# OUR ANNUAL REPORT

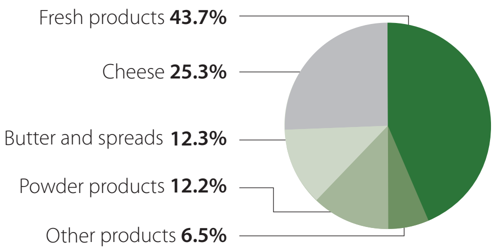
2006

# Financial highlights[1)]

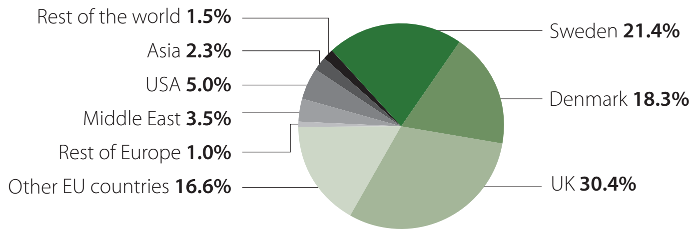
| Group<br>DKK million | 01.01.2006<br>31.12.2006 | 01.10.2005<br>31.12.2005 | 01.10.2004<br>30.09.2005 | 01.10.2003<br>30.09.2004 | 30.09.2002<br>30.09.2003 |
|---|---|---|---|---|---|
| **Profit** | | | | | |
| Revenue | 45,491 | 11,487 | 46,351 | 47,263 | 40,647 |
| Outside DK/SE | 27,393 | 6,955 | 27,784 | 28,137 | 20,781 |
| % outside DK/SE | 60% | 61% | 60% | 60% | 51% |
| Operating profit | 1,161 | 113 | 1,459 | 1,193 | 1,242 |
| Net financial items | −409 | −124 | −573 | −423 | −245 |
| Profit for the year | 933 | 30 | 755 | 1,019 | 1,094 |
| Supplementary payments | 336 | 75 | 369 | 586 | 546 |
| Consolidation | | | | | |
| Reconsolidation acc. to the articles of association | 122 | 0 | 247 | 123 | 123 |
| Change in policy | 91 | −45 | −46 | – | – |
| Delivery-based owner certificates | 184 | 0 | 185 | – | – |
| Strategy fund | 200 | – | – | – | – |
| Other consolidation | 0 | 0 | 0 | 310 | 425 |
| **Financing** | | | | | |
| Total assets | 26,611 | 27,057 | 26,336 | 26,043 | 26,845 |
| Fixed assets | 15,762 | 15,682 | 15,593 | 15,441 | 14,759 |
| Investments in property, plant and equipment | 1,792 | 599 | 2,499 | 2,981 | 2,062 |
| Equity | 7,971 | 7,411 | 7,435 | 7,361 | 7,155 |
| **Equity ratios (%)** | | | | | |
| Equity | 30% | 27% | 28% | 28% | 27% |
| Equity + subordinate bond loan | 34% | 31% | 32% | 32% | – |
| **Inflow of raw milk** | | | | | |
| Total million kg. weighed in in the group | 8,592 | 2,063 | 8,415 | 8,512 | 7,241 |
| Members in DK | 4,047 | 970 | 4,058 | 4,053 | 4,137 |
| Members in SE | 2,067 | 499 | 2,114 | 2,141 | 2,114 |
| Others | 2,478 | 594 | 2,243 | 2,318 | 990 |
| **Number of members** | | | | | |
| In DK | 4,591 | 4,987 | 5,197 | 5,877 | 6,625 |
| In SE | 4,817 | 5,288 | 5,360 | 5,728 | 6,133 |
| Total | 9,408 | 10,275 | 10,557 | 11,605 | 12,758 |
| **Employees** | | | | | |
| Average number of full-time employees | 17,933 | 19,356 | 20,076 | 20,855 | 17,791 |

*1) As from 2006, the financial year was changed to follow the calendar year, the period 1 October – 31 December 2005 being the transitional period. The financial highlights for this financial year therefore only comprise three months.*

## Revenue
In per cent by product category



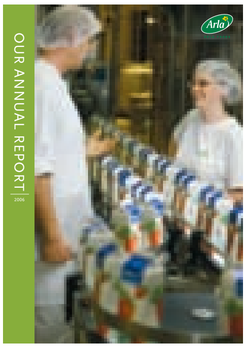

## Revenue
In per cent by market

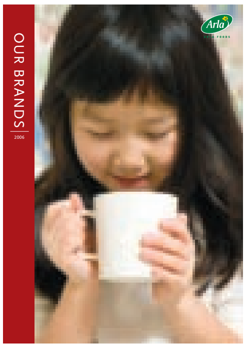


# Contents



**FRONT COVER:**
Søren Kristensen and Christina Josephsen, Brabrand Mejeri.




**»OUR ANNUAL REPORT«** is Arla Foods' formal annual report for the 2006 financial year. Readers wishing to know more about some of our selected brands and markets should refer to the supplement **»OUR BRANDS 2006«**. This can be ordered from Arla Foods or downloaded at www.arlafoods.com.

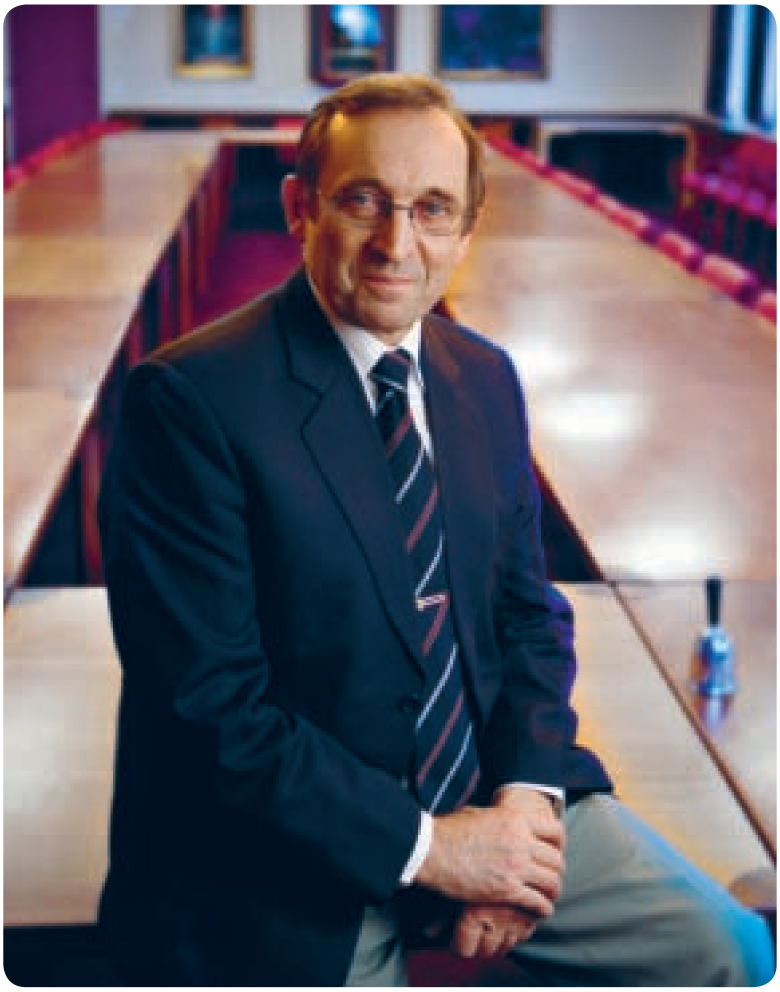
# The Chairman's Report

**THE YEAR STARTED** with a great deal of optimism and hope that we would be able to keep the milk price unchanged from 2005. Sadly, as early as February 2006, we were hit by the widespread and entirely unforeseen consumer boycott in the Middle East which incurred substantial losses. As these losses, of course, could not have been envisaged, they were unaccounted for in the budget for the year.

*» The Supervisory Board is confident that the milk price will improve when we invest in new markets.«*

Consequently, we failed to achieve the budgeted result, but we are satisfied that, by the end of the year, we had recovered more than 50 per cent of the Middle Eastern market. It is also encouraging that we are in line to reach pre-boycott levels by the end of 2007. Throughout all this, Arla Foods displayed great strength and our Middle Eastern staff have worked hard to re-establish the business.

The crisis in the Middle East has illustrated the importance of Arla Foods' offensive strategy which focuses on diversifying sales across a range of important markets. In keeping with this, we decided to strengthen our Nordic business in 2006 by purchasing 30 per cent of the Finnish dairy company, Ingman Foods Oy. Moreover, in September 2006, we acquired Tholstrup Cheese in a move that strengthens our position within speciality cheese. These long-term investments are important in a highly competitive dairy market. The Board is confident that the investments in new markets will also improve the milk price.



Finally, we examined the potential for acquiring the remaining 49 per cent of the shares in Arla Foods' UK subsidiary, Arla Foods UK plc. The offer has been sent to the other shareholders and a decision is expected in April 2007.

## Lower export subsidies

The direct impact of political decisions in the EU and WTO with regard to trade agreements and agricultural reform impacted significantly on milk producers during the year. As export subsidies declined substantially, this has had a direct effect on the milk price. The reallocation of subsidies from export subsidies to direct subsidies has, to some extent, compensated for the fall in the milk price paid to milk producers in Denmark and Sweden.

Internally, we have started to discuss our response to the cessation of the EU milk quotas expected to disappear in 2015 and the consequences for milk production in Sweden and Denmark.

In Denmark, we are witnessing increased capitalisation – not only of agricultural land but also of the quotas. The considerable interest in buying I see as an expression of optimism in Denmark although we have not yet reached the same stage in Sweden. The industry organisation, Svensk Mjölk, has set a series of initiatives in motion to stimulate investments and encourage milk producers to see the opportunities within Swedish milk production in the future.

**Ready for new challenges**
During the year, we also took a closer look at corporate governance. We have discussed our democratic organisation, the size of the Supervisory Board and the allocation of responsibilities. This has been an inspiring process which has indicated that the co-operative ownership system is ready to face the challenges ahead.

*»It is a great pleasure for me to look back on an exciting period, the challenging work and my rewarding relations with so many interesting people.«*

**New strategy fund approved**
We also decided to set up a so-called strategy fund at a meeting of the Board of Representatives in December 2006. The purpose of the fund is to assist Arla Foods' strategic development and alleviate the negative effects on the accounts caused by potential new acquisitions.

**Retiring as Chairman**
After many years in the dairy industry, I have decided that the time has come for me to retire from the Supervisory Board. It is a great pleasure for me to look back on an exciting period, the challenging work and my rewarding relations with so many interesting people.

With Arla Foods facing major challenges, we must now strive even more to maintain a strong dialogue with our co-operative members and the consumers.

Knud Erik Jensen
*Chairman*

# The Executive Directors' Report

**THE BUDGET FOR 2006** was ambitious. With expected earnings per kg weighed-in co-operative member milk of DKK 2.28/SEK 2.81 the budget was somewhat above expectations compared to international economic trends and especially in relation to the impact of the CAP reforms.

Operating profit, however, differs substantially from the budget and the result for 2006 is, therefore, unsatisfactory. The key reason is the unforeseen boycott of Danish products in the Middle East. The boycott's negative impact, however, is to a large extent offset by a high level of one-off income such as profits from the disposal of companies and properties. Overall, therefore, the net result is satisfactory.

»After a huge effort, not least by staff in the Middle East, some of the distribution was re-established in late spring.«

## Consumer boycott blocked growth

The widespread Middle Eastern consumer boycott, a reaction to the satirical cartoons of the Prophet Mohammed carried in a Danish newspaper in 2005, dominated everything else in 2006. Within a few days in February 2006, Arla Foods' products had been removed from the shelves of more than 50,000 stores across the Middle East. As sales largely came to a complete standstill, several decades of progress and growth lay in ruins. Production was subsequently closed down at several dairies in Denmark forcing more than 300 million litres of milk to be re-routed to other dairies within the Group while 55 employees were made redundant. After a huge effort, not least by staff in the Middle East, some of the distribution was re-established in late spring. At the close of 2006, Arla Foods' brands had recovered approximately 50 per cent of their original sales.

The situation in the Middle East will also impact on 2007 earnings in that, under the most positive scenario, the Group does not expect to return to normal sales levels until the end of the year.

