Fonterra Co-operative Group Limited
Results for Announcement to the Market

Reporting Period	12 months to 31 July 2017
Previous Reporting Period	12 months to 31 July 2016

	Amount (m's)	Percentage Change
Revenue from ordinary activities	NZ$19,232	12%
Profit (loss) from ordinary activities after tax attributable to security holder[1]	NZ$745	(11)%
Net profit (loss) attributable to security holders	**NZ$734**	**(9)%**

1 Net profit attributable to shareholders of the company is equivalent to profit from ordinary activities after tax attributable to shareholders of the company (as required to be disclosed pursuant to Clause 1.2 of Appendix 1 of the Fonterra Shareholders' Market Listing Rules, and Clause 1.2 of Appendix 1 of the NZX Debt Market Listing Rules).

Interim/Final Dividend	Amount per Security	Imputed Amount per Security
Final dividend	NZ$0.20	$0.00

Record Date	9 October 2017
Dividend Payment Date	20 October 2017

Comments	On 23 September 2017, the Board of Directors declared a dividend of 20.0 cents per share to be paid on 20 October 2017 to Shareholders on the share register at 9 October 2017.

To be followed by the balance of the information required in the report pursuant to Appendix 1 – Including the Net Tangible Asset amount per security for the current and previous reporting period.

Media release

25 September 2017

FONTERRA CO-OPERATIVE GROUP ANNOUNCES SOLID YEAR END RESULTS

Highlights

- 2016/2017 Total Cash Payout $6.52, up 52% on last season
  - Farmgate Milk Price $6.12 per kgMS
  - Dividend of 40 cents per share
- Revenue $19.2 billion, up 12%
- Normalised EBIT $1.155 billion, down 15%
- Net Profit After Tax (NPAT) $745 million, down 11%
- 46c earnings per share
- Significant growth in Consumer and Foodservice – additional 576 million LME
- Advanced Ingredients sales growth up 9%
- Group Return on Capital of 11.1%

Annual results

Fonterra has today announced a significant increase in total payout for its farmer shareholders and a solid overall operating and financial performance, as part of its 2017 Annual Results.

The Co-operative has confirmed a final Cash Payout of $6.52 for the 2016/2017 season for a 100% share-backed farmer. This is made up of a Farmgate Milk Price of $6.12 per kgMS and a dividend of 40 cents per share.

Revenue increased by 12% to $19.2 billion, with rising prices offsetting a 3% decline in volumes at 22.9 billion LME. Normalised EBIT of $1.2 billion was down 15% as a result of reduced margins across the business which also influenced net profit after tax, down 11% at $745 million.

Chairman John Wilson said the Co-operative's ability to maintain its forecast dividend despite the Milk Price increasing by 57% over the year and the impact of negative stream returns was an excellent result.

"We will always need to manage variability across our Co-operative – both in global markets and in our local farming conditions. We've demonstrated our ability to deal with those conditions and deliver on our strategy again this year," said Mr Wilson.

"Over recent seasons, our farmers have made significant personal sacrifices to reduce costs through a sustained low milk price period.

"As part of our continued business transformation, the Co-operative has also made a fundamental shift in the way it operates, continuing the strong focus on increased efficiency and developing new revenue streams.

“Despite lower milk volumes due to poor weather in parts of the season, the business delivered a good result by prioritising higher value Advanced Ingredients and growing our sales of these in-demand and specialised products by 473 million LME this year.”

Our Consumer and Foodservice business continues its strong performance. This year we sold more than 5.5 billion LMEs, an additional 576 million LME on last year. This volume growth across these two portfolios has delivered normalised EBIT of $614 million, an increase of 6% on last year.

“Today’s announcement will be welcome news for our farmers, who remain focused on carrying their on-farm efficiencies through to the new season to make the most of improved prices,” said Mr Wilson.

Our business performance

Chief Executive Theo Spierings said the quality of the Co-operative’s performance and its solid earnings resulted from two consistent themes.

“We have been clear and single minded about delivering to strategy, leveraging our scale efficiencies and prioritising value and higher margin products. At the same time, we have tapped into the expertise of our people to come up with innovative ways to generate higher returns for the future,” said Mr Spierings. “Within our Ingredients business, our higher value Advanced Ingredients segment achieved a 9% increase in sales volumes. This includes sales of products such as functional proteins, high-spec whole milk powder and extra-stretch cheese. These Advanced Ingredients made up 19% of our total external sales volumes this year.

“Our new product development and strong customer relationships in our key markets is capturing more and more of our full potential in our Consumer and Foodservice categories, evidenced by our Anchor Food Professionals Foodservice business which grew at 10 times the market growth rate over the past 12 months.

Mr Spierings said that, over the past year, Fonterra had commissioned or announced new investments across the full range of our Consumer and Foodservice product portfolio. This included new UHT lines at Waitoa, butter and cream cheese expansions at Te Rapa, construction of the Co-operative’s largest mozzarella plant at Clandeboye, two new cream cheese plants at Darfield, and the reopening of its cheese and whey plants at Stanhope in Australia.

“Foodservice, in particular, is a demand-led business and each of these investments is backed by a growing customer order book. Having the capacity and agility to quickly meet demand in this segment is critical to developing customer relationships and is our ticket to the game in many of our key markets,” said Mr Spierings.

The next step in the Fonterra strategy

“New Zealand milk remains at the very core of our Co-operative, and our future requires us to be strongly connected to the diverse and ever-changing needs of consumers,” said Mr Spierings.

“Our V3 strategy of driving more Volume into higher Value at Velocity is at the heart of our ambition, and provides the foundation for us to fund and drive innovation and sustainable value creation. This year, our V3 strength has secured our ability to deliver solid earnings in an environment of rapidly increasing milk prices.

“To remain successful, we need to be agile in every facet of our Co-operative – on-farm, across our manufacturing and distribution footprint, right through to the food we produce and how we produce it. Our investment in innovation and advanced technologies, and an ongoing focus on creating sustainable, long-term value will become the foundation on which we continue to build strength into our Co-operative,” Mr Spierings said.

Global Outlook

The forecast total available for payout to farmers in the 2017/18 season is $7.20 − $7.30 per kgMS, made up of:

- Forecast Farmgate Milk Price of $6.75 per kgMS
- Forecast earnings per share range of 45-55 cents per share.

"We are well positioned to deliver higher volumes and new product formats in our Consumer, Foodservice, and Advanced Ingredients portfolios, and are confident in our forecast earnings per share range of 45-55 cents," said Mr Wilson.

NB: All dollars quoted are New Zealand dollars

\- ENDS -

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Non-GAAP financial information

Fonterra uses several non-GAAP measures when discussing financial performance. These measures include normalised segment earnings, normalised EBIT, EBIT, normalisation adjustments and payout. These are non-GAAP financial measures and are not defined by NZ IFRS. Management believes that these measures provide useful information as they provide valuable insight on the 4underlying performance of the business. They are used internally to evaluate the underlying performance of business units and to analyse trends. These measures are not uniformly defined or utilised by all companies. Accordingly, these measures may not be comparable with similarly titled measures used by other companies. Non-GAAP financial measures should not be viewed in isolation nor considered as a substitute for measures reported in accordance with NZ IFRS. These non-GAAP measures are not subject to audit unless they are included in Fonterra's annual financial statements.

Definitions of the non-GAAP measures used by Fonterra, and reconciliations of the NZ IFRS measures to the non-GAAP measures can be found on pages 104 to 105 of Fonterra's Annual Review that is available on Fonterra's website.

FONTERRA
DAIRY FOR LIFE

ANNUAL REVIEW 2017
FONTERRA CO-OPERATIVE GROUP LIMITED

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Please refer to page 104 for the reconciliation of the NZ IFRS measures to the non-GAAP measures and page 105 for definitions of the non-GAAP measures used by Fonterra.

OUR CO-OPERATIVE

Our Co-operative's strength comes from our common goal. Our job is to produce the best milk and secure the best returns, while maintaining our commitment to sustainability and our communities.

FONTERRA FARM SOURCE™ REWARDS AND BENEFITS AND DISCOUNTS

$50M

FARMERS TOOK ADVANTAGE OF INTEREST-FREE AND DEFERRED PAYMENTS

4,000

$6.52 PER KGMS

TOTAL CASH PAYOUT FOR 2016/17 SEASON

1,526 M KGMS

NEW ZEALAND MILK COLLECTION FOR THE 2016/17 SEASON

40CPS

FINANCIAL YEAR 2017 TOTAL DIVIDEND PER SHARE

OUR POTENTIAL

We are continuing to grow value by converting more of our farmers' milk into higher-value products for customers around the world.

