

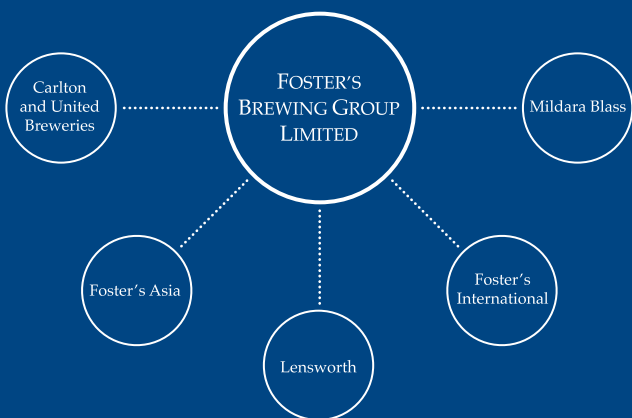


FOSTER'S BREWING GROUP LIMITED

Report to shareholders for the six months ended 31 December 1998



Foster's Brewing Group is a global beer and wine company dedicated to delivering premium branded products to consumers in more than 135 countries around the world.



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- Profit before interest and tax up 15.7%, with average funds employed down 19.6%.
- All operating divisions contributed to profit growth:
 - profit from ongoing businesses up 33.5%, on a 20.1% increase in sales
 - Carlton and United Breweries profit up 14.1%
 - Mildara Blass profit up 27.1%.
- On track for a significant rise in full year rates of return.
- Earnings per share up 15.6%.
- Interim dividend up 10%, fully franked.



FOSTER'S®

OFFICIAL BEER OF THE
SYDNEY 2000 OLYMPIC GAMES



SUPPORTER

This set of half-year results marks an important milestone for our company. For the first time in recent years, every business has contributed an improved result to the bottom line. We have produced the sort of solid operational performance and consistent results you can now expect of Foster's.

I urge you to read this report, not only for an appreciation of the excellent results produced across the board by our businesses, but also to gain an understanding of the potential returns we expect to deliver from some of our strategic growth initiatives. This report again highlights outstanding results from our cornerstone businesses, CUB and Mildara Blass. Alongside these, you will find evidence of growing returns from initiatives such as our European wine clubs, our hotels and leisure strategy, the development of Foster's in more than 135 global markets, our Asian strategy and international winemaking projects.

The picture which emerges more strongly than ever this half, is of a company which is moving forward, working hard on building shareholder value in all of its businesses.

We are coming out of a period of change, and we thank you for your support during the process. We will maintain our focus on delivering results for all shareholders.



Ted Kunkel

President and Chief Executive Officer

Divisional Summary

- Carlton and United Breweries (CUB) profit rose 14.1%.
- Mildara Blass profit was 27.1% higher.
- Foster's International profit increased from \$0.5 million to \$5.2 million.
- The loss from Foster's Asia was cut from \$21.6 million to \$15.1 million.
- Profits from Lensworth rose from \$5.1 million to \$37.4 million.

Foster's Brewing Group Limited (Foster's) increased its earnings to 11.1 cents a share in the six months ended 31 December 1998, an increase of 15.6% compared with earnings of 9.6 cents a share in the previous corresponding period.

Net profit increased 13.9% to \$191.1 million. In the earlier period, there was an abnormal charge of \$2.0 million. There were no abnormal charges in the latest period.

The underlying operating performance continues to improve with each division meeting its key operating objectives for the period. Profit before interest and tax rose by 15.7% to \$327.5 million. The increase in operating profit was achieved despite a fall of 19.6% in average funds employed during the half. The dramatic fall in funds employed followed the sale in June 1998 for \$1.1 billion of the 50% interest previously held in Molson Breweries, the Canadian brewing partnership.

Because of its sale, there was no contribution from Molson in the latest period. Profit before interest and tax from the ongoing businesses rose by 33.5% in the six month period.

With the sharply reduced level of funds employed and the improved underlying operating performance of the group, the return on overall funds employed will be significantly higher

The underlying operating performance continues to improve, with each operating objective.

during the current financial year than the return which was generated during 1997/98 and in excess of the current average cost of capital.