## Strategic acquisitions

Despite the crisis in the Middle East, the Executive Management Board and the Supervisory Board were determined to stick to the strategy plan and implement a number of strategic acquisitions. The Danish dairy company, Tholstrup Cheese, became part of the Arla Foods' Group, contributing well-known products and high quality to the mould cheese segment, one of the Group's strategic product categories. This was followed by the purchase of, initially, 30 per cent of the shares in Ingman Foods Oy in Finland, an acquisition which was approved by the EU in January 2007. The new Arla Ingman Oy AB will be a strong component of the Group's Nordic strategy.

In the United States, we bought the White Clover Dairy which, over the past decade, has produced cheese for Arla Foods for the local US market. The acquisition is part of Arla Foods' strategy for North America and follows the purchase of National Cheese in Canada in 2005. A broader analysis of the Group's future strategic development in the region will now be carried out.

At the beginning of 2006, we established the joint venture company, Mengniu Arla, which will build a substantial position within retail-packed milk powder in China over the coming years. Eight months later, it was decided to further expand production in China to approximately 40,000 tons. The expansion programme is expected to be completed in 2008.

At the end of the year, the company took a further step towards acquiring the remaining 49 per cent of the shares in the listed UK subsidiary, Arla Foods UK plc. At the end of February 2007, the other shareholders had not yet finalised their position.

Towards the end of the year, Arla Foods' Board of Representatives decided to establish a strategy fund to contribute to the company's ongoing strategic development and secure stable development in the milk price.

»Eight months later, it was decided to further expand production in China.«

**Extensive savings programme**

In 2006, intensive efforts were directed at rationalising the company's portfolio of activities, and the disposal of several non-core activities was implemented. Among the most significant were Frödinge Dairy in Sweden and the doorstep business in the UK.

In 2006, we also undertook a range of extraordinary cost saving measures across the Group. Having achieved considerable savings in the autumn of 2006, it was decided to extend the efficiency measures to comprise the Group's administrative functions.

**New tool to secure transparent management**

In organisational terms, Human Resources was strengthened over the past year through the development of better and clearer relations between staff and the Group's long-term development.

New management programmes were developed during the year and existing ones improved. The aim is to assist managers achieve their targets through motivating and involving staff on the basis of clear management principles. In 2007, a tool will be launched to help the organisation evaluate the development potential of individual managers.

The whole organisation, not just the HR department, embarked on an extensive reorganisation aimed at strengthening the company in the face of global competition. This work will continue over the coming years.

As Arla Foods faces up to the challenges in the global market, a strong corporate identity is required. Consequently, in 2006, a great deal of work was dedicated to Arla Foods' corporate identity which identifies the Group's values and links them to our mission, vision and strategy. The new values will be presented in 2007 and implemented across the Group over the next three years.

During 2006, Arla Foods carried out a staff satisfaction survey known as The Barometer for the fourth time. The survey, which comprised 82 per cent of the staff, showed that overall satisfaction had increased compared to the previous survey. Among other things, the result underlined the importance of relations between staff and their immediate superior. As a result of The Barometer survey, Arla Foods has decided to prioritise the following areas: leadership, stress and bullying.

**Products must match consumer requirements**
Arla Foods' product development activities moved nearer to our markets in 2006 when the functional area began to report directly to the business areas. The purpose is to establish a close link between consumer wishes and the Group's prioritisation of its product development work.

In 2006, considerable effort was made in terms of gathering the company's research strategy into Forskningsstrategi 2012 where, in addition to the focus areas of food safety, nutrition, processing and product, there will be new focus on differentiated production of raw milk. The strategy is expected to be approved in 2007.

Together with the rest of the Danish dairy industry, we have taken on the task of providing the necessary documentation for Danish production of cheese based on raw milk. The scope of the work means that Arla Foods' research will continue its work within this area, especially in relation to safety issues.

Arla Foods is also part of a High Technology Fund project centred on the development of ingredients and milk proteins, an effort that will contribute to the Group's knowledge of proteins. The Foodturum department, which works with radical product development, from idea to reality, by researching new technologies and challenging new markets, plays an active role which can strengthen and supplement current skills. In partnership with the business groups, new business opportunities will be created through the provision of tools and project management for across-the-board innovative projects.


Arla Foods invests in modern vehicles equipped with engines that minimise pollution. The lorries' routes are planned to eliminate unnecessary driving and drivers are trained to drive economically. On-board computers record each lorry's fuel consumption and assist drivers to adjust their driving accordingly.

**New environmental goals**
In 2006, Arla Foods completed an environmental plan for the years up to 2010 aimed at reducing consumption of water and energy by 5 per cent each. The environmental plan also aims to reduce the number of industrial accidents and absenteeism caused by illness by 25 per cent each.

The dairies' water consumption has been continually reduced through increased use of recycled water and the dairies' own awareness of the need for better environmental practices.

Energy consumption must be reduced in production as well as transport. Within production, investment in new technology and stronger focus on cost savings has, so far, reduced energy consumption by around 5 per cent and thus lowered $CO_2$ and $NO_x$ pkt emissions to air.

In recent years, Arla Foods has developed its operations so as to become almost exclusively fully automised. Almost all jobs susceptible to Repetitive Strain Injury have been eliminated. At the same time automation poses new demands with regard to safety in the machinery area. To minimise the risk of injury, all machinery at all production plants in Denmark and Sweden have now been risk assessed, replaced or modified if they did not comply with safety requirements.

**22 million potential consumers in the Nordic area**
At year end 2005, Arla Foods' new joint Nordic organisation came into being. Consequently, Arla Foods now considers the Nordic countries as one market with 22 million potential consumers. The amalgamation has created stronger cohesion in the organisation, but has also resulted in a reduction of approximately 100 jobs. Consequently, Arla Foods is now better prepared to meet the competitive

In 2006, the advertising campaign featuring the milk producer, Elin, (in the photo) attracted huge attention in the Swedish media and won the Swedish advertising industry's award.

challenges in the Nordic market where the battle to win retailers' favour is hardening all the time. As a result of the competitive situation in Sweden and Denmark, Consumer Nordic did not meet its budget for 2006.

It was gratifying that, during the autumn 2006, we took an important step into the Finnish market by purchasing Ingman Foods Oy. The Finnish market is a good match for our Nordic range.

Work aimed at reducing the number of brands was also initiated in 2006. The purpose is to ensure that Arla Foods' brands across the Nordic countries have a greater impact while, at the same time, obtaining more efficient production. At the same time, a decision was made to establish a broad Nordic platform for dairy-based cooking products. Arla Foods believes that the Nordic »kitchen« offers some exciting opportunities.

On the production side, work aimed at rationalising and reducing costs continues. Production facilities are being examined in order to reduce wastage and increase efficiency on individual production lines. In 2006, operations at Karlskrona Dairy ceased. Similarly, the Supervisory Board has decided to close down Örebro Dairy in 2007 and Alingsås Dairy in early 2008. Production of fruit juice and fruit drinks from Alingsås will be transferred to the Rynkeby plant in Denmark.

On the distribution side, Arla Foods started nationwide distribution in Sweden – a project that, in view of Sweden's size, presents a special challenge. The fact that the Swedish Norrmejerier dairy company and Arla Foods embarked on a distribution partnership at the end of 2006 is a particularly welcome development.

*»It was gratifying that, during the autumn 2006, we took an important step into the Finnish market.«*

**British butter sales at an historic high**

Sales of Lurpak® and other export products to the UK are now at an all-time high. In 2006, earnings from these products showed further advances.

Since Arla Foods UK plc's disposal of its doorstep business in 2006, we have completed the business plan developed following the merger between Express Dairies and Arla Foods' UK subsidiary. It was, therefore, natural for Arla Foods amba to initiate negotiations for the remaining 49 per cent of the shares in Arla Foods UK plc. In January 2007, Arla Foods tabled an offer for the shares. As at the end of February, the other shareholders had not yet announced their response.

All in all, the UK market has fulfilled expectations not least with regard to exports of products to the UK.

Sales of butter and spreads in the UK continue to show strong growth. Lurpak® and Anchor® both grew by 6 per cent whereas the butter and spreads category in general only achieved growth of 1 per cent. Sales of Arla Foods' Cravendale® milk rose by close to 20 per cent on the year.

The UK company, therefore, remains a leading supplier of fresh milk and cream to the multiples. In terms of volume, sales of fresh milk increased by approximately 7 per cent during the year.

Market pressures combined with increased costs impacted considerably on Arla Foods UK plc's accounts during the first six months although the situation

In the summer of 2006, Arla Foods UK plc sold its doorstep business to Dairy Crest Group plc in part owing to declining doorstep sales which required rationalisation within this area. Sales of Arla Foods' Cravendale® milk rose by almost 20 per cent on the year.


2006 saw the successful launch of the spread, Kærgården, in the German market. The product is available in more than 30,000 stores and its prospects are encouraging.

improved in the second half year owing to a series of price increases and better capacity utilisation at our UK dairies.

In the summer of 2006, Arla Foods UK plc sold its doorstep business to Dairy Crest Group plc as declining doorstep sales to British households called for rationalisation measures.

**A tough international year**

2006 saw considerable differences in international markets. In general, results materialised slower than desired. The main cause was the boycott of Arla Foods' dairy products in the Middle East. Another factor behind the failure to meet financial expectations was the strong competition in European markets.

In 2006, Germany accounted for approximately one fourth of Consumer International's turnover. Consumer surveys show that major marketing efforts during the year resulted in the Arla Foods' name now being known by more than half of all German households and that consumers associate the brand with high quality. Despite the growth in the market, profits fell below expectations largely owing to greater competition in the yellow cheese category. The positive developments included the successful launch of the spreadable Kærgården®. The product is sold in more than 30,000 German stores and prospects are encouraging.

In 2006, Arla Foods established a regional office in Warsaw from where Business Unit Eastern Europe's activities are conducted. Arla Foods' market position in Poland is expected to expand in terms of both production and sales. In 2006, we achieved fair progress primarily due to increasing sales of the feta cheese Apetina®.

Mould cheese is one of the four cheese types in which Arla Foods has invested heavily in recent years.

In the North American market, Arla Foods expanded its local cheese production during the year under review.

With the acquisition of the White Clover Dairy in Wisconsin and Tholstrup Cheese's dairy in Michigan in 2006, Arla Foods has secured a local production which will account for an increasing share of earnings in 2007.

For 2007, we plan to expand production in Canada to comprise blue mould cheese. The development of local market positions should contribute towards better opportunities for imports from Sweden and Denmark.

In recent years, Arla Foods has invested considerably in the production of cream cheese, mould cheese, feta and mozzarella for international markets. The acquisition of Tholstrup Cheese represents a further strengthening of the company's strategy in the speciality cheese area. As part of the integration of the two companies into Arla Foods, the Supervisory Board, in the autumn of 2006, decided to combine all production of decorated cream cheese at Korsvej Dairy. As a result, Arla Foods' dairy in Vrinners will cease production in May 2007.

A major expansion of Holstebro Butter Dairy in Denmark is planned for 2007. Production of liquid cooking fat will be in-sourced to Götene Butter Dairy in Sweden.

**China at the centre of Global Ingredients' business in 2006**

During the year, Arla Foods launched an important initiative in the Chinese market when production of retail packed milk powder for consumers began in a joint venture with a strong Chinese partner, China Mengniu Dairy Company. The company has got off to a good start and eight months after the opening it was decided to expand production by 30,000 tons to a total of 40,000 tons. The new plant is expected to be ready for commissioning in 2008.

The overall result within the milk powder area was affected by the boycott in the Middle East, the low dollar rate and the EU's CAP policy which, in 2006, took further significant steps towards abandoning export subsidies. Arla Foods' milk powder for the retail sector is sold in several markets in Africa, Latin America, the Middle East and in Asia under the brand names Dano® and Milex®.

The milk protein segment saw further advances, especially within proteins developed for the nutrition industry. In respect of the market, China also increasingly contributes to earnings.

Some of the raw material for the development of more milk proteins will derive from the planned expansion of our operations in Argentina which we own jointly with the Argentinian company, SanCor. The rest will come from strategic partnerships with other large dairy companies.