OUR PERFORMANCE

A solid performance building on a significantly higher milk price through the execution of our strategy and strong financial discipline.

ADDITIONAL MILK CONVERTED INTO CONSUMER AND FOODSERVICE

576 M LME

ADDITIONAL MILK CONVERTED INTO ADVANCED INGREDIENTS

473 M LME

GROUP VOLUME

23 B LME

GROUP REVENUE

$19 B

STRONG V3 CO-OP

DEMAND-LED STRATEGY TO OPTIMISE NEW ZEALAND MILK, SUPPORTED BY MILK POOLS

$1,155 M

GROUP NORMALISED EBIT (NZD)

INNOVATIVE CO-OP

INVESTING IN TECHNOLOGY AND PEOPLE FOR THE FUTURE

11%

RETURN ON CAPITAL

SUSTAINABLE CO-OP

CREATING SUSTAINABLE VALUE FOR ALL STAKEHOLDERS

$745 M

NET PROFIT AFTER TAX (NZD)

LETTER FROM **THE CHAIRMAN**

We started the 2016/17 season facing the prospect of a third year of unsustainably low global prices, but ended it with our Co-operative in a strong financial position and a return to a sustainable Farmgate Milk Price for our farmers' milk.

$6.52

CASH PAYOUT
Our Co-operative ended the 2016/17 season with a total cash payout up 52 per cent on the prior season.

WITH GLOBAL DAIRY PRICES IMPROVING ACROSS THE YEAR AND FURTHER PROGRESS WITH OUR STRATEGY OF SHIFTING MORE MILK INTO HIGHER VALUE PRODUCTS, OUR CO-OPERATIVE ENDED THE 2016/17 SEASON WITH A TOTAL CASH PAYOUT OF $6.52 PER KGMS, UP 52 PER CENT ON THE PRIOR SEASON.

This reflects the positive performance across the business, with the final Farmgate Milk Price of $6.12 per kgMS and a dividend of 40 cents per share from an earnings per share of 46 cents.

Our Co-operative's ability to maintain its forecast dividend despite a 57 per cent increase in the Farmgate Milk Price over the year is an excellent result. In delivering it, the business managed the downside of relative stream returns of $180 million, by maintaining an owners' mind-set that continued to drive new revenue streams and improve accountability for costs in the business.

The result comes after two seasons of low global prices and is pleasingly $1.47 kgMS ahead of DairyNZ's on-farm breakeven point for the season. Our transparent Farmgate Milk Price and demand-led strategy of shifting more milk into higher value products have seen the total payout to our New Zealand farmers largely return to parity when compared to farmers internationally.

We knew that the events which impacted global dairy markets from 2013 – 2015 did not represent a structural shift in prices. It is a credit to our farmers who responded to the circumstances, sharpening their systems, maximising the natural strength of New Zealand's pasture-based model to reduce costs, and in all cases made significant personal sacrifices through this sustained low milk price period.

Prolonged wet weather in many regions over the 2017 season made farming conditions difficult, contributing to a decline in milk volumes of three per cent to 1,526 million kgMS. However the increased Farmgate Milk Price offset this and means our farmers will receive more than $3 billion additional payments compared to last year.

Farmers will be focused now on carrying their cost efficiencies and pasture-based advantages through to the new season to make the most of improving prices.

STRONGER TOGETHER

We have helped farmers keep their costs down by lowering the cost of farm supplies through our Farm Source™ stores and by offering competitive terms. More than 4,000 shareholders and sharemilkers took advantage of extended interest free and deferred payment terms and $17.8 million worth of Farm Source™ Rewards Dollars over the year.

Our Farm Source™ store offering has delivered the average sized Fonterra farm approximately 10 cents per kgMS in savings and rewards if they purchased farm supplies exclusively with Farm Source™.

Improvements in the forecast Farmgate Milk Price over the season will trigger a first repayment of the Fonterra Support Loan when the total advance rate exceeds $6.00 in October.

It was pleasing to be able to use the financial strength of the Co-operative to help farmers during this time. The loan, launched in the 2015/16 season, was interest free until May 31 2017. It was taken up by 76 per cent of farmers and $383 million in support was provided. After the October 2017 payment, there will be $190 million outstanding.

Our regional leadership model is going from strength to strength, connecting our local farmers and their communities with our management team so they are more responsive to local needs.

There have been many examples of this over the year but perhaps it was best demonstrated in April when Cyclone Cook caused widespread flood damage to homes and farms in Edgecumbe, Te Puke, Galatea and Reporoa. Following the initial flooding, our Farm Source™ team and staff from our Edgecumbe site transformed the site into a hub for the community, and a base for clean-up operations in the area. The team then took to the streets, helping the town with the clean-up. A Farm Source™ flood relief package was pulled together to help ease the pressure and support local farmers. Well done to all of the team who came together and supported their communities at difficult times during the year.

LETTER FROM **THE CHAIRMAN**

10c

HELPING KEEP COSTS DOWN

Our Farm Source™ store offering has delivered the average sized Fonterra farm approximately 10 cents per kgMS in savings and rewards if they purchased farm supplies exclusively with Farm Source™.

OUR STRATEGY IS DELIVERING

Our Co-operative increased revenue by 12 per cent to $19.2 billion, with rising prices offsetting a three per cent decline in volumes at 22.9 billion LME. Normalised EBIT of $1.2 billion was down 15 per cent as a result of reduced margins across the business which also influenced net profit after tax, down 11 per cent at $745 million.

Ingredients

Ingredients sales volumes were down five per cent, partially as a result of lower milk collections that were restricted by New Zealand weather conditions and by the historically low opening inventory levels.

Our Ingredients business generated $943 million in normalised EBIT, a 22 per cent reduction on last year. That result reflects downward pressure on gross margins in our Ingredients business, which reduced by 20 per cent primarily due to materially lower stream returns.

Over this financial year, the relative prices of non-reference products over reference products narrowed significantly, reflected in the 30 per cent increase in revenue per metric tonne for reference products versus a 12 per cent increase for non-reference products. This resulted in negative stream returns of $40 million, a decline of $180 million relative to last year.

This year we have reported our Advanced Ingredients segment for the first time. Advanced Ingredients are differentiated products that attract premium prices over base ingredients through superior product performance. Whey protein isolate and medical grade lactose are good examples. We shifted 473 million LME into this segment, an increase of nine per cent on last year.

Consumer and Foodservice

This year a further 576 million LME went into higher value products in Consumer and Foodservice, bringing the total to 5.5 billion compared to last year's 4.9 billion. We remain on-track to reach our overall goal of 10 billion LME in Consumer and Foodservice by 2025.

Our progress continues to be demand driven, supported by investments in capacity to produce high value products. Foodservice volumes grew by 27 per cent to 2.3 billion LME, helped by 46 per cent volume growth in Greater China and increased sales across all of our Asia markets. Revenue from our Foodservice business alone crossed the $2 billion threshold for the first time.

DOLLARS DEALS AND DISCOUNTS

More than 4,000 shareholders and sharemilkers took advantage of extended interest free and deferred payment terms and $17.8 million worth of Farm Source™ rewards dollars over the year.

4,000

FARM SOURCE™ FLOOD RELIEF

A Farm Source™ flood relief package was pulled together to support Bay of Plenty farmers after Cyclone Cook.

Our Soprole business in Latin America delivered a strong sales performance through the execution of its consumer focussed innovations. Soprole drove the 18 per cent increase in Consumer and Foodservice volumes in Latin America. However, adverse economic conditions in Brazil and Venezuela resulted in our overall normalised earnings for Latin America being down five per cent at $103 million.

In Australia the successful turnaround of our local business contributed to a four per cent increase in normalised earnings in Oceania. We finished the year by reaching a significant milestone with the re-opening of our Stanhope cheese plant in Victoria, two and a half years after fire destroyed the previous plant. With the turnaround complete, Australia is now a global ingredients hub for Fonterra's cheese, whey and nutritionals, complementing our Consumer and Foodservice businesses.

The strong performance of our overall Consumer and Foodservice business delivered a return on capital of 47 per cent up from 42 per cent last year. This is a good result given the higher Farmgate Milk Price contributed to a four per cent reduction in Consumer and Foodservice margins.