Net debt at the end of the period was \$1,098.1 million compared with \$607.7 million at the end of June 1998 and \$2,163.3 million at the end of December 1997. Gearing (measured as net debt to book equity) was 41.1% compared with 24.1% and 90.7%, respectively.

During the period, capital expenditures and investments amounted to \$501 million.

Income from Other Investments

Following the end of the financial year, Foster's announced that it had reached agreement with BHP to sell its shareholding in Beswick Pty Ltd for \$73.6 million. The arrangements are subject to agreement at a meeting of BHP shareholders in February and, if passed, would lead to a profit contribution to Foster's for the full year of \$6.3 million.

Performance of the company division meeting its key



Crown Lager

Interest Expense

Interest expense fell from \$56.4 million to \$36.7 million, primarily reflecting lower average debt levels from selling the 50% interest in the Molson Breweries partnership at the end of June 1998.

Interest cover (pre abnormal) was 8.9 times compared with 5.0 times in the previous corresponding period.

Tax Expense

The tax expense rose from \$58.0 million to \$99.8 million.

The increase reflected the higher level of profitability of the group in the current year as well as a favourable one time tax benefit which arose in North America in the first half of 1997/98. The latter factor served to reduce the tax expense in the previous corresponding period.

Dividend

The directors declared an interim dividend of 5.5 cents a share payable on 19 March 1999, an increase of 10% from the interim dividend of 5.0 cents a share paid in 1997/98.

The dividend will be fully franked as was the interim dividend for 1997/98.

CUB increased profit by 14.1% Higher beer volumes, improved were all contributing factors.

Carlton and United Breweries (CUB), which accounted for 76% of group profit before interest and tax, maintained its momentum during the half and continued to meet its financial and operating objectives by expanding its share of the value chain, raising brand equity and improving returns from its asset base.

Profit before interest and tax rose by 14.1% to \$247.7 million. Higher beer volumes, improved prices, lower unit costs and a rising contribution from its Australian Leisure and Hospitality arm (ALH) all contributed to the improved performance.

The Australian beer market was little changed in the half compared to the previous corresponding period. A fall in volumes of bulk beer was offset by an increase in packaged beer sales.

CUB's domestic volumes rose by 0.6% to 5.24 million hectolitres in the half. Its bulk beer sales rose by just under 1% despite the decline in the overall market segment.

Following CUB's success in establishing itself as the leading brewer in New South Wales in recent years, greater attention has been focused on the State markets in which CUB does not have the leading position. Highly satisfactory results

to \$247.7 million. prices and lower unit costs



Victoria Bitter

were achieved in each of those markets during the last half. Volumes sold in Queensland rose by just over 1% despite a decline in the overall size of that State's market. Volumes sold in Western Australia increased by just under 16% while that State's market also declined marginally. And, in South Australia, CUB's volumes rose by 3.5% in a market which was 1.9% higher.

Net beer sales revenue was 3.9% higher at \$727.8 million following price increases in February and August 1998 and a continuing change in the mix of sales in favour of higher priced premium brands such as Crown Lager, Cascade Premium, Carlton Premium Dry and the imported beers distributed by CUB. During the half, CUB also launched Cascade Premium Light, the first low alcohol beer in the premium market segment.

The margin from beer sales continued to benefit from initiatives put in place during the past two years to improve the way in which business is conducted.

These initiatives have been driven by a commitment to the "Lead Enterprise" vision of how the company should operate. This vision emphasises continuing innovation, teamwork and rewards for performance. It has been at the heart of

The profit from CUB's hotel and rose by 50% to \$38.0 million in rose by 70% to \$329.1 million.

establishing a culture which can continue to achieve sustainably higher profits within a low growth environment.

The benefits from the changes have been seen in the past six years during which time CUB's operating profit has increased at an average annual rate of 14%.

In September 1998, CUB acquired the assets and business of the Austotel Trust from Brierley Investments for \$310 million. Austotel was the next largest pub group in Australia after CUB's ALH division. Subsequently, a further six hotels were purchased in South Australia, with payment in January 1999, to add to the company's Australian pub-based assets. At the end of 1998, Foster's had funds employed of slightly more than \$700 million within its Australian Leisure and Hospitality activities.