Arla Foods has established a joint venture with China's leading dairy company, Mengniu Dairy Company. Arla Foods holds 49 per cent of the shares and Mengniu 51 per cent. The Chinese venture was the first important step towards strengthening the processing of nutritional milk powder products, increasing focus on brands and investments in emerging markets to offset the reduction of export subsidies under the EU's Common Agricultural Policy.

**Expectations for 2007 results**

Arla Foods plans for the ongoing liberalisation of world markets through strategic growth in the main markets and within the strategic product categories. At the same time, rationalisation programmes will be maintained across the Group.

The EU's Common Agricultural Policy continues to impact negatively on the European dairy industry. Arla Foods looks forward to the time when the industry, over the next few years, will emerge from the period of reform, which is having a considerable deflationary effect on European milk prices. In addition, it is crucial to the industry that the outcome of WTO negotiations is positive, opening up further markets.

Expectations for 2007 are for a minor advance in profits, not including profits from company disposals. As in 2006, the net result for 2007 is expected to be affected by both acquisitions and disposals.

Peder Tuborgh
*CEO*

# Financial review

## Income statement

### *Profit for the year, supplementary payment and consolidation*

Profit for the year came in at DKK 933 million as against DKK 30 million for the transitional period 1 October – 31 December 2005. The extensive Middle Eastern boycott of Danish products had a severely adverse impact on results. However, this was mostly offset by a high level of non-recurring income in the form of gains on the disposal of companies and properties. In addition, the results were adversely affected by continuously reduced restitutions and the fierce competition encountered on the domestic markets. The significant events during the first months of the year resulted in a lower on-account price for co-operative member milk from 1 April 2006, increasing group net results.

Arla Foods' earnings per kg milk weighed in by co-operative members reached 226.66 Danish øre/281.22 Swedish öre as against 216.53 Danish øre/272.67 Swedish öre during the transitional period.

Supplementary payments accounted for DKK 336 million as against DKK 75 million for the transitional period. Net consolidation is 6.29 Danish øre/7.81 Swedish öre per kg weighed in co-operative member milk. The consolidated amount is recognised in reserves in respect of delivery-based owner certificates at an amount of 3.02 Danish øre/3.75 Swedish öre and 3.27 Danish øre/4.06 Swedish öre in respect of a recently established strategy fund.

### *Changes in accounting policies*

As stated in the section »Accounting policies«, the company has changed its accounting treatment of minority assets. The monetary consequences are referred to in the accounting policies.

### *Revenue*

Revenue reached DKK 45,491 million in 2006 as against DKK 11,487 million for the transitional period. Revenue was affected by a number of issues, for instance the acquisition of the Tholstrup Cheese Group by mid-September and the divestment of doorstep milk business in the UK by mid-August, the Middle Eastern boycott of Danish products, reduced restitutions, exchange rate movements and the international price level of dairy products.

### *Operating profit*

Operating profit totalled DKK 1,161 million in 2006 as against DKK 113 million for the transitional period. Production costs include an on-account payment to co-operative members of DKK 13.0 billion as against DKK 3.2 billion for the transitional period.

As stated, operating profit was adversely affected by the Middle Eastern boycott of Danish products, deemed to have affected the member earnings by approx. DKK 450 million, which is up on the amount of DKK 400 million stated in the annual report for the transitional period. Following the reduction of the on-account price at 1 April, the company's results are negatively affected by a net amount of approx. DKK 300 million.

Non-recurring items had a positive net impact of DKK 50 million on operating profit and thereby, to a certain degree, managed to reduce the impact on the results of the Middle Eastern boycott.

Depreciation/amortisation and impairment were slightly on the increase, while other costs were kept at a low level as a result of staff reductions, rationalisation and optimisation.

The year's total milk volume weighed in represented 8,592 million kg, of which co-operative member milk amounted to 6,114 million kg. British suppliers account for the vast part of non-co-operative member milk.

### *Profit from ordinary activities before tax*

Gain on the divestment of enterprises came in at DKK 364 million as against DKK 0 million for the transitional period.

Despite an increasing market interest rate, net financing costs were down on previous years, primarily as a result of debt restructuring.

The tax charge for the year was affected by improved profit from ordinary activities in the British subsidiary.

## Balance sheet

### *Total assets*

Total assets were reduced to DKK 26,611 million at 31 December 2006 as against DKK 27,057 million at 31 December 2005.

### *Fixed assets*

Intangible assets came in at DKK 3,068 million as against DKK 2,754 million and consist, for the most part, of group goodwill arising from the acquisition of Express Dairies in the UK at the beginning of 2003/2004, the IT development project Ett Arla and goodwill arising from the acquisition of Tholstrup Cheese. Additions in the year comprised Tholstrup Cheese, Ett Arla and the trademark, Bregott.

Property, plant and equipment represented DKK 10,827 million as against DKK 11,018 million. The additions for the year amounting to DKK 1,792 million include the acquisition of Tholstrup Cheese and other investments in the UK, Sweden and Denmark. The disposals for the year totalling DKK 689 million were, for the most part, attributable to the divestment of the doorstep milk business in the UK and the disposal of properties.

Investments reached DKK 1,867 million as against DKK 1,910 million. Deferred tax assets were down by DKK 95 million, primarily prompted by reduced pension provisions in the UK. Investments in associates were on the increase, among other things as a consequence of the investment in Mengniu Arla in China.

### *Equity*

Equity at 31 December 2006 was DKK 7,971 million, representing an increase of DKK 560 million on 31 December

2005. The portion of results used for consolidation totalled DKK 597 million. Of this amount, DKK 122 million are attributable to the re-consolidation of distributions according to the articles of association. The equity ratio measured as equity in proportion to total assets accounted for 30% at 31 December 2006, which was up on the 27% at year end 2005. The acquisition in Finland in January 2007 will – together with the expected acquisitions in the UK – reduce the equity ratio to approx. 27%.

The equity ratio including the subordinate bond loan of DKK 1,000 million accounted for 34% at 31 December 2006, which was also up on the 31% at year end 2005.

### *Provisions*

Pension commitments relate to the UK and Sweden (defined benefit schemes) and reached DKK 2,875 million as against DKK 3,035 million the year before. The decline was, for the most part, the result of increased pension fund contributions.

### *Liabilities*

The group is primarily financed through mortgage loans and loans with other credit institutions as well as a subordinate bond loan of DKK 1 billion.

## Financial risks and management thereof

### *Group policy for financial risk management*

As a result of Arla Foods' international activities, the group results and balance sheet are exposed to financial risks. The overall objectives and policies of Arla Foods' financial risk management are laid down in the group's finance policy, which is revised annually and adopted by the Supervisory Board. However, specific finance and liquidity policies apply to the group's listed British subsidiary, Arla Foods UK plc.

The finance policy lays down the framework for the procedures governing the group's foreign exchange, financing, liquidity, interest and credit risk and provides documentation of adopted financial instruments and counterparties.

### *Foreign exchange risks*

Foreign exchange matters pose a significant risk to Arla Foods and, therefore, have a major impact on the income statement and balance sheet. Commercial risks are hedged to a wide extent. Under group policy, the individual business units are responsible for their hedging transactions. The vast part of external hedging transactions is handled centrally by the finance department.

GBP, SEK, DKK, EUR and USD account for the major part of revenue, while production and other operating costs, for the most part, are settled in GBP, DKK and SEK. Expected currency flows may be hedged for up to 15 months by way of forward exchange and option contracts with matching terms. Of the group's total revenue of DKK 45 billion, other currencies than DKK accounted for approx. 82%.

Arla Foods' investments in foreign subsidiaries and associates are generally not hedged. However, each case is assessed individually.

Operating results for 2006 include profit of an estimated DKK 80 million prompted by hedging transactions while at 31 December 2006 an amount of DKK 25 million was taken directly to equity, which is equivalent to the market value of the hedging instruments used after the balance sheet date.

### *Financing and interest rate risks*

The finance policy underpins the group's objectives and strategies and reduces the refinancing risk.

The group's policy is to hold long term debt with diversified maturity.

Long-term, fixed-interest rate loans represent the group's most important source of financing. New loans are raised as floating-rate loans, and interest swaps and interest options are used for managing the interest rate risk, ensuring efficient interest rate management and a higher degree of flexibility.

At 31 December 2006, the total interest-bearing liabilities including the group's pension commitments in the UK and Sweden amounted to DKK 12,119 million. If the pension commitments are disregarded, the average term to maturity of long-term interest-bearing liabilities is approx. 6.5 years.

To hedge the group's interest expenses, hedging agreements have been concluded. At 31 December 2006, the market value of these agreements came in at a negative DKK 3 million, which was taken directly to equity.

In the medium term, Arla Foods' results are affected by interest rate development. By contrast, an increase in the interest level of 1 percentage point in the coming year is not deemed to have a significant impact on results.

### *Liquidity risks*

The group manages its liquidity risk by ensuring the availability of sufficient operating liquidity and liquidity for major changes in the consolidated balance sheet. Borrowing facilities related to such changes are separately assessed. Prompted by its recommended and binding bid for the residual 49% shares in Arla Foods UK plc, the group has entered into a binding loan agreement ensuring the conclusion of the transaction.

The group uses a central cash pool arrangement generating a reasonable return on excess liquidity. A Commercial Paper programme of SEK 2.5 billion is available for the issue of securities with terms of up to one year by Arla Foods amba and Arla Foods AB. At present, the programme remains unused. As at 31 December 2006, the group's liquidity reserve was specified as follows:

| | DKKm |
|---|---|
| Cash at bank and in hand | 601 |
| Securities | 772 |
| Undrawn facilities | 3,201 |
| **Total liquidity reserve** | **4,574** |

The majority of the undrawn facilities are short-dated.

### *Credit risks*

Arla Foods' trade receivables are not deemed to be exposed to any unusual risks. Credit management is continuously in focus in the Group's entities. Bad debt losses are in line with previous years.

In order to reduce its credit risk, the group regularly credit rates its customers and co-operative partners. Credit insurance is taken out for customers deemed to pose a risk. Financial instrument counterparties must at least be rated »investment grade« by either Moody's or Standard & Poors.

## Events after the balance sheet date

On 8 November 2006, Arla Foods announced the acquisition of 30% of Ingman Foods Oy with a pre-emptive right to acquire the residual 70% within the next three years. On 15 January 2007, the acquisition was adopted by the competition authorities and will be included in the annual report for 2007.

On 22 January, Arla Foods made a recommended and binding bid for the residual 49% of the share capital of Arla Foods UK plc. Assuming that the acquisition is realised, the accounting consequences thereof will impact on the annual report for 2007.

# Statement by the Executive and Supervisory Board

The Executive and Supervisory Boards have today discussed an approved the annual report of Arla Foods amba for 2006, which comprises the statement by the Executive and Supervisory Boards on the annual report, Management's review, accounting policies, income statement, balance sheet, statement of changes in equity, cash flow statement and notes.

The annual report has been prepared in accordance with the Danish Financial Statements Act. We consider the accounting policies used to be appropriate. Accordingly, the annual report gives a true and fair view of the group's and the parent company's financial position at 31 December 2006 and of the results of the group's and the parent company's operations and consolidated cash flows for the financial year 1 January – 31 December 2006.

We recommend that the annual report be approved by the Board of Representatives.

Aarhus, 28 February 2007

*Executive Board:*

| | | | |
|---|---|---|---|
| Peder Tuborgh<br>*CEO* | Povl Krogsgaard<br>*Vice CEO* | Andreas Lundby<br>*Vice CEO* | / Jørn Wendel Andersen<br>*Executive Director / CFO* |

*Supervisory Board:*

| | | | |
|---|---|---|---|
| Knud Erik Jensen<br>*Chairman* | Åke Hantoft<br>*Vice Chairman* | | |
| Leif Backstad | Anders Ericsson | Steen Nørgaard Madsen | Johan von Schéele |
| Viggo Ø. Bloch | Leif Eriksson | Torben Myrup | Pejter Søndergaard |
| Steen Bolvig | Thomas Johansen | Ove Møberg | Bent Juul Sørensen |
| Bjarne Bundesen | Erik Karlsson | Jan Toft Nørgaard | |
| Bengt Darhult | Sören Kihlberg | Gunnar Pleijert | |

# Independent auditors' report

### *To the members of Arla Foods amba*

We have audited the annual report of Arla Foods amba for the financial year 1 January – 31 December 2006, which comprises the statement by the Executive and Supervisory Boards on the annual report, Management's review, accounting policies, income statement, balance sheet, statement of changes in equity, cash flow statement and notes. The annual report has been prepared in accordance with the Danish Financial Statements Act.

