Annual Report 2002/03

Financial highlights

GROUP MDKK	02.09.30 –03.09.30	01.10.01 –02.09.29	00.10.02 –01.09.30	00.04.17 –00.10.01
Profit				
Turnover	40.647	39.441	38.133	17.453
outside DK / SE	20.781	19.807	18.823	8.200
% outside DK / SE	51%	50%	49%	47%
Operating profit	1.242	1.411	1.596	547
Interest income and expense etc.	–245	-367	–381	-159
Profit for the year	1.094	1.085	1.157	392
Supplementary payments	546	575	690	276
Consolidation:				
Reconsolidation	123	126	122	0
Other consolidation	425	384	345	116
Financing				
Balance sheet total	26.845	22.017	20.858	21.275
Fixed assets	13.973	10.395	10.523	11.055
Investments in tangible assets	2.062	1.919	1.804	875
Capital base	7.399	7.101	6.448	6.343
Equity ratio				
Measured in %	28%	32%	31%	30%
Inflow of raw milk				
Total million kg. weighed in in the group	7.241	7.041	7.085	3.344
hereof in DK	4.137	3.964	3.967	1.914
hereof in SE	2.114	2.157	2.167	993
others	990	920	951	437
Number of members	**12.758**	**13.642**	**14.909**	**16.121**
hereof in DK	6.625	7.103	7.921	8.639
hereof in SE	6.133	6.539	6.988	7.482
Employees				
Number of employees (man years)	17.791	17.866	18.200	18.622

The comparative figures for the years 2000 and 2000 / 2001 have not been changed in connection.

TURNOVER

DKK million	02.09.30 –03.09.30	01.10.01 –02.09.29
Analysed by markets		
1. Sweden	10.216	10.281
2. Denmark	9.650	9.353
3. Other EU countries	13.694	12.960
4. Rest of Europe	885	770
5. Middle East	2.628	2.445
6. North America	1.030	1.018
7. Central and South America	707	871
8. Asia	1.248	1.264
9. Africa	561	457
10 Other	28	22
Total	**40.647**	**39.441**

DKK million	02.09.30 –03.09.30	01.10.01 –02.09.29
Analysed by product groups		
11 Fresh products	16.115	15.893
12 Cheese	10.784	10.606
13 Butter and spreads	5.325	5.120
14 Condensed milk products	5.812	5.410
15 Packaging	729	974
16 Other goods	1.882	1.438
Total	**40.647**	**39.441**

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The United Kingdom became a major focus area during the 2002/03 financial year after Arla Foods announced on March 27 that it had started merger negotiations with Express Dairies plc. The merger was approved on October 15, 2003 and the new company, Arla Foods UK plc, is now the UK's leading supplier of dairy products.

Erik Refner is responsible for the photographs in this Annual Report which depict aspects of daily life in Arla Foods' third home market, the UK.


LURPAK
BUTTER
SLIGHTLY SALTED

The Chairman’s report

In September, the Board of Representatives finally parted with the two companies, MD Foods and Arla ek. för and, at the same time, welcomed the new joint company with a common milk price for Danish and Swedish co-operative members from October 1, 2003.

Thus we have achieved the goal we set ourselves three years ago: to harmonise all important aspects of our operations to create identical conditions for all co-operative members.

From October 2004, we shall, therefore, introduce common conditions for our organic members and the tax issues relating to payments have been clarified so that we can operate on the basis of one common payment system. The Articles of Association are also in place with regard to all important economic conditions although the softer issues, electoral eligibility and the electoral system, have yet to be harmonised. With regard to these, we have decided to maintain respect for the national democratic traditions.

The debate regarding consolidation continues among co-operative members. The aim is to present a proposal on the issue to the Board of Representatives in 2004.

The pleasure in coming so far in the merger process is, however, overshadowed by the fall in the milk price and a decline in our earnings as milk producers. In view of this, the structural development among milk producers will continue undiminished. The dairy sector now faces considerable challenges with regard to generating increased earnings for the owners.

We were, however, not unprepared for the EU reform. Now that we are familiar with its content and realise that the cutbacks will not stop here, the framework for the further process has been laid down.

We should take pride in the fact that, over many years, we have invested in the development of a dairy group with the capacity for providing its customers with added value products.

Together with rigorous efficiency requirements, the continued development of our company will contribute towards ensuring our survival. On the backdrop of the substantial price pressure to which the company is subject, the 2002/03 results can be regarded as satisfactory.

Moreover, we were delighted to obtain the UK authorities’ approval of the merger between Arla Foods plc and Express Dairies plc. The British milk market has been characterised by considerable instability and the merger will significantly contribute to greater stability in the market.

Over the coming period, we shall continue to debate Arla Foods’ Vision 2010. The current strategy plan is nearing completion and based on the objective of ensuring the best possible milk price for milk producers, we shall now strive to agree on how we proceed towards this goal.

Finally, I would like to extend my sincere thanks to our retiring Managing Director, Jens Bigum, for his great contribution to the company over the past 33 years.

Knud Erik Jensen
Chairman

Since it was named “a product of the highest quality” at the World Exhibition in London in 1879, Danish butter, under the name of Lurpak, has enjoyed a prominent position in the UK market. Douglas the Butterman, who has represented Lurpak in TV commercials since 1986, has become as famous as the butter itself.

Management's report

Falling exchange rates, unfavourable economic trends and a decline in export subsidies are now fully impacting on the Group. Accordingly, the forecasts given in April's Interim Report have proved accurate. Under such difficult conditions, Arla Foods' result for 2002/03 should be regarded as satisfactory.

As expected, clearer contours for the future emerged during the year. First and foremost, the politicians agreed on a reform of the EU's agricultural policy under which the intervention prices for butter and skimmed milk powder will be reduced in increments from July 1, 2004. Then followed the EU's decision concerning the forthcoming enlargement towards the East which, in the short-term, will create turbulence in the market, particularly for skimmed milk powder, but which will, in the longer-term, open up opportunities in the new member states.

In 2002/03, the markets were characterised by increased pressure on sales of bulk products and the multiples' strategy of increasing sales of own label products.

The home markets in Sweden and Denmark were characterised by tougher competition from, for instance, imports of yoghurt in the Swedish market and general pressure from importers in the Danish market. The result in the UK was highly satisfactory – both in terms of local milk production and products imported from Denmark and Sweden.

Sales in the Middle East and North America developed satisfactorily, although trends in South East Asia were adversely affected by the SARS outbreak in the summer of 2003.

Devaluations had a negative effect on sales in South America. However, this had the reverse effect on locally produced milk proteins from Arla Foods' protein factory in Argentina. Production here is running on schedule and milk proteins are exported to several countries in the region, including Mexico.

Strategy plan

The highlight of the year was the breakthrough in the UK market where Arla Foods' UK subsidiary announced a merger with Express Dairies plc in late March 2003. The merger, which was approved by the British competition authorities in October 2003, makes the new joint company the largest supplier of liquid milk in the UK market.

The ongoing company, Arla Foods UK plc, is listed on the London Stock Exchange.

Late in the financial year, Arla Foods Board of Representatives initiated a new vision debate: Vision 2010. The draft for the vision will be discussed among Arla Foods' co-operative owners in the winter of 2003/04 so that the Board of Representatives can consider it during the current financial year.

The products

The low dollar rate adversely affected Arla Foods' earnings on exports outside Europe. The stronger Euro resulted in price pressure in the European cheese market – not least in Germany where consumers are increasingly opting for discount lines as a replacement for the more expensive products in the delicatessen counters.

During the year, a joint marketing plan for Arla Foods' products for the Scandinavian market was drawn up comprising a range of fermented products and snacks.

Sales of butter increased, particularly in Danish butter's undisputed key market, the UK. There were also increasing sales of butter in a number of Middle Eastern markets, with the exception of Saudi Arabia.

Within the Ingredients area, the market was characterised by pressure on added value ingredients to the food industry.

Structural plan

The year saw strong focus on continued rationalisation of the production and comprehensive rationalisation measures were implemented within administration and production. On the production side, it was decided to close 7 dairies in accordance with the structural plan of 2001.

Of the 18 projects covered in the structural plan, 13 have been, or are about to be, implemented. Two have been put on hold indefinitely and three have not yet been approved.

The projects under the structural plan are expected to be completed during 2005.

Ett Arla

A wide ranging project for the integration of working procedures and management systems was initiated in order to achieve a more integrated company with simpler and more efficient working procedures. Ett Arla, therefore, will create stronger cohesion across divisions and national borders.

At year end, the first part of the project was implemented in the central administration and at a number of dairies. Most of the work was carried out concurrently with daily tasks which involved a significant extra workload for many staff. The project is of considerable importance to the company's daily business and future management.

HR

In 2002, the Group carried out a job satisfaction survey among its employees which showed job satisfaction among Arla Foods' employees to be good and comparable with the average for this type of survey. Managers across the organisation worked seriously with the results of the survey and a new poll was taken in November 2003. At the time of publication of this Annual Report, the results are still to be processed.

With regard to the recruitment of new dairy trainees, the desired number of trainees was recruited despite the fact that fewer younger people joined the general labour market.

Many employees across the organisation also took part in extensive further training programmes. Training programmes for staff from Sweden, UK and Denmark were also initiated.

In May 2003, the Group announced a cut of 600 in the number of administrative employees over three years. This aims at achieving stronger integration of the two former companies. The cutbacks will apply across the entire organisation.

The future

Four factors will characterise the coming year: first and foremost, the EU reform will come into force and put further pressure on the milk price. In the short-term, it is difficult to predict the full market effect of this. For the 2003/04 budget, the company has given notice of a negative change in the milk price.

Secondly, there are uncertainties regarding international economic trends. Thirdly, the EU enlargement towards the East with 10 countries joining in May 2004, is set to have a short-term negative effect with pressure on the ceiling for intervention. Finally, developments in foreign exchange markets are likely to create problems for the Group.

All in all, the future contains considerable challenges for the company and its co-operative owners. The EU reform and the enlargement towards the East have made the Group's future tasks clearer.

Jens Bigum
Managing Director

Production

During the financial year, the Danish and Swedish plants produced the following volumes within the four main areas:

1,645,000 tons fresh products
330,000 tons cheese
185,000 tons butter and spreads
305,000 tons ingredients and powder products

The most important year on year change is the significant increase in volume of butter and spreads. This is a consequence of Arla Foods assuming responsibility for Fonterra's packing of butter and spreads for the UK market from October 1, 2002.

The following changes were carried out in the production structure during 2002/03:

Cheese:

Operations at Hellevad Dairy were shut down in June 2003 and production was transferred to other Danish cheese dairies.

Falkenberg Dairy is being expanded with the intention of closing down Stånga Dairy. The process is expected to be completed by March 2004.

Kalmar Dairy is being extended in order to close Borgholm Dairy. This process is expected to be completed by June 2004.

In early summer 2003, an extension programme was initiated for Høgelund Dairy in preparation for the closure of Grenå Dairy at the end of 2004. Arla Foods' Danish Blue production will centre on Høgelund. Work is in progress to significantly expand capacity at Hostebro Flødeost.

Snejbjerg Dairy will cease operations in December 2003.

Glejbjerg Dairy will be closed on April 1, 2004 and the production will be transferred to Taulov Dairy.

Vellev Dairy will be closed on September 1, 2004 after which Hjørring Dairy will take over Vellev's production. Åseda and Vestervik dairies will be cease operations by the end of 2004. The dairies' production will be transferred to Nr. Vium Dairy and Falkenberg Dairy.

Butter:

Götene Dairy has been expanded to prepare for the transfer of butter production from Gothenburg dairy from October 1, 2003.

Fresh products:

Production at Halmstad Dairy was terminated in June 2003 and the majority of production transferred to Gothenburg Dairy.

Ingredients

In Sweden, the construction of the new powder plant in Vimmerby began in August 2003. The plant, which will have an annual capacity of 380 million kg milk, is expected to commence trial production by the end of 2004. The milk powder factories at Mjölby and Kimstad will then close. At the same time, powder production at various cheese dairies will cease.

The expansion programme at the plant at Visby has been completed, doubling the plant's capacity to an annual production of 16 million kg powder.

In Denmark, the expansion of Akafa and Arinco milk powder factories has largely been completed. As of March 31, 2004, production at the milk powder plant in Kjersing will be terminated and divided between Akafa and Arinco.

TV's Bob the Builder and his friends are a great hit with children – as are Bob the Builder cartons of fromage frais. Produced at Brabrand Dairy in Denmark, the Bob the Builder range contributes to the increasing volumes of imported brands to the UK.


87p
every day
low price

Home markets

Market conditions changed gradually during the financial year. First and foremost, the competitive pressures on all businesses within the food sector increased under the impact of strong growth within the own label and discount sectors. This, of course, also applied to Arla Foods.

In addition, the internationalisation of Arla Foods' customers continues while, multiples are expanding across national borders. At the same time, customer demand for more own label products, which favours large international operations, is increasing. In future, customer demands on Arla Foods – besides competitive and low prices – will include advanced added value and category management.

Price awareness among consumers was strengthened under the impact of the growing discount sector and the general economic slowdown. It is estimated that branded products will continue to come under pressure from competitors and, not least, from own label products. Consequently Arla Foods' is faced with the challenge of forging stronger links to consumers and meeting genuine consumer preferences with regard to the company's brands.

In the battle for market share, however, Arla Foods must also meet customer wishes for own label products within the product areas that the Group and its customers regard as suitable.

Co-operation and synergies between Denmark and Sweden are now materialising. The Denmark Division and the Sweden Division, for instance, initiatied a Nordic marketing plan in 2002/03. So far, a 100% Nordic brand has been developed which involves identical marketing and design for the Høng and Minimeal brands. The same is planned for Buko, Yoggi and Cultura. The Nordic marketing plan aims at managing the Group's Nordic brand and range development over the coming years by making use of the red Arla master brand. So far, Arla is the master brand for both countries' entire milk ranges.

Denmark

Sold volumes declined slightly during the financial year due to price pressure from own label and discount chains which now control 30% of the market for convenience goods.

There were, however, substantial differences in development within the individual categories. Sales of soups and sauces increased considerably and fermented products, flavoured milk, cheese for cooking and cream, processed and sliced cheese also advanced. Milk sales were stable as was firm cheese. However, declining EU prices for dairy products had a knock-on effect within this area. Sales within the BSM category continue to decline, but Arla Foods succeeded in stabilising its market share for butter and spreads. Organic products also suffered a slight decline.

In 2003, Arla Foods provided support to a humanitarian organisation. Via the newly developed organic product, Smoothie, Arla Foods donated DKK 1 per unit sold to the Red Cross.

The food service sector continues to grow. One of the new initiatives within this area is a chef project in which Arla Foods collaborates with several leading chefs for the purpose of creating gourmet type products for the country's top chefs.

With effect from April 1, 2003, Arla Foods acquired Karoline's Kitchen from the Danish Dairy Board in a move that will lead to increased product development of cooking products.

In the distribution area, 150 staff at the Christiansfeld Fresh Goods Terminal were made redundant towards the end of the year after the Co-op took back the distribution of fruit and vegetables. In return, the Co-op moved its milk distribution to Arla Foods. The overall outcome, therefore, was positive.

In view of Arla Foods' strong position within dairy products, it is only natural to define the main competitors outside the dairy category, e.g. the suppliers of drinks, cooked meat, breakfast products, cooking products etc. The challenge, therefore, is to ensure that the Group – with its firm base in milk – is capable of creating an attractive range which is easily accessible to future consumers in all situations.

Sweden

Arla remains a strong brand in Sweden – perhaps the strongest in the country. Nevertheless, the challenge remains to provide consumers with dairy products for all times of the day. This applies to the product itself, packaging and distribution. The work aimed at increasing the level of added value and building more convenience into the products continues.