Since embarking on the leisure destination strategy in 1995, CUB has taken several steps to improve the returns from its assets within this business segment by

- refurbishing pub sites to incorporate high quality bar and dining facilities;

leisure operations the last half. Revenue



Cascade Premium Light

- introducing gaming machines as an added attraction in the venues;
- improving overall customer service standards;
- raising efficiencies within the hotel network by taking advantage of economies from running a large portfolio of sites; and,
- introducing the "Liquor Express" brand into the Queensland and Victorian retail markets.

The profit from CUB's hotel and leisure operations rose by 50% to \$38.0 million in the last half. Revenue rose by 70% to \$329.1 million. The Austotel acquisition, which was consolidated from the beginning of September, contributed to the improved profit.

While the acquisition of Austotel has raised the absolute level of profits immediately, it will initially reduce somewhat the rate of return available on the funds employed of the combined group. The integration of the two business groups is proceeding satisfactorily, and benefits from the combination are expected to be evident in CUB's financial results in the near term.

Mildara Blass contributed \$66.1 million to operating profit, an increase of 27.1%. Operating revenue was 27% higher.

Mildara Blass, the wine division of Foster's, achieved a significant improvement in its underlying profitability.

Mildara Blass contributed \$66.1 million to operating profit, an increase of 27.1%. The profit gain was after an amortisation charge of \$6.5 million compared with a charge in the previous corresponding period of \$4.5 million. Operating revenue of \$282.0 million was 27% higher.

While the acquisitions of Bourse du Vin (The Wine Exchange), Maglieri Wines (both effective from 1 July 1998) and Pallhuber (December 1998) had a positive impact on the result, underlying profitability – reflecting growth in domestic sales, exports, higher operating margins and new membership within the existing wine clubs – also improved significantly.

In the five months ended November, growth in the domestic bottled wine market decelerated from 5% during 1997/98 to 2%. Despite the slowdown in growth and more aggressive competitor activity, Mildara Blass's domestic trade volume increased by 1% in the six months ended December. Importantly, however, with the help of its relatively strong brand portfolio, Mildara Blass was able to achieve a 5.5% increase in sales revenue and an improvement in its margin.

There was also a noticeable slowdown in the industry's rate of export growth from the 28% achieved during 1997/98 and the

million to operating profit, revenue of \$282.0 million



Jamiesons Run Reserve

five year average of 17%. Exports of bottled wine by the Australian industry were 8% higher in the six months to December than they had been in the previous corresponding period.

Mildara Blass's export volume growth was, however, four times the industry growth rate. Its exports were 32% higher than in the first half of 1997/98. One of the reasons for Mildara Blass's superior growth performance was the commitment made in 1993 to begin a major vineyard expansion programme, the benefits of which, including greater red wine availability and the pricing and margin flexibility which that brings, are now flowing.

The export sales revenue increase of 44% was helped also by a more favourable foreign exchange hedge rate than had been in place in the previous year.

Mildara Blass achieved strong growth in volumes to all major export destinations. Exports to North America, which accounted for just under 50% of total exports, rose by 22% with particularly strong gains in both volume and margin coming from Canada. European exports and Asian exports also grew strongly.

Among the key brands in export markets, Wolf Blass remains the most important, and achieved growth in volumes of just under 40%. The Black Opal brand and Jamiesons Run were also significant contributors to the growth.

Mildara Blass will continue to of building an international wine rate of return.

For the first time, sales of Mildara Blass's international production have been included in the operating result. Small quantities of the Bayliss & Fortune brand, from Mildara Blass's initial Californian production, were sold in the USA during the half. During 1998/99, the first wine from Mildara Blass's joint venture in Chile is also scheduled to enter the market.

The acquisition of a controlling interest in Heinrich Maximilian Pallhuber GmbH (Pallhuber), a German based wine club, in December 1998 took the group's wine club strategy of becoming world leader a step further. One month's profit contribution from Pallhuber was included in the result for the half.

In Australia, Cellarmaster Wines increased revenue by 25%. The number of active members was 9% higher as a result of new members being recruited and a marketing campaign directed toward existing members.