Greater China

Our Greater China business continues to deliver both volume and value growth with an additional 402 million LME this year and normalised earnings of $209 million, up 60 per cent on last year. Our Ingredients business sold four billion LME, and our China Foodservice business delivered another strong performance, with volume growth of 48 per cent this year.

Two important parts of our China strategy are Beingmate and our China Farms.

Beingmate's performance, while very disappointing, is a reflection of China's market conditions, which remain challenging for everyone in the infant formula market due to the impact of regulatory changes. Beingmate was amongst the first to receive regulatory approval and will be well-positioned as the regulations come into full effect and the market stabilises.

Our China Farms continued to focus on operational improvement, significantly reducing cash costs by 0.21 RMB per litre or six per cent. After a long period of establishment, these farms are now complete with 335 million LME produced this year. While local farmgate milk prices have remained low, Fonterra is now increasing its sales of fresh liquid milk to our customers and Consumer and Foodservice business in-market, complementing milk from our New Zealand farmers.

LETTER FROM **THE CHAIRMAN**

INVESTING IN THE FUTURE

We are strengthening our position by utilising advances in technology and innovation, especially those which protect and enhance our premium position, building on the more than $1 billion we have spent on research and development over the last 10 years.

Operating costs and debt

As our farmers have done, our Co-operative's management team continued their push to reduce costs and maximise returns for our farmers.

Operationally, our New Zealand sites delivered further improvements in yields and managed cost of quality to similar levels as last year, despite tightening standards. The unusual profile of milk collections over the season provided some challenges to operational planning but savings were generated across the supply chain and management continued its focus on controlling operating costs across the business. As a result, operating expenses were down six per cent.

At 44 per cent, our gearing is the same as reported in 2016 and within our target range of 40–45 per cent.

STRENGTHENING OUR STRATEGY

New Zealand farmers have always been quick to adopt new technology and drive innovation, it's a culture that our people across Fonterra have embraced. Our people must earn the right to transform our business into the dairy industry of tomorrow, by delivering for our farmers today.

Maintaining financial discipline and a strong balance sheet has enabled us to help farmers through difficult years. Our business transformation work over the past two years has also reinforced this discipline, reducing costs, enabling faster decision making and giving our people ownership of their business targets and accountability for their delivery.

Our people are excited by innovation and the prospects for positive changes to the way we grow, make and deliver food to our customers.

We have a genuine advantage. Our traditional pasture-based model produces some of the best milk in the world, both in quality and nutrition, at a time when consumers are increasingly willing to pay a premium for food that has been produced in a socially and environmentally responsible way. Our Trusted Goodness™ quality seal, launched last year, provides our customers with that assurance.

RIPARIAN PLANTING
Dairy farmers have spent more than $1 billion on environmental improvements, including riparian planting.

We are strengthening our position by utilising advances in technology and innovation, especially those which protect and enhance our premium position, building on the more than $1 billion we have spent on research and development over the last 10 years. This innovation will help secure our ability to generate sustainable value for all of our stakeholders, from our farmers through to customers, consumers and communities.

Advancements in farming practices and on-farm technology have helped to improve land productivity of dairy farms by 84 per cent since the year 2000, up to $7,893 of export value per hectare. They have also contributed to a 70 per cent increase in export revenue per cow since 2001.

There will always be a global, growing market for natural dairy given its complex mixture of proteins, fats, minerals and other nutrients. Alongside that, we're investigating consumers' attitudes to alternative proteins to look at the role they may play in future nutrition.

Alternative products have been in the market for many years, including soy, rice and nut products. With global demand for food expected to increase 50 per cent by 2050 there will be a place for both categories but it is clear that the natural strength of dairy, and its nutritive value and efficacy, will be the premium nutrition of choice.

SUSTAINABLE FARMING

Sustainability is at the forefront of everything we do. Our farmers continue to make significant investments and management changes as they grapple with rapid and challenging regional policy changes.

Two recent independent reports show that, while there is undoubtedly work to do, dairy farmers are leading the way in the protection of our waterways by fencing waterways and investing in additional riparian planting and in their farm management practices to effectively manage nutrients.

This year Fonterra and DairyNZ released the Dairy for Climate Change Action Plan which will help the industry to contribute to New Zealand meeting the Paris Climate Agreement by helping dairy farmers to better understand and manage their farming emissions.

The United Nation's Food and Agriculture Organisation already puts New Zealand as a world-leader for efficiently producing milk on a greenhouse gas per unit of milk basis, and our science community has confidence in new and emerging technologies to manage ruminant emissions further.

New Zealand farmers have always been quick to adopt these types of new technologies. Our future success relies on investment in science and innovation, and our willingness to continue to evolve our practices based on that science.

LETTER FROM **THE CHAIRMAN**

HALF THE PIZZAS IN CHINA
Fonterra mozzarella tops over half the pizzas in China.

Sharing the continued hard work of our farmers, and the positive environmental outcomes that all New Zealanders enjoy as a result, will remain a priority for the Co-operative.

TRADE

In the current geopolitical climate, we are seeing a concerning trend towards rising protectionism and reduced international co-operation, both of which could slow global trade growth.

Connecting our premium dairy products with global consumers relies on quality trade agreements in our key markets.

Trading dairy nutrition is not easy. Tariffs on our products distort global dairy markets and mask pricing signals to international farmers. Ideally, we would have free trade into all of the markets in which we operate. Currently, 87 per cent of all New Zealand dairy exports are restricted by quotas or tariffs of more than 10 per cent. Lowering import tariffs will help countries to address food security concerns and lower food prices. They will also ensure New Zealand dairy products and dairy innovation remain price competitive and accessible to consumers in our key markets.

Opening up market access and tackling non-tariff barriers must remain a priority for the New Zealand Government.

ACKNOWLEDGEMENTS

Being first to market with new innovations, or adapting quickly to new technologies that are changing the way our customers want to do business with us are key to our continued success.

Our people are at the heart of our Co-operative's adaption to these changes and I'd like to thank them for their willingness to accept change, seek out new opportunities for our business, and continue to focus on achieving the best possible returns for our farmer owners.

Our people have strong co-operative values and have dedicated and hard-working leaders whose examples they can follow. We have seen a significant transformation in Fonterra over the last three or four years, all with our farmers' interests and returns at the forefront. Thank you to the management team for the effort to date, and for your willingness to drive the further changes which are a certainty over the next 3–4 years if we are to stay at the forefront of global dairy. Those changes aren't possible without the support of our customers and suppliers who work with us as partners for mutual long-term success.

This year we welcomed two new Directors onto the Board, Scott St John, an Independent Director, and Donna Smit, a Farmer Director.

84%

IMPROVED PRODUCTIVITY

Advancements in on-farm technology have helped to improve land productivity 84 per cent since the year 2000.

Scott is one of New Zealand's leading investment advisors. He has almost 30 years of experience with funds management and securities transactions which have involved him advising the boards and senior managers of prominent companies and organisations in New Zealand and globally.

Donna, a Chartered Accountant, owns with her family, dairy farms in Eastern Bay of Plenty and Oamaru. She is a Director of Ballance Agri Nutrients and Primary ITO and a Trustee of Taratahi Agricultural Training Centre and Eastern Bay Energy Trust.

On behalf of our farmers, I want to thank Independent Director David Jackson and Farmer Director Ian Farrelly as they retire from the Board. Special mention must also go to Michael Spaans who stepped down from our Board this year but continues to show strong leadership in our industry.

David has given us 10 years of leadership and wise counsel through some of the most significant stages of our evolution including the implementation of our Milk Price, Trading Among Farmers and our Governance and Representation Review. He is a strong advocate for our strategy and a firm believer in our people's ability to execute it to secure the best returns for farmers.

David's commitment to reporting transparency and governance disciplines has been very important to our Board and wider Co-operative.

In January, Michael Spaans made the difficult decision to step down from our Board for health reasons. Michael's contribution to the New Zealand dairy industry has been significant both inside and outside the Fonterra boardroom. We wish Michael all the best with his continued recovery.

After making the decision to retire from our Board at the 2016 Annual Meeting, we welcomed Ian Farrelly back onto the Board part way through the year to fill the casual vacancy created by Michael's retirement. I'd like to personally thank Ian for returning to our Board, putting our Co-operative's interests first and making a significant contribution this year.

John Wilson
Chairman

1.5M

TRUST IN DAIRY

1.5 million New Zealanders feel Fonterra is making a change for the better.

SHARING OUR STORY IS IMPORTANT TO US – WE WANT NEW ZEALANDERS TO KNOW WHO WE ARE AND WHAT WE STAND FOR.

