Impacts on transition

The impact of transition to NZ IFRS 16 is summarised below:

$'000	1 July 2019
Right-of-use assets presented in property, plant and equipment	7,869
Lease accruals as at 30 June 2019, set off against right-of-use assets recognised	236
Lease liabilities	(8,105)

When measuring lease liabilities, the Group discounted lease payments using its incremental borrowing rates at 1 July 2019. The weighted-average rate applied was 3.29%.

$'000	1 July 2019
Operating lease commitments at 30 June 2019 as disclosed in the Group's consolidated financial statements	10,145
Discounted using incremental borrowing rates as at 1 July 2019	(1,370)
Recognition exemption for leases with less than 12 months of lease term at transition	(670)
Lease liabilities recognised at 1 July 2019	8,105

Notes to the interim financial statements for the six months ended 31 December 2019 (continued)

1. Basis of preparation (cont.)

Adoption of NZ IFRS 16: *Leases* (cont.)

Impacts for the period

Under NZ IFRS 16 the Group has recognised depreciation and interest costs, instead of operating lease expense. During the six months ended 31 December 2019, the Group recognised $714,000 of depreciation charges and $162,000 of interest costs.

New standards and interpretations not yet adopted

There are no new standards and interpretations that are issued, but not yet effective as at 31 December 2019, that are expected to have a material impact on the Group in current or future reporting periods.

2. Operating segments

The Group's key performance measures are segment revenue and segment results before interest, tax, depreciation and amortisation (Segment EBITDA, a non-GAAP measure). Further information and analysis of performance can be found in the Operating and financial review, which forms part of this interim report.

For management purposes, the Group is organised into business units based on geographical location along with a corporate function, and has four reportable operating segments as follows:

- The *Australia and New Zealand segment* receives external revenue from infant formula, milk and other dairy products, along with royalty and licence fee income.
- The *China and other Asia segment* receives external revenue from infant formula, milk and other dairy products.
- The *USA segment* receives external revenue from milk sales.
- The *UK segment* (discontinued operation, refer Note 4).

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is assessed on segment EBITDA and is measured in conformity with the accounting policies adopted for preparing and presenting the financial statements of the Group.

From 1 July 2019, infant formula sales previously reported in the UK segment are allocated to the China and other Asia segment. Comparative information for the six months ended 31 December 2018 has been restated to reflect the change in allocation.

2. Operating segments (cont.)

Six months to 31 December 2019	Continuing operations					
	Australia and New Zealand	China and other Asia	USA	Total	Discontinued operation UK	Total
	$'000	$'000	$'000	$'000	$'000	$'000
Consolidated sales	459,851	317,140	27,955	804,946	1,397	806,343
Other revenue	354	20	–	374	–	374
Reportable segment revenue	**460,205**	**317,160**	**27,955**	**805,320**	**1,397**	**806,717**
Reportable segment results (Segment EBITDA)	**227,943**	**117,470**	**(30,006)**	**315,407**	**(3,239)**	**312,168**
Corporate EBITDA				(48,939)	–	(48,939)
Group EBITDA				266,468	(3,239)	263,229
Reconciliation to consolidated statement of comprehensive income						
Interest income						3,055
Interest expense						(174)
Depreciation and amortisation						(1,769)
Income tax expense						(79,415)
Consolidated profit after tax						184,926

Six months to 31 December 2018	Continuing operations					
	Australia and New Zealand	China and other Asia	USA	Total	Discontinued operation UK	Total
	$'000	$'000	$'000	$'000	$'000	$'000
Consolidated sales	418,211	179,459	12,959	610,629	2,246	612,875
Other revenue	235	–	–	235	–	235
Reportable segment revenue	**418,446**	**179,459**	**12,959**	**610,864**	**2,246**	**613,110**
Reportable segment results (Segment EBITDA)	**191,953**	**73,278**	**(17,277)**	**247,954**	**(2,126)**	**245,828**
Corporate EBITDA				(27,421)	–	(27,421)
Group EBITDA				220,533	(2,126)	218,407
Reconciliation to consolidated statement of comprehensive income						
Interest income						1,615
Depreciation and amortisation						(965)
Income tax expense						(66,362)
Consolidated profit after tax						152,695

Notes to the interim financial statements for the six months ended 31 December 2019 (continued)

3. Revenue

Disaggregation of revenue

In the following table, revenue is disaggregated by geographical location (reportable segments) and major product types.