Sales volumes in the Swedish market are relatively stable. In 2002/03, sales of milk were more or less as the year before. Fermented products, however, did not benefit from the same positive development as in the previous financial year. In particular, the market for fruit yoghurt was affected by tough competition causing Arla Foods to lose market share even if the market as a whole experienced growth. For the coming year, the objective is to regain market share. Cream products performed extremely well during 2002/03. Advances within the soup area should be mentioned, too.

Although imports of yellow cheese increased, Arla Foods is maintaining its market share in this tough market. Capacity at the cheese dairies was optimised and high and stable supply reliability was maintained. The sale of fresh cheese products, however, declined somewhat during the year. Fruit drinks saw increased competition from own label products and Arla Foods lost some volume, particularly within the long-life range.

One year ago, some supply problems arose within the fresh products range following the many production restructurings relating to the new structure for speciality products. However, the problems were quickly solved. Since November 2002, supply reliability has been very stable.

At Jönköping, a new chilling room was commissioned and work continues on increasing the level of automation to improve the working environment and to increase efficiency. During 2003/04, investments will be channelled into the construction of an extension of the packing line at Linköping and a new production line at Allingsås.

2003/04 will offer considerable challenges for the Arla Foods' organisation in Sweden. Although competition is increasing, the company must maintain and develop its market share. It is expected that the result will be somewhat lower, largely because rising costs are unlikely to be compensated for by price increases. This means, of course, that focus will be on cost reducing projects.

United Kingdom

The UK market achieved considerable success during the 2002/03 financial year when Arla Foods achieved its best ever result. This was driven by increased growth and profit improvement in the fresh milk business, Cravendale PurFiltre and sterilised milk. Furthermore, volumes of imported branded products also made considerable gains and for the first time exceeded 100,000 tons.

The year's dominant event in the UK was the merger with Express Dairies plc.

As part of the negotiations, it was agreed that:

- The Arla Foods Group will not increase its ownership share of 51% for a period of 2 years.
- The Arla Foods Group has 3 out of the 7 external seats on the Board of Directors.
- The Arla Foods Group will extend subordinate loan capital of GBP 91.5 million (approx. DKK 1 billion) to strengthen the company's financial base.

The new and enlarged company, Arla Foods UK plc, is the category leader in liquid milk and cream and a leading supplier of flavoured milk. The company also has a strong position in both the food service and doorstep milk sectors.

Another important event was the acquisition in November 2002 of H.T. Webb & Co., the UK's leading importer of speciality cheese.

In the BSM category, Lurpak, the second largest brand in the market, continued its growth thanks to the success of Lurpak Spreadable and Lurpak Lighter Spreadable. As Arla Foods also markets the third largest brand, Anchor, the Group now occupies the leading position within the whole of the category.

In cheese, Arla Foods made further advances with the relaunch of the Discover range of speciality cheeses and through the sale of soft cheese to UK retailers. At the same time, the Anchor range was expanded through the addition of convenience cheese products. Overall, the acquisition of H.T. Webb represents a decisive move into the growing market for speciality cheese.

The doorstep milk market continues to decline although this has been managed through a combination of rationalisation and in-fill depot acquisitions. This strategy meant that this part of the business weathered the decline better than the market in general.

New investments were channelled into the Oakthorpe Dairy in London. Last autumn the cold store operations were moved from Oakthorpe to the new depot in Stratford.

The construction of the new dairy at Stourton, near Leeds, which will be operational by the autumn of 2004, is progressing well. On October 1, 2003, Arla Foods took over the management of the cold store at Stourton which had been managed by a distribution company. On a site adjacent to the new dairy, the new leased head office for Arla Foods UK plc is being completed according to plan.

As a consequence of the merger with Express Dairies plc full consolidation of Express Dairies plc's balance sheet has been made in the annual accounts as at 30.9.2003. The total effect on the balance sheet is approx. DKK 5 billion.

In terms of operations, the merger will take effect from October 2003. Consequently, the profit and loss account for 2002/03 and the Group's equity as at 30.9.2003 have not been affected.

With regard to Arla Foods' consolidated balance sheet as at 30.9.2003, the full pension commitments in both existing and acquired UK companies have been taken into account as have expected restructuring costs. The amount totals approx. DKK 2.1 billion.

The expected tax effect of these items is entered as a tax asset in the balance sheet and will be realised as the costs are defrayed. The tax asset increased by approx. DKK 0.7 billion.

Consequently, goodwill is calculated at approx. DKK 1.8 billion which is capitalised and will be depreciated over a maximum of 20 years.

The coming year will focus on the integration of the two original companies into the new Arla Foods UK plc.

The former Express Dairies plc operates eight dairies. The dairy in Ashby produces milk and fruit juice. Prior to the merger with Arla Foods plc, fresh milk and cream accounted for almost all Express Dairies plc's sales.

Other European markets

Market conditions for butter and cheese products in Europe continued to be characterised by tough price competition especially for standard cheeses. This development was further accelerated by the economic slowdown in Europe which is encouraging consumers to shop in discount outlets or to opt for low-cost alternatives. In the past year, the market share of low price products increased in Europe, while delicatessen products and branded products came under pressure.

The situation varies greatly from country to country, but conditions in Arla Foods' most important European market, Germany, were once again difficult.

European cheese production remained high, leading to consistently low price levels.

Within the European retail sector, discounters have experienced growth in recent years. In addition, they are operating ever more internationally. The largest retail chains continue to gain market shares and are becoming more dominant.

All things considered, Arla Foods had a satisfactory year in European markets with added value and branded products accounting for an increasing share of the profits. The continued strengthening of brand positions and product development will be highly prioritised over the coming years.

In addition, more resources will be invested in enhancing professional services to the multiples.

In connection with the launch of the Arla master brand, the first major marketing initiatives were implemented in selected markets with highly satisfactory results. In markets where consumer marketing is applied, the Arla master brand has achieved a satisfactory level of awareness and it is expected that the brand will become familiar to almost 100 million European consumers over the next 3-4 years.

Germany

The competitive situation in the German market tightened further during the year as reflected in the continuing fall in the German milk price which is now at 1999 levels. The result is a hardened competitive situation on the supply side. The weak economic development in Germany led to a situation where consumers are increasingly turning towards cheap products. This trend is benefitting the discount sector and own label products.

In the traditional food sector, sales of speciality products from delicatessen counters continue to decline. Although the decline has, to some degree, levelled out, sales have fallen by 30% over the two recent calendar years. Increased sales of added value products from in-store self-service counters have, however, compensated for the negative development in sales of cheese from serviced cheese counters.

Holland

In the past year, Arla Foods further strengthened its direct service of the retail sector. Initial results have been particularly positive and these endeavours will be intensified over the coming year.

Arla Foods has a strong position as a foreign supplier of speciality cheese.

Belgium

In the Belgian market, Arla Foods partners Valio Vache Bleue, a subsidiary of the Finnish dairy company, Valio, with regard to sales of products to the retail sector. During the past year, sales developed satisfactorily with sales of Apetina Feta showing particular strength. On the other hand, sales of delicatessen products fell.

The Faroe Islands and Greenland

Arla Foods exports a wide range of fresh products, BSMs and cheese to the North Atlantic markets. Sales developed positively during the year.

Poland

The year was characterised by the preparations for Poland's membership of the European Union in May 2004. This meant

In the autumn of 2003, the roof was put on the new dairy at Stourton, south of Leeds. With a capacity of 250 million litres liquid milk per year, Stourton will be one of Arla Foods' largest liquid milk dairies. It will start operations at the end of 2004 and employ approx. 260 employees when it reaches its full capacity.

that Arla Foods' Polish subsidiary started exporting to some EU countries, that the organisation was strengthened further and that local activities in the Polish market were enhanced. The initiatives aim at ensuring the strongest possible platform for future growth in Poland.

Purchasing power remains low compared to the rest of Europe, but living standards are expected to rise following Poland's membership of the EU. Exports of added value products to Poland doubled over the year, although they remain at a fairly low level. Profit margins were affected by the fact that local activities are still under development. The price level of dairy products remains low.

The rest of Eastern Europe

While significant differences in purchasing power are expected between the new member countries and the current EU members for some years to come, some of the markets already have well developed retail and dairy sectors. Arla Foods has strengthened its focus on these markets in order to secure a share of the growth potential over the coming years.

Finland

In general, Arla Foods enjoyed a satisfactory year in the Finnish market, a year that was characterised by a strong performance in added value products and brands. Marketing campaigns for Apetina

Feta were organised under the new Arla master brand. However, sales of volume products were disappointing particularly due to tough competition from low price products from German and Dutch cheese producers.

Next year, Arla Foods will build on this to develop market shares within both branded and volume products.

Norway

Arla Foods had a particularly good year in the Norwegian market with sales growth exceeding 15%. During the year, the quota system between Norway and the EU was renegotiated with the result that the quota was expanded. It is anticipated that this will lead to stronger competition in a market where demand for foreign cheese is rapidly increasing.

Over the year, the Norwegian krone fluctuated considerably. Its recent weakening has put earnings under pressure.

The retail sales partnership with the local company, Synnøve Finden, was terminated and Arla Foods has set up an independent sales operation.

Italy

The result was satisfactory, not least on the backdrop of substantially increased price competition for yellow cheese. In general, the Italian subsidiary succeeded in maintaining firm price policies for volume products. Further work will aim at extending the range and improving distribution through the retail trade. Lurpak is seeing satisfactory development where in-store marketing is increasing alongside the introduction of more varieties of the famous butter brand.

Rationalisation measures were implemented during the year. A contract for the sale of warehouse and office premises in Lomazzo was signed and the organisation was streamlined.

Spain

Sales of cheese to the Spanish market continue to grow while, at the same time, Spain has become an important market for butter and blends. Ordinary profit was particularly satisfactory and Spain is now Arla Foods' fifth largest market within the EU.

As part of the strategy to service parts of the retail trade directly, a new sales company was established in Madrid at the beginning of the new financial year. It is expected that the new company, coupled with further investments in marketing, will generate increased growth in the Spanish market for Arla Foods.

France

Both sales and profit margins showed sound progress in the French market. Direct sales to the retail trade rose by 15% on the year. Industrial sales volumes also performed well.

Greece

The results from the Greek business were unsatisfactory. This is partly due to the fact that the Greek market, in line with other European markets, received a substantial supply of very cheap cheese products from local producers as well as from importers.

Although it was possible to sustain earnings from exports of cheese and butter to the Greek market, generating satisfactory earnings from local activities was less successful. A restructuring of the company is planned so that the overall product offering will make a positive contribution to the company's operations. Costs relating to these restructurings had a negative effect on the 2002/03 result.

Overseas markets

The Middle East, North America and Asia continue to rank among Arla Foods' most important markets outside Europe in terms of sales of butter and cheese. In the year under review, substantial volume growth was achieved and an important part of this growth derived from Middle Eastern markets.

In terms of foreign exchange, the majority of overseas markets are dependent on the US dollar rate. As the dollar developed negatively for most of the year, this impacted on the financial result.

Nevertheless, through hedging and price increases it was possible to offset a significant proportion of the fall in the exchange rate. The fact that it proved possible to implement price increases is largely due to Arla Foods' added value range and strong market positions for established brands such as Lurpak, Puck, Three Cows and Power Cow.

During the year, positions were further enhanced in most focus markets and new initiatives were taken in relevant markets – including the United Arab Emirates / Oman and Russia.

The development in the value of export subsidies and the allocation of export licences were fairly favourable for most of the year.

Saudi Arabia

All product groups – especially focus products – experienced fair growth in tonnage. Earnings were affected by foreign exchange developments, which necessitated price increases. Again this year, Arla Foods' dairy in Riyadh invested in production facilities and prospects for growth are regarded as positive for the coming years.

The United Arab Emirates/Oman

On January 1, 2003, Arla Foods embarked on a joint venture with the previous local distributor, National Food Product Company. The joint venture, which covers the Emirates and Oman, aims at ensuring the necessary focus on Arla Foods' brands and main product groups. In the Emirates, in particular, the retail sector is experiencing strong development in which the number of supermarkets is growing while smaller shops are coming under pressure. The development in tonnage and market shares for focus products were particularly encouraging. With the new joint venture, the necessary platform for future growth has been created.

Bahrain/Kuwait/Qatar

The close relations with local distributors were further enhanced through the appointment of a key account manager. Sales growth was positive and the combination of the company's strong regional brands combined with ongoing product development is set to ensure continued growth in these markets over the coming years.

Lebanon

The past year saw particularly satisfactory growth for cheese. Puck, Arla Foods' most important cheese brand in the Lebanese market, enjoys a healthy market share and the Puck range will now be extended to further exploit the brand's potential.

USA

A weak US economy, a sharp fall in the rate of the dollar as well as historically low American milk prices put massive pressure on growth and earnings. Nevertheless, Arla Foods achieved considerable growth in added value brands. Local production of Havarti cheese also saw positive development.

Consolidation of the US retail sector continues. During the year, Arla Foods' relations with the leading multiples strengthened and the company enjoyed particular success in terms of increasing sales through the growing "warehouse club" segment.

Marketing efforts were centred on the Lurpak and Rosenborg brands. US economic trends are expected to improve over the coming year and moderate sales growth is anticipated. Some uncertainty relates to the impending US legislation against biological attacks which may incur some non-budgeted costs.

Canada

Once again, highly satisfactory results were achieved in the Canadian market. The Canadian dollar lost only moderate ground against the Danish kroner and internal price trends were stable. During the year, focus was on generating growth in the added value product range. In addition, several new products were launched, distribution was extended and local production developed positively. The prospects are for continued growth in volume and profitability.

Brazil

A weak economy with declining purchasing power and a strong rise in the price of milk had a negative impact on the result for Arla Foods' joint venture, DanVigor. During the year, major cutbacks were successfully introduced into the organisation and a significant improvement in the result is expected for the coming year.

Japan

In recent years, the Japanese economy has suffered from an economic slowdown which has been exacerbated by similar trends in the US and Asia. As private consumption has declined, there has been more focus on price, partly to the detriment of the normally high quality requirements. Developments in foreign exchange markets contributed to reducing

the price competitiveness of European dairy products. Despite the negative developments, Arla Foods experienced fair sales growth of approximately 10% on the year.

It is to be hoped that the economy will recover and that this will lead to growth in cheese consumption.

South Korea

Despite tough price competition, Arla Foods' exports to South Korea developed positively with a marked increased in tonnage compared to the 2001/02 financial year. The Korean economy is showing signs of improvement following a slowdown in recent years and the consumption of cheese has seen a moderate rise, although it remains below 1 kg per capita per annum. Expectations for the coming year are relatively optimistic.

Australia

Sales to Australia increased markedly by approx. 30% on the year. The increase derives from a broad range of products, not least Rosenborg which has received widespread recognition.

India

Although Arla Foods' products are in demand, sales fell below expectations. This is primarily due to the Indian authorities' protectionist attitude to imported dairy products and to logistic challenges, including the requirement for an unbroken chilled chain.

Although India's overall imports of cheese and butter are increasing, they remain limited.

Pakistan

Despite a very limited marketing effort, Pakistan has been a solid and stable market for Lurpak and Puck for several years. The coming year will see increased focus on Pakistan which is expected to have an immediate effect on sales.

South East Asia

Sales to the region, where Hong Kong and Singapore remain the largest markets, continue the positive development of recent years. Irrespective of difficult conditions such as SARS, terrorist activity and the negative development in the US dollar, sales rose by 14% on the year.

For the coming year, the outlook is for continued advances although the ever increasing competition from Oceania in terms of volume products means that even more retail products must be developed and marketed under the two main brands, Lurpak and Arla. On the backdrop of a significant demand for light products, Arla Foods expects to launch several products within this growing segment.

Russia

On the basis of the substantial potential and the economic recovery since the crisis in the Russian market in 1998, a new Region East has been established. The region will primarily focus on Russia.

Arla Foods regards Russia as a future market with large potential. Various strategic considerations concerning the future are expected to be completed in the New Year.