From the tech-savvy farmers who own our Co-operative, to our commitment to clean waterways, we are letting the world in on what matters most to us.

LETTER FROM THE **CHIEF EXECUTIVE**

The world is experiencing huge momentum across markets, industries and geographies.

473M LME SALES VOLUME GROWTH

ADVANCED INGREDIENTS
Sales in highly specialised, high margin ingredients formed a key part of our solid result.

WE TRADE ACROSS GLOBAL BORDERS AND CONNECT WITH MORE THAN A BILLION CONSUMERS EVERY YEAR, AND ARE WELL ON OUR WAY TO MAKING A DIFFERENCE IN THE LIVES OF TWO BILLION PEOPLE BY 2025.

We will do this by building on the strength of our Co-operative to take on challenges and make the most of new opportunities. Our grass to glass business means we are well-placed to succeed.

This year, we have concentrated on making the most of every opportunity as milk prices returned to more normal levels, bringing the benefits of better demand and improving returns to our farmers. At the same time we have maximised earnings by moving more volume into higher value products.

SALES VOLUME GROWTH
5.5 billion LMEs sold in Consumer and Foodservice – an additional 576 million on last year.

We are working with new technologies and finding new ways of thinking about dairy nutrition. We are delivering on our strategy which gives us the right to be able to look into the future, using the benefits and versatility of dairy to create sustainable value for our farmer shareholders and unitholders.

STRONG V3 CO-OPERATIVE

We are implementing our strategy across three strategic horizons – Strong V3 Co-operative, Innovative Co-operative, and Sustainable Co-operative. New Zealand milk remains at the very core of our Co-operative, and it is clear that our future requires us to be strongly connected to the diverse and ever-changing needs of our customers and consumers.

Our V3 strategy of Volume, Value and Velocity is at the heart of our ambition, and provides the foundation for us to fund and drive innovation and sustainable value creation. This has been a year where our V3 strength has made sure that we can deliver solid earnings alongside rapidly increasing milk prices.

ADVANCED INGREDIENTS

Examples of Advanced Ingredients include functional proteins, high-spec WMP, and extra-stetch cheese.

In Ingredients, we achieved a nine per cent increase in sales volumes for our higher value Advanced Ingredients, such as functional proteins, high-spec whole milk powder and extra-stretch cheese.

These Advanced Ingredients grew in volume by 473 million LME this year, increasing Advanced Ingredients to 19 per cent of total external sales.

Margins for our non-reference products were down 14 per cent per tonne this year, but through our manufacturing flexibility we have been able to partially offset this by making the best choices in our product mix.

Our Consumer and Foodservice businesses saw continued growth, as our global customer teams sold almost 5.5 billion LMEs, an additional 576 million LME on last year. This is further demonstration that our new product development and strong customer relationships in our key markets are locking in good market shares. Each year we capture more and more of the full potential in these categories.

Higher input costs this year provided some pressure in our Consumer and Foodservice businesses but our strategy to drive more milk into higher margin products allowed us to achieve a normalised EBIT of $614 million, an increase of six per cent over last year.

We have also continued to do what we said we would do in Australia. Australia contributed well to Oceania's normalised EBIT, up four per cent to $101 million in Consumer and Foodservice, with Australia Ingredients achieving $62 million in normalised EBIT despite lower sales volumes.

LETTER FROM THE **CHIEF EXECUTIVE**

TRUSTED GOODNESS

Our story of grass-fed dairy in New Zealand produced by a farmer Co-operative and underpinned by world-class food safety and quality systems, goes to the essence of Fonterra's Trusted Goodness.™

DISRUPT

This year, our Disrupt programme generated new sources of revenue by creating future business models which will meet the needs of the consumer of the future.

Velocity

We have continued to deliver against our strategic priorities.

This has been helped considerably by the determination of our teams to embed this way of working over the last two years. It seeks to remove barriers to delivery, and builds in an owners' mind-set.

Our Velocity business transformation has freed up cash and created additional efficiency, and our three-year targets were reached in two years. This provides us with resilience to deal with expected and unexpected headwinds, and ensures that we are better placed to deliver consistent earnings despite volatility in global dairy markets.

We will continue to look for additional efficiency but Velocity will increasingly be used to lock in additional sources of revenue, leveraging new ways of working and future technologies.

Our reputation

We know that our customers want to know who produces their food, where it comes from, and that it's safe and good to consume. Our story of grass-fed dairy in New Zealand, produced by a farmer co-operative and underpinned by world-class food safety and quality, goes to the essence of Fonterra's Trusted Goodness.

FROM 9 TO 5

Fonterra's reputation has improved from ninth to fifth over the last year, when benchmarked against other comparable organisations.

The best way to share our story is through our farmers. Through the year they have shared with New Zealand and our global markets the remarkable and unique story built on the connections between our farmers, our people, and our communities.

We are committed to being a Co-operative that inspires and constantly delivers on the expectations of all stakeholders in a rapidly changing world. It remains a key part of our identity and we will keep working to achieve it.

FONTERRA VENTURES CO-LAB

In the past 12 months alone, we have scanned more than a thousand potential partners to help accelerate change as part of these initiatives.

INNOVATIVE CO-OPERATIVE

The world's population is growing, and quickly. It is estimated that by 2050 there will be more than 9.7 billion people, doubling the global demand for food.

This is a world where demand is outstripping supply, high energy protein-rich diets are becoming more common and the consumer of the future is shaping the way we will approach food production and supply.

GLOBAL PARTICIPATION

1,400 people have participated in Fonterra's Disrupt programme – around five per cent of the global workforce.

To succeed in this future we need to be more agile. Embracing change means looking at every facet of our Co-operative – on-farm, across our manufacturing assets and supply chain, our office functions, right through to the food we produce and how we produce it.

Our farmers have a history of innovation, and this has always been a feature of the Co-operative. We will continue to build on our already strong base, being well prepared for the fast pace of change and rapid development in technology facing us in the future.

Our ongoing progression in being an Innovative Co-operative is covered in more detail in the Our Potential section of this report.

This year, our Disrupt programme generated new sources of revenue by creating future business models which will meet the needs of the consumer of the future. To date, more than 1,400 people across Fonterra have participated in Disrupt – around five per cent of our global workforce.

True innovation comes from leveraging the strength of many. This year, we launched Fonterra Ventures Co-Lab, an initiative that has seen us partner with others in the field of innovation. In the past 12 months alone, we have scanned more than a thousand potential partners to help accelerate change as part of these initiatives.

LETTER FROM THE **CHIEF EXECUTIVE**

MEETING THE CHANGING NEEDS OF OUR CONSUMERS

Building on the foundations of natural, high quality dairy nutrition, Fonterra is well placed to meet the diverse and evolving preferences in the future of food.

From within our business, we are identifying the capabilities and cross-functional collaboration needed to meet the needs of future consumers. We are calling this VelocityNXT, and it will see us take our first exciting steps into new consumer and technology trends emerging around the world.

Our investment in innovation is enabled by the Strong V3 Co-operative of today. Investing in advanced technologies now will pave the way for exciting new drivers of value in the future.

Without question, the face of the food industry is already undergoing a major shift. What we will be eating in another 20 years will be very different to what we're eating today. Consumer expectations continue to evolve, signalling a need for more agile, responsive and sustainable sources of nutrition. Food tailored to meet individual consumers' needs is not far away, but we are well placed through our Innovative Co-operative strategy and with the foundations of natural, high quality nutrition already well established.

SUSTAINABLE CO-OPERATIVE

Our Fonterra Story talks about building on the proud heritage of the New Zealand dairy industry for future generations. To do this we need to make sure that we have an enduring business. This is not just about sustainability, it's about looking at everything we do and making sure it contributes to creating sustainable, long-term value.

CREATING SUSTAINABLE VALUE

Being truly sustainable means refining our farming practices, our role in the future of food, through to supporting a sustainable global dairy industry.

The Sustainable Co-operative does not stand alone from our Strong V3 Co-operative and Innovative Co-operative; they're intertwined. The Sustainable Co-operative will challenge us along our strategic horizons to make plans and decisions to deliver value for all our stakeholders, infinitely into the future.

SUSTAINABLE VALUE

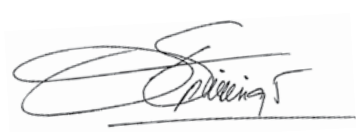
Sustainable value will require innovation and we will constantly look for alternatives in the energy and clean technology arena, helping us reduce our footprint and improve our operating efficiency while increasing our returns through the farming generations.