Six months to 31 December 2019	Continuing operations					
	Australia and New Zealand	China and other Asia	USA	Total	Discontinued operation UK	Total
	$'000	$'000	$'000	$'000	$'000	$'000
Infant formula	352,036	307,202	–	659,238	–	659,238
Liquid milk	74,682	1,778	27,955	104,415	1,397	105,812
Other	33,487	8,180	–	41,667	–	41,667
	460,205	317,160	27,955	805,320	1,397	806,717

Six months to 31 December 2018	Continuing operations					
	Australia and New Zealand	China and other Asia	USA	Total	Discontinued operation UK	Total
	$'000	$'000	$'000	$'000	$'000	$'000
Infant formula	321,557	173,924	–	495,481	–	495,481
Liquid milk	67,077	1,097	12,959	81,133	2,246	83,379
Other	29,812	4,438	–	34,250	–	34,250
	418,446	179,459	12,959	610,864	2,246	613,110

4. Results of discontinued operation

On 20 August 2019, the Board announced its decision to withdraw from fresh milk operations in the UK (reported in the UK segment) to focus instead on strengthening the Group's position in core regions.

All the UK fresh milk trading operations ceased in the period.

	31 Dec 19 $'000	31 Dec 18 $'000
Results		
Revenue	1,397	2,246
Expenses	(4,670)	(4,383)
Results from operating activities	(3,273)	(2,137)
Net finance income	5	21
Income tax	–	(172)
Results from operating activities, net of tax	(3,268)	(2,288)
Earnings per share		
Basic and diluted (cents per share)	(0.44)	(0.31)
Cash flow		
Operating	(2,824)	(4,099)
Investing	–	(35)
Net cash outflow for the period	(2,824)	(4,134)

5. Administrative and other expenses

	31 Dec 19 $'000	31 Dec 18 $'000
The following items of expenditure are included in administrative expenses:		
Salary and wage costs	29,921	20,737
Equity settled share-based payments	2,404	5,904
Salary and wage costs include amounts provided related to the previous CEO		
The following items of expenditure are included in other expenses:		
Professional service fees	19,140	9,981
Depreciation and amortisation	1,733	952
Patents, trademarks and research and development	3,500	2,853
Carbon credits	4,576	–
The value of offsets incurred in the period includes credits purchased to offset emissions for the year ended 30 June 2019, and amounts accrued for the six months to 31 December 2019.		

Notes to the interim financial statements for the six months ended 31 December 2019 (continued)

6. Share capital

Movements in contributed equity:	Number of shares	Share Capital $'000
Fully paid ordinary shares:		
Balance 30 June 2019	735,048,405	144,495
Movements in the period:		
Exercise of options	700,000	441
Gift offer	3,693	–
Share match program	6,316	84
Vesting of time-based rights	122,184	–
Share issue costs	–	(32)
	832,193	493
Balance 31 December 2019	735,880,598	144,988

7. Inventories

	31 Dec 19 $'000	30 Jun 19 $,000
Raw materials	12,018	9,933
Finished goods	71,814	59,556
Goods in transit	34,330	38,964
Total inventories at the lower of cost and net realisable value	118,162	108,453

Movements in goods in transit balances result from the timing of shipments of infant formula and milk powder products from New Zealand to Australia and China.

8. Financial assets and liabilities

Other financial assets of $277,143,000 (30 June 2019: $286,807,000) consist of shares in Synlait Milk Limited (Synlait), a dairy processing company listed on the New Zealand Stock Exchange and the Australian Securities Exchange.

This listed investment is the only financial instrument carried by the Group at fair value and is classified at fair value through other comprehensive income; valued using Level 1 valuation inputs: quoted prices (unadjusted) in active markets for identical assets or liabilities.

A fair value (loss) of $9,664,000 was recognised for the period.

The carrying amounts of cash and short-term deposits, and trade and other receivables and payables are a reasonable approximation of their fair values.

9. Reconciliation of after tax profit with net cash flows from operating activities

	31 Dec 19 $'000	31 Dec 18 $'000
Net profit for the period	**184,926**	**152,695**
Adjustments for non-cash items:		
Depreciation and amortisation	1,769	965
Share-based payments	2,404	5,904
Net foreign exchange loss/(gain)	4,025	(929)
Deferred tax	319	948
Changes in working capital:		
Trade and other receivables	(5,546)	(17,272)
Prepayments	(6,190)	(12,092)
Inventories	(9,709)	(8,648)
Trade and other payables	15,648	(615)
Customer contract liabilities	4,433	10,979
Income tax payable	(31,524)	(19,638)
Net cash inflow from operating activities	**160,555**	**112,297**

Notes to the interim financial statements for the six months ended 31 December 2019 (continued)

10. Share-based payments

Long-term incentives (LTI)

The LTI plan is designed to retain and motivate senior executives and management to achieve the Group's long term strategic goals by providing rewards that align the interests of the executives and management with shareholders. Performance rights and time-based rights are currently issued under the LTI plan.