### *The Executive and Supervisory Boards' responsibility for the annual report*

The Executive and Supervisory Boards are responsible for the preparation and fair presentation of this annual report in accordance with the Danish Financial Statements Act. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of an annual report that is free from material misstatement, whether due to fraud or error, selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

### *Auditors' responsibility and basis of opinion*

Our responsibility is to express an opinion on this annual report based on our audit. We conducted our audit in accordance with Danish Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the annual report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the annual report. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the annual report, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the company's preparation and fair presentation of the annual report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Executive and Supervisory Boards, as well as evaluating the overall presentation of the annual report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Our audit did not result in any qualification.

### *Opinion*

In our opinion, the annual report gives a true and fair view of the group's and the parent company's financial position at 31 December 2006 and of the results of the group's and the parent company's operations and consolidated cash flows for the financial year 1 January – 31 December 2006 in accordance with the Danish Financial Statements Act.

Aarhus, 28 February 2007

KPMG C. Jespersen
*Statsautoriseret Revisonsinteressentskab*

KPMG Bohlins AB, Sverige

Finn L. Meyer
*State Authorised Public Accountant*

Carl Lindgren
*Authorised Public Accountant*

# Accounting policies

**General information**

The annual report of Arla Foods amba for 2006 has been prepared in accordance with the provisions applying to reporting class C large enterprises under the Danish Financial Statements Act.

As from 2006, the financial year was changed to follow the calendar year with a transitional period from 1 October – 31 December 2005. Meaningful restatement of the comparative figures for the calendar year 2005 has not been feasible. The comparative figures accordingly represent the figures for the transitional period.

*Changes in accounting policies*

The accounting policies are consistent with those applied last year apart from the accounting for minority assets.

Previously, the minority interests' share of any positive excess (goodwill) arising on the acquisition of a subsidiary with negative equity was recognised as intangible assets and amortised until the minority interest again was positive. The results from the enterprise acquired were recognised in full in the group's profit until the company again realised positive equity. Amortisation for the year of minority assets was determined allowing only the group's share of results to be recognised in order to obtain accelerated amortisation of the excess.

In 2006, this policy was changed allowing the part of the positive excess (goodwill) relating to the minority to be amortised as other goodwill in future. The comparative figures have been restated to comply with the new policy. At 1 January 2006, the balance sheet and equity were reduced by DKK 91 million (DKK 46 million at 1 October 2005) as a result of the change in policy. The change affected the profit for the year positively by DKK 93 million (adversely affected by DKK 45 million for the period 1 October – 31 December 2005). The balance sheet and equity at 31 December 2006 were increased by DKK 2 million.

A few reclassifications have been made in the annual report. These reclassifications will not affect the profit or equity. Comparative figures have been restated.

*Consolidated financial statements*

The consolidated financial statements comprise the parent company, Arla Foods amba, and subsidiaries in which Arla Foods amba directly or indirectly holds more than 50% of the voting rights or which it, in some other way, controls. Enterprises in which the group holds between 20% and 50% of the voting rights and over which it exercises significant influence, but which it does not control, are considered associates.

The consolidated financial statements are prepared by aggregating similar items from the parent company's and the individual subsidiaries' annual reports. On consolidation, intra-group income and expenses, shareholdings, intra-group balances and dividends and unrealised gains and losses on intra-group transactions are eliminated.

*Business combinations*

The operations of enterprises acquired and sold are included in the consolidated financial statements for the part of the year in which the enterprises have been owned by the Arla Foods Group.

Acquisitions of enterprises are accounted for using the purchase method, according to which the identifiable assets and liabilities acquired are measured at their fair values at the date of acquisition. Provision is made for costs related to adopted and announced plans to restructure the acquired enterprise. The tax effect of fair value adjustments is taken into account.

Any positive excess of the cost of the acquired investment over the fair value of the assets and liabilities acquired (goodwill) is recognised as intangible assets. Where fair value adjustments of the assets and liabilities acquired result in a negative net asset value of the acquired enterprise, minority interests' share is included in the positive excess. Any positive excess is amortised in the income statement based on an individual assessment of the useful life, not exceeding 20 years.

Any negative excess representing an anticipated adverse development in the acquired enterprises (negative goodwill) is recognised in the balance sheet as deferred income and recognised in the income statement as the adverse development is realised.

Gains or losses on disposal, in whole or in part, of subsidiaries and associates are stated as the difference between the sales amount and the carrying amount of net assets at the date of disposal plus non-amortised goodwill and disposal costs. Gains or losses are recognised in the income statement in the item disposal of enterprises.

*Minority interests*

In the consolidated financial statements, the items of subsidiaries are recognised in full. The minority interests' proportionate shares of the subsidiaries' results and equity are adjusted annually and recognised separately in the income statement and balance sheet.

*Foreign currency translation*

On initial recognition, transactions denominated in foreign currencies are translated at the exchange rates at the transaction date. Foreign exchange differences arising between the exchange rates at the transaction date and at the date of payment are recognised in the income statement as financial income or financial expenses.

Receivables and payables and other monetary items denominated in foreign currencies are translated at the exchange rates at the balance sheet date. The difference between the exchange rates at the balance sheet date and at the date at which the receivable or payable arose or the exchange rate recognised in the latest financial statements is recognised in the income statement as financial income or financial expenses.

On recognition of foreign subsidiaries, the income statements are translated at average exchange rates, and the balance sheet items are translated at the exchange rates at the balance sheet date.

On recognition of foreign associates, the shares of profit are recognised at average exchange rates and the share of net asset value is recognised at the exchange rates at the balance sheet date.

Foreign exchange differences arising on translation of the opening equity of foreign subsidiaries at the exchange rates at the balance sheet date and on translation of the income statements from average exchange rates to the exchange rates at the balance sheet date are recognised directly in equity.

### *Derivative financial instruments*

Derivative financial instruments are initially recognised in the balance sheet at cost and are subsequently measured at fair value. Positive and negative fair values of derivative financial instruments are included in other receivables and payables, respectively.

Changes in the fair value of derivative financial instruments designated as and qualifying for recognition as a hedge of the fair value of a recognised asset or liability are recognised in the income statement together with changes in the fair value of the hedged asset or liability.

Changes in the fair value of derivative financial instruments designated as and qualifying for recognition as a hedge of future cash flows are recognised directly in equity. Income and expenses relating to such hedging transactions are transferred from equity on realisation of the hedged item and recognised in the same item as the hedged item.

For derivative financial instruments that do not qualify for hedge accounting, changes in fair value are recognised in the income statement.

### *Subsidies*

EU subsidies and subsidies from other public authorities for investments in fixed assets are deducted from the purchase price.

Subsidies granted for product development, etc. are entered as income under the item other operating income at the time when the repayment obligation is no longer contingent.

## Income statement

### *Revenue*

Revenue is recognised in the income statement provided that transfer of risk to the buyer has taken place and comprises the year's invoiced sales less sales discounts. Any restitutions and production subsidies from the EU are included in revenue.

The revenue for Arla Foods amba also includes declared supplementary payments from other sales companies within the Arla Foods Group.

### *Production costs*

Production costs include cost of sales, including purchases from Arla Foods' members as well as costs, including depreciation and impairment of plant, etc. and wages and salaries incurred to realise the revenue for the year. Purchases from members are recognised at on-account prices for the year and therefore do not include supplementary payments.

### *Distribution costs*

Costs incurred in distributing goods sold during the year and in conducting sales campaigns etc. during the year are recognised as distribution costs. Also, costs relating to sales staff, sponsor, advertising, exhibitions and depreciation are recognised as distribution costs.

### *Joint costs, including administration*

Joint costs, including administrative expenses comprise expenses incurred during the year for group management and administration, including expenses for administrative staff, office premises and office expenses, and depreciation.

### *Other operating income and costs*

Other operating income and costs comprise items secondary to the principal activities of the enterprises, including gains and losses on disposal of properties.

### *Profits/losses from investments in subsidiaries and associates*

The proportionate share of the results after tax of the individual subsidiaries is recognised in the income statement of the parent company after full elimination of intra-group profits/losses and less declared supplementary payments.

The proportionate share of the results after tax of the associates is recognised in both the parent company and the consolidated income statement after elimination of the proportionate share of intra-group profits/losses.

*Divestment of enterprises*
Net book profits/losses on the disposal of companies and activities are recognised in this item.

*Financial income and expenses*
Interest income and expenses are recognised in the income statement at amounts relating to the financial year.

Furthermore, financial items comprise both realised and unrealised value adjustments of securities and foreign exchange adjustments as well as the interest part of the finance lease payment.

*Tax on profit/loss for the year*
The taxable income of the companies is calculated in accordance with the national rules in force from time to time. Tax is computed based on co-operative taxation and corporate taxation. For jointly taxed enterprises, tax on the results for the financial year is expensed at the current tax rates, calculated on the basis of the pre-tax results for the year, adjusted for non-taxable income and expenses. The current Danish corporation tax is allocated between the jointly taxed Danish companies in proportion to their taxable income (full absorption with refunds for tax losses).

Deferred tax and adjustment thereof for the year is measured using the balance sheet liability method on all temporary differences between the carrying amount and the tax base of assets and liabilities

## Balance sheet

*Intangible assets*
Intangible assets are measured at cost less accumulated amortisation and impairment.

Intangible assets comprise goodwill from the acquisition of enterprises, product development projects, the IT development project Ett Arla, licences, trademarks, etc.

Product development projects qualifying for recognition in the balance sheet are measured at cost, including indirect costs incurred. Other development costs are recognised in the income statement when they occur.

For the IT development project Ett Arla, only external costs for the establishment of the Group's IT system are capitalised. Internal systems development costs are recognised on a regular basis in the income statement.

The assets are amortised on a straight-line basis over their expected useful lives:

| | |
|---|---|
| Goodwill | 3–20 years |
| Licences and trademarks, etc. | 10 years |
| Product development projects | 3 years |
| The IT development project Ett Arla | 5–8 years |

Intangible assets are amortised from the date of acquisition or when the assets are taken into use.

Intangible assets are assessed regularly and any impairment need is assessed in relation to the expected future net income from the enterprise or activity to which the asset relates.

*Property, plant and equipment*
Property, plant and equipment are measured at cost less accumulated depreciation and impairment.

Cost comprises the purchase price and any costs directly attributable to the acquisition until the date when the asset is available for use.

Depreciation is provided on a straight-line basis over the expected useful lives of the assets from the time of acquisition or commissioning. The expected useful lives are as follows:

| | |
|---|---|
| Office buildings | 50 years |
| Production buildings | 20–30 years |
| Plant and machinery | 5–10 years |
| Fixtures and fittings, tools and equipment | 3–7 years |

Assets are written down to the recoverable amount (net realisable value) if this is lower than the carrying amount.

Assets in course of construction and land are not depreciated.

Assets with a short useful life, minor acquisitions and minor costs of improvement are expensed in the year of acquisition.

Gains and losses on the realisation of property, plant and equipment are recognised as other operating income and expenses in the income statement.

Lease contracts regarding property, plant and equipment, where the group holds all major risks and rewards incident to ownership (finance lease), are measured at their initial recognition in the balance sheet at the lower of fair value and the present value of the future lease payments. For the calculation of the net present value, the interest rate implicit in the lease or an approximation thereof is used as the discount rate. Assets held under finance lease are hereafter treated as the company's other property, plant and equipment.

The capitalised residual lease payments are recognised in the balance sheet as a liability and the interest part of the lease payment is recognised in the income statement over the term of the contract.

*Investments*

Investments in subsidiaries and associates are measured according to the equity method.

Investments in subsidiaries and associates are measured at the proportionate share of the enterprises' net asset values calculated in accordance with the parent company's accounting policies minus or plus unrealised intra-group profits and losses.

For those cooperative societies that form part of the group, the ownership share, and thereby the share of the net asset value, has been calculated in accordance with the Articles of Association of the individual companies.