In New Zealand and everywhere we operate around the world, sustainable value means many things, such as refining our farming practices, our role in the future of food, considering how diets are changing and how dairy can solve some of the world's nutrition challenges, obesity and malnutrition – right through to our support for a sustainable global dairy industry through dairy development.

Sustainable value will require innovation and we will constantly look for alternatives in the energy and clean technology arena, helping us reduce our footprint and improve our operating efficiency while increasing our returns through the farming generations.

We are already well on track to deliver against our targets. There will be challenges, that is certain, but I firmly believe they will be some of the most formative in the history of Fonterra and our global dairy industry, and that is exciting.

None of this is achievable without the passion and commitment of our people. Our future is exciting, and I know we will exceed the ambitions that might now seem like lofty goals. I would like to thank the Board for their ongoing support, my colleagues on the Fonterra Management Team for their dedication and strong advice, and all of our people around the world for coming to work each and every day determined to make a difference for our farmers, our customers and our Co-operative.



Theo Spierings
Chief Executive

89%

FARMING SMART
89 per cent of Fonterra farms are connected to the Co-operative through smartphones or tablets.

FROM SMARTPHONES, THROUGH TO ROBOTIC MILKING, AND DRONE MAPPING.

Our farmers are increasingly using on-farm innovations that increase efficiency, productivity and sustainable outcomes.


WEIGHT
490 KGS
COW **828**
COW **799**

STRONGER **TOGETHER**

Fonterra farmers are at the beginning of our value chain and the heart of our Co-operative. We are constantly working to develop new tools and solutions to support our farmers.

IT STARTS WITH THE BASICS, LIKE LOWERING THE COST OF FARMING SUPPLIES ONLINE AND THROUGH OUR 71 FARM SOURCE™ STORES, SECURING DISCOUNTS ON SERVICES SUCH AS POWER, FUEL, VEHICLES, TYRES AND INSURANCE AND PROVIDING EXTRA PURCHASING POWER THROUGH OUR FARM SOURCE™ REWARDS DOLLARS.

We have also used our strong Farm Source™ balance sheet to provide financial support during tough times with more than 4,000 shareholders and sharemilkers taking advantage of extended interest free and deferred payment terms over the season.

DIGITAL TOOLS FOR REAL TIME INFORMATION

As technology evolves, we do too, making farming business easier with our apps On Farm, My Co-op and Monthly Plant Check.

My Co-op provides constantly updated news and information from across the Co-operative and the industry including milk price announcements, updates from the Chairman and CEO and rural and regional council news. The On Farm app provides daily milk production and quality information, comparisons against last season volumes, tanker ETA and summary reports of key milk performance information for the last 30 days.

The Monthly Plant Check app makes it easier for farmers to complete this assessment with diagrams, space to record notes and a 'farm summary' screen that shows what checks have been completed and what checks still need to be done. The apps complement our Farm Source™ website, which offers the same or more detailed data online back at the farm office.

FONTERRA GRASS ROOTS FUND

Fonterra has provided more than 10,000 high visibility vests to schools around New Zealand.

Launched this year, the Agrigate online tool developed by Farm Source™ and LIC combines all the key data farmers need to make faster and smarter decisions on one, easy to use online dashboard. By bringing together this data into one platform, Agrigate will help with future traceability of end products, creating additional value in our supply chain. On-farm, this data helps farmers to assess the interaction between different on-farm factors, such as weather conditions, animal health, milk production, financials, pasture cover and fertiliser applications.

A REGIONAL NETWORK TO SUPPORT OUR FARMERS

Farmers are fast adopters of technology, but apps can't replace real people, including our Area Managers, Sustainable Dairying Advisors, feed experts, Technical Sales Reps and Food Safety Managers. These are our local people, there to support farmers with a sounding board, practical solutions and direct links to senior people who can handle concerns or questions.

The value of our regional model is no more evident than during severe weather events or natural disasters and many regions of New Zealand experienced that this year.

In April, Cyclone Cook caused widespread flood damage to homes and farms in Edgecumbe, Te Puke, Galatea and Reporoa. Following the initial flooding, our Farm Source™ team and staff from our Edgecumbe site, and the Co-operative's Emergency Response Team transformed the local site into a hub of operations and meeting place for the community.

Our people went to work sandbagging properties threatened by rising flood waters, and then as the water receded, helped the town to fill 120 rubbish skips each day as part of the clean-up. We also provided tankers to be used for transporting drinking water to local residents.

TIAKI: FARM SOURCE™ SUSTAINABLE DAIRYING

As a responsible Co-operative, sustainable dairying is core to our long-term strategy. Our customer and community expectations continue to rise, so it's our ability to produce high quality dairy within environmental limits that will create the most long-term value for our farmers. Our Tiaki programme is designed to support our farmers to meet these standards.

As part of our wider sustainability strategy, Tiaki brings together our Co-operative's on-farm sustainability tools and services, tailored to individual farm needs. We have built up a team of skilled experts over the years in every region to work with farmers in key areas like nutrient management.

Through Tiaki, our Sustainable Dairy Advisors are helping to develop Farm Environment Plans to assist farmers in meeting regional regulatory requirements. They are using the best tools and technology such as innovative Geographic Information Systems (GIS) mapping technology to manage and mitigate the environmental impacts of farming. They help farmers to navigate through resource consent processes which vary by region.

OUR
CO-OPERATIVE

SHARING OUR FARMERS' STORY
Our Co-operative's reputation shifted from ninth to fifth in our reputation comparison set.

This is part of our philosophy of delivering solutions to farmers, helping them to manage their businesses within ever-evolving regulatory environments.

SHARING OUR FARMERS' STORY: FROM HERE TO EVERYWHERE

We continued to tell our farmers' story to the New Zealand public by sharing our Co-operative's efforts to take Kiwi innovation and dairy nutrition to the world. We know that when the public have a better understanding of who's behind our Co-operative and what we stand for, they feel more positive towards us. The support of New Zealand is important to our farmers and our people.

We measure our reputation using a system called RepZ, which is the global standard for reputation measurement. It compares us against nine organisations, that are either similar to Fonterra, or have public reputations similar to where we want the Co-operative to be.

At the start of the year we were last in our comparative set. Over the course of the year, our reputation work focused on giving our farmers an opportunity to talk about all of the good things their Co-operative does for New Zealand, and the areas that we know are important to the public and that we are trying to improve.

We finished the year fifth equal in our comparative set, an improvement in RepZ which is virtually unprecedented in New Zealand.

DAIRY DEVELOPMENT

New Zealand farmers are considered to be among the best in the world. Through our Dairy Development programme they share their skills with their counterparts overseas, either as volunteers abroad or by hosting farmers from developing dairy regions back here in New Zealand.

Dairy Development supports local farmers to produce consistently safe, quality milk that local consumers can trust. In the process, it improves livelihoods and creates thriving communities by generating sustainable employment.

We work with small-scale farmers to teach global best practice techniques for food quality and safety, and animal husbandry.

We have a new exchange scheme this year for young Chilean farmers. The first group of 11 arrived in New Zealand in June for a year of paid hands-on work experience at participating farms.

CONTRIBUTING TO OUR COMMUNITIES

The Fonterra Grass Roots Fund

Our Grass Roots Fund financially supports initiatives that help to strengthen our dairy communities, bringing them together, caring for the environment and promoting safe and healthy lifestyles. Launched in 2007, we now have

FONTERRA MILK FOR SCHOOLS
More than 1,450 schools and around 140,000 children take part in our Milk for Schools programme.

Grass Roots Funds in New Zealand, Australia and Sri Lanka. This year more than 430 grants were awarded with more than $750,000 donated.

In New Zealand, the fund is helping to provide safety, rescue and lifesaving equipment, providing more than 10,000 high-visibility vests to school children, and helping the Whakatane Kiwi Trust to buy equipment to protect the kiwi.

In Australia, many of the grants supported sports and kids' education. We helped three pre-schools to establish garden beds to grow fruit and vegetables to learn about healthy eating and sustainability.

The focus in Sri Lanka has been on education. At Moragahahena Maha Vidyalaya, Horana, a school attended by some of our farmers' children, there was no water during the frequently occurring periods of drought. Funding and volunteer time from staff have seen their old well fully renovated, providing a permanent water solution.

IN-SCHOOL PROGRAMMES

Fonterra Milk for Schools

We are making a difference to the health of future generations of Kiwi kids by offering a free serving of cold milk to primary-aged children every school day. Over five years since it was launched, participation is still strong with more than 1,450 schools and around 140,000 children taking part, drinking upwards of 87 million individual packs to date.