During FY19 a revised remuneration policy for the Group was finalised. This review resulted in the temporary deferral of the LTI plan for participating Group employees in the 2019 financial year.

During the period the Board authorised the issue of 959,941 performance rights, and 198,306 time-based rights to senior employees under the LTI plan.

Performance rights

To offset the deferral of the LTI programme in FY19, the performance rights issued in the period are in two tranches, with differing performance periods and performance hurdles as set out below.

The performance rights vest subject to:

- Continuing employment.
- Minimum performance hurdles of both:
  - A minimum diluted earnings per share (EPS) compound annual growth rate (CAGR) increase of 15% over the performance period (E-CAGR); and
  - A minimum normalised sales CAGR increase of 15% over the performance period (S-CAGR).
- No awards will vest if E-CAGR or S-CAGR is less than 15% over the respective performance periods.
- 50% of the awards will vest if E-CAGR and S-CAGR of 15% is achieved, up to a maximum of 100% of the award vesting if S-CAGR of either 22% or more, or 25% or more is achieved, as follows:

Performance rights grants:	Performance period	EPS hurdle	Normalised sales hurdles		
			50%	85%	100%
Tranche 1					
384,783 rights	2 years to 30 June 2021	15%	15%	20%	25%
Tranche 2					
575,158 rights	3 years to 30 June 2022	15%	15%	18.5%	22%

Diluted earnings per share are as reported in the Company's Annual Report in respect of that financial year.

Normalised sales in respect of a financial year, means sales plus such additional revenue or income items less such unusual and one-off items (in each case, as may be determined by the Board in its absolute discretion) based on relevant financial information reported in the Company's Annual Report in respect of that financial year.

10. Share-based payments (cont.)

Time-based rights

Vesting of the time-based rights issued in the period is subject to continuing employment, with no other performance conditions, vesting as follows:

Number of time-based rights granted:	Grant dates	Vesting dates
9,868	19 Nov 2019	21 Aug 2020
94,219	19 Nov 2019	24 Aug 2020
94,219	19 Nov 2019	23 Aug 2021
198,306		

No amount is payable upon vesting of the performance and time-based rights and conversion to shares. Each exercised right is an entitlement to one fully paid ordinary share in the Company.

Fair value of performance and time-based rights

The fair value of services received in return for performance and share-based rights granted to employees is measured by reference to the fair value of the rights granted. The estimate of the fair value of the services received is measured by reference to the vesting conditions specific to the grant based on a simplified Black-Scholes option pricing model.

Fair value of performance and time-based rights granted during the period and assumptions	Performance rights		Time-based
	Tranche 1	Tranche 2	
Grant date	19 Nov 19	19 Nov 19	19 Nov 19
Fair value at measurement date	$14.03	$13.86	$14.08
Share price at grant date	$14.12	$14.12	$14.12
Performance rights life	1.75yrs	2.76yrs	–

Other employee equity schemes

In the period, employees not participating in the LTI plan were invited to participate in the following new schemes:

- Gift offer: employees received Company shares to the value of approximately A$500 each.
- Share Match Program: employees undertaking to purchase Company shares for a minimum value of A$200 to a maximum value of A$2,000 up to 30 September 2020 from their after-tax pay will receive matching shares from the Company equal to the number of shares acquired and retained under the scheme, subject to continuing employment up to September 2021.

Amounts recognised in the consolidated statement of comprehensive income

During the period a $2,404,000 expense was recognised in the consolidated statement of comprehensive income for equity settled share-based payment awards (2018: $5,904,000).

11. Subsequent events

As at 31 December 2019 the market value of the Company's investment in Synlait Limited was $277,143,000 ($8.89 per share). As at 25 February 2020 the market value has decreased to $197,336,000 ($6.33 per share). The investment is measured at fair value through other comprehensive income so that any changes in market value are recognised through the fair value revaluation reserve, with no effect on profit or loss.