Investments in subsidiaries and associates with negative net asset values are measured at DKK 0 (nil), and any amounts owed by such enterprises are written down by the group's share at the negative net asset value if the amount owed is irrecoverable. If the negative net asset value exceeds the receivable, the remaining amount is recognised under provisions to the extent the group has a legal or constructive obligation to cover the deficit of the enterprise.

Net revaluation of investments in subsidiaries and associates is transferred to the reserve for net revaluation according to the equity method in equity to the extent that the carrying amount exceeds cost.

Other investments are measured at fair value at the balance sheet date.

*Inventories*

Raw materials, consumables and goods for resale are measured at cost. The cost of the milk included in inventories has been recognised at the settlement price, including expected supplementary payments to Arla Foods amba's members.

Work in progress and finished goods are measured at cost consisting of the cost of raw materials and consumables with the addition of processing costs and other costs directly or indirectly related to the individual goods. Indirect production overheads comprise indirect materials and wages and salaries as well as depreciation of production equipment.

Inventories are measured at cost in accordance with the FIFO method. Where the net realisable value is lower than cost, inventories are written down to this lower value. The net realisable value of inventories is determined taking into account marketability, obsolescence and development in expected sales price.

*Receivables*

Receivables are measured at amortised cost less write-down for bad debt losses based on an individual assessment of receivables. Amortised cost corresponds in all material respects to nominal value.

Prepayments comprise costs incurred concerning subsequent financial years.

*Other current assets*

Securities are measured at the current market value at the balance sheet date.

*Tax and deferred tax*

Current tax payable and receivable is recognised in the balance sheet as tax computed on the taxable income for the year, adjusted for tax on the taxable income of prior years and for tax paid on account.

Deferred tax is measured using the balance sheet liability method on all temporary differences between the carrying amount and the tax base of assets and liabilities.

Deferred tax assets, including the tax base of tax loss carryforwards, are recognised at the expected value of their utilisation; either as a set-off against tax on future income or as a set-off against deferred tax liabilities in the enterprises forming part of the joint taxation.

Deferred tax is measured according to the tax rules and at the tax rates applicable in the respective countries at the balance sheet date when the deferred tax is expected to crystallise as current tax.

*Other provisions*

*Pensions:*

The group has entered into pension agreements with many of the group's employees.

The pension schemes comprise defined contribution schemes and defined benefit schemes.

As regards the defined contribution schemes used in the Danish companies, the group currently pays fixed contributions to independent pension funds. The group has no commitments of additional payments.

Defined benefit schemes, which are primarily used by the group's undertakings in Sweden and the UK, are those for which the company is committed to pay a certain amount from the date of retirement, depending on employee's length of service and final salary.

The commitment regarding defined benefit schemes is calculated annually by means of an actuarial computation based on the expected future development in interest, inflation and average life expectancy.

Costs in the income statement regarding defined benefit schemes are based on the above-mentioned actuarial calculations.

The actuarially calculated present value of defined benefit obligations less the market value of any assets related to the schemes are provided in the balance sheet under pension commitments.

If the actuarial assumptions change, gains and losses exceeding 10% of the present value of the pension commitments or 10% of the fair value of the plan assets will consequently only be recognised in the income statement over the average remaining service life of the employees covered by the pension scheme (the corridor method).

*Other provisions*

Other provisions include insurance provisions and obligations in connection with business combinations, restructuring and lawsuits, etc.

### *Liabilities other than provisions*

Amounts owed to mortgage credit institutions and banks as well the subordinate bond loan are recognised at the date of borrowing at the net proceeds received less transaction costs paid. In subsequent periods, the financial liabilities are measured at the capitalised value.

Financial liabilities also include the capitalised residual obligation on finance leases.

Other liabilities, comprising supplementary payments to members, trade payables, amounts owed to group enterprises and associates and other payables, are measured at amortised cost – usually corresponding to the nominal value.

Deferred income comprises payments received concerning income in subsequent years.

## Cash flow statement

The consolidated cash flow statement is prepared in accordance with the indirect method on the basis of the consolidated results. The statement shows the cash flows of the group, divided into operating, investing and financing activities and how these cash flows have affected the group's cash funds.

The cash flow from operating activities is calculated as the consolidated results adjusted for non-cash operating items such as depreciation and impairment and changes in the working capital.

The cash flow from investing activities comprises cash flows in connection with the purchase and sale of intangible assets and property, plant and equipment as well as investments.

The cash flow from financing activities comprises the raising and repayment of long-term and short-term debt to financial institutions, mortgage lenders and payments to cooperative members.

The cash funds are made up of cash at bank and in hand and listed bonds recognised in the balance sheet as current assets.

The cash flow statement cannot be derived solely from the consolidated financial statements.

# Income statement

| Parent company | | | | Group | |
|---|---|---|---|---|---|
| 01.10.05<br>31.12.05 | 01.01.06<br>31.12.06 | DKK million | Note | 01.01.06<br>31.12.06 | 01.10.05<br>31.12.05 |
| 6,594 | 24,046 | **Revenue** | 1 | 45,491 | 11,487 |
| −5,906 | −21,620 | Production costs | 2/3 | −36,374 | −9,253 |
| **688** | **2,426** | **Gross profit** | | **9,117** | **2,234** |
| −353 | −1,339 | Distribution costs | 2/3 | −5,827 | −1,590 |
| −178 | −697 | Joint costs including administration | 2/3/4 | −2,370 | −553 |
| 44 | 99 | Other operating income | | 422 | 69 |
| −26 | −15 | Other operating expenses | | −181 | −47 |
| **175** | **474** | **Operating profit** | | **1,161** | **113** |
| −104 | 471 | Results in subsidiaries | 9 | – | – |
| 0 | −7 | Results in associates | 9 | −9 | 0 |
| 0 | 0 | Divestment of enterprises | | 364 | 0 |
| −31 | 24 | Net financial items | 5 | −409 | −124 |
| **40** | **962** | **Profit from ordinary activities before tax** | | **1,107** | **−11** |
| −10 | −29 | Tax | 6 | −170 | 41 |
| **30** | **933** | **Profit for the year** | | **937** | **30** |
| – | – | Minority interest share of results in subsidiaries | 10 | −4 | 0 |
| **30** | **933** | **Arla Foods amba's share of results for the year** | | **933** | **30** |
| | | **Proposed profit appropriation** | | | |
| 75 | 336 | Supplementary payment to Arla Foods' members | | 336 | 75 |
| | | Transferred to capital account | | | |
| 0 | 122 | Reconsolidation acc. to the articles of association | | 122 | 0 |
| −45 | 91 | Other transfers | | 91 | −45 |
| −45 | 213 | Total | | 213 | −45 |
| 0 | 184 | Delivery-based owner certificates | | 184 | 0 |
| – | 200 | Strategy fund | | 200 | – |
| 0 | 0 | Net revaluation acc. to the equity method | | – | – |
| – | – | Other reserves | | 0 | 0 |
| **30** | **933** | **Total** | | **933** | **30** |

# Balance sheet

| Parent company | | Assets | | Group | |
|---|---|---|---|---|---|
| Balance sheet at 31.12.05 | Balance sheet at 31.12.06 | DKK million | Note | Balance sheet at 31.12.06 | Balance sheet at 31.12.05 |
| | | **Fixed assets** | | | |
| | | *Intangible assets* | 7 | | |
| 0 | 0 | Licences and trademarks, etc. | | 163 | 152 |
| – | – | Group goodwill | | 2,284 | 1,847 |
| 713 | 578 | Development projects | | 621 | 755 |
| **713** | **578** | **Total** | | **3,068** | **2,754** |
| | | *Property, plant and equipment* | 8 | | |
| 1,726 | 1,628 | Land and buildings | | 4,986 | 4,918 |
| 2,051 | 2,129 | Plant and machinery | | 4,894 | 4,914 |
| 49 | 55 | Fixtures and fittings, tools and equipment | | 392 | 405 |
| 346 | 213 | Assets in course of construction | | 555 | 781 |
| **4,172** | **4,025** | **Total** | | **10,827** | **11,018** |
| | | *Investments* | 9 | | |
| 1,115 | 1,736 | Investments in subsidiaries | | – | – |
| 2,456 | 3,322 | Subordinate loans to subsidiaries | | – | – |
| 24 | 143 | Investments in associates | | 501 | 288 |
| – | – | Deferred tax assets | | 654 | 749 |
| 703 | 150 | Other securities and investments | | 712 | 873 |
| **4,298** | **5,351** | **Total** | | **1,867** | **1,910** |
| **9,183** | **9,954** | **Total fixed assets** | | **15,762** | **15,682** |
| | | **Current assets** | | | |
| | | *Inventories* | | | |
| 590 | 569 | Raw materials and consumables | | 960 | 989 |
| 769 | 755 | Work in progress | | 795 | 850 |
| 233 | 226 | Finished goods and goods for resale | | 1,866 | 1,854 |
| **1,592** | **1,550** | **Total** | | **3,621** | **3,693** |
| | | *Receivables* | | | |
| 995 | 1,074 | Trade receivables | | 5,120 | 5,140 |
| 1,607 | 2,662 | Amounts owed by subsidiaries | | – | – |
| 55 | 6 | Amounts owed by associates | | 22 | 77 |
| 214 | 114 | Other receivables | | 566 | 940 |
| 77 | 87 | Prepayments | | 147 | 163 |
| **2,948** | **3,943** | **Total** | | **5,855** | **6,320** |
| **0** | **276** | **Securities** | | **772** | **644** |
| **21** | **74** | **Cash at bank and in hand** | | **601** | **718** |
| **4,561** | **5,843** | **Total current assets** | | **10,849** | **11,375** |
| **13,744** | **15,797** | Total assets | | **26,611** | **27,057** |

| Parent company | | Equity, minority interests and liabilities | | Group | |
|---|---|---|---|---|---|
| Balance sheet at 31.12.05 | Balance sheet at 31.12.06 | DKK million | Note | Balance sheet at 31.12.06 | Balance sheet at 31.12.05 |
| | | **Equity** | | | |
| 6,505 | 6,757 | Capital account | | 6,757 | 6,505 |
| 275 | 183 | Reserve fund A | | 183 | 275 |
| 185 | 335 | Delivery-based owner certificates | | 335 | 185 |
| – | 200 | Strategy fund | | 200 | – |
| 500 | 500 | Reserve fund B | | 500 | 500 |
| 0 | 0 | Net revaluation acc. to the equity method | | – | – |
| −54 | −4 | Hedging instruments | | 22 | −81 |
| – | – | Other reserves | | −26 | 27 |
| **7,411** | **7,971** | **Total equity** | | **7,971** | **7,411** |
| **–** | **–** | **Minority interests** | 10 | **62** | **14** |
| | | **Provisions** | | | |
| 0 | 0 | Deferred tax | 11 | 302 | 331 |
| 0 | 0 | Pension commitments | 12 | 2,875 | 3,035 |
| 62 | 38 | Other provisions | 13 | 394 | 273 |
| **62** | **38** | **Total provisions** | | **3,571** | **3,639** |
| | | **Liabilities other than provisions** | | | |
| | | *Long-term liabilities* | 14 | | |
| 1,000 | 1,000 | Subordinate bond loan | | 1,000 | 1,000 |
| 99 | 66 | Subordinate loan, Arla ekonomisk förening | | 66 | 99 |
| 1,704 | 1,882 | Mortgage credit institutions | | 2,946 | 2,659 |
| 889 | 870 | Credit institutions | | 3,454 | 3,372 |
| **3,692** | **3,818** | **Total** | | **7,466** | **7,130** |
| | | *Short-term liabilities* | | | |
| 73 | 53 | Short-term portion of long-term liabilities | | 71 | 217 |
| 2 | 44 | Bank loans and overdrafts | | 1,707 | 2,771 |
| 75 | 336 | Supplementary payments | | 336 | 75 |
| 1,110 | 1,190 | Trade payables | | 3,287 | 3,396 |
| 550 | 1,746 | Amounts owed to subsidiaries | | – | – |
| 0 | 0 | Amounts owed to associates | | 3 | 23 |
| 26 | 0 | Tax | | 47 | 62 |
| 743 | 582 | Other payables | | 2,071 | 2,319 |
| 0 | 19 | Deferred income | | 19 | 0 |
| **2,579** | **3,970** | **Total** | | **7,541** | **8,863** |
| **6,271** | **7,788** | **Total liabilities other than provisions** | | **15,007** | **15,993** |
| **13,744** | **15,797** | Total equity, minority interests and liabilities | | **26,611** | **27,057** |
| | | Contingent liabilities, securities, etc. | 15 | | |
| | | Related parties | 16 | | |