New research[1] from Massey University shows children who regularly drink milk as part of the programme had significantly improved bone health when compared to a control group who do not participate in the Milk for Schools programme. It also confirmed that Fonterra Milk for Schools has increased the proportion of children achieving the Ministry of Health's recommended number of serves of dairy on weekdays.

KickStart Breakfast

KickStart Breakfast helps Kiwi kids achieve their potential, not only by providing a nutritious breakfast, but also by providing a supportive, nurturing environment. Through a partnership between the Ministry of Vulnerable Children, Sanitarium and Fonterra, the programme provides children with Weet-Bix™ and Anchor™ milk and supports the local community volunteers who run the breakfast clubs.

This year KickStart Breakfast reached 946 clubs serving breakfasts to more than 29,000 children and young people every week.

1 *In addition to the findings by University of Auckland reported last year.*

EXPERTISE IN INNOVATION

Fonterra's Research and Development Centre in New Zealand is one of the largest of its kind in the world, with around 250 scientific and technical staff.

HIGH QUALITY MILK PROTEIN CONCENTRATES MADE FROM THE MILK OF FONTERRA FARMERS.

These are used in formulations both in New Zealand and overseas to help millions of people recovering from surgery and serious accidents.

OUR **POTENTIAL**

Fonterra continues towards its ambition to make a difference in the lives of two billion people by 2025 and through our strategy, we are making good progress.

A SIMPLE STRATEGY

To help satisfy the world's demand for dairy – supplementing our New Zealand milk by growing our global milk supply and creating more value from every drop of milk.

WE SET OUR SIGHTS FIRMLY ON VALUE CREATION FOR OUR FARMERS AND BUILDING A CO-OPERATIVE WITH THE STRENGTH AND CAPABILITY TO DELIVER – AND WE FEEL WELL SET FOR THIS WITH OUR LEGACY OF CHALLENGING THE BOUNDARIES OF WHAT WE THOUGHT WAS POSSIBLE.

Our world continues to shift, with population, global economic, technology, science, consumer and food consumption trends all moving fast. To keep pace, we too are evolving in our approach to providing sustainable, affordable dairy nutrition to meet growing global demand.

The foundation of our strategy still remains the same – to build a strong Co-operative with our V3 strategy delivering consistent strong results over the long-term.

STRONG V3 CO-OPERATIVE

Our Strong V3 Co-operative remains the solid foundation needed to build our business and move into leadership areas where future value will be uncovered.

We have consistently delivered on this strategy since its inception, and this will continue to be the platform we leverage for our other strategic horizons.

Grow Volume with Value at Velocity

Emerging markets, growing populations and a desire for safe, accessible and nutritious food is driving strong demand for our natural dairy nutrition.

Our strategy is simple – to help satisfy the world's demand for dairy – supplementing our New Zealand milk by growing our global milk supply and creating more value from every drop of milk through the right mix of products, services and global partnerships, and of course doing this at pace.

When this strategy is executed well we are at our best, delivering strong returns to our farmers and enabling our business to reinvest in initiatives to promote growth and additional value.

BUILDING AN ACTIVE LIVING PORTFOLIO

Advanced adult nutrition is becoming more important and mainstream.

Sustainable value from NZMP

Dairy Ingredients remain at the core of our business and are the foundation on which we build our Strong V3 Co-operative. Keeping this engine tuned and performing is key to achieving our ambition.

To build sustainable value from our engine, we are investing in the application of technology to further lift quality and productivity, improve our operating efficiency and maximise value achievement through customised nutritional solutions for our customers.

Our NZMP teams around the world have a strong track record of delivering improved margins above Global Dairy Trade (GDT) prices through the strong NZMP brand proposition.

Focused growth in our Consumer portfolio

By 2050, global demand for food is projected to double.

Staying ahead of demand will mean being closer to our consumers, anticipating their consumption needs and being more visible in the places and platforms where they choose to purchase.

To achieve this, we are investing in capabilities such as agile product development and concentrating our efforts on the fastest growing categories in key markets. These include dairy beverages, yoghurts and cheeses. Our three global brands – Anchor™, Anlene™ and Anmum™ – will carry the banner for growth across these product categories and remain our most trusted hero brands in each of our key regions.

Foodservice expansion

The development of our Foodservice capability is a very strong growth story. It continued over the past 12 months as our focused product range and innovative chef-led strategy delivered a 27 per cent growth in sales volume. This was off the back of rapidly changing consumer preferences towards out-of-home consumption.

Over the past four years, Fonterra has invested more than $850 million in plants dedicated to making Foodservice products to support the steady increase in demand.

This investment is delivering strong results for the business, supporting our double-digit growth strategy for Foodservice.

Building an Active Living portfolio

More than ever before, consumers are conscious of the role nutrition plays in maintaining a healthy lifestyle. Once, protein powders were seen as nutrition for elite athletes, but as people live longer and populations age, advanced adult nutrition is becoming more important and mainstream.

As consumer awareness of the role of nutrition in health rises, demand for sports and medical nutrition will continue to grow, across both the developed and developing world. This will be an area of significant focus for us in meeting our V3 targets.

OUR **POTENTIAL**

POTENTIAL OF OUR PEOPLE

Fonterra has accelerated its performance culture through new programmes with people, diversity and innovation at their core.

Selective investments in milk growth

Globally, demand for dairy nutrition is growing each year by more than 25 times New Zealand's ability to sustainably grow supply.

The high quality milk supplied by our New Zealand farmers is and always will be the essence of our Co-operative but, as demand grows, our ability to supplement our New Zealand milk supply from other sources will be key.

Over recent years, we have invested in supplementary milk sources in Australia, Chile, China and the Netherlands, allowing us to keep growing sustainably. Our presence in these markets also brings us closer to our customers.

To support our New Zealand Ingredients, our goal is to reach 30 billion litres of milk around the world by 2025, something we are well positioned to achieve.

INNOVATIVE CO-OPERATIVE

We already have a strong history of innovation within our Co-operative and a shift to even more innovative value creation will be needed to set us up for success in a rapidly changing world.

Our new markets will be defined by fast-moving trends, immediacy of consumer behaviour and unprecedented technology change. To keep pace with this market evolution will require businesses to be increasingly agile in their operation and service to both customers and consumers.

Idea generation and the creation of a performance culture

This year has seen the acceleration of our performance culture in Fonterra with a strong focus on value creation.

Through a number of programmes that drive innovation we have brought a more entrepreneurial approach to parts of our business, accelerating our most promising ideas through incubators.

With support from the business and a mandate to 'win or fail fast', this environment encourages our people to back their ideas and bring in the resources to help them succeed.

Velocity and VelocityNXT

Velocity has turned the focus of all our people across each of our global markets, to accountability and a bias to action. To date, the programme has been responsible for uncovering significant value in our business across working capital, earnings and Milk Price. Over the last two years, more than 3,600 initiatives have been completed by employees in every part of our business around the world – an exceptional strike rate.

Building on Velocity, VelocityNXT takes the next step into true innovation, harnessing emerging technologies that will streamline our business, improve processes and ensure Fonterra is well set up to capture value in new ways.

AN INNOVATION CULTURE
VelocityNXT is part of Fonterra's drive to create sustainable returns through future-focused solutions.

Through VelocityNXT, we have created an internal incubator enabling our people to go after the big, exciting changes that may have previously been seen as too difficult because we did not yet have the necessary capabilities.

Supported by a venture capital board, and internal and external coaches, our people are taking their game changing ideas for the future of Fonterra through from concept to delivery.

VelocityNXT and our own people will be responsible for many of the big changes you will see in Fonterra in the coming years, as we adopt the technologies that will make us a sustainable, future-proofed Co-operative.

Disrupt

Disrupt is a platform that challenges our people to create new sources of revenue for our Co-operative, and leverages the diversity and creativity of our global business to deliver the best results.

Disrupt has involved 1,400 people contributing their ideas – aged from 21 years to 60, split almost evenly between males and females and with at least eight languages and around 27 different nationalities and ethnic backgrounds.

This is the strength of our global business – the diversity of thought we can tap into is one of our biggest assets in idea generation.

Since Disrupt launched last year, our people have generated 189 ideas for potential new consumer and customer-facing business models. Of these, two have received investment and have been launched as major ventures, with a number more currently in the pipeline.

In the first six months of trading, $3.4 million in revenue was generated from the two successful ideas, which are projected to deliver further returns in the coming years.