Cravendale PurFiltre® is produced at Arla Foods' dairy in Hatfield Peverel in Essex where the milk passes through a process of special filtration after conventional pasteurisation. While almost all bacteria is eliminated, the milk retains its natural content of vitamins and calcium and can be kept longer than ordinary milk.

Ingredients

A difficult year for ingredients and milk powder was characterised by tough competition for both speciality and standard products. Moreover, pressure on the US dollar and falling export subsidies made an impact. Arla Foods Ingredients, however, retained its position as the leading and preferred supplier of added value milk-based ingredients products for selected global customers.

Turnover for the year was DKK 5,193 million which is on a par with last year.

When the structural plan for processing milk powder in Denmark and Sweden is completed at the end of 2004, Arla Foods will boast one of the world's most efficient and advanced production plants for processing milk-based ingredients.

Arla Foods' ingredients business is divided into four business areas: industry, retail, own label milk powder and sales of ingredients.

Industry

This business area comprises the production and sale of added value ingredients for global food producers. Developments within the field of functional milk proteins for the dairy industry were good, with strong focus on reduced fat products. Within this field, Arla Foods is now a world market leader.

In the field of special nutrition, the production of hydrolysates expanded during the year. Some special products have, however, encountered increased competition in world markets due to a larger supply from Oceania and the US.

Sales of cheese powder met the high expectations for this business area.

In view of China's rapid growth, Arla Foods set up a representative office here in 2002/03.

Arla Foods' joint venture with the Argentinian dairy company, SanCor, is proceeding well with Central America buying substantial amounts of milk proteins from the factory in Argentina.

Towards the end of the financial year, a joint venture for production of the milk-based, low calorie sweetener, Gaio tagatose, was formed with one of Europe's leading sugar producers, Nordzucker, in Nordstemmen, Germany. The product was launched commercially in the US where it is used by, among others, PepsiCo. Approval of Gaio tagatose has also been obtained in Korea and is underway in Japan. EU approval is expected to be forthcoming within the next few years. If warranted by future demand, production capacity will be significantly increased over a two-three year period.

Retail

Arla Foods' milk powder sold in retail outlets occupies a significant position in several markets, including the Dominican Republic, Yemen and Bangladesh. The products are sold in consumer packs under the DANO and Milex brands. In the key markets, the weaker US dollar and local devaluations meant price increases for imported milk powder. As a result, Arla Foods' competitiveness was somewhat weakened.

Own label milk powder

Today Arla Foods is a global leader within own label production of milk-based nutrition products. With the completion of the plant structure plan, Danish production facilities have been substantially upgraded to ensure efficient and profitable operations. A pilot plant for smaller special productions, which can subsequently be used for clinical trials for customers, has also been established.

The business area continues to offer considerable potential as major international companies outsource parts or the whole of their production. The significant growth in tonnage and earnings is expected to continue in the coming year.

Ingredients sales

Sales of standard products were characterised by fair prices early in the financial year. However, a substantial increase in supplies, particularly from Oceania, combined with a low US dollar rate meant that prices reached a historic low (measured in Danish kroner) during the spring/summer 2003. Nevertheless, the prices for both milk powder and milk proteins began to show a slight upward trend late in the year.

With a milk production of approx. 14 billion kg, the UK ranks third in the EU after Germany and France. There are around 30,000 British milk producers.

Relations with co-operative owners

In September, three years after the merger between Arla and MD Foods, the two companies' Boards of Representatives were finally able to close the two companies down and approve the new common Articles of Association for Arla Foods amba.

The completion of several large projects concerning co-operative ownership generated many member meetings in 2002/03.

The new joint quality programme, Arlagården, was finalised and came into force, as planned, on October 1, 2003. Based on customers' and consumers' rising demand for food safety, its objectives are based on the quality policy's cornerstones: milk quality, food safety, animal welfare and the environment. The programme is intended to emphasise Arlagården's importance as the first link in the company's value chain and thus contribute to the enhancement of the competitiveness of Arla Foods' products.

On October 1, 2003, a new common payment model came into force in keeping with the harmonisation process between Danish and Swedish co-operative members. The model, however, also reflects adjustments to market demands. Since demand for milk proteins is rising at the cost of milk fat, the relation between fat and protein has shifted considerably in favour of protein.

Based on the launch of the quality programme and the new payment model, a new common databased payment system became operative on October 1, 2003 as part of Ett Arla.

Within the organic area, a decision was taken as to how the organic business should be harmonised. As part of this process, an alignment of the received volumes of organic milk in relation to volumes sold will be carried out in Denmark. It was also decided to set up an organic committee comprising Swedish and Danish organic co-operative members to deal with a variety of issues. In Denmark, the contracts with organic co-operative members will be renewed during the autumn of 2003. The Swedish organic co-operative members' contracts will be reviewed early in 2004.

Fewer co-operative members

In 2002/03, the number of Arla Foods' Danish and Swedish co-operative members fell to 12,758 at year end. In Sweden, the total number declined to 6,133, i.e. 6.3%, while the fall in Denmark was 6.8%, i.e. 6,625 members. This means that the trend towards fewer, but larger, farms is continuing. The total amount of milk received, 6,252 million kg, was 2% higher on the year. This means that the annual average supply per farm is now 615,000 kg in Denmark and 341,000 kg in Sweden.

Overall, Arla Foods has approx. 900 organic co-operative members, with a total production of 490 million kg milk.

Inter-dairy transport

In line with previous years, inter-dairy transport was rationalised and streamlined further during the year. In Denmark, the transition to the 24 hour milk collection system continues alongside the introduction of the so-called tractor/trailer system.

In Sweden, faster emptying of farm milk tanks by new tankers with increased pumping capacity has led to more efficient collection and thus a reduction in the number of tankers.

New common collection rules were introduced during the financial year.

A special co-operative member appendix has been prepared for the Annual Report. This contains information of particular interest to Arla Foods' co-operative members.

Rosenborg is the UK market's biggest blue cheese brand. In order to meet consumers' requirements, new packaging and portions, e.g. slices and cubes, are being developed. Special focus is on strengthening the brand in supermarkets' delicatessen counters.


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Innovation

Each year, Arla Foods Innovation develops approx. 200 new products. Development takes place within a project environment in which staff work in teams comprising colleagues from production, marketing and innovation.

During the past year, research and product development were largely unchanged in terms of costs. Increasing efficiency in both the selection and implementation of projects, however, enhanced the real value of the work.

Product development

Ongoing work aims at maintaining and developing each of the Group's product areas. Basic products are improved and upgraded and new consumer opportunities and segments are analysed.

Changes to eating patterns and meal times, consumer preferences for low calorie products, frequent shifts in taste and a higher level of convenience in the shape of new packaging and increased preparation levels present a constant demand for innovation.

In the Danish, Swedish and UK markets, where Arla Foods has a particular commitment to a high launch frequency and service to consumers, around 125 products are launched each year. This will also be the case in the coming year.

A dominant consumer trend is the demand for products with fewer calories. This is why, for many years, Arla Foods has been developing a comprehensive range that meets this demand: Minimilk with 0.5% fat, fermented products with 0.1% fat, yellow cheese with 5% fat and cream cheese with 0.1% fat, to name just a few examples. Arla Foods can, therefore, offer consumers healthy milk components with a limited calorie intake.

In the ingredients area, work continues to identify new functional milk proteins for the global food industry. This applies to products within the so-called functional food area and to products with consistency-giving properties.

Technology development

Through the continual development of process technology, Innovation can improve production calculations and lay the foundation for entirely new products. In connection with the implementation of Arla Foods' structural plan, which comprises dairy closures as well as the opening of new plants – and thus the transfer of productions – there is a need for advanced technological support to ensure that, for instance, a cheese maintains its high flavour quality. Innovation has developed high-tech methods which make for the smooth transfer and preservation of the quality of products between production plants.

Research

The Group's long-term – and crucial – focus on research is reflected in Arla Foods' research strategy. The research topics are divided into three areas: a product orientated area such as milk fat, bioactive components and raw milk quality; a process-orientated area such as process technology, biotechnology and food informatics, and finally, a consumer-orientated area such as food safety and quality experience.

This research is carried out in conjunction with universities in Denmark, Sweden and other European countries.

Cravendale PurFiltre® has made huge advances and now ranks, as expected, among the UK's 100 largest brands.


Arla
CRAVENDALE
PurFiltre®
the best tasting
Fresh Milk

The environment and working environment

Arla Foods' environmental responsibilities begin at the farms which, in Denmark and Sweden, are a key component of the quality programme, Arlagården which, among other things, focuses on the reduction of environmental impact.

The moment the milk leaves the farm, the company assumes direct environmental responsibility for the ensuing processes, including the transport of milk from farm to dairy, production at the dairies, the transport of products to the stores and for the packaging of the products. Arla Foods is also responsible for ensuring that the milk and other ingredients used in production are produced in an environmentally sustainable manner.

Arla Foods' ambition is to continue to reduce the environmental impact from farm to table and to retain focus on a healthy and safe working environment in order to promote sustainable development.

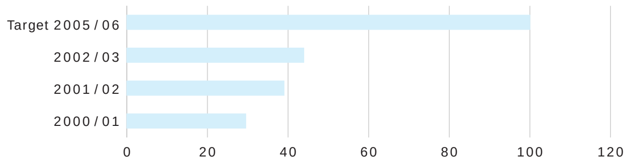
Arla Foods' environmental work takes place within the framework of the Group's environmental policy and the related targets for the environment and the working environment. The environmental targets must be met before 2005/06.

So far, targets have been prescribed for: water consumption, energy consumption, emission of CO_2 and NO_X from production and transport, environmental accreditation, industrial injuries and chemicals.

The graphs, which cover the Group (with the exception of the UK), provide an overview of the status of the targets.

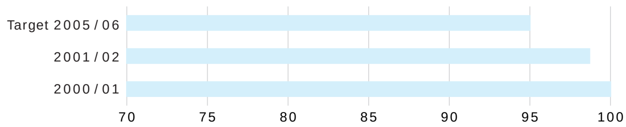
ISO 14001 accredited units

Arla Foods in Sweden and Denmark



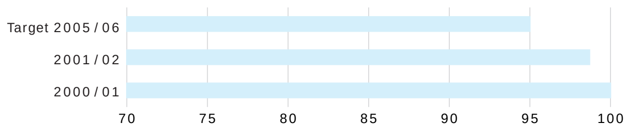
Water consumption

(index, water consumption in relation to raw materials and finished products)



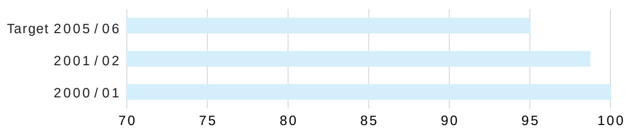
Energy consumption

(index, energy consumption in relation to raw materials and finished products)



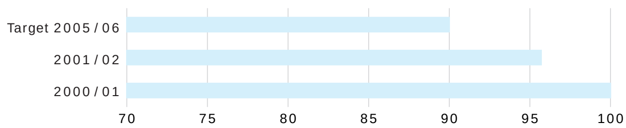
CO_2 emission

(index, CO_2 emission in relation to raw materials and finished products)



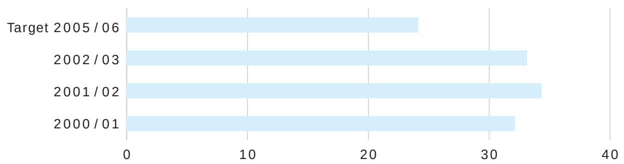
NO_X emission

(index, NO_X emission in relation to raw materials and finished products)



Accident frequency - DK

(Number of accidents per 1 million working hours)



Chemicals

The properties of all chemical products used at the Group's plants must be assessed in relation to the effect on health and the environment no later than the end of the 2005 / 06 financial year. At present, cleaning and disinfectants have been assessed and divided into the following colour-coded categories:

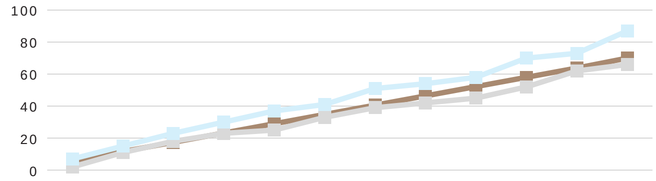
Green: Complies with the general environmental requirements or carries an environmental stamp

Yellow: Does not entirely comply with the requirements, but meets the defined requirements and exceptions

Red: Does not comply with the environmental and / or health requirements

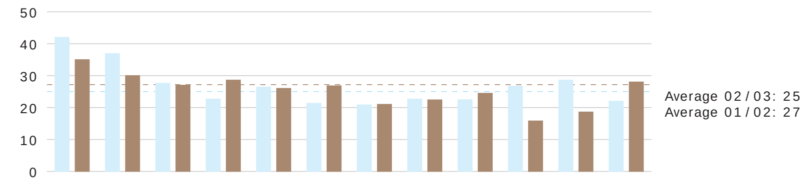
The plants can select chemicals from the best categories providing hygienic requirements are met.

Figure 1: Accumulated accidents per period in the UK



	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2001 / 2002	7	15	23	30	37	41	51	54	58	70	73	87
2002 / 2003	2	11	18	23	25	33	39	42	45	52	62	66
Target	5,8	11,6	17,4	23,2	29	34,8	40,6	46,4	52,2	58	63,8	70

Figure 2 Accident frequency rate in the UK



	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2001 / 2002	42,0	36,9	27,6	22,7	26,4	21,3	20,8	22,7	22,4	26,7	28,6	22,0
2002 / 2003	35,0	30,0	27,0	28,6	26,0	26,8	21,0	22,4	24,5	15,8	18,6	28,0

Environmental work in the UK

Arla Foods has set out clear targets in relation to the environment and working environment at its UK plants. In order to achieve these targets, co-ordinators have been appointed within the area of health, safety and the environment at all plants. The work is centrally managed by a group that advises on control and regulatory compliance. During 2002 / 03, the new organisation produced a range of major improvements:

Energy consumption was reduced by 11% and water consumption cut by 16%

Within the field of the working environment, the number of accidents leading to absences of more than three days fell by 25% (see fig. 1). The accident rate also fell (see fig. 2).

Before April 1, 2005, all Arla Foods' production plants in the UK must be IPPC approved (IPPC – Integrated Prevention Pollution Control), which is currently the biggest challenge facing the company's environmental endeavours. In order to establish an overview of the resources required to achieve IPPC accreditation, the environmental conditions at the plants were examined and the reports on "best practice" are now being discussed at the plants as well as in the relevant working groups.

Environmental approvals

The Group's units in Denmark, Sweden and the UK, which account for 99% of the Group's total production, are all subject to common EU regulations. In Denmark and Sweden these EU regulations concerning environmental approvals have been implemented.

Subsidiaries

Dairy activities

AM Foods

Arla Foods produces and sells milk-based vending machine products primarily to the food service sector in Scandinavia, Central and Eastern Europe. However, the products are also sold to Scandinavian retailers. In the financial year 2002/03, turnover totalled DKK 260 million against DKK 240 million in 2001/02.

Operating profit continues to develop positively and totalled DKK 19.2 million in 2002/03 against DKK 14.5 million in 2001/02.

The largest product groups are chocolate, cappuccino and toppings. With sales of 14,000 tons during the 2002/03 financial year, AM Foods is a leading supplier in the European market for vending machine products. In France, AM Foods expanded its sales force and improved its market position by 15%.

In view of the general economic slowdown in the food service sector and substantial price increases for raw materials, AM Foods achieved a particularly satisfactory result. For the coming year, the company expects the positive development in key markets to continue at a sales growth of at least 5%.