# Statement of changes in equity

**Group**

| DKK million | Balance at 31.12.05 | Profit for the year | Exchange rate adjustments | Other adjustments | Payments for the year | Balance at 31.12.06 |
|---|---|---|---|---|---|---|
| Capital account before change in policy | 6,596 | – | – | – | – | – |
| Effect of changes in accounting policy | −91 | – | – | – | – | – |
| **Capital account after change in policy** | **6,505** | 213 | 28 | 11 | 0 | 6,757 |
| Reserve fund A | 275 | 0 | 0 | 0 | −92 | 183 |
| Delivery-based owner certificates | 185 | 184 | 0 | 0 | −34 | 335 |
| Strategy fund | – | 200 | 0 | 0 | 0 | 200 |
| Reserve fund B | 500 | 0 | 0 | 0 | 0 | 500 |
| Hedging instruments | −81 | 0 | 0 | 103 | 0 | 22 |
| Other reserves | 27 | 0 | 0 | −53 | 0 | −26 |
| **Total** | **7,411** | **597** | **28** | **61** | **−126** | **7,971** |

**Parent company**

| DKK million | Balance at 31.12.05 | Profit for the year | Exchange rate adjustments | Other adjustments | Payments for the year | Balance at 31.12.06 |
|---|---|---|---|---|---|---|
| Capital account before change in policy | 6,596 | – | – | – | – | – |
| Effect of changes in accounting policy | −91 | – | – | – | – | – |
| **Capital account after change in policy** | **6,505** | 213 | 28 | 11 | 0 | 6,757 |
| Reserve fund A | 275 | 0 | 0 | 0 | −92 | 183 |
| Delivery-based owner certificates | 185 | 184 | 0 | 0 | −34 | 335 |
| Strategy fund | – | 200 | 0 | 0 | 0 | 200 |
| Reserve fund B | 500 | 0 | 0 | 0 | 0 | 500 |
| Net revaluation acc. to the equity method | 0 | 0 | 0 | 0 | 0 | 0 |
| Hedging instruments | −54 | 0 | 0 | 50 | 0 | -4 |
| **Total** | **7,411** | **597** | **28** | **61** | **−126** | **7,971** |

The parent company's equity at 31.12.06 consists of:

*Capital account:*
The company's capital account consists of the undistributed equity of the company.

*Reserve fund A:*
Reserve A is reserves in return for personal accounts in the former MD Foods amba, for which the following terms apply:

1. The Board of Representatives may yearly decide for the reserves to carry interest, however not exceeding the official Danish discount rate.
2. Any decisions concerning distribution from the personal accounts shall be made by the Board of Representatives.
3. The plan is for the reserve fund to be paid out up to and including the financial year 2008.

If payments are made from Reserve A, a corresponding amount shall be paid into the capital account. In addition, DKK 280 million shall be added to the capital account through consolidation and concurrently with payments from Reserve A. DKK 210 million of this amount has been transferred to the capital account up to and including the financial year 2006 (31.12.2005: DKK 175 million).

*Delivery-based owner certificates:*
The certificates have been established in accordance with section 19, subsection 1(3) of the articles of association and accompanying regulations. Deposits on the certificates of each owner are payable on termination of membership of Arla Foods amba in accordance with the provisions of the regulations and subject to the approval of the Board of Representatives.

*Strategy fund:*
The fund was established in 2006 pursuant to article 19 (1)(7) of the Company's Articles. The Board of Representatives may decide to use the strategy fund to offset significant and temporary negative liquidity effects arising on acquisitions and integration of large companies or strategic structural measures. Notwithstanding the above objective of the fund, the Board of Representatives may use any given year's payment to the fund after a period of five years counting the year in which the contribution was made.

*Reserve fund B:*
Reserve B comprises the reserves set aside on the incorporation of the company.

*Net revaluation according to the equity method:*
The account includes net revaluation in accordance with the equity method for subsidiaries and associates.

*Hedging instruments:*
The account includes changes in the fair value of derivative financial instruments designated as and qualifying for recognition as a hedge of future cash flows.

No payments shall be made to the members of Arla Foods amba which reduce the total of the company's capital account, Reserve A and transfers from the annual profit appropriations to net revaluation according to the equity method.

# Cash flow statement

| | Group | |
|---|---|---|
| DKK million | 01.01.06<br>31.12.06 | 01.10.05<br>31.12.05 |
| **Cash flows from operating activities** | | |
| Profit for the year | 933 | 30 |
| Depreciation and impairment and other operating items without cash impact | 1,937 | 410 |
| Share of results in associates | 9 | 0 |
| Gains on disposals | −593 | 0 |
| Changes in deferred tax assets | 108 | −17 |
| Changes in inventories | 72 | −98 |
| Changes in receivables | 465 | −928 |
| Changes in provisions | −162 | −5 |
| Changes in trade payables and other payables | −312 | −410 |
| Tax paid | −103 | −25 |
| **Cash flows from operating activities** | **2,354** | **−1,043** |
| **Cash flows from investing activities** | | |
| Investment in intangible assets, net | −696 | −47 |
| Investment in property, plant and equipment | −1,792 | −599 |
| Disposals for the year of property, plant and equipment | 1,282 | 92 |
| Other investments, net | −62 | 23 |
| **Cash flows from investing activities** | **−1,268** | **−531** |
| **Cash flows from financing activities** | | |
| Supplementary payments regarding previous financial years | −75 | −369 |
| Paid out from equity | −126 | 0 |
| Changes in long-term liabilities | 190 | −256 |
| Changes in short-term liabilities | −1,064 | 1,805 |
| **Cash flows from financing activities** | **−1,075** | **1,180** |
| **Changes in cash funds and securities** | **11** | **−394** |
| Cash funds and securities at 01.01.2006 | 1,362 | 1,756 |
| **Cash funds and securities at 31.12.2006** | **1,373** | **1,362** |

# Notes

## 1 Revenue

| DKK million | Group 01.01.06 31.12.06 | Group 01.10.05 31.12.05 |
|---|---|---|
| Dairy activities | 43,547 | 11,049 |
| Other activities | 1,944 | 438 |
| **Total revenue** | **45,491** | **11,487** |

Revenue is analysed by product lines and geographical markets and is disclosed in the financial highlights.

## 2 Staff costs

| Parent company 01.10.05 31.12.05 | Parent company 01.01.06 31.12.06 | DKK million | Group 01.01.06 31.12.06 | Group 01.10.05 31.12.05 |
|---|---|---|---|---|
| | | **Staff costs:** | | |
| −560 | −2,189 | Wages, salaries and remuneration | −5,728 | −1,455 |
| −80 | −154 | Pensions | −430 | −162 |
| −6 | −13 | Other social security costs | −543 | −150 |
| **−646** | **−2,356** | **Total** | **−6,701** | **−1,767** |
| | | **Staff costs relate to:** | | |
| −498 | −1,901 | Production costs | −3,796 | −948 |
| −48 | −176 | Distribution costs | −2,046 | −560 |
| −100 | −279 | Joint costs including administration | −859 | −259 |
| **−646** | **−2,356** | **Total** | **−6,701** | **−1,767** |
| **6,250** | **5,823** | **Average number of full-time employees** | **17,933** | **19,356** |

Salaries and remuneration incl. pensions for the group include the parent company's Executive Board of DKK 13 million (01.10.2005–31.12.2005: DKK 3 million) Fees to the parent company's Supervisory Board and Board of Representatives represented DKK 14 million (01.10.2005–31.12.2005: DKK 4 million).

## 3 Depreciation/amortisation and impairment

| Parent company 01.10.05 31.12.05 | Parent company 01.01.06 31.12.06 | DKK million | Group 01.01.06 31.12.06 | Group 01.10.05 31.12.05 |
|---|---|---|---|---|
| | | **Depreciation/amortisation and impairment:** | | |
| −38 | −188 | Intangible assets | −401 | −79 |
| −135 | −593 | Property, plant and equipment | −1,448 | −355 |
| **−173** | **−781** | **Total** | **−1,849** | **−434** |
| | | **Depreciation/amortisation and impairment relate to:** | | |
| −133 | −602 | Production costs | −1,286 | −319 |
| −4 | 0 | Distribution costs | −243 | −64 |
| −36 | −179 | Joint costs including administration | −320 | −51 |
| **−173** | **−781** | **Total** | **−1,849** | **−434** |

## 4 Fee to the auditors appointed by the Board of Representatives

| Parent company | | | Group | |
|---|---|---|---|---|
| 01.10.05 31.12.05 | 01.01.06 31.12.06 | DKK million | 01.01.06 31.12.06 | 01.10.05 31.12.05 |
| | | *Audit fee* | | |
| −2 | −3 | KPMG | −12 | −5 |
| −1 | – | PricewaterhouseCoopers | – | −3 |
| | | *Other services* | | |
| −1 | −20 | KPMG | −25 | −2 |
| 0 | – | PricewaterhouseCoopers | – | 0 |
| **−4** | **−23** | **Total** | **−37** | **−10** |

## 5 Net financial items

| Parent company | | | Group | |
|---|---|---|---|---|
| 01.10.05 31.12.05 | 01.01.06 31.12.06 | DKK million | 01.01.06 31.12.06 | 01.10.05 31.12.05 |
| | | *Expenses* | | |
| 0 | −23 | Interest expenses, group enterprises | – | – |
| −82 | −203 | Other financing charges | −493 | −152 |
| **−82** | **−226** | **Total** | **−493** | **−152** |
| | | *Income* | | |
| 45 | 211 | Interest income, group enterprises | – | – |
| 6 | 39 | Other financing income | 84 | 28 |
| **51** | **250** | **Total** | **84** | **28** |
| **−31** | **24** | **Net financial items** | **−409** | **−124** |

## 6 Tax

| Parent company | | | Group | |
|---|---|---|---|---|
| 01.10.05 31.12.05 | 01.01.06 31.12.06 | DKK million | 01.01.06 31.12.06 | 01.10.05 31.12.05 |
| −12 | −32 | Tax on taxable income for the year | −93 | −4 |
| −14 | 0 | Adjustment of deferred tax | −82 | −3 |
| 16 | 3 | Correction of tax from previous years | 5 | 48 |
| **−10** | **−29** | **Total** | **−170** | **41** |

## 7 Intangible assets

**Group**

| DKK million | Licences and trademarks, etc. | Group goodwill | Product development projects | IT development project |
|---|---|---|---|---|
| Cost at 01.01.2006 before change in policy | 217 | 2,361 | 123 | 936 |
| Effect of change in accounting policy | – | –27 | – | – |
| **Cost at 01.01.2006 after change in policy** | **217** | **2,334** | **123** | **936** |
| Exchange rate adjustments | –18 | 40 | 0 | 1 |
| Additions during the year | 46 | 611 | 31 | 40 |
| Disposals during the year | 0 | –32 | 0 | 0 |
| **Cost at 31.12.2006** | **245** | **2,953** | **154** | **977** |
| Amortisation and impairment at 01.01.2006 before change in policy | –65 | –423 | –66 | –238 |
| Effect of change in accounting policy | – | –64 | – | – |
| **Amortisation and impairment at 01.01.2006 after change in policy** | **–65** | **–487** | **–66** | **–238** |
| Exchange rate adjustments | 3 | –8 | –1 | 1 |
| Amortisation and impairment for the year | –20 | –175 | –36 | –170 |
| Amortisation and impairment, discontinued assets | 0 | 1 | 0 | 0 |
| **Amortisation and impairment at 31.12.2006** | **–82** | **–669** | **–103** | **–407** |
| **Carrying amount at 31.12.2006** | **163** | **2,284** | **51** | **570** |

**Parent company**

| DKK million | | | Product development projects | IT development project |
|---|---|---|---|---|
| Cost at 01.01.2006 | | | 79 | 906 |
| Additions during the year | | | 20 | 33 |
| Disposals during the year | | | 0 | 0 |
| **Cost at 31.12.2006** | | | **99** | **939** |
| Amortisation and impairment at 01.01.2006 | | | –40 | –232 |
| Amortisation and impairment for the year | | | –24 | –164 |
| Amortisation and impairment, discontinued assets | | | 0 | 0 |
| **Amortisation and impairment at 31.12.2006** | | | **–64** | **–396** |
| **Carrying amount at 31.12.2006** | | | **35** | **543** |

## 8 Property, plant and equipment

**Group**

| DKK million | Land and buildings | Plant and machinery | Fixtures and fittings, tools, etc. | Assets in course of construction |
|---|---|---|---|---|
| Cost at 01.01.2006 | 5,863 | 9,326 | 1,374 | 781 |
| Exchange rate adjustments | 81 | 137 | 11 | 13 |
| Additions during the year | 507 | 473 | 262 | 550 |
| Transferred during the year | 173 | 616 | 0 | −789 |
| Disposals for the year | −583 | −726 | −298 | 0 |
| **Cost at 31.12.2006** | **6,041** | **9,826** | **1,349** | **555** |
| Depreciation and impairment at 01.01.2006 | −945 | −4,412 | −969 | 0 |
| Exchange rate adjustments | −10 | −62 | −15 | 0 |
| Depreciation and impairment for the year | −300 | −1,007 | −141 | 0 |
| Depreciation and impairment, discontinued assets | 200 | 549 | 168 | 0 |
| **Depreciation and impairment at 31.12.2006** | **−1,055** | **−4,932** | **−957** | **0** |
| **Carrying amount at 31.12.2006** | **4,986** | **4,894** | **392** | **555** |
| **Assets held under finance lease** | **7** | **133** | **6** | **0** |

The latest official annual valuation of Danish land and buildings with a carrying amount of DKK 2,139 million is assessed at DKK 1,512 million.