Tomorrow's innovation in what we do today

Through these new ideas, trends and ventures, we are developing and embedding the right capabilities in our Co-operative to keep up with the rapid pace of change around us.

We have the opportunity to innovate right along our value chain, from on-farm technology and automation, such as robotics and sensor systems, to highly automated and data-driven production, resulting in precise, efficient operations more aligned to our customers' needs – allowing our people to spend more time focusing on customer experience and preferences. This will form part of our drive towards generating truly sustainable value across our Co-operative.

OUR POTENTIAL

PROTECTING OUR FUTURE

Fonterra farmers have invested more than $1 billion into environmental care and improvements.

Digital consumers

Consumers are now more connected than ever and are increasingly looking for highly tailored, personalised, seamless experiences. They are able to research and compare products in an instant, shop globally for the best range and price, and embrace new channels as they look for the products to meet their needs.

To ensure we are present in the places where these consumers are buying their dairy, our business is becoming more mobile, connected 24/7, and constantly looking for new opportunities and different ways to understand and interact with our customers. Anticipating needs and delivering innovative solutions that put the customer and consumer at the centre of everything we do must be our biggest driver and will be the key to success for organisations competing for visibility in the digital age.

Central to this will be our ability to meet the 'convenience' needs of our consumers. Shopping is becoming increasingly connected with our everyday environment and technology.

We know that health solutions will become one of the biggest selling points for these consumers, with personalised nutrition and foods based on genomics setting the trend. Genomics allows people to choose what they eat based on their specific DNA and predisposition to certain illnesses and diseases or performance goals. Foods that are proven to improve their health through new product development and nutrient enrichment are already emerging and will be a focus for our business in the coming years.

SUSTAINABLE CO-OPERATIVE

The Sustainable Co-operative considers the long-term challenges and shifts we face as a global food producer. It ensures we are acting and planning today with a long-term view, managing the risks and identifying the opportunities to deliver a sustainable business.

Our progress towards a Sustainable Co-operative started many years ago. It's been demonstrated through our farmers' investments in on-farm environmental care and improvements, which is more than $1 billion in New Zealand. A sustainable future for our Co-operative is now an integrated part of the core strategy, and how we create long-term value as an organisation for our future generations.

Our future operating context

The world's population is currently 7.5 billion, and is projected to increase to almost 10 billion by 2050. With limited opportunities to increase food production through traditional means, this presents a phenomenal challenge for global food production which requires transformational thinking to overcome.

Further disruption to food production will be likely through changes in climate and increased climate variability. Food production must play an immediate role in long-term emissions reductions.

As populations grow, the link between nutrition and health is a growing focus. Diseases caused by poor diet and lifestyle are now the leading cause of death in all regions

INNOVATION STARTS AT THE SOURCE
New technologies will be at the forefront of sustainable value creation across our entire value chain.

TRUST IN SOURCE
Through a constant focus on maintaining the highest standards of food safety and quality, our consumers know they are receiving dairy nutrition they can trust for them and their families.

except Africa. These health challenges will become a major driver of product innovation.

We already see consumers taking greater interest in social and environmental factors when making purchase decisions. Trends towards natural foods, higher standards of animal welfare, or lower environmental impacts are already being demonstrated by consumers who are willing to pay more for products which create broader value to society. With this in mind, we expect shifts towards diets with lower environmental footprints.

Leading the future of sustainable, responsible dairy products

Access to affordable nutrition is a significant health issue in many developing countries. As we export to more than 100 countries, we have an opportunity to address this health problem by delivering affordable nutrition for those who are not wealthy enough to access 'everyday nutrition'.

We will achieve affordability through innovation in nutritional formulation, product manufacturing and distribution and working with the right partners. This has the potential to also provide local employment, adding further value to communities. An early example is our Anchor™ fortified milk-based drink in Ethiopia, created in consultation with the Food and Nutrition Society of Ethiopia to address local nutritional needs. This is blended and packaged in partnership with a local company.

Over-nutrition is a significant challenge in many markets, with health concerns increasingly influencing consumer preferences and regulation. To take a lead in nutrition, and to ensure the relevance of our products in a health-conscious market, we are already taking steps to reformulate products to address concerns such as added sugars.

Creating long-term value for stakeholders

Our ability to produce nutritious food from a healthy environment into the future rests upon a thriving, responsible and sustainable dairy industry. A commitment to a strong Co-operative that provides financial returns for reinvestment in innovation, sustainable infrastructure, and our communities is key. As a Sustainable Co-operative we will deliver value to our stakeholders in the widest sense.

For our farmers it's about a healthy income, not just to operate their farms but to continue their investment in the activities supporting on-farm innovation – to improve productivity, quality and environmental impact and deliver regional economic development through the generations.

Our own people must be fit to face these future challenges and that means building a great place to work, with a diverse, capable and engaged workforce.

Generating prosperity in rural communities, supporting dairy development in emerging markets and providing dairy nutrition around the world in an environmentally and socially responsible way will create our Sustainable Co-operative.

TRUSTED GOODNESS

Our Trusted Goodness™ quality seal is at the heart of our promise to provide trusted, high quality dairy nutrition.

NZMP LAUNCHED GRASS-FED AND NON-GMO FARM PRACTICE CLAIMS WITHIN THE LAST YEAR TO DELIVER EVEN GREATER VALUE TO OUR CUSTOMERS.

Through this programme, NZMP has so far delivered US$4.7M price achievement, with further growth projected into the future – a clear demonstration of the value of pure, New Zealand dairy.

GROUP **OVERVIEW**

Delivery of our strategy to optimise our farmers' New Zealand milk by moving more volume into higher value products has led to a solid operating and financial performance by the Co-operative, alongside a higher Farmgate Milk Price.

$745M

NET PROFIT AFTER TAX
With stable dividend per share.

HIGHLIGHTS

- Significant growth in Consumer and Foodservice – additional 576 million LME
- Advanced Ingredients LME growth of 473 million, an increase of nine per cent
- $745 million net profit after tax, delivering 46 cents earnings per share
- Solid return on capital of 11.1 per cent
- Further improvement in working capital days
- Continued strong balance sheet and financial discipline

The 2016/2017 season saw a pleasing return to a more sustainable Farmgate Milk Price. At $6.12 per kgMS, a 57 per cent increase, our farmer shareholders will receive over $3 billion additional payments compared to last season. Improved prices are a reflection of continued balancing of supply and demand in the globally traded dairy market. The increase included an additional nine cents per kgMS due to changes in the Farmgate Milk Price assumptions. This year, an amended methodology for determining revenues delivered an additional six cents, with the remaining three cents mainly due to lower capital costs.

In the 2017 financial year, Fonterra significantly increased its sales volume of higher value products. This includes a 12 per cent increase in Consumer and Foodservice volumes and a nine per cent increase in Advanced Ingredients. These increases were achieved despite lower milk collections in New Zealand and alongside a significant increase in the Farmgate Milk Price.

Lower collections this year contributed to overall sales volumes declining five per cent in the Ingredients business. An unusually wet spring in New Zealand led to peak milk production being around six per cent lower than the previous season (and 11 per cent lower than the record volumes in the 2014/15 season). Conditions improved during the summer and into autumn, resulting in collections for the full season being down three per cent on the previous season.

SALES REVENUE
Revenue grew 12 per cent on the back of strong demand.