Delimo A/S

In 2003, Arla Foods acquired all the shares in the cheese importing company, Delimo A/S. In September 2003, Delimo acquired the cheese importing company, Olaf Sørensen. Delimo's concept for sliced speciality cheese achieved double digit growth which is expected to continue in 2003/04. Over

the coming year, Delimo is increasing its focus on supplying cheese from selected European brand suppliers to the retail trade in Denmark, while its broad cheese portolio will continue to be sold to delicatessens and restaurants. Next year will also focus on developing sales of speciality cheese for the other Nordic countries.

Andelssmør A.m.b.a.

Arla Foods owns approx. 94% of the company which handles the vast majority of Danish butter exports. The company operates as an integral part of Arla Foods. The result for the year is satisfactory.

Other activities

Rynkeby Foods A/S

For the financial year 2002/03, turnover for Rynkeby Foods fell to DKK 790 million against DKK 823 million last year. However, operating profit was DKK 36 million against DKK 32 million the previous year. The decline in turnover stems from product areas that have been terminated – or are being terminated – in connection with the closure of the factory in Rynkeby.

Within the core areas of fruit juice and squash, the market again developed positively and Rynkeby Foods achieved a modest increase in turnover. The market was characterised by changes in trading patterns where the discount sector and own label are gaining increasing market shares in a highly competitive environment. This impacted on the product mix and sales costs and, in conjunction with declining turnover, put operating profit under pressure.

The explanation for the substantial improvement in the year's profits, from DKK 4 million last year to DKK 36 million this year, lies partly with the increase in the operating profit and partly with the items that relate to the closure of the factory in Rynkeby. In 2001/2002, DKK 22 million was expensed for this purpose, of which DKK 6 million was carried back in 2002/03.

As planned, the factory in Rynkeby was closed on June 1, 2003 and its production was either outsourced or wound down. With regard to the latter, this involved some major licensed production agreements.

The construction of a new fully automatic warehouse began in August 2002 at the factory in Ringe. The warehouse will be commissioned in March 2004.

In a market that remains under pressure, Rynkeby Foods expects a reasonable increase in turnover within its core areas for 2003/04, with particularly good growth in the chilled juice sector. At the same time, the cessation of licensed production agreements and the range reduction in 2002/03 will take full effect in 2003/04. Overall turnover, therefore, is only expected to see a modest increase.

JO Bolaget AB

JO Bolaget, which is jointly owned by Arla Foods and Skånemejerierne with 50% each, produces fruit juice, fruit drinks and fruit soups.

Sales totalled 117 million litres and turnover increased by DKK 21 million to SEK 906 million in the 2002/03 financial year. Fruit juice accounts for 93% of the turnover with chilled juice accounting for 60%. During the financial year, this segment grew by 9%.

Prospects for the next financial year are good although volume sales are not anticipated to rise. However, the value shift from aseptic to chilled juice is expected to continue. Among other positive factors are the dollar rate at the beginning of the new financial year and the prices for orange juice concentrate.

The integrated partnership between Rynkeby Foods A/S and JO Bolaget AB developed positively in 2002/03. The partnership focuses on activiti-

As the biggest producer of fresh milk and supplier of Lurpak, the second largest brand in the BSM category, Arla Foods UK plc plays a prominent role on many UK consumers' breakfast tables.

es within purchasing, development and marketing, joint brands and production under a common management team.

Between them, the two companies are the Nordic area's largest fruit juice producer and the objective is to provide continued growth in the two home markets and expansion in the other Nordic countries. So far, the partnership has performed well within the fields of joint purchasing, product development and product plans. As part of a joint Nordic strategy for chilled juice, Rynkeby Foods launched "Rigtig Juice" in a new Scandinavian design and, in collaboration with JO Bolaget, also launched a product called "Rigtig Juice Smoothies."

De danske Mejeriers Fællesindkøb amba

In the financial year 2002/03, De danske Mejeriers Fællesindkøb amba achieved a turnover of DKK 643 million against DKK 656 million in 2001/02. The consolidated operating profit was DKK 6 million against DKK 15 million last year.

During the year, the number of co-operative members was reduced to one, i.e. Arla Foods amba. The other co-operative members were bought out during the spring of 2003.

The change in the ownership is part of the ongoing restructuring of De danske Mejeriers Fællesindkøb amba. The plan is to divide the group into three independent operating units: Procudan A/S, Dairy Fruit A/S and A/S Crispy Food International.

The Trading Department Procudan's field of operations has consequently undergone changes and adjustments. The part of the company that was previously responsible for purchasing on behalf of Arla Foods was transferred to Arla Foods Global Purchasing and individual productions have been shut down. In order to strengthen the Export Department, a branch office was opened in Sweden and the company expects to see an increase in ingredients sales. The Trading Department is expected to be converted to Procudan A/S in the new financial year.

During the financial year, Dairy Fruit A/S expanded its business to include licensed production of fruit porridge and marmelade. The full effect will materialise during the coming financial year. The result of this, together with an increased sales effort in near export markets, is expected to increase earnings in 2003/04. One negative element, however, is that raw material prices for primary fruit types are expected to increase.

During the past financial year, A/S Crispy Food International worked towards enhancing its market profile and the result has been a fair increase in turnover. The initiatives are expected to impact fully in the coming year during which growth in turnover is expected to continue.

Danapak

The packaging group, Danapak, posted a loss on ordinary operations of DKK minus 46 million for the financial year 2002/03 against a loss of DKK 22 million in 2001/02. The result was strongly influenced by developments in Westergaard & Philipson A/S which performed unsatisfactorily. Turnover for the financial year was DKK 429 million against DKK 771 million the previous year. The turnover is, however, not directly comparable with the previous financial year in that it was affected by the group's restructuring. Within the continuing cartons business, turnover fell from DKK 434 million in 2001/02 to DKK 429 million in 2002/03.

During 2002/03, Danapak continued its efforts to adapt the company to the ever increasing competition in the market place.

In May 2003, Danapak acquired the remaining 40% of the shares in Westergaard & Philipson A/S.

At the end of the financial year, it was decided to transfer the company's production to two other Danapak Kartonnage plants which now operate production in Korsør, Herning and Bremen. The disposal of W&P has resulted in a loss of DKK 25 million.

The joint venture with the Teich Group produced a loss for Danapak of DKK 12 million, which is mainly due to costs relating to the closure of the factory in Derby.

In 2002/03, the investment programme amounted to DKK 19 million.

Market conditions in Germany were influenced by the general economic slowdown which is expected to continue. In general, the German market is suffering from over capacity and consolidation within the sector is minimal. Danapak wishes to participate in – and promote – further consolidation.

With the establishment of a North European joint venture in the field of flexible packaging, the conditions for increasing competitiveness within the industry have been enhanced. Danapak expects to improve its ordinary result for the coming year.

Frödinge Dairy AB

Besides the Swedish speciality, cheesecake, Frödinge Dairy AB produces and sells frozen layer cake and tarts to markets in Sweden, the rest of the Nordic area, Germany and the UK. During the year under review, the company's turnover was SEK 300 million against SEK 309 million the previous year. The decline is owing to falling sales in the Swedish and German markets coupled with the Swedish krona's relatively strong rate in relation to the euro and sterling. Profit on ordfinary operation was SEK 17.2 million which is in line with earnings in percentage of turnover.

In the Swedish domestic market, sales of cheesecakes and tarts fell marginally. Sales of frozen layer cake continue to develop favourably although sales of savoury tarts are suffering as retailers reduce the number of products in their range and increasingly rely on own label products. However, Frödinge Dairy AB has chosen to adhere to its strategy of selling its own branded products within all product ranges.

The company increased its export share of total produced volumes to approx. 42%.

During the year, the company set up its own representative office at Arla Foods' office in Düsseldorf in Germany. Sales in the German market have, however, been negatively affected by the German economic slowdown. Sales to the UK rose, although failing to meet the budgeted levels. The positive development in Finland is being maintained and in Norway a number of products were listed with a major retailer.

During the year, SEK 8 million was invested in production.

Turnover is expected to increase over the coming financial year while exports, primarily to the UK and German markets, will account for the biggest volume growth.

Medipharm AB

Medipharm AB produces bacteria cultures for the agricultural and food industries and the products are marketed in Sweden as well as abroad.

Sales failed to meet last year's level which resulted in a fall in turnover from SEK 136 million to SEK 126 million, while operating profit totalled SEK 9 million against SEK 18 million last year.

The fall is at least partly due to the summer's hot and dry weather conditions in Southern and Central Europe which more or less halved the market for Medipharm's ensiling products. Exchange rate developments also had a negative impact on Medipharm's result.

The starter cultures (kefir) and human and feed probiotica product areas, however, experienced reasonable growth.

During the year, a significant investment programme was implemented aimed at increasing capacity within the fields of freeze drying and fermentors. The investments have prepared the company for further expansion in the market.

During the year, the company assumed all responsibility for the subsidiary, Medipharm Investment Ltd., in the US, following which a new business system was set up leading to a general strengthening of the company's organisation.

The subsidiaries in the Czech Republic and Hungary were also affected by the climate which impacted negatively on the expected growth.

Over the past five years, growth of 17% has been achieved. However, the objective remains to increase turnover by 25% per year.

Semper AB

During the year, Semper further strengthened its market positions especially within the fields of infant food in Sweden, Finland and Russia and within gluten-free products, health food and special nutrition.

As Semper's business areas are no longer part of Arla Foods' future core business, the subsidiary was sold in July 2003 at a profit of DKK 220 million.

Arla Foods Holding A/S

Wholly-owned by Arla Foods, Arla Foods Holding A / S is the holding company for a number of Arla Foods' shareholdings, including Medani A / S, Arla Insurance Company (Guernsey) Ltd. and Rynkeby Foods A / S.

The result for the year is satisfactory.

Medani A/S

The company owns Arla Foods' head office, Ravnsbjerg Erhvervscenter. The company is also responsible for a number of financing and investment activities. Medani achieved a satisfactory result.

Arla Insurance Company (Guernsey) Ltd.

The company acts as a reinsurance company for the Arla Foods group. The rising costs of liability insurances resulted in a need to strengthen reserve provisions. The company, therefore, achieved a small, negative result.

The former Express Dairies plc was the UK's largest supplier of fresh milk to leading supermarket chains as well as having the largest doorstep sales where milk and other products are delivered to more than one and a half million private customers nationwide.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Managing financial risks at Arla Foods

During the financial year 2001/2002, the Supervisory Board of Arla Foods amba adopted a new finance policy laying down guidelines for the group's financial risk profile.

The main objective of Arla Food's finance policy is to ensure a stable cash flow and financial flexibility in a volatile market.

The finance policy is designed to ensure compliance with best practice and with the tightened accounting requirements on large international companies.

The finance policy underpins the group's strategic plans.

The general finance policy determines the allocation of responsibilities between the Supervisory Board, the Management Board and the Finance Department. It also specifies which financial products and counterparts can be used. The requirements are that a well-functioning market exists for such products and that they can be reliably measured.

Financial counterparts are selected based on a wish for a long-standing mutual association benefiting both parties. The Group's international strategy makes higher and higher requirements with respect to the internationalisation of our bankers. Risks are minimised by selecting partners with high rating only.

In addition, the finance policy sets out the Group's general credit policy as well as specifies the systems for operational management. To manage the intragroup accounts, the Finance Department has implemented SAP R3 In House Cash, which functions as a management tool for the Group's internal bank. Medani A/S serves as internal bank for a number of the Group's subsidiaries.

The foreign currency policy sets out the framework for maximising long-term earnings based on market conditions. According to group policy, individual business units are responsible for foreign exchange hedging whereas all external hedging for the divisions is effectuated by the central Finance Department.

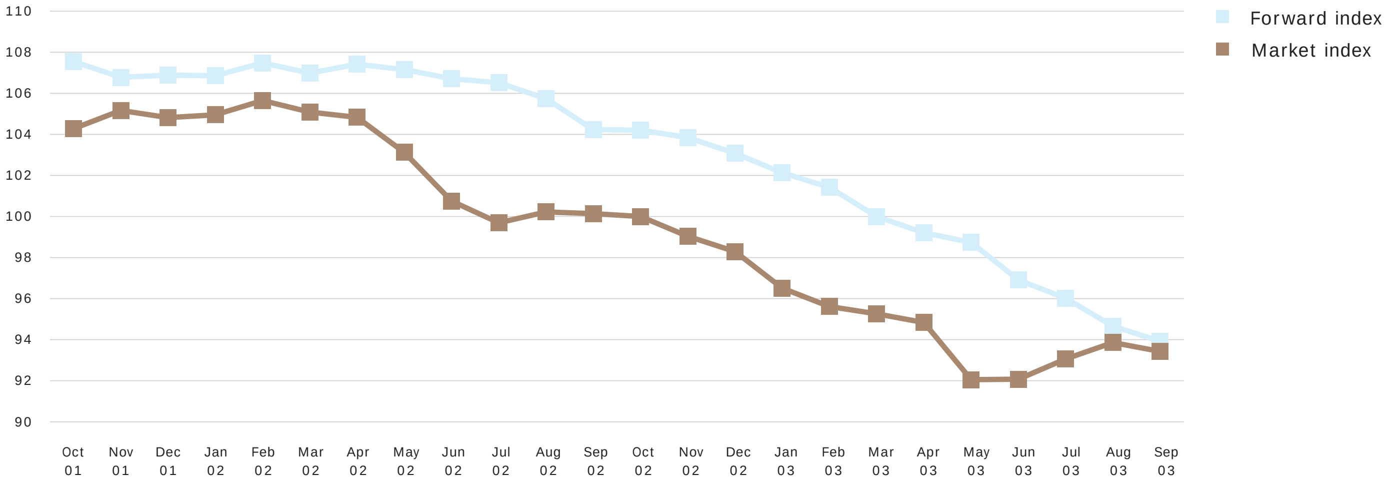
The main purpose of hedging by way of financial instruments is to generate a stable cash flow to minimise fluctuations in the milk price. The Group uses both forward exchange contracts and option strategies for currency hedging to ensure flexibility.

The company's total exports in foreign currencies from Denmark and Sweden amount to approx. DKK 10 billion, of which approximately 48% is in EUR, 26% in USD, 16% in GBP and 5% in SAR (Saudi Arabia).

Foreign exchange hedging is based on commercial considerations. To measure the effectiveness of the hedging, a foreign exchange index has been set up. This index measures the results of hedging in relation to market developments. The foreign exchange index, figure 1 below, demonstrates that the consequences of recent years' decreases in currency rates have been minimised by means of financial transactions. The market index for October 2002 is set at 100.

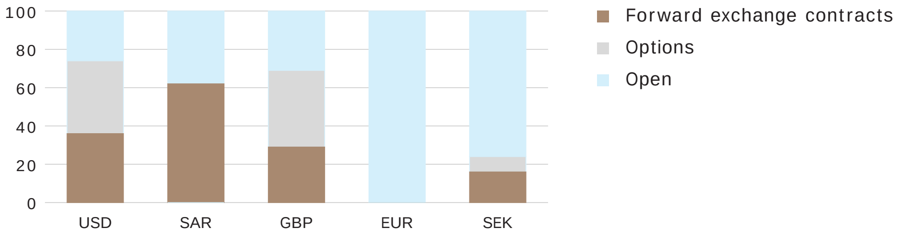
In addition, the Group's currency risks are measured by means of the international standard for measuring financial risks, Value-at-Risk (VaR), which provides 95% probability in measuring the currency risks that Arla Foods faces on a month-for-month basis.

Figure 1: Foreign exchange index



In 1990, the then MD Foods (now Arla Foods) began investing in the British milk industry. The first acquisition was the Leeds-based, Associated Fresh Foods, which also operated production units in Settle and Newcastle. Two further acquisitions were to follow. In 1992, MD Foods bought Oakthorpe Dairy in North London from CRS and in 1993, Bamber Bridge dairy was acquired from Dairy Crest. In 1996, MD Foods bought Hatfield Peverel from Lord Rayleigh in 1996.