**Parent company**

| DKK million | Land and buildings | Plant and machinery | Fixtures and fittings, tools, etc. | Assets in course of construction |
|---|---|---|---|---|
| Cost at 01.01.2006 | 2,366 | 4,319 | 91 | 346 |
| Additions during the year | 36 | 225 | 25 | 213 |
| Transferred during the year | 32 | 314 | 0 | −346 |
| Disposals for the year | −73 | −182 | −11 | 0 |
| **Cost at 31.12.2006** | **2,361** | **4,676** | **105** | **213** |
| Depreciation and impairment at 01.01.2006 | −640 | −2,268 | −42 | 0 |
| Depreciation and impairment for the year | −137 | −441 | −15 | 0 |
| Depreciation and impairment, discontinued assets | 44 | 162 | 7 | 0 |
| **Depreciation and impairment at 31.12.2006** | **−733** | **−2,547** | **−50** | **0** |
| **Carrying amount at 31.12.2006** | **1,628** | **2,129** | **55** | **213** |
| **Assets held under finance lease** | **0** | **23** | **0** | **0** |

The latest official annual valuation of Danish land and buildings with a carrying amount of DKK 1,628 million is assessed at DKK 1,016 million.

## 9 Investments

**Group**

| DKK million | | | Investments in associates | Deferred tax assets | Other securities and investments |
|---|---|---|---|---|---|
| Cost at 01.01.2006 | | | 368 | 812 | 815 |
| Additions during the year | | | 214 | 0 | 716 |
| Disposals during the year | | | 0 | 0 | –809 |
| **Cost at 31.12.2006** | | | **582** | **812** | **722** |
| Adjustments at 01.01.2006 | | | –80 | –63 | 58 |
| Results for the year | | | –9 | –108 | 0 |
| Exchange rate adjustments | | | –3 | 13 | 2 |
| Disposals, adjustments | | | 0 | 0 | –50 |
| Other adjustments | | | 11 | 0 | –20 |
| **Adjustments at 31.12.2006** | | | **–81** | **–158** | **–10** |
| **Carrying amount at 31.12.2006** | | | **501** | **654** | **712** |
| **Of which goodwill at 31.12.2006** | | | **7** | | |

A deferred tax asset of DKK 90 million has not been recognised as it is not expected to be utilised.

**Parent company**

| DKK million | Investments in subsidiaries | Subordinate loans to subsidiaries | Investments in associates | Deferred tax assets | Other securities and investments |
|---|---|---|---|---|---|
| Cost at 01.01.2006 | 1,375 | 2,474 | 39 | – | 618 |
| Additions during the year | 512 | 875 | 127 | – | 8 |
| Disposals during the year | 0 | –38 | 0 | – | –513 |
| **Cost at 31.12.2006** | **1,887** | **3,311** | **166** | **–** | **113** |
| Adjustments at 01.01.2006 before change in policy | –169 | –18 | –15 | – | 85 |
| Effect of change in accounting policy | –91 | – | – | – | – |
| **Adjustments at 01.01.2006 after change in policy** | **–260** | **–18** | **–15** | **–** | **85** |
| Distribution/dividends during the year | –384 | – | 0 | – | 0 |
| Results for the year | 492 | – | 0 | – | 0 |
| Goodwill amortisation for the year | –23 | – | –7 | – | 0 |
| Changes in intra-group profit on inventories | 2 | – | 0 | – | 0 |
| Exchange rate adjustments | 25 | – | 1 | – | 2 |
| Disposals, adjustments | 0 | 29 | 0 | | –57 |
| Other adjustments | –3 | 0 | –2 | – | 7 |
| **Adjustments at 31.12.2006** | **–151** | **11** | **–23** | **–** | **37** |
| **Carrying amount at 31.12.2006** | **1,736** | **3,322** | **143** | **–** | **150** |
| **Of which goodwill at 31.12.2006** | **107** | | **7** | | |

## 10 Minority interests

**Group**

| DKK million | 01.01.06 31.12.06 | 01.10.05 31.12.05 |
|---|---|---|
| Minority interests, beginning of year | 14 | 14 |
| Share of results for the year | 4 | 0 |
| Additions and disposals, changes in ownership shares, etc. | 44 | 0 |
| **Minority interests, year end** | **62** | **14** |

## 11 Deferred tax

| Parent company | | | Group | |
|---|---|---|---|---|
| 01.10.05<br>31.12.05 | 01.01.06<br>31.12.06 | DKK million | 01.01.06<br>31.12.06 | 01.10.05<br>31.12.05 |
| | | **Provided for deferred tax** | | |
| 14 | 0 | Deferred tax, beginning of year | 331 | 313 |
| 0 | 0 | Exchange rate adjustments | 10 | −2 |
| – | – | Disposal on divestment of subsidiary | −13 | 0 |
| −14 | 0 | Other changes during the year | −26 | 20 |
| **0** | **0** | **Provided for deferred tax, year end** | **302** | **331** |

Deferred tax primarily relates to property, plant and equipment in the UK and Sweden.

## 12 Pensions

**Group**

The provision comprises defined benefit schemes in Sweden and the UK. The defined benefit schemes ensure pension to the employees covered based on final salary.

*The net pension commitment is recognised in the balance sheet as follows:*

| DKK million | 31.12.06 | 31.12.05 |
|---|---|---|
| Present value of defined benefit schemes | 8,951 | 8,567 |
| Market value of plan assets | −6,180 | −5,584 |
| Net pension commitment | 2,771 | 2,983 |
| Non-recognised actuarial gains, net | 104 | 52 |
| **Total** | **2,875** | **3,035** |

*Development in net pension commitment:*

| DKK million | 01.01.06<br>31.12.06 | 01.10.05<br>31.12.05 |
|---|---|---|
| Net pension commitment recognised in the balance sheet, beginning | 3,035 | 3,063 |
| Exchange rate adjustments | 84 | −23 |
| Expensed in the income statement, net | 25 | 75 |
| Group payments, plan assets | −269 | −80 |
| **Net pension commitment recognised in the balance sheet, year end** | **2,875** | **3,035** |

The defined benefit schemes in the UK are administered by independent pension funds who invest the amounts paid to cover the commitments. The actuarial present value of the commitments (DKK 8,034 million at 31.12.2006 against DKK 7,663 million at 31.12.2005) less the market value of the assets (DKK 6,180 million at 31.12.2006 against DKK 5,584 million at 31.12.2005) amounts to DKK 1,854 million. Following the use of the corridor method, the actuarial gain of DKK 197 million has not reduced the provision, as the net commitment therefore totalled DKK 2,051 million at 31.12.2006.

The defined benefit schemes in Sweden are not covered by payments to pension funds.

The actuarial present value of the commitments is recognised in the balance sheet at DKK 917 million against DKK 904 million at 31.12.2005. As the limit value of the corridor was exceeded at 01.01.2006, DKK 3 million was expensed during the year. Following the use of the corridor method, the actuarial loss of DKK 93 million has not increased the provision, and the net commitment therefore totalled DKK 824 million at 31.12.2006.

Pension costs for the year regarding defined benefit schemes total DKK 25 million. These costs are recognised in note 2.

## 12 Pensions (continued)

*Pension assets relate to:*

| DKK million | 31.12.06 | 31.12.05 |
|---|---|---|
| Shares | 3,599 | 3,906 |
| Bonds | 1,649 | 1,279 |
| Properties | 708 | 389 |
| Other assets | 224 | 10 |
| **Total** | **6,180** | **5,584** |

*Return on pension assets:*

| DKK million | 01.01.06<br>31.12.06 | 01.10.05<br>31.12.05 |
|---|---|---|
| Expected return on plan assets | 342 | 92 |
| Actuarial gains/losses on plan assets for the year (not recognised) | 159 | 236 |
| **Actual return on plan assets** | **501** | **328** |

The group expects to pay DKK 339 million to defined pension schemes in 2007.

*The assumptions for the actuarial calculations at the balance sheet date are as follows (on average):*

| | 31.12.06 | 31.12.05 |
|---|---|---|
| Discounting rate | 5.01% | 4.66% |
| Future payroll increase | 2.7–4.5% | 2.7–4.15% |
| Expected return on plan assets | 6.39% | 7.02% |
| Expected return on plan assets is determined by external actuaries based on the composition of assets and general expectations of the financial development | | |

## 13 Other provisions

| Parent company | | | Group | |
|---|---|---|---|---|
| 01.10.05<br>31.12.05 | 01.01.06<br>31.12.06 | DKK million | 01.01.06<br>31.12.06 | 01.10.05<br>31.12.05 |
| 79 | 62 | Other provisions, beginning of year | 273 | 293 |
| 0 | 18 | Provisions during the year | 226 | 30 |
| −17 | −42 | Disposals during the year | −105 | −50 |
| **62** | **38** | **Other provisions, year end** | **394** | **273** |
| 31.12.05 | 31.12.06 | DKK million | 31.12.06 | 31.12.05 |
| 0 | 0 | Insurance provisions | 113 | 85 |
| 21 | 7 | Restructuring | 25 | 21 |
| 41 | 31 | Other provisions | 256 | 167 |
| **62** | **38** | **Total** | **394** | **273** |

## 14 Long-term liabilities

| Parent company | | | Group | |
|---|---|---|---|---|
| 31.12.05 | 31.12.06 | DKK million | 31.12.06 | 31.12.05 |
| | | *Long-term liabilities falling due more than five years after the balance sheet date* | | |
| 1,000 | 1,000 | Subordinate bond loan | 1,000 | 1,000 |
| 920 | 1,823 | Other long-term liabilities | 2,380 | 1,920 |
| **1,920** | **2,823** | **Total** | **3,380** | **2,920** |

## 15 Contingent liabilities, security, etc.

| Parent company | | | Group | |
|---|---|---|---|---|
| 31.12.05 | 31.12.06 | DKK million | 31.12.06 | 31.12.05 |
| 4,508 | 3,944 | Surety and guarantee obligations | 667 | 1,043 |
| 90 | 127 | Operating lease commitments | 1,367 | 1,622 |
| 395 | 404 | Obligations relating to agreement on delivery of fixed assets | 548 | 753 |
| | | *To cover exchange risks, the following forward contracts have been entered into:* | | |
| 422 | 668 | Forward contracts (buying) | 1,551 | 2,094 |
| 5,883 | 5,247 | Forward contracts (selling) | 5,564 | 6,271 |
| 1,277 | 2,376 | Interest swaps | 3,955 | 2,755 |
| | | *The following assets are deposited as security for debt:* | | |
| 155 | 118 | Owner's mortgage in real estate | 1,342 | 1,076 |
| 544 | 255 | with a carrying amount of | 1,199 | 1,045 |
| 0 | 0 | Securities, carrying amount | 0 | 410 |

*Share-based remuneration schemes in subsidiary:*
There are a number of share option schemes in the subsidiary Arla Foods UK plc whose values depend on the price of the shares in Arla Foods UK plc. These remuneration schemes give employees and Management in Arla Foods UK plc the opportunity to buy shares in the company over a number of years at a predetermined price provided that certain conditions are fulfilled. The total costs for share-based remuneration totalled DKK 5 million in the year 01.01.2006 – 31.12.2006 (DKK 3 million in 01.10.2005–31.12.2005). The shares that may be acquired by Management and employees by using the share option schemes comprise 1.4% of the total share capital in Arla Foods UK plc. Neither the Executive nor the Supervisory Board of Arla Foods amba have received share-based remuneration giving the opportunity to buy shares in Arla Foods UK plc.