Bourse du Vin (The Wine Exchange), a Dutch-based wine club operator which sells French wines in Holland, Belgium, France and the USA, was acquired in June 1998 and made a full six month profit contribution to the group. During the period, some of the sales initiatives which had been successfully developed in Australia over a number of years were introduced into the Dutch business with considerable success, including a rise in club membership of more than 70%. There are good grounds for

pursue its strategy business with a rising



Annie's Lane

believing that this increase in membership will translate into a correspondingly higher level of sales in the coming 12 to 18 months.

These developments ensure that the minimum required rates of return from the wine club investments are exceeded. They also represent strong evidence to back the group's view that, with its skill base, there are significant opportunities available to develop the potential of the wine club market outside Australia.

Mildara Blass will continue to pursue its strategy of building an internationally oriented wine business with a rising rate of return through:

- domestic market growth;
- developing export markets;
- expanding its international production base;
- building its international wine club activities; and,
- improving operating margins through consolidating winemaking facilities and taking advantage of its vineyard development initiatives, including its higher rate of grape self-sufficiency and relatively high proportion of red wine grape varieties.

In pursuing its strategy, Mildara Blass intends to remain committed to the premium end of the wine market and hence limit the impact on its financial performance of changes in the demand/supply balance for grapes.

Sales from the China breweries reduced. Volumes grew strongly sales exceeded expectations.

The financial and operating outcomes within Foster's Asia improved significantly. Sales from the breweries in China improved and cost reductions were achieved to bring the breweries more into line with local conditions. Volumes grew strongly in Vietnam and the opening sales from the Indian brewery significantly exceeded expectations.

The loss from Foster's Asia was reduced from \$21.6 million to \$15.1 million.

In China, as previously foreshadowed, steps have been taken to sell two of the three breweries which have been operated by Foster's Asia. While sales have not been finalised, negotiations are well advanced. Meanwhile, action has been taken to significantly reduce the costs associated with the two breweries being sold and the losses have been substantially lowered.

Once the Guangdong and Tianjin breweries are sold, the focus of attention will be on Shanghai. The volume of beer sold in Shanghai during the six months to December was 29% higher than in the previous corresponding period. Average realised prices increased and the overall margin on beer sales was also higher. The loss from the Shanghai operation was reduced by nearly 30% compared with a year earlier.

improved and costs were in Vietnam and Indian



Foster's Lager

Initiatives have been taken to restructure the sales activity and to improve the focus on the Foster's brand which continues to improve its penetration in the key Shanghai/Yangtze area. Initial sales of Shanghai brand beer have been made in the UK and the USA as part of an attempt to build the brand's standing as a premium product in those markets.

In India, a new brewery was opened in July 1998 and sales immediately exceeded expectations. The 100,000 hectolitre brewery is being fully utilised with the production of Foster's Lager and consideration is being given to an expansion of its capacity.

In Vietnam, excellent progress has been made in consolidating the position of the local brands and the longer term work of building brand awareness and distribution for Foster's Lager has commenced.

Volumes of beer sold from the two breweries were 49% higher than in the previous corresponding period (although Foster's did not acquire the Vietnamese assets until October 1997). With improved volumes, the size of the losses being generated on acquisition have been significantly reduced despite the additional market development support which has been provided to the brands.

The profit contribution from the compared with a contribution of corresponding period.

Foster's International is the division responsible for actively promoting Foster's as a world brand. Over 90 million case equivalents of Foster's brand product are distributed in more than 135 countries. Foster's is produced and distributed under licence in the UK and North America and in several other European and Asian locations.

The profit contribution from the group was \$5.2 million compared with a profit contribution of \$0.5 million in the previous corresponding period. Foster's International has three principal sources of income:

- royalty payments, mainly arising from its licensing agreements with Scottish & Newcastle in Europe and Molson and Miller Brewing in North America;
- income from Molson USA, the partnership in charge of sales, marketing and distribution of Foster's brand products in the USA, in which Foster's took a 24.95% equity interest in November 1997; and,
- gross margin generated from Australian exports.