Figure 2: Hedging compared to annual budget



Hedging of foreign currency positions is assessed currently and this year a number of hedging transactions have been made regarding the most sensitive currencies such as USD, GBP and SAR. Figure 2 shows that approx. 75% of the most risky currencies are hedged by a combination of forward exchange contracts and options.

The financing policy underpins the Group's strategic plans and its wish to minimise the risk of impacts from financial instability.

The overall objective of the financing policy is to minimise the long-term borrowing costs while ensuring a loan composition that reduces the risks of refinancing.

The Group has a conservative loan policy. Loans are raised when the Group believes the terms to be attractive and the financing of the Group's strategic initiatives is in this way analysed in advance.

Both lenders and loan repayment periods are diversified to achieve this. As the international awareness of the Group increases, the plan is to utilise the international capital markets as a supplement to our existing lenders. At the moment, Arla Foods has issued a Commercial Paper Programme in Sweden with duration of up to 12 months.

The financing policy lays down the broad targets for the Group's overall capital structure as well as internal rules for the financing of the Group's entities.

The duration indicates how long the interest rate on the debt will be fixed on average.

The duration target is applied in connection with the management of the Group's interest risks on financial assets and liabilities. The duration of the long-term portion of the debt should be between 0-7 years. Throughout the year, several long-term fixed interest loans have been raised so that the duration of the debt is maintained at approx. 3.2 years.

Furthermore, the policy specifies that the short-term portion of the total interest-bearing loans must not be higher than the corresponding ratio between current assets and fixed assets.

The average repayment period of the long-term debt increased from approx. 5.2 years to approx. 5.8 years thereby fulfilling the finance policy of at least 2 years. At 30 September 2003, the total interest-bearing debt amounted to approx. DKK 8,971 million compared to approx. DKK 8,019 million last year.

The currency risks on investments in foreign subsidiaries are normally not hedged if they are part of the Group's long-term strategy. At the end of the financial year, the distribution of interest-bearing debt was 60% in DKK, 16% in SEK, 14% in GBP, 7% in USD and 3% in other currencies. Lea-

Approx. 1250 milk producers are affiliated to Arla Foods UK plc. The total weighed in milk of the former Arla Foods plc amounted to 0.9 billion kg, of which approx. 350 million kg came from about 400 farmers on contract. Nearly half of the former Express Dairies plc' weighed in quantities of 1.4 billion kg milk came from approx. 850 farmers. The rest of the milk is purchased through milk collection societies.

sing is only utilised when deemed to be attractive for the Group.

The liquidity policy is linked to the company's financing policy and ensures that the liquidity risk is minimised. This is achieved by maintaining sufficient operating liquidity and sufficient liquidity for acquisitions. During the year, the Finance Department has worked and is still working on an optimisation of the cash flow and the need for drawing rights in the banks, among other things, by establishing an internal bank and cash pools in Denmark, Sweden and the Euro Zone.

The total liquidity reserve amounted to approx. DKK 4.8 billion at 30 September 2003. The risks relating to receivables from debtors are not considered unusual.

During the financial year, initiatives have been taken to adjust the Group's balance sheet to strengthen the solidity and to minimise the need for working capital. The coming year will also focus on initiatives to reduce the balance sheet total and to strengthen the solidity.

Management's statement

The Management Board and the Supervisory Board have today discussed and adopted the annual report of Arla Foods amba for the financial year 30 September 2002 – 30 September 2003.

The annual report has been prepared in accordance with the Danish Financial Statements Act. We consider the accounting policies applied to be appropriate. Accordingly, the annual report gives a true and fair view of the Group's and the parent company's assets, liabilities and financial position at 30 September 2003 as well as of the results of the Group's and the parent company's activities and cash flows for the financial year 30 September 2002 - 30 September 2003.

We recommend that the annual report be approved by the Board of Representatives.
Aarhus, 26 November 2003

Management Board of Arla Foods amba

Jens Bigum
Man. Director

Åke Modig
Dep. Man. Director

Jørn Wendel Andersen
Finance Director

Supervisory Board of Arla Foods amba

Knud Erik Jensen
Chairman

Åke Hantoft
Deputy Chairman

Leif Backstad

Sören Kihlberg

Viggo Ø. Bloch

Ove Møberg

Steen Bolvig

Per Norstedt

Bjarne Bundesen

Jan Toft Nørgaard

Christer Eliasson

Kaj Ole Pedersen

Anders Ericsson

Gunnar Pleijert

Leif Eriksson

Søren Rasmussen

Elisabeth Gauffin

Pejter Andersen Søndergaard

Thomas Erling Johansen

Bent Juul Sørensen

Auditors' report

To the members of Arla Foods amba

We have audited the annual report of Arla Foods amba for the financial year 30 September 2002 – 30 September 2003.

The annual report is the responsibility of the company's Management Board and Supervisory Board. Our responsibility is to express an opinion on the annual report based on our audit.

Basis of opinion

We conducted our audit in accordance with International and Danish Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance that the annual report is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the annual report. An audit also includes assessing the accounting policies used and significant estimates made by the Management Board and the Supervisory Board, as well as evaluating the overall annual report presentation. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not resulted 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 assets, liabilities and financial position at 30 September 2003 and of the results of the Group's and the parent company's operations and cash flows for the financial year 30 September 2002 – 30 September 2003 in accordance with the Danish Financial Statements Act.

Aarhus, 26 November 2003

KPMG C. Jespersen
Statsautoriseret
Revisionsinteressentskab

E. Black Pedersen
State Authorised Public Accountant

J. Bräuner Knudsen
State Authorised Public Accountant

PricewaterhouseCoopers
Statsautoriseret
Revisorinteressentskab

Göran Tidström
Authorised Public Accountant

Jesper Lund
State Authorised Public Accountant

Accounting policies

General information

The annual report of Arla Foods amba for 2002 / 03 has been prepared in accordance with the provisions applying to large class C enterprises under the Danish Financial Statements Act.

Changes in accounting policies

As a result of the new Danish Financial Statements Act, the accounting policies have been changed in the following areas:

1. **Product development projects**
   Product development costs are recognised in the balance sheet and amortised over three years provided that certain criteria have been met. Previously, all development costs were recognised in the profit and loss account when incurred. In accordance with the transitional provisions of the Danish Financial Statements Act, the application of this policy will have effect from this year and onwards.

2. **Finance leases**
   Assets held under finance lease are recognised in the balance sheet and depreciated in accordance with the general depreciation principles of the Group. The capitalised value of the residual lease payments is recognised as a liability in the balance sheet and the interest part of the lease payment is recognised in the profit and loss account. Previously, lease payments were recognised directly in the profit and loss account.

3. **Investments in subsidiaries and associates**
   The proportionate share of the individual subsidiaries' and associates' profit is recognised in the profit and loss account of the parent company. Previously, the results of non-dairy companies were not recognised in the profit and loss account of the parent company, but taken directly to equity. Non-dairy companies were defined as companies whose primary activities do not relate to the processing / selling of the milk weighed in from Arla Foods amba's members.

4. **Other investments**
   Other investments are measured at fair value. Previously, other investments were recognised and measured at cost.

5. **Derivative financial instruments**
   Derivative financial instruments are measured at fair value and recognised as other receivables / other payables. If the instruments are designated as hedges of future assets and liabilities, the changes in the value of the hedging instrument are recognised directly in capital and reserves until the hedged item is realised. Previously, the value of derivative financial instruments designated as hedges of future assets and liabilities was not recognised in the balance sheet.

6. **Deferred tax assets**
   Deferred tax assets are recognised in the balance sheet at the expected value of their utilisation. Previously, deferred tax assets were not recognised in the balance sheet.

Apart from the capitalisation of product development projects, the comparative figures for 2001 / 02 have been restated to comply with the changed accounting policies.

The accumulated effect of the changes in accounting policies for the parent company is an increase in profit for the year of DKK 315 million (2001 / 2002: DKK 96 million) of which DKK 313 million (2001 / 2002: DKK 172 million) relates to shares of profits in non-dairy related enterprises. The balance sheet total increases by DKK 186 million (DKK 199 million at 29 September 2002), whereas the equity at 30 September 2003 increases by DKK 149 million (DKK 146 million at 29 September 2002).

The accumulated effect of the changes in accounting policies for the Group is an increase in profit for the year of DKK 2 million. The balance sheet total increases by DKK 435 million, whereas the equity at 30 September 2003 increases by DKK 149 million.

The changes in accounting policies have had the following effect on the Group:

THE GROUP:	Profit		Assets		Equity	
DKK million	2001/02	2002/03	2001/02	2002/03	2001/02	2002/03
According to previous policies	1,161	1,092	21,736	26,410	6,632	7,006
Changes:						
Development projects	–	34	–	34	–	34
Finance leases	0	0	135	286	0	0
Other investments	–57	–6	16	23	16	23
Derivative financial instruments	0	0	30	18	30	18
Deferred tax assets	–19	–26	100	74	100	74
After changes in policies	1,085	1,094	22,017	26,845	6,778	7,155

In addition to the changes in accounting policies, the layout of the financial statements have been changed within the following areas:

Goodwill regarding investments in subsidiaries and associates

Goodwill regarding investments in subsidiaries and associates are recognised as investments. Previously, these were recognised separately as intangible assets in the parent company's balance sheet.

Other provisions

Some amounts previously shown as other payables have been transferred to other provisions.

In connection with the transition to the new Danish Financial Statements Act, the description of the accounting policies have been amplified and the terminology has been changed accordingly. The effect of the alteration on the annual report is purely editorial.

Consolidation

The consolidated financial statements comprise Arla Foods amba (the parent company) and those subsidiaries, cf. the list of group companies on pages 61-62, in which the parent company directly or indirectly holds more than 50% of the voting rights or in which the parent company in other ways has a controlling interest. 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 have been prepared by a consolidation of similar items from the parent company's and the individual subsidiaries' annual reports. Intra-group income and expenses, shares, outstanding accounts, dividends and unrealised gains and losses have been eliminated.

As regards the acquisition and sale of subsidiaries, the operations of such subsidiaries have been included in the consolidated financial statements for that part of the year in which the subsidiaries 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 the restatement of fair values is taken into account.

Gains or losses on full or part disposal of subsidiaries are stated as the difference between the sales amount and the carrying amount of net assets at the date of disposal including non-amortised goodwill and anticipated disposal costs. Gains and losses are recognised in the profit and loss account.

Any excess of the cost of the acquisition over the fair value of the identifiable assets and liabilities acquired (goodwill) is recognised as intangible assets and amortised in the profit and loss account based on an individual assessment of the useful life of the asset, not exceeding 20 years. Any excess of the fair values of the identifiable assets and liabilities acquired over the cost of the acquisition (negative goodwill), representing an anticipated adverse development in the acquired enterprises, is recognised in the balance sheet as deferred income and recognised in the profit and loss account as the adverse development is realised.

If the restatement of the fair values of the acquired enterprise's assets and liabilities results in negative net asset values in the acquired enterprise, then any minority assets are recognised as part of the positive difference. The positive difference relating to the minority asset is amortised until the minority interest represents a liability again. At the same time, the results from the acquired enterprise is recognised in full in the consolidated results. Amortisation for the year on the minority asset is determined so that the impact on the group's results is that only the group's share of the results is recognised.

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 capital and reserves are adjusted annually and recognised separately in the profit and loss account and balance sheet.

Foreign currency translation

For foreign subsidiaries, the profit and loss accounts are translated using the average exchange rates, whereas the balance sheet items are translated using the exchange rates at the balance sheet date.

For foreign associates, the shares of results are recognised at average exchange rates and shares of net book value are recognised at the exchange rate at the balance sheet date.

The translation differences that may arise on translation of the foreign companies' opening equity using the exchange rates at the balance sheet date and the translation differences resulting from translation of the foreign companies' profit and loss accounts using the average rates are adjusted over the equity.

Derivative financial instrument

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 profit and loss account together with changes in the 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 the equity. Income and expenses relating to such hedging transactions are transferred from the 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 profit and loss account when they occur.

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 a repayment obligation is no longer contingent.

Profit and loss account

Turnover

The turnover includes the year's invoiced sales less sales discounts. Any refunds and production subsidies from the EU are included in the turnover.

The turnover 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, wages and salaries incurred to realise the turnover for the year. Purchases from members do not include supplementary payments.

Share of the results in subsidiaries and associates

The proportionate share of the results after tax of the individual subsidiaries is recognised in the profit and loss account 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 profit and loss accounts after elimination of the proportionate share of intra-group profits / losses.

Financial items

Interest income and expense are recognised in the profit and loss account at amounts relating to the financial year.

Furthermore, financial items comprise both realised and unrealised value adjustments of securities and exchange rate adjustments.

Corporation tax

The taxable income of the companies is calculated in accordance with the national rules in force from time to time. For companies, which are jointly taxed, tax on the results for the financial year is entered at the current tax rate, calculated on the basis of the pre-tax results for the year, adjusted for non-taxable income and expenses. The deferred tax is measured at the current tax rate on all temporary differences between the carrying amount and the tax base.

Balance sheet

Fixed assets in generel

Fixed assets are written down to the recoverable amount (net realisable value) if this is lower than the carrying amount. Annual impairment tests are conducted of individual assets or groups of assets. Impairment tests are made for goodwill in relation to the expected future net income from the business or activities to which the goodwill relates.

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. as well as the equalisation sum for former members of Kløver Mælk A.m.b.A.

Product development projects qualifying for recognition in the balance sheet are measured at cost, including indirect costs incurred. Other development costs are recognised currently in the profit and loss account.

For the IT development project Ett Arla, only external costs for the establishment of the Group's future IT system are capitalised. Internal systems development costs are recognised currently in the profit and loss account.

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

Goodwill	3-20 years
Licences and trademarks, etc.	10 years
Equalisation sum	3 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.

Tangible assets

Tangible fixed assets are valued 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.

The assets are depreciated on a straight-line basis as from the time of acquisition or commissioning based on the expected useful lives of the assets 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

The carrying value of plant and machinery, fixtures and fittings, etc. at the establishment of the Arla Foods Group on 17 April 2000 is, however, depreciated on a straight-line basis over five years from this date.

Assets in course of construction and land are not depreciated.

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

Gains and losses on the realisation of tangible assets are recognised as depreciation.

Lease contracts regarding tangible assets, 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 discount rate. Assets held under finance lease are hereafter treated as the company's other tangible assets.

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 profit and loss account 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 in the balance sheet at the proportionate share of the enterprises' net asset values calculated in accordance with the parent company's accounting policies plus or minus 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.

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

Other investments (shares, mortgage deeds, bond holdings, etc.) are measured at fair value at the balance sheet date.

Stocks

Raw materials, consumables and goods for resale are measured at cost. The cost of the milk that forms part of stock has been recognised at the on-account 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.

Stocks are measured according to the FIFO method. If the cost exceeds the net realisable value, write-down is made to the net realisable value. The net realisable value is determined based on the turnover rate, marketability and development in the expected sales price of the goods.

Receivables

Receivables are recognised at amortised cost less write-down for anticipated bad debts based on an individual assessment. Amortised costs correspond in all material respects to nominal values.

Prepayments comprise costs

incurred concerning subsequent financial years.

Other current assets

Securities are measured at market value at the end of the financial year.

Equity

The parent company's equity at 30 September 2003 consists of:

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

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

1. The Board of Representatives may 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 to be paid out in the course of the 2000/2001 – 2007/2008 financial years.

No payments shall be made to the members of Arla Foods amba which reduce the total of the company's capital account and Reserve A. If such 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 105 million of this amount has been transferred to the capital account up to and including the financial year 2002/2003.

Reserve 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.

Subordinate loan capital

Pursuant to the Memorandum of Association, Arla ekonomisk förening contributed SEK 330 million in the form of subordinate loan capital, which in the event of the bankruptcy of the company ranks after other claims. The loan, on which interest accrues at the same rate as Reserve A, shall be repaid by one eighth annually, the first time in the 2001/2002 financial year.