No other matters or circumstances have arisen since the end of the period which have significantly affected or may significantly affect the operations, the result of these operations or state of affairs of the Group in subsequent periods.

Corporate directory

Company	The a2 Milk Company Limited Level 10 51 Shortland Street Auckland 1010 New Zealand
New Zealand share registry	Link Market Services Limited PO Box 91976 Victoria Street West Auckland 1142 New Zealand Telephone: +64 9 375 5998
Australian share registry	Link Market Services Limited Locked Bag A14 Sydney South NSW 1235 Australia Telephone: +61 1300 554 474
Auditor	Ernst & Young 200 George Street Sydney NSW 2000 Australia
Registered offices	Level 10 51 Shortland Street Auckland 1010 New Zealand Level 4 182 Blues Point Road McMahons Point NSW 2060 Australia Telephone: +61 2 9697 7000
Corporate website	www.thea2milkcompany.com
Company directors	David Hearn (Chair and Non-Executive Director) Julia Hoare (Deputy Chair and Independent, Non-Executive Director) Pip Greenwood (Independent, Non-Executive Director) Warwick Every-Burns (Independent, Non-Executive Director) Jesse Wu (Independent, Non-Executive Director)

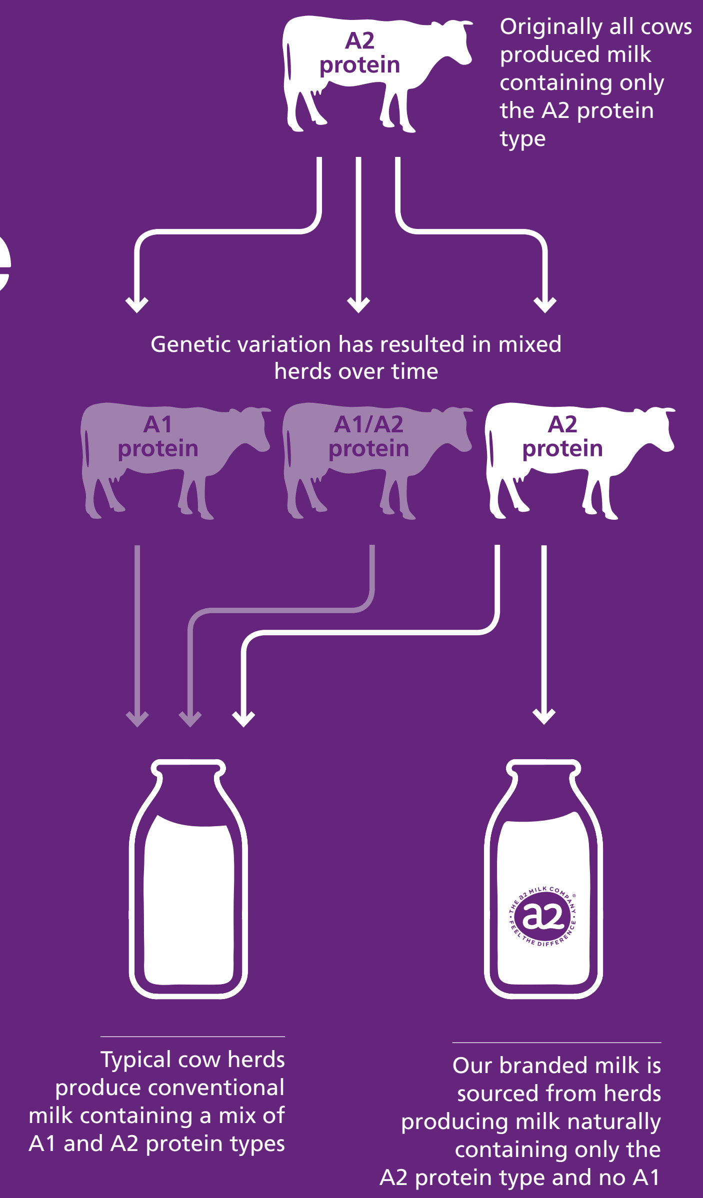
The A2 protein difference

Conventional cows' milk contains two main types of beta casein protein, A2 protein and A1 protein – our branded milk is different from conventional cows' milk because it comes from cows selected to naturally produce only the A2 protein type and no A1.

Our milk is comparable to conventional cows' milk in other respects.

Our branded milk is naturally occurring and not a product of genetic engineering or technological processes.

Many consumers and healthcare professionals report that certain people who experience challenges drinking conventional cows' milk may experience benefits when they switch to a2 Milk™.



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