*Lawsuits:*
The group is a party to a few lawsuits. The outcome of these cases is not expected to significantly affect the assessment of the financial position.

## 16 Related parties

Arla Foods amba has no related parties exercising control.

Related parties exercising significant influence comprise the Board of Representatives, the Executive and the Supervisory Boards. In addition, group enterprises and associates are related parties, see the group chart on pages 32–33.

Members of the Board of Representatives and/or the Supervisory Board are paid for milk deliveries to Arla foods amba on equal terms with other members of the company.

There have been no other transactions with related parties during the year apart from intra-group transactions that have been eliminated in the consolidated financial statements.

Salaries and remuneration have been disclosed separately in the note regarding staff costs.

# Group chart

## Subsidiaries, associates and other investments at 31 December 2006

**Ownership** **Subsidiaries**

100% **Arla Foods AB, Sweden**

- L&L International (Sweden) aktiebolag, Sweden (100%)
- Bregott AB, Sweden (98%)
- FRAS Integration AB, Sweden (69%)

100% **Arla Foods Holding AB, Sweden**

- Oy Arla Foods AB, Finland (100%)

100% **Arla Foods Holding A/S, Denmark**

- Arla Foods International A/S, Denmark (100%)
    - Danya Foods Ltd., Saudi-Arabia (75%)
    - Arla Foods UK Holding Ltd., the UK (100%)
        - Arla Foods UK Plc., the UK (51%)
            - Arla Foods Ltd., the UK (100%)
            - Express Ltd., the UK (100%)
                - Claymore Dairies Ltd., the UK (75%)
- AF A/S, Denmark (100%)
    - Arla Foods Finance A/S, Denmark (100%)
        - Kingdom Food Products ApS, Denmark (100%)
        - Ejendomsanpartsselskabet St. Ravnsbjerg, Denmark (100%)
    - Rynkeby Foods A/S, Danmark (50%. The remaining 50% is held by Kinmaco ApS)
    - Kinmaco ApS, Denmark (100%)
        - Arla Foods Energy A/S, Denmark (100%)
    - Arla Insurance Company (Guernsey) Limited, Guernsey (100%)
    - Arla Foods Trading A/S, Denmark (100%)
- Arla Foods Distribution A/S, Denmark (100%)
    - Danmark Protein A/S, Denmark (100%)
    - Delimo A/S, Denmark (100%)
        - Delimo Sverige AB, Sweden (100%)
            - Rosamunda AB, Sweden (51%)
                - Delimo AB, Sweden (100%)
- Medlemsartikler ApS, Denmark (100%)
- Arla Foods Ingredients GmbH, Germany (100%)
- Fidan A/S, Denmark (100%)
    - Dairy Fruit A/S, Denmark (100%)
    - A/S Crispy Food International, Denmark (100%)
- Procudan A/S, Denmark (51%)
- Danapak Holding A/S, Denmark (100%)
    - Danapak A/S, Denmark (100%)
        - Danapak WP A/S, Denmark (100%)
- Tholstrup International B.V., the Netherlands (100%)
    - Tholstrup Cheese Holding A/S, Denmark (99%)
        - Tholstrup Cheese A/S, Denmark (100%)
            - Tholstrup Cheese GmbH & Co KG, Germany (100%)
            - Thosltrup Cheese USA Inc, USA (100%)
        - Tholstrup Cheese AB, Sweden (100%)
        - Pastella A/S, Denmark (100%)
- Arla Kallassi Foods Lebanon S.A.L., Lebanon (50%)

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|---|---|
| 100% | Arla Foods AS, Norway |
| 100% | Arla Foods Inc., Canada |
| 100% | Arla Foods GmbH, Germany |
| 100% | Arla Foods S.r.l., Italy |
| 100% | Arla Foods Inc., USA |
| 100% | Arla Foods S.A.R.L., France |
| 100% | Arla Foods S.A., Spain |
| 100% | Arla Foods Hellas S.A., Greece |
| | |
| 100% | **Arla Foods Ingredients amba, Denmark** |
| | Arla Foods Ingredients Inc., USA (100%) |
| | Arla Foods Ingredients KK, Japan (100%) |
| | Arla Foods Ingredients AB, Sweden (100%) |
| | Arla Foods Ingredients S.A. de C.V., Mexico (100%) |
| | Arla Foods Ingredients Korea Co. Ltd., South Korea (70%) |
| | |
| 100% | Arla Foods Sp. Z o.o., Poland |
| 100% | Arla Foods SA, Poland |
| 100% | Frödinge Holding AB, Sweden |
| | |
| 100% | **Medipharm Holding AB, Sweden** |
| | Medipharm AB, Sweden (100%) |
| | Medipharm Investments Ltd., USA (100%) |
| | Medipharm CZ s.r.o., Czech Republic (100%) |
| | Medipharm Hungary Kft, Hungary (66%) |
| | |
| 100% | Rasmus Hansen Eksport K/S, Denmark[1)] |
| 100% | Danos Eksport K/S, Denmark[1)] |
| 100% | Kohave Foods Eksport K/S, Denmark[1)] |
| 100% | Chesco Cheese Eksport K/S, Denmark[1)] |
| 100% | Rasmus Hansen Oversøisk K/S, Denmark[1)] |
| 100% | DOFO Cheese Eksport K/S, Denmark[1)] |
| 100% | Danske Landmænd Eksport K/S, Denmark[1)] |
| 100% | Oerum Dairies Eksport K/S, Denmark[1)] |
| 100% | Boel Foods Eksport K/S, Denmark[1)] |
| 100% | Marygold Trading K/S, Denmark[1)] |
| 100% | Enico Trading K/S, Denmark[1)] |
| 95% | Andelssmør A.m.b.a., Denmark |
| 92% | Mejeriforeningen, Denmark |
| | MA PROJECT A/S, Denmark (100%) |
| 75% | AFF P/S, Denmark |
| | |
| | **Associates** |
| 50% | JO-Bolaget Fruktprodukter HB, Sweden (owned through Arla Foods AB) |
| 50% | HB Grådö Produktion, Sweden (owned through Arla Foods AB) |
| 50% | Synbiotics AB, Sweden (owned through Medipharm AB) |
| 50% | Arla Foods Ingredients S.A., Argentina (owned through Arla Foods Ingredients amba) |
| 50% | Biolac GmbH & Co. KG, Germany, (owned through Arla Foods Ingredients GmbH) |
| 50% | Dan Vigor Ltda., Brazil (owned through Arla Foods International A/S) |
| 50% | Cocio Chokolademælk A/S, Denmark (owned through Danmark Protein A/S) |
| 50% | Staplemead Dairy Products Ltd., the UK (owned through Express Ltd.) |
| 50% | Agri-Norcold A/S, Denmark (owned through Mejeriforeningen) |
| 49% | Mengniu Arla (inner Mongolia) Dairy Products Co., Ltd, People's Republic of China |
| 42% | Svensk Mjölk Ekonomisk förening, Sweden |
| 40% | Arla Foods Qatar WLL (owned through Arla Foods Holding A/S) |
| 40% | Danapak Flexibles Group, Denmark (owned through Danapak A/S) |
| 40% | Arla National Food Products LLC, United Arab Emirates |
| 35% | K/S Danske Immobilien, Denmark (owned through Arla Foods Finance A/S) |
| | |
| | **Other investments** |
| 19% | Lantbrukarnas Riksförbund, förening upa, Sweden |

*1) The companies are owned equally by Arla Foods amba and Arla Foods Ingredients amba (50/50).*

The group moreover owns a number of companies without commercial activities.

# Supervisory Board

*From left:*
Chairman **Knud Erik Jensen**, born 1943
330 cows, Grenå, Denmark
Board member since 1981

**Anders Ericsson,** born 1942
195 cows, Ramdala, Sweden
Board member since 1988

**Pejter Søndergaard**, born 1947
120 cows, Vestervig, Denmark
Board member since 2002

*From left:*
Deputy Chairman **Åke Hantoft**, born 1952
220 cows, Laholm, Sweden
Board member since 1998

**Jan Toft Nørgaard**, born 1960
300 cows, Skærbæk, Denmark
Board member since 1998

**Erik Karlsson**, born 1954
75 cows, Karlskoga, Sweden
Board member since 2005

*From left:*
**Leif Backstad**, born 1947
Employee, Lindhagensgatan in Stockholm.
Lives in Ekerö, Sweden
Board member since 2001

**Sören Kihlberg**, born 1955
60 cows, Björkvik, Sweden
Board member since 1996

**Bent Juul Sørensen**, born 1958
283 cows, Ærøskøbing, Denmark
Board member since 1998

*From left:*
**Bengt Darhult**, born 1945
320 cows, Heberg, Sweden
Board member since 2005

**Viggo Ølgaard Bloch**, born 1955
120 cows, Varde, Denmark
Board member since 2003

**Bjarne Bundesen**, born 1958
Employee at Christiansfeld Dairy Centre.
Lives in Rødekro, Denmark
Board member since 2003

*From left:*
**Ove Møberg**, born 1948
80 cows, Hejnsvig, Denmark
Board member since 1992

**Gunnar Pleijert**, born 1949
100 cows, Mörlunda, Sweden
Board member since 2003

**Steen Nørgaard Madsen**, born 1956
135 cows, Silkeborg, Denmark
Board member since 2005

*From left:*
**Thomas Johansen**, born 1959
165 cows, Egtved, Denmark
Board member since 2002

**Steen Bolvig**, born 1956
Employee, Hoco.
Lives in Holstebro, Denmark
Board member since 2003

**Torben Myrup**, born 1956
150 cows, Aars, Denmark
Board member since 2006

**Johan von Schéele**, born 1946
150 cows, Hasselfors, Sweden
Board member since 2005

*Not present for the photograph:*
**Leif Eriksson,** born 1951. Works at the powder plant in Götene, lives in Lidköping, Sweden. Board member since 1998.

# Executive Management Board

**CORPORATE CENTRE**
EXECUTIVE BOARD

CEO **Peder Tuborgh**

Vice CEO **Andreas Lundby**

Vice CEO **Povl Krogsgaard**

**CORPORATE FINANCE/IT**

Executive Director, CFO
**Jørn Wendel Andersen**

**CONSUMER NORDIC**

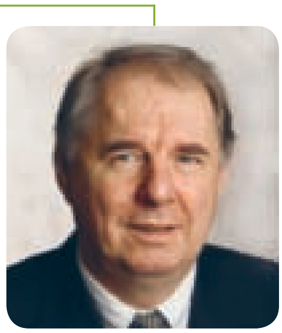
Executive Director
**Hans-Åke Hammarström**

**CONSUMER UK**

Executive Director
**Kim Nielsen**

**CONSUMER INTERNAT.**

Executive Director
**Mikael Sternberg Christiansen**



**GLOBAL INGREDIENTS**

Executive Director
**Peter Lauritzen**

Project co-ordinator Arla Foods:
Lisbeth Storgaard, Ulrika Gyllenvik and
Carsten Just Andersen
Design: Waldton
Production: Formalix
Project co-ordinator agency: Anna Michélsen
Illustrations: Martin Gradén
Translation: Katie Schwarck
Photo: cover and portraits: Niels Åge Skovbo,
Photo: Supervisory Board: Jörgen Lindström, other
Håkan Lindgren, Fabio Galli, Lisbeth Storgaard and
Jörgen Lindström.
Printing: Scanprint A/S

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