Corporation 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 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 jointly taxed enterprises.

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.

Tax assets are set off in the balance sheet against tax liabilities within the same legal tax entity.

Other provisions

Pensions:
The Group has entered into pension agreements with many of the Group's employees.

The pension schemes comprise the defined contribution schemes and the 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 not 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 in connection with retirement, depending on e.g. the seniority of the employees.

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.

The actuarially calculated present value less the fair value of any assets related to the scheme are provided in the balance sheet under pension commitments.

Actuarial gains and losses arising as a consequence of the changed assumptions in the calculation of the pension commitment or in the computation of the assets related to the pension scheme are recognised in the profit and loss account over the anticipated service lives of the employees.

If the total actuarial gains and losses exceed 10% of the present value of the pension commitment, any excess amounts above the 10% will be recognised in profit and loss account over the average remaining service life of the employees covered by the pension scheme.

In connection with the acquisition of 51% of the shares in Express Dairies plc., the full pension commitment in both existing and acquired enterprises in the UK was recognised in the balance sheet at 30 September 2003.

Other provisions:
Other provisions comprise, in particular, the provisions for obligations in connection with mergers and reorganisations.

Liabilities

Amounts owed to mortgage credit institutions and banks 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 amortised cost.

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

Other liabilities, such as 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 cash flow statement is prepared according to 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 write-downs and changes to the working capital.

The cash flow from investing activities comprises cash flows in connection with the purchase and sale of intangible and tangible assets 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 as well as mortgage lenders.

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.

Segment information

Information is provided for dairy activities and other activities.

The items recognised in the profit for the year, including investments in associates and financial items, are allocated based on whether the items relate directly or indirectly to the activities. Other items are allocated proportionately.

Segment fixed assets comprise fixed assets used directly or indirectly in the operating activities of the segment.

Segment liabilities comprise liabilities resulting from the operating activities of the segment, including trade payables and other payables.

Profit and loss account

PARENT COMPANY				GROUP	
2001.10.01 –2002.09.29	2002.09.30 –2003.09.30	MDKK million	Note	2002.09.30 –2003.09.30	2001.10.01 –2002.09.29
25,751	26,034	**Turnover**	1	40,647	39,441
–22,904	–23,175	Production costs	2	–32,873	–31,909
2,847	**2,859**	**Gross profit**		**7,774**	**7,532**
–1,363	–1,395	Sales and distribution costs	2	–4,941	–4,791
–404	–475	Administrative and joint costs	2 / 3	–1,433	–1,304
50	41	Other operating income		125	187
–97	–183	Other operating expenses		–283	–213
1,033	**847**	**Operating profit**		**1,242**	**1,411**
95	83	Results in subsidiaries	8	–	–
3	–2	Results in associates	8	–20	–6
111	220	Divestment of subsidiary		220	111
–141	–37	Net financial items	4	–245	–367
1,101	**1,111**	**Profit from ordinary activities before tax**		**1,197**	**1,149**
–16	–17	Corporation tax	5	–106	–66
1,085	**1,094**	**Profit for the year**		**1,091**	**1,083**
–	–	Minority interest share of results in subsidiaries	9	3	2
1,085	**1,094**	**Arla Foods amba's share of results for the year**		**1,094**	**1,085**
		Proposed profit appropriation:			
575	546	Supplementary payments to Arla Foods' members		546	575
		Tranferred to capital account:			
126	123	Reconsolidation acc. to the articles of association		123	126
286	344	Other transfers		344	286
412	467	Total		467	412
98	81	Net revaluation acc, to the equity methods		–	–
–	–	Other reserves		81	98
1,085	**1,094**	**Total**		**1,094**	**1,085**

Balance sheet

PARENT COMPANY Balance sheet at 02.09.29	PARENT COMPANY Balance sheet at 03.09.30	DKK million	Note	GROUP Balance sheet at 03.09.30	GROUP Balance sheet at 02.09.29
		ASSETS			
		Fixed assets			
		Intangible assets	6		
0	0	Licences and trademarks, etc.		53	75
–	–	Group goodwill		2,260	642
92	0	Equalisation sum		0	92
–	359	Development projects		375	–
92	**359**	**Total**		**2,688**	**809**
		Tangible assets	7		
1,389	1,423	Land and buildings		3,906	3,209
1,905	1,948	Plant and machinery		4,678	3,944
105	105	Fixtures and fittings, tools and equipment		523	615
142	325	Tangible assets in course of construction		932	481
3,541	**3,801**	**Total**		**10,039**	**8,249**
		Investments	8		
2,628	1,977	Investments in subsidiaries		–	–
0	1,147	Subordinate loans to subsidiaries		–	–
99	96	Investments in associates		281	274
830	833	Other securities and investments		958	1,060
0	0	Other receivables		7	3
3,557	**4,053**	**Total**		**1,246**	**1,337**
7,190	**8,213**	**Total fixed assets**		**13,973**	**10,395**
		Current assets			
		Stocks			
442	491	Raw materials and consumables		780	783
730	682	Work in progress		1,119	1,125
206	256	Finished goods and goods for resale		1,906	1,852
1,378	**1,429**	**Total**		**3,805**	**3,760**
		Receivables			
1,120	1,178	Trade receivables		4,604	4,022
3,871	3,013	Amounts owed by group enterprises		0	0
158	119	Amounts owed by associates		158	360
770	434	Other receivables		1,229	1,459
–	–	Deferred tax assets	11	786	100
6	9	Prepayments		79	81
5,925	**4,753**	**Total**		**6,856**	**6,022**
0	**0**	**Securities**		**785**	**927**
502	**874**	**Cash at bank and in hand**		**1,426**	**913**
7,805	**7,056**	**Total current assets**		**12,872**	**11,622**
14,995	**15,269**	**TOTAL ASSETS**		**26,845**	**22,017**

Balance sheet

PARENT COMPANY Balance sheet at 02.09.29	PARENT COMPANY Balance sheet at 03.09.30	DKK million	Note	GROUP Balance sheet at 03.09.30	GROUP Balance sheet at 02.09.29
		EQUITY, MINORITY INTERESTS AND LIABILITIES			
		Equity			
5,174	5,895	Capital account		5,895	5,174
555	461	Reserve A		461	555
500	500	Reserve B		500	500
539	299	Net revaluation acc. to the equity method		0	0
10	0	Hedging instruments		18	30
–	–	Other reserves		281	519
6,778	**7,155**	**Total equity**		**7,155**	**6,778**
–	**–**	**Minority interests**	9	**44**	**87**
236	**200**	**Subordinate loan capital**	10	**200**	**236**
7,014	**7,355**	**Total capital base**		**7,399**	**7,101**
		Provisions			
24	22	Deferred tax	11	342	240
0	0	Pensions	12	2,966	699
266	127	Other provisions	13	575	824
290	**149**	**Total provisions**		**3,883**	**1,763**
		Liabilities			
		Long-term liabilities	14		
1,882	1,791	Mortgage credit institutions		2,423	2,461
1,376	1,624	Banks, etc.		3,290	2,238
3,258	**3,415**	**Total**		**5,713**	**4,699**
		Short-term liabilities			
383	24	Short-term portion of long-term liabilities		31	451
380	463	Credit institutions		2,297	2,070
575	546	Supplementary payments		546	575
1,088	909	Trade payables		2,930	2,676
1,538	1,413	Amounts owed to group enterprises		1,206	1,156
0	13	Amounts owed to associates		13	0
29	26	Corporation tax		137	44
407	956	Other payables		2,571	1,449
33	0	Deferred income		119	33
4,433	**4,350**	**Total**		**9,850**	**8,454**
7,691	**7,765**	**Total liabilities**		**15,563**	**13,153**
14,995	**15,269**	**TOTAL EQUITY, MINORITY INTERESTS AND LIABILITIES**		**26,845**	**22,017**
		Contingent liabilities, guarantees, etc.	15		
		Related parties	16		

Equity movements

GROUP

DKK million	Balance at 02.09.29 according to previous policy	Changed accounting policies	Balance at 02.09.29 according to new policy	Profit for the year	Other adjustments	Total
Capital account	5,311	–137	5,174	467	254	5,895
Reserve A	555	–	555	–	–94	461
Reserve B	500	–	500	–	–	500
Net revaluation acc. to the equity method	0	0	0	0	0	0
Hedging instruments	–	30	30	–	–12	18
Other reserves	266	253	519	81	–319	281
Total	**6,632**	**146**	**6,778**	**548**	**–171**	**7,155**

PARENT COMPANY

DKK million	Balance at 02.09.29 according to previous policy	Changed accounting policies	Balance at 02.09.29 according to new policy	Profit for the year	Other adjustments	Total
Capital account	5,311	–137	5,174	467	254	5.895
Reserve A	555	–	555	–	–94	461
Reserve B	500	–	500	–	–	500
Net revaluation acc. to the equity method	266	273	539	81	-321	299
Hedging instruments	0	10	10	–	–10	0
Total	**6,632**	**146**	**6,778**	**548**	**–171**	**7,155**

Cash flow statement

DKK million	GROUP 2002/2003	2001/2002
Cash flows from operating activities		
Profit for the year	1,094	1,085
Depreciation and other operating items without cash impact	1,796	1,432
Share of results in investments	20	6
Changes in provisions	43	49
Changes in stocks	41	–277
Changes in receivables	570	–896
Changes in trade payables and other payables	–722	–336
Corporation tax paid	–66	–71
Cash flows from operating activities	**2,776**	**992**
Cash flows from investing activities		
Investment in intangible assets, net	–286	–119
Investment in tangible assets, net	–1,983	–1,110
Other investments, net	112	231
Cash flows for investing activities	**–2,157**	**–998**
Cash flows from financing activities		
Changes in debt to banks and mortgage credit institutions	–385	–19
Cash flows from financing activities	**–385**	**–19**
Changes in cash funds and securities	**234**	**–25**
Cash funds and securities at 30 September 2002	1,840	1,865
Addition of cash on acquisition of enterprise	137	0
Cash funds and securities at 30 September 2003	**2,211**	**1,840**

Notes

Note 1: **Segment information**

Group 2002/03

DKK million	Dairy activities	Other
Turnover	37,693	2,954
Operating profit	1,087	155
Total fixed assets	13,022	951
Total liabilities	14,783	780

The geographical distribution is shown on page 2 of the annual report.

Note 2: **Costs**

PARENT COMPANY			GROUP	
2001/2002	2002/2003	DKK million	2002/2003	2001/2002
		Staff costs:		
		By function		
–1,901	–1,979	Production	–3,769	–3,672
–176	–170	Sale and distribution	–1,580	–1,582
–223	–269	Administration and joint costs	–671	–622
–2,300	**–2,418**	**Total**	**–6,020**	**–5,876**
		By type		
–2,156	–2,259	Wages, salaries and remuneration	–5,088	–4,976
–130	–144	Pensions	–378	–374
–14	–15	Other social security costs	–554	–526
–2,300	**–2,418**	**Total**	**–6,020**	**–5,876**
6,770	**6,742**	**Average number of employees (man years)**	**17,791**	**17,866**

Salaries and remuneration incl. pensions for the Group include the parent company's Management Board of DKK 7 million (2001/02: DKK 7 million) and fees to the parent company's Supervisory Board and Board of Representatives of DKK 10 million (2001/02: DKK 10 million).

PARENT COMPANY			GROUP	
2001/2002	2002/2003	DKK million	2002/2003	2001/2002
		Depreciation:		
		By function		
–92	–92	Equalisation sum (production)	–92	–92
–499	–557	Production	–1,149	–996
–14	–39	Sale and distribution	–162	–154
0	0	Administration	–144	–140
6	3	Profit/loss on sale of intangible and tangible assets	2	–11
–599	**–685**	**Total**	**–1,545**	**–1,393**

Notes

Note 3: **Fee to the auditors appointed by the Board of Representatives**

PARENT COMPANY 2001/2002	PARENT COMPANY 2002/2003	DKK million	GROUP 2002/2003	GROUP 2001/2002
		Audit fee:		
–4	–4	KPMG C. Jespersen	–10	–9
–2	–2	PricewaterhouseCoopers	–7	–6
–	–	Others	–1	–1
		Other services:		
–3	–3	KPMG C. Jespersen	–15	–17
–1	–1	PricewaterhouseCoopers	–12	–2
–10	**–10**	**Total**	**–45**	**–35**

Note 4: **Net financial items**

PARENT COMPANY 2001/2002	PARENT COMPANY 2002/2003	DKK million	GROUP 2002/2003	GROUP 2001/2002
		Expense:		
–24	–16	Interest expense to group enterprises	–11	–17
–260	–234	Other financing charges	–415	–486
–284	**–250**	**Total**	**–426**	**–503**
		Income:		
121	130	Interest income from group enterprises	6	9
22	83	Other financing income	175	127
143	**213**	**Total**	**181**	**136**
–141	**–37**	**Net financial items**	**–245**	**–367**

Note 5: **Corporation tax**

PARENT COMPANY 2001/2002	PARENT COMPANY 2002/2003	DKK million	GROUP 2002/2003	GROUP 2001/2002
–33	–29	Tax on taxable income for the year	–95	–74
10	2	Adjustment of deferred tax	–23	–8
7	10	Correction of tax from previous years	12	16
–16	**–17**	**Total**	**–106**	**–66**

Notes

Note 6: **Intangible fixed assets**

GROUP

DKK million	Licences and trademarks, etc.	Group goodwill	Equalisation sum	Product development projects	IT development project
Cost at 30.09.2002	103	812	276	–	0
Exchange rate adjustments	–1	–21	0	–	0
Additions on acquisition of enterprises	0	1.978	0	0	0
Additons during the year	0	4	0	40	341
Disposals during the year	–23	–306	–276	0	0
Cost at 2003.09.30	**79**	**2.467**	**0**	**40**	**341**
Amortisation and impairment 30.09.2002	–28	–170	–184	–	0
Exchange rate adjustments	2	6	0	–	0
Amortisation and impairment for the year	–12	–93	–92	–6	0
Depreciation and impairment, disc. assets	12	50	276	0	0
Amortisation and impairment 2003.09.30	**–26**	**–207**	**0**	**–6**	**0**
Carrying amount at 2003.09.30	**53**	**2,260**	**0**	**34**	**341**

PARENT COMPANY

DKK million	Group goodwill	Equalisation sum	Product development projects	IT development project
Cost at 30.09.2002	323	276	–	0
Transferred to investments	–323	0	–	–
Additions during the year	0	0	22	341
Disposals for the year	0	–276	0	0
Cost at 2003.09.30	**0**	**0**	**22**	**341**
Amortisation and impairment 2002.09.30	–46	–184	–	0
Transferred to investments	46	0	–	–
Amortisation and impairment for the year	0	–92	–4	0
Amortisation and impairment, disc. assets	0	276	0	0
Amortisation and impairment 2003.09.30	**0**	**0**	**–4**	**0**
Carrying amount at 2003.09.30	**0**	**0**	**18**	**341**

Notes

Note 7: **Tangible fixed assets**

DKK million	GROUP Land and buildings	Plant and machinery	Fixtures and fittings, tools, etc.	Assets in course of construction
Cost at 2002.09.30	3,702	5,468	943	481
Change in accounting pol., finance leases	10	71	123	–
Exchange rate adjustments	–52	–46	–7	–6
Additions on acquisition of enterprises	647	693	57	0
Additions for the year	348	992	80	642
Transferred during the year	91	94	0	–185
Disposals for the year	–55	–87	–118	0
Cost at 2003.09.30	**4,691**	**7,185**	**1,078**	**932**
Depreciation and impairment 2002.09.30	–503	–1.581	–396	0
Change in accounting pol., finance leases	0	–14	–55	–
Exchange rate adjustments	7	20	4	0
Depreciation and impairment for the year	–302	–972	–195	0
Depreciation and impairment, disc.assets	13	40	87	0
Depreciation and impairment 2003.09.30	**–785**	**–2.507**	**–555**	**0**
Carrying amount at 2003.09.30	**3,906**	**4,678**	**523**	**932**
Assets held under finance lease	**9**	**206**	**49**	**0**

Depreciation and impairment include DKK 125 million regarding structure rationalisation write-downs. The amount is transferred from the balance sheet item Other provisions and has therefore not affected the profit and loss account for 2002/03.
Additions for the year have been reduced by EU subsidies and subsidies from other public authorities of DKK 1 million.
The official annual valuation of Danish land and buildings with a carrying amount of DKK 1,858 million is assessed at DKK 1,890 million at 1 January 2003, to which should be added investments subsequent to this date.