The improved profitability arose from an increase in royalty payments from the UK, the commencement of income from Molson USA, as well as improved margins from export sales.

group was \$5.2 million
\$0.5 million in the previous



Foster's Lager

The total volume of beer for which Foster's International has responsibility grew by 14.3%.

In the UK, Foster's continues to grow strongly. Volumes of Foster's brand products sold under licence were 12.1% higher, consolidating Foster's as one of the top two selling beer brands in the country. The brand also continued its positive performance in the USA, with volumes up 12.3%.

The 'Australian for Beer' media campaign throughout the US National Football League finals, together with increased national distribution, has reaffirmed the brand's status as a top five priority national brand for Miller Brewing. In South America, where market development efforts have been continuing in the past year, volumes remain small but have grown significantly and the outcomes are running at better than originally targeted rates.

Export sales, which accounted for only 3% of the total volumes for which Foster's International is responsible, continued to be detrimentally affected by the economic and political situation in Asia and, consequently, were only 0.9% higher than a year earlier.

While the profit contribution for this year is biased in favour of the first half, Foster's International is set to show continued strong growth in profitability in coming years as a result of further guaranteed increases in royalties to be paid by Scottish & Newcastle and increasing sales in the USA.

Since 1992/93, Lensworth has generated net operating cash flows of \$1.3 billion.

Lensworth is responsible for managing the assets remaining from the restructuring of Foster's which began in the early 1990s.

Since 1992/93, Lensworth has generated net operating Cash Flows of \$1.3 billion.

During the six months ended December, cash inflows from asset realisations totalled \$93 million. The profit contribution from Lensworth was \$37.4 million compared with a contribution in the previous corresponding period of \$5.1 million. The sharp increase in profitability reflected the 'lumpy' nature of the asset realisations with one transaction alone contributing a profit in excess of \$25 million.

The Lensworth result for 1998/99 is expected to be heavily biased toward the first half of the year. While further realisations are anticipated during the balance of the year, it is unlikely that they will generate significant additional profit for the group.

At 31 December 1998, Lensworth had net external assets of \$259 million after specific and general provisions compared with reported assets at the end of June 1998 of \$278 million.

The management and Board regularly review the realisation programme and the appropriateness of carrying values.

In addition to specific provisions, there is a general provision equivalent to 22% of the written down asset value which the company believes is conservative.

Lensworth Portfolio – Geographic Distribution of Assets

| A\$ million | Residential Property | Other Property | Other Assets | Total |
|---------------------|----------------------|----------------|--------------|-------|
| Australia | 81 | 17 | 29 | 127 |
| North America | - | 185 | 10 | 195 |
| UK | - | 6 | 2 | 8 |
| Total | 81 | 208 | 41 | 330 |
| General provision | | | | (71) |
| Net external assets | | | | 259 |

FINANCIAL SUMMARY

Six months ended 31 December 1998

Consolidated Profit and Loss

| A\$ million | Current half year | Previous corresponding half year |
|--|----------------------|--|
| Operating revenue | | |
| Net beer sales | 779.5 | 1,073.0 |
| Other brewing group trading revenue | 436.5 | 282.9 |
| Wine group net trading revenue | 272.7 | 219.7 |
| Net sales revenue | 1,488.7 | 1,575.6 |
| Other revenue | 167.4 | 691.5 |
| Total operating revenue | 1,656.1 | 2,267.1 |
| Operating profit before abnormal items and tax | 290.8 | 226.6 |
| Abnormal items | - | (2.0) |
| Operating profit before tax | 290.8 | 224.6 |
| Income tax expense | (99.8) | (58.0) |
| Operating profit after tax | 191.0 | 166.6 |
| Outside equity interest | 0.1 | 1.2 |
| Operating profit after tax attributable to members of the company | 191.1 | 167.8 |