DKK million	PARENT COMPANY Land and buildings	Plant and machinery	Fixtures and fittings, tools, etc.	Assets in course of - construction
Cost at 2002.09.30	1,634	2,700	90	142
Change in accounting pol., finance leases	–	8	77	–
Additions during the year	116	462	42	325
Transferred during the year	69	72	0	–142
Disposals for the year	–10	0	–24	0
Cost at 2003.09.30	**1,809**	**3,242**	**185**	**325**
Depreciation and impairment 2002.09.30	–245	–802	–31	0
Change in accounting pol., finance leases	0	–1	–31	–
Depreciation and impairment for the year	–145	–491	–28	0
Depreciation and impairment, disc. assets	4	0	10	0
Depreciation and impairment 2003.09.30	**–386**	**–1,294**	**–80**	**0**
Carrying amount at 2003.09.30	**1,423**	**1,948**	**105**	**325**
Assets held under finance lease	**0**	**5**	**34**	**0**

Depreciation and impairment include DKK 72 million regarding structure rationalisation write-downs.The amount is transferred from the balance sheet item Other provisions and has therefore not affected the profit and loss account for 2002/03.
Additions for the year have been reduced by EU subsidies and other public authorities of DKK 1 million.
The official annual valuation of land and buildings at 1 January 2003 is assessed at DKK 1,439 million, to which should be added investments subsequent to this date.

Notes

Note 8: **Investments**

DKK million	Investments in associates	Other securities and investments	Other receivables
	GROUP		
Cost at 2002.09.30	287	1.047	3
Exchange rate adjustments	–8	3	0
Additions on acquisition of enterprises	45	0	2
Additions during the year	85	94	5
Disposals during the year	–95	–221	–3
Cost at 2003.09.30	**314**	**923**	**7**
Adjustments at 2003.09.30	–13	6	0
Changes in accounting policies	–	7	–
Results for the year	–20	13	–
Other adjustments	0	9	0
Adjustments at 2003.09.30	**–33**	**35**	**0**
Carrying amount at 2003.09.30	**281**	**958**	**7**

DKK million	Investments in subsidiaries	Subordinate loans to subsidiaries	Investments in associates	Securities and other investments
		PARENT COMPANY		
Cost at 2002.09.30	1.812	0	104	812
Tranferred from goodwill	323	–	–	–
Exchange rate adjustments	–69	0	0	2
Additions during the year	153	1.147	66	10
Disposals during the year	–541	0	–67	–31
Cost at 2003.09.30	**1,678**	**1,147**	**103**	**793**
Adjustments at 30.09.2002	350	0	–5	11
Change in accounting policies	189	0	0	7
Tranferred from goodwill	–46	–	–	–
Disitribution / dividends	–306	0	0	0
Profit for the year	98	0	3	13
Amortisation of goodwill for the year	–15	0	–5	0
Changes in intra-group profit on stocks	16	0	0	0
Other adjustments	13	0	0	9
Adjustments at 2003.09.30	**299**	**0**	**–7**	**40**
Carrying amount at 2003.09.30	**1,977**	**1,147**	**96**	**833**
Of which goodwill 30.09.2003	**138**	**–**	**30**	**–**

Notes

Note 9: **Minority interests**

DKK million	GROUP 2002.09.30 –2003.09.30	2001.10.01 –2002.09.29
Minority interests beginning of year	87	85
Share of results for the year	–3	-–2
Changes in ownership shares, withdrawn minority interests etc.	–40	4
Minority interests, year end	**44**	**87**

Note 10: **Subordinate loan capital**

PARENT COMPANY 2001.10.01 –2002.09.29	2002.09.30 –2003.09.30	DKK million	GROUP 2002.09.30 –2003.09.30	2001.10.01 –2002.09.29
252	236	Subordinate loan capital, beginning	236	252
18	3	Exchange rate adjustments	3	18
–34	–39	Repayments during the year	–39	–34
236	**200**	**Subordinate loan capital, year end**	**200**	**236**

Note 11: **Deferred tax**

PARENT COMPANY 2001.10.01 –2002.09.29	2002.09.30 –2003.09.30	DKK million	GROUP 2002.09.30 –2003.09.30	2001.10.01 –2002.09.29
33	24	Deferred tax, beginning of year	140	370
–	–	Changes in accounting policies	–	–119
1	0	Exchange rate adjustments	13	15
–	–	Addition on acquisition of enterprises	–607	–
–	–	Disposal on sale of subsidiary	–13	–134
–10	–2	Other changes in deferred tax	23	8
24	**22**	**Deferred tax, year end**	**–444**	**140**

Deferred tax in the Group consists of an liability of DKK 342 million (DKK 240 million at 29 September 2002) and a deferred tax asset of DKK 786 million (DKK 100 million at 29 September 2002). The change for the year of DKK 23 million (2001/2002: DKK 8 million) represents a reduction of DKK 3 million (a reduction of DKK 11 million in 2001/2002) regarding the liability and a reduction of DKK 26 million (a reduction of DKK 19 million in 2001/2002) regarding deferred tax assets.

Notes

Note 12: **Pensions**

The provision comprises defined benefit schemes in Sweden and the UK and is computed as follows:

DKK million	GROUP 2003.09.30	GROUP 2002.09.29
Present value of the pension commitments	6,750	1,885
Non-included actuarial losses	0	–441
Market value of the assets of the pension schemes	–3,784	–745
Total	**2,966**	**699**

Development in provisions for the year can be specified as follows:

DKK million	2002.30.09 –2003.30.09	2001.10.01 –2002.09.29
At the beginning of the year	699	609
Exchange rate adjustments	10	39
Additions on acqusition of enterprises	1,690	–
Transferred from other provisions	531	–
Other movements, net	36	51
At year end	**2,966**	**699**

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 6,019 million at 30 September 2003 against DKK 1,199 million at 29 September 2002) less the market value of the assets (DKK 3,784 million at 30 September 2003 against DKK 745 million at 29 September 2002) amounts to DKK 2,235 million.

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 731 million.

Note 13: **Other provisions**

PARENT COMPANY 2001.10.01 –2002.09.29	PARENT COMPANY 2002.30.09 –2003.30.09	DKK million	GROUP 2002.30.09 –2003.30.09	GROUP 2001.10.01 –2002.09.29
193	266	Other provisions, beginning of year	824	748
–	–	Additions on acquisition of enterprises	293	–
–	–	Transferred to pensions	–531	–
117	51	Provided during the year	184	126
–44	–190	Applied during the year	–195	–50
266	**127**	**Other provisions, year end**	**575**	**824**

Note 14: **Long-term liabilities**

PARENT COMPANY 2001.10.01 –2002.09.29	PARENT COMPANY 2002.09.30 –2003.09.30	DKK million	GROUP 2002.09.30 –2003.09.30	GROUP 2001.10.01 –2002.09.29
2,112	2,526	Long-term payables falling due after five years after the balance sheet date	2,944	2,722

Notes

Note 15: **Contingent liabilities, guarantees, etc.**

PARENT COMPANY			GROUP	
2001.10.01 –2002.09.29	2002.09.30 –2003.09.30	DKK million	2002.09.30 –2003.09.30	2001.10.01 –2002.09.29
		Contingent liabilities		
2,444	2,371	Surety and guarantee obligations	999	1,121
46	38	Operating leases obligations	748	269
314	476	Obligations relating to agreement on the supply of fixed assets	1,278	475
		To cover exchange risks, the following forward contracts have been entered into:		
869	998	Forward contracts (buying)	1,159	1,262
4,856	4,563	Forward contracts (selling)	4,613	5,162
1,050	1,050	Interest swaps	1,216	1,213
		The following assets are deposited as security for debt:		
170	170	Owner's mortgage in real estate	375	463
448	422	with a carrying amount of	1,099	1,221
0	0	Securities, carrying amount	336	587
590	604	Arla Foods amba has received guarantee certificates from members of the cooperative. The basis for these guarantees is the individual member's deliveries over the past 5 financial years, calculated as DKK 20 per 1,000 kg milk delivered.	604	590
		DKK 0 has been provided as security for debt.		

There are a number of share option schemes in the former Express Dairies plc, which gives the employees and management the opportunity to buy shares in the company over a number of years on a predetermined price. The schemes comprise a total of 0.8% of the share capital.

The group is a party to a few lawsuits. The outcome of these cases is not expected to significantly affect the profit for the year or the assessment of the financial position of the group.

Note 16: **Related parties**

Related parties comprise the Board of Representatives, the Management Board and the Supervisory Board, group enterprises and associates, cf. the group chart on pages 60-61.

Related parties with controlling interest comprise MD Foods amba and Arla Ek. f. Members of the Board of Representatives and the Supervisory Board are paid for milk deliveries by MD Foods amba and Arla Ek. f. on equal terms with other members of these two companies.

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 including pensions have been disclosed separately in the note regarding staff costs.

Group companies

Subsidiaries, associates and investments at 30 September 2003

Subsidiaries	**Ownership**
Arla Foods AB, Sweden	100.0%
ASM Mjölksocker AB, Sweden (100.0%)	
Arla Ost och Smör Produktion AB, Sweden (100.0%)	
Arla Foods Specialost AB, Sweden (100%)	
Bregott AB, Sweden (62.4%)	
Arla Foods Distribution amba, Denmark	100.0%
Danos A / S, Denmark (100.0%)	
Gredstedbro Ost A / S, Denmark (100.0%)	
Danmark Protein A / S, Denmark (100.0%)	
Delimo A / S, Denmark (100.0%)	
Økomælk A / S, Denmark (100.0%)	
Enigheden A / S, Denmark (100.0%)	
Arla Foods Holding AB, Sweden	100.0%
Oy Arla Foods Ab, Finland (100.0%)	
Arla Foods AS, Norway	100.0%
Arla Foods Inc., Canada	100.0%
Arla Foods GmbH, Germany	100.0%
Arla Foods S.r.l., Italy	100.0%
Arla Foods Inc., USA	100.0%
Arla Foods S.A.R.L., France	100.0%
Arla Foods S.A., Spain	100.0%
Andelssmør A.m.b.a., Denmark	95.4%
AFF P / S, Denmark	75.0%
Arla Foods Ingredients amba, Denmark	100.0%
Arla Foods Ingredients GmbH, Germany (100.0%)	
Arla Foods Ingredients Inc., USA (100.0%)	
Arla Foods Ingredients KK, Japan (100.0%)	
Arla Foods Ingredients AB, Sweden (100.0%)	
Arla Foods Ingredients Ltd., England (100.0%)	
Arla Foods Ingredients Korea Co. Ltd., South Korea (70.0%)	
AM Produktion K / B, Sweden (66.7%. The remaining 33.3% is owned by Arla Foods AB)	
AM Foods K / S, Denmark (66.7%. The remaining 33.3% is owned by Arla Foods amba)	
Arla Foods Sp. Z o.o., Poland	100.0%
Arla Foods International A / S, Denmark	100.0%
Danya Foods Ltd., Saudi Arabia	
Arla Foods UK Plc., England	
Arla Foods Plc., England	
Express Ltd., England	
Arla Foods Holding A / S, Denmark	100.0%
Medani A / S, Denmark (100.0%)	
Kingdom Food Products ApS, Denmark (100.0%)	
Arla Foods Leasing A / S, Denmark (100.0%)	
Ejendomsanpartsselskabet St. Ravnsbjerg, Denmark (100.0%)	
Rynkeby Foods A / S, Denmark (50.0%. The remaining 50.0% is owned by Kinmaco ApS)	
Kinmaco ApS, Denmark (100.0%)	
GB Finans A / S, Denmark (100.0%)	
Arla Insurance Company (Guernsey) Limited, Guernsey (100.0%)	
Arla Foods Trading A / S, Denmark (100.0%)	

Group companies

Subsidiaries, associates and investments at 30 September 2003

(continued)

Subsidiaries	Ownership
De Danske Mejeriers Fællesindkøb Amba, Denmark	100.0%
Dairy Fruit A / S, Denmark (100.0%)	
A / S Crispy Food International, Denmark (100.0%)	
Ejendomsselskabet Østre Gjesingvej 19 A / S, Denmark (100.0%)	
Danapak A.m.b.a., Denmark	94.2%
Danapak A / S, Denmark (100.0%)	
Danapak Kartonnage A / S, Denmark (100.0%)	
Danapak Plast A / S, Denmark (100.0%)	
Tölkki OY, Finland (100.0%)	
Danapak Faltschachtelsysteme GmbH, Germany (100.0%)	
Danapak Cartons Ltd., England (100.0%)	
Danapak Leasing ApS, Denmark (100.0%)	
Danapak WP A / S, Denmark (100.0%)	
Frödinge Holding AB, Sweden	100.0%
Frödinge Mejeri AB, Sweden (100.0%)	
Medipharm Holding AB, Sweden	100.0%
Medipharm AB, Sweden (100.0%)	
Munka Invest AB, Sweden (100.0%)	
Medipharm Investments Ltd., USA (100.0%)	
Medipharm CZ s.r.o., The Czech Republic (100.0%)	
Medipharm Hungary Kft, Hungary (51.0%)	
Associates	
JO-Bolaget Fruktprodukter HB, Sweden (owned through Arla Foods AB)	50.0%
HB Grådö Produktion, Sweden (owned through Arla Foods AB)	50.0%
Synbiotics AB, Sweden (owned through Arla Foods AB)	50.0%
Arla Foods Hellas S.A., Greece	60.0%
Arla Foods Ingredients S.A., Argentina (owned through Arla Foods Ingredients amba)	50,0%
Biolac KG, Germany, (owned through Arla Foods Ingredients GmbH)	50.0%
Dan Vigor Ltd. Brazil (owned through Arla Foods International A / S)	50.0%
Danske Immobilien K / S, Denmark (owned through Medani A / S)	35.0%
Cocio A / S, Danmark (owned through Danmark Protein A / S)	50.0%
The Danapak Flexibles Group, Denmark (owned through Danapak A / S)	40.0%
Arla National Food Products LLC, The United Arab Emirates	40.0%
Kronost AB, Sweden (owned through Arla Foods AB)	25.0%
Other investments	
Mejeriforeningen, Denmark	91.3%
Svensk Mjölk Ekonomisk förening, Sweden	42.0%
Lantbrukarnas Riksförbund, förening upa, Sweden	19.0%

According to Section 127(4) of the Danish Financial Statements Act, information about individual subsidiaries has not been disclosed, as it is believed that such information may cause significant damage to these enterprises.

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

Management and Supervisory Board


Jens Bigum
Man. Director


Åke Modig
Dep.-Man. Director


Knud Erik Jensen
Chairman


Åke Hantoft
Deputy Chairman


Leif Backstad


Viggo Ø. Bloch


Steen Bolvig


Bjarne Bundesen


Christer Eliasson

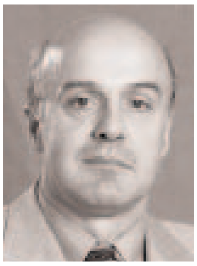

Anders Ericsson


Leif Eriksson


Elisabeth Gauffin


Thomas Johansen


Sören Kihlberg


Ove Møberg


Per Norstedt


Jan Toft Nørgaard


Kaj Ole Pedersen

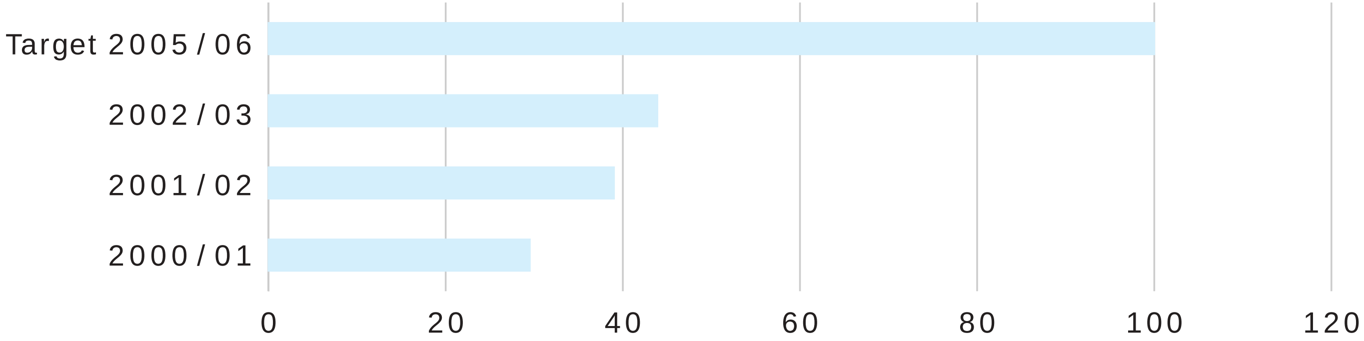

Gunnar Pleijert


Søren Rasmussen


Pejter Søndergaard

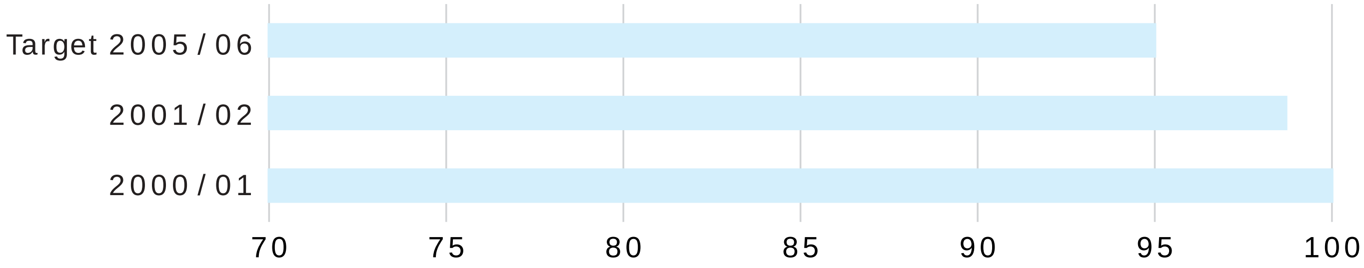

Bent Juul Sørensen

ISO 14001 accredited units
Arla Foods in Sweden and Denmark



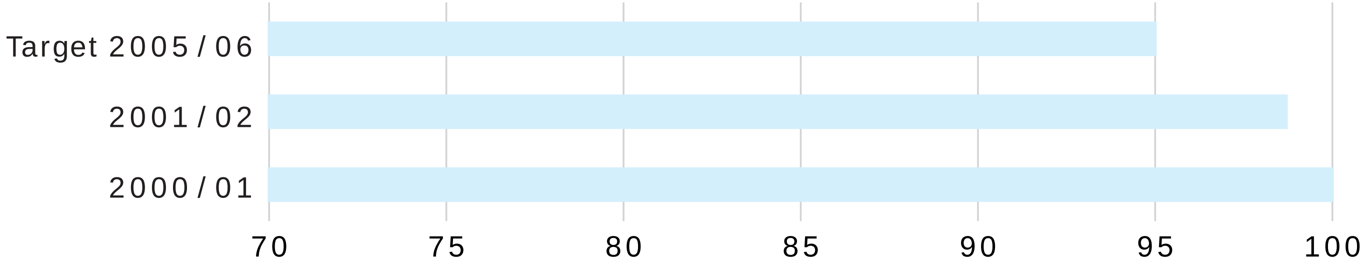
Water consumption

(index, water consumption in relation to raw materials and finished products)



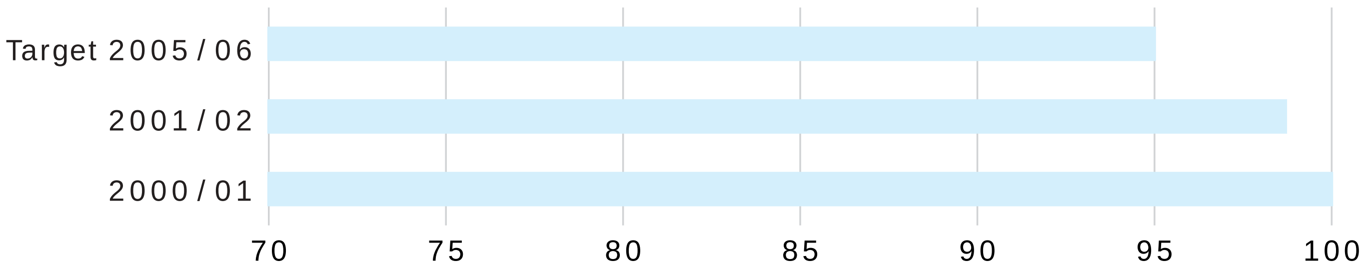
Energy consumption

(index, energy consumption in relation to raw materials and finished products)



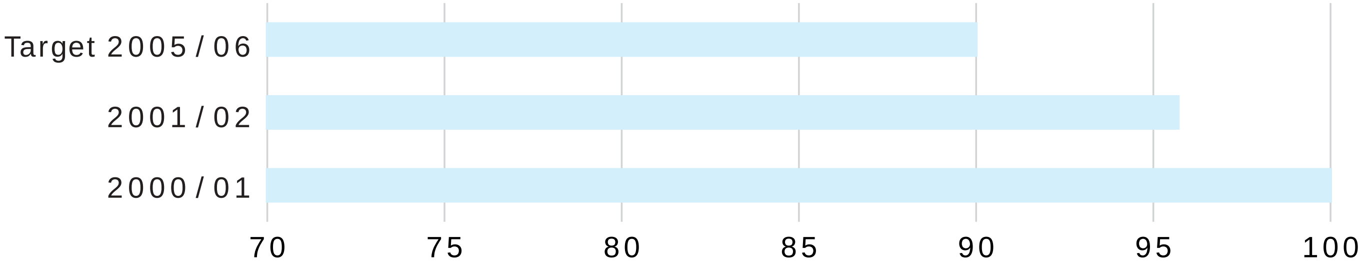
CO_2 emission

(index, CO_2 emission in relation to raw materials and finished products)



NO_x emission

(index, NO_x emission in relation to raw materials and finished products)



Accident frequency - DK

(Number of accidents per 1 million working hours)

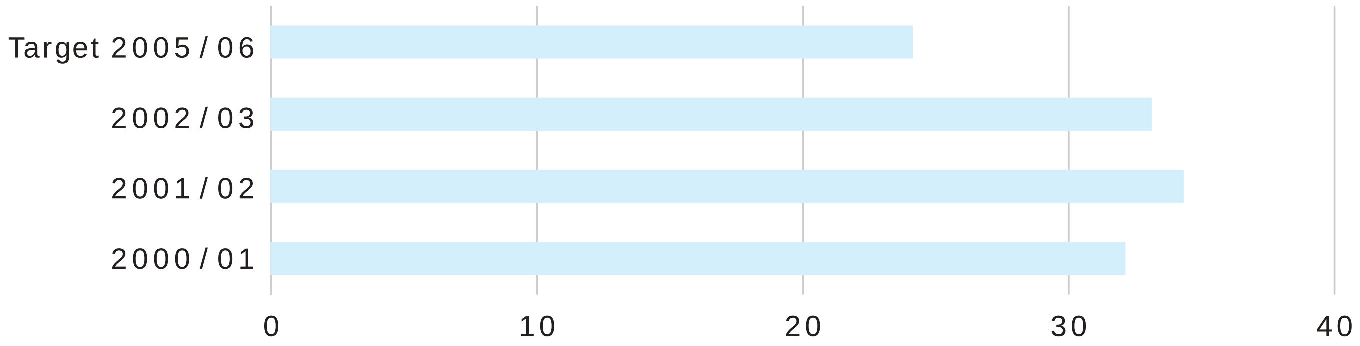
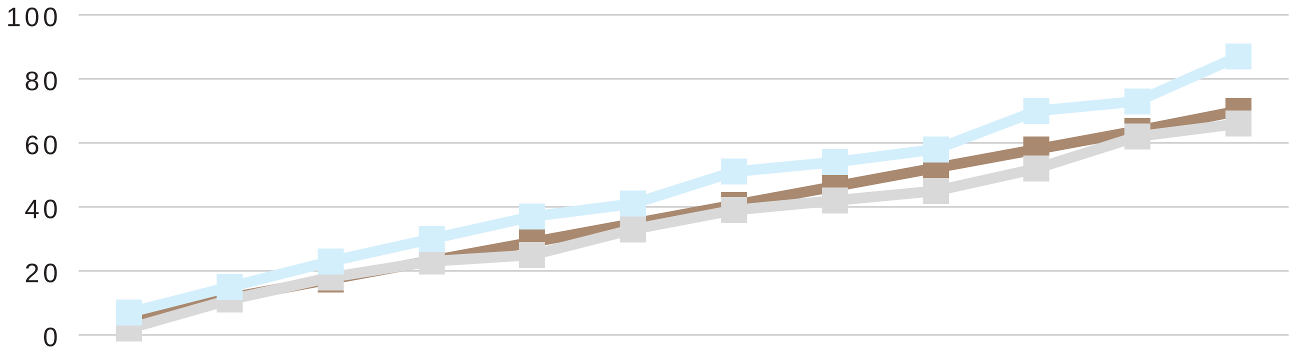
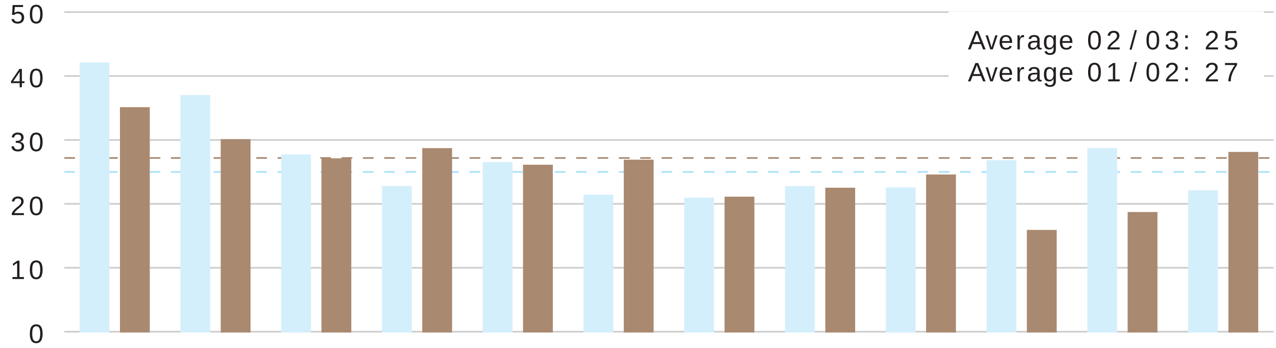


Figure 1: Accumulated accidents per period in the UK



	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2001/2002	7	15	23	30	37	41	51	54	58	70	73	87
2002/2003	2	11	18	23	25	33	39	42	45	52	62	66
Target	5,8	11,6	17,4	23,2	29	34,8	40,6	46,4	52,2	58	63,8	70

Figure 2 Accident frequency rate in the UK



	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2001/2002	42,0	36,9	27,6	22,7	26,4	21,3	20,8	22,7	22,4	26,7	28,6	22,0
2002/2003	35,0	30,0	27,0	28,6	26,0	26,8	21,0	22,4	24,5	15,8	18,6	28,0

Figure 1: Foreign exchange index

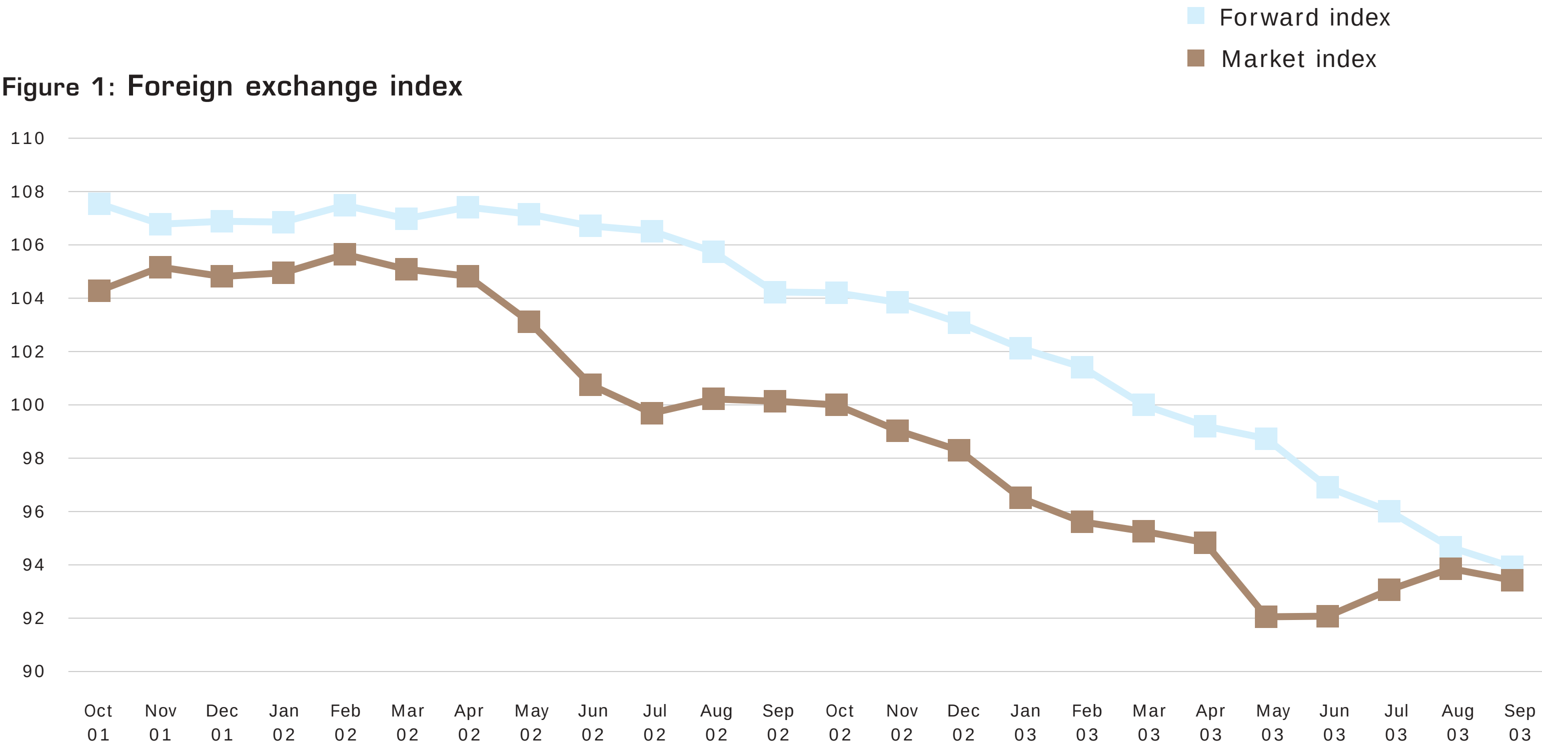


Figure 2: Hedging compared to annual budget