Consolidated Statement of Cash Flows

| A\$ million | Current half year | Previous corresponding half year |
|--|----------------------|--|
| Net Operating Cash Flows | 3.7 | 110.9 |
| Cash Flows Related to Investing Activities | | |
| Payment for purchases of property, plant and equipment | (320.6) | (116.6) |
| Proceeds from sale of property, plant and equipment | 8.0 | 53.7 |
| Payments to acquire controlled entities | (179.9) | (133.6) |
| Payments for acquisition of investments and other assets | - | (247.9) |
| Proceeds from sale of controlled entities, investments and other assets | 59.7 | 224.2 |
| Net loans repaid by other entities | 27.9 | 14.4 |
| Net Investing Cash Flows | (404.9) | (205.8) |
| Cash Flows Related to Financing Activities | | |
| Share buy-back | - | (625.0) |
| Proceeds from issues of shares | 9.2 | - |
| Proceeds from borrowings, net of repayments | 410.1 | 988.8 |
| Dividends paid | (103.0) | (102.5) |
| Equity contribution from outside equity interests | - | 2.4 |
| Net Financing Cash Flows | 316.3 | 263.7 |
| Net (decrease) / increase in cash held | (84.9) | 168.8 |

Consolidated Balance Sheet

| A\$ million | At end of current half year | As shown in last annual report | As shown in last half yearly report |
|--|-----------------------------|--------------------------------|-------------------------------------|
| Current assets | | | |
| Cash | 205.8 | 299.5 | 290.5 |
| Receivables | 440.0 | 292.3 | 820.2 |
| Inventories | 354.4 | 348.2 | 263.9 |
| Investments | 67.3 | 19.0 | 62.8 |
| Other | 34.4 | 20.9 | 43.0 |
| Total current assets | 1,101.9 | 979.9 | 1,480.4 |
| Non-current assets | | | |
| Receivables | 73.8 | 48.1 | 83.2 |
| Inventories | 304.1 | 283.2 | 283.4 |
| Investments | 50.7 | 141.1 | 886.0 |
| Property, plant and equipment | 2,075.3 | 1,714.8 | 1,849.4 |
| Intangibles | 1,279.0 | 1,166.2 | 1,135.6 |
| Other | 84.0 | 86.5 | 95.7 |
| Total non-current assets | 3,866.9 | 3,439.9 | 4,333.3 |
| Total assets | 4,968.8 | 4,419.8 | 5,813.7 |
| Current liabilities | | | |
| Accounts payable | 486.3 | 457.7 | 470.1 |
| Borrowings | 71.6 | 162.4 | 188.9 |
| Provisions | 308.9 | 294.7 | 223.5 |
| Total current liabilities | 866.8 | 914.8 | 882.5 |
| Non-current liabilities | | | |
| Accounts payable | 24.7 | 32.3 | 20.0 |
| Borrowings | 1,232.3 | 744.8 | 2,264.9 |
| Provisions | 172.5 | 209.0 | 261.8 |
| Total non-current liabilities | 1,429.5 | 986.1 | 2,546.7 |
| Total liabilities | 2,296.3 | 1,900.9 | 3,429.2 |
| Net assets | 2,672.5 | 2,518.9 | 2,384.5 |
| Shareholders' equity | | | |
| Share capital | 2,027.3 | 1,713.4 | 1,713.4 |
| Reserves | 263.9 | 554.8 | 498.7 |
| Retained profits | 342.3 | 245.9 | 134.7 |
| Shareholders' equity attributable | | | |
| to members of the chief entity | 2,633.5 | 2,514.1 | 2,346.8 |
| Outside equity interest in controlled entities | 39.0 | 4.8 | 37.7 |
| Total shareholders' equity | 2,672.5 | 2,518.9 | 2,384.5 |

Change in accounting policy

As a consequence of the abolition of the concepts of the "par value" of shares by the Company Law Review Act 1998, an amount of \$283.9m, comprising share premium reserve of \$274.7m, capital redemption reserve of \$6.0m and capital reconstruction reserve of \$3.2m, was transferred from reserves to share capital account.

Events since the end of the current half year

A general meeting of shareholders was held on 27 January 1999 which approved a proposal to buy-back the partly paid shares of the company.

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Enquiries

If you have any questions about your shareholding, share transfers or dividends, please contact our share registrar:

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It would be helpful if shareholder reference numbers were included in all correspondence to the share registrar.

For enquiries relating to the operations of the company, please contact the Foster's Brewing Group Investor Relations department on

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