$19.2B

NZD MILLION	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016	CHANGE
Volume (LME, billion)	**22.9**	23.7	(3%)
Volume ('000 MT)	**4,180**	4,313[5]	(3%)
Sales revenue	**19,232**	17,199	12%
Gross margin	**3,264**	3,632	(10%)
Gross margin percentage	**17.0%**	21.1%	–
Operating expenses	**(2,370)**	(2,528)	(6%)
Reported EBIT	**1,120**	1,431	(22%)
Normalised EBIT	**1,155**	1,358	(15%)
Net finance costs	**(355)**	(499)	(29%)
Tax (expense)/credit	**(20)**	(98)	(80%)
Net profit after tax	**745**	834	(11%)
Earnings per share (cents)	**46**	51	(10%)
Adjusted earnings per share[1] (cents)	**47**	54	(13%)
Dividend per share (cents)	**40**	40	0%
Adjusted debt to EBITDA[2] (ratio)	**3.5**	2.8	–
Gearing ratio[3]	**44.3%**	44.3%	–
Return on capital[4]	**11.1%**	12.4%	–
Free cash flow	**670**	2,184	(69%)
Capital expenditure	**851**	944	(10%)

1 *Adjusted earnings per share excludes certain non-cash items.*
2 *Ratio is economic net interest bearing debt divided by earnings before interest, tax, depreciation and amortisation (EBITDA). Both debt and EBITDA are adjusted for the impact of operating leases.*
3 *Gearing ratio is economic net interest bearing debt divided by economic net interest bearing debt, plus equity, excluding hedge reserves.*
4 *Return on capital is calculated as normalised EBIT, less equity-accounted investees' earnings, less a notional tax charge divided by capital employed. Capital employed excludes brands, goodwill and equity-accounted investments. Return on capital, including brands, goodwill and equity-accounted investments was 8.3 per cent (2016: 9.2 per cent).*
5 *China Farms volumes for the 2016 financial year have been restated to aid comparability between segments. Previously China Farms volumes were converted to metric tonnes based on the litres of raw milk sold. These volumes are now converted based on weight of milk solids (i.e. fat and protein content) in line with the Ingredients methodology, where 1 litre of milk converts to approximately 0.07 kg.*

GROUP **OVERVIEW**

576 M LME

INCREASE IN VOLUMES

Consumer and Foodservice sales grew by 12 per cent.

The overall tighter supply environment, in combination with low opening inventories, supported improved pricing through the year. Despite the supply constraints, the Ingredients business prioritised the sale of higher value Advanced Ingredients, the volume of which grew by 473 million LME this year.

Our Consumer and Foodservice businesses had another strong year of sales growth. The 576 million increase in LMEs sold was supported by growth in both Consumer and Foodservice, the latter increasing 27 per cent this year. The standout performer was Greater China, where our successful Foodservice model continued to deliver growth in volume and earnings. Robust growth was also seen in our Soprole business in Chile, as well as in our operations in Sri Lanka.

LIQUID MILK EQUIVALENT

LME is a standard measure of the litres of milk allocated to each product based on the amount of fat and protein in the product relative to standardised raw milk. For example, a 1kg block of cheese equates to approximately 6.5 LME.

China Farms had its first full year of production with our two hubs fully stocked with livestock. Total sales volume increased 47 per cent to 335 million LME, driven by larger herds and increased on-farm productivity.

In a year that saw a 57 per cent increase in the Farmgate Milk Price, Fonterra delivered a solid earnings performance. Normalised EBIT for the Group was $1,155 million, delivering a net profit after tax of $745 million, 11 per cent lower than last year. Combined with continued strong financial discipline, the Co-operative maintained a 40 cents per share dividend. Overall, Group return on capital was 11.1 per cent reflecting solid earnings generation off a relatively stable capital base.

Our Ingredients business generated $943 million in normalised EBIT, a 22 per cent reduction on last year. This decrease was primarily the result of less favourable stream returns, which were $180 million lower than last year. Earnings were also impacted by changes to the Farmgate Milk Price Manual and the natural lag in contracts where pricing is set periodically, as these tend to underperform in a rising commodity environment.

Normalised EBIT for Consumer and Foodservice was up six per cent at $614 million. This reflects strong growth where higher volumes and improved pricing offset the compressed gross margins from increased input costs. Our Consumer businesses maintained stable gross margins of 29 per cent. Foodservice delivered strong gross margins of 22 per cent, a decline from last year, primarily due to the significantly higher global prices of fat-based products.

At the beginning of the year, responsibility for the sale of China Farms' milk shifted to our Ingredients team in Greater China. The operations are now exclusively focussed on producing high-quality fresh milk in the most efficient and sustainable way, and our Ingredients business is responsible for capturing the greatest value from that milk. This is supported by the introduction of an internal raw milk price reflective of the long-term milk price forecast for high quality milk in China.

44%

GEARING RATIO

Significant improvement in the gearing ratio from last year maintained.

STANHOPE

First production from our new cheese lines in Australia.

One of the highlights for the year was the performance of the Australian business. After a multi-year transformation the Ingredients, Consumer and Foodservice businesses are performing well, generating sustainable profits while paying a competitive milk price to our supplying farmers. This turnaround is reflected in our milk collections in Australia, where volumes grew by four million kgMS, up three per cent for the season despite the country's overall production declining seven per cent. We have also re-opened our facility at Stanhope. This plant will produce a range of cheeses for the domestic and global markets.

The carrying value of our investment in Beingmate has been reduced this year to reflect the impact of the changing Chinese market for infant formula prior to a new regulatory framework being in place from 1 January 2018. The impact was $76 million overall, $41 million in losses reflecting Fonterra's 18.8 per cent share of Beingmate's performance, and a $35 million impairment of the value of Fonterra's investment. This was partially offset by the $42 million gain on sale for Beingmate's 51 per cent share of the Darnum site in Australia.

The Group result continues to reflect the benefits of our on-going Group-wide business transformation. This is evidenced by the further six per cent decrease in Group operating expenses, on top of last year's eight per cent reduction.

Total net profit after tax reflected more favourable finance costs and tax expense for the year. Net finance costs were $144 million lower than last year due to lower average debt through the year and a change in accounting treatment for certain non-cash fair value adjustments. Total tax expense was 80 per cent lower than last year at $20 million, partly due to lower operating profit and one-off capital gains taxes recognised last year.

The Co-operative again maintained strong financial discipline in a year where earnings performance was more challenging. The Group's gearing ratio remained 44.3 per cent, the same as last year. This was the result of an increase of $173 million on the equity side of the calculation, which offset the $128 million higher closing balance for economic net interest-bearing debt.

Fonterra generated free cash flow of $670 million and again lowered working capital as measured in days' sales, coming in at 75 days compared to 77 days last year. Working capital efficiency is a strategic focus across the organisation, with a particular focus on efficiently managing inventory. Due to a 54,000 MT reduction in inventory, the value of inventory only increased eight per cent, in a year where the average value increased 20 per cent per metric tonne due to higher global dairy prices. Capital expenditure was down ten per cent to $851 million, in line with expectations.

Another year of strong operating performance and continued financial discipline resulted in the Board declaring a full-year dividend of 40 cents, the same level as last year. This level is consistent with the Board's policy to pay out 65-75 per cent of adjusted net profit after tax over time.

INGREDIENTS

This includes the global sales from our Ingredients businesses in New Zealand, Australia and Latin America. It also includes the Fonterra Farm Source™ rural supplies retail chain in New Zealand.

NORMALISED EBIT

Ingredients normalised EBIT of $943 million, a decline of 22 per cent.

$943M

INVENTORY DOWN

Year-end inventory was 15 per cent down on last year, historically low levels.

HIGHLIGHTS

- Advanced Ingredients LME growth of 473 million, an increase of nine per cent
- Normalised EBIT of $943 million, down on last year primarily due to lower stream returns
- Increased production for Foodservice to support our growth strategy
- Return on capital of 10.3 per cent
- Historically low closing inventory levels
- Australian Ingredients delivering higher quality earnings

VOLUME

Milk collection across New Zealand for the 2016/17 season was 1,526 million kgMS, down three per cent compared to the previous season. Farmers experienced wet conditions in both the North and South Islands through the peak collection months of spring, significantly lowering peak production. However, improved conditions in summer and autumn resulted in a lift in production in the later part of the season. Overall, collections in the North Island were down four percent, with South Island collections flat.

In Australia, milk collection for the 2016/17 season was 125 million kgMS, three per cent higher than the previous season, despite overall milk production in Australia declining seven per cent. These volumes include milk collected directly and through third parties. Favourable weather conditions in autumn and an increase in market share have resulted in these higher collection volumes.

Ingredients sales volumes were down five per cent for the year, driven by lower opening inventories, and the lower collections in New Zealand. Our total Ingredients sales now include 335 million LME from our China Farms, as we progressed our strategy of a vertically integrated milk pool in China. We transitioned the sale of raw milk to our Ingredients sales team in China who are responsible for capturing the greatest value from that milk.

NON-REFERENCE PRODUCTS

Gross margin for non-reference products favoured their production over reference products.

NZD MILLION	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016	CHANGE
Volume (LME, billion)	**21.3**	22.4	(5%)
Volume ('000 MT)	**3,018**	3,074	(2%)
Sales revenue	**15,284**	13,005	18%
Total gross margin	**1,489**	1,862	(20%)
– New Zealand Ingredients	**1,239**	1,605	(23%)
Reference products	**428**	634	(32%)
Non-reference products	**811**	971	(16%)
– Australia Ingredients	**78**	58	34%
– China raw milk[1]	**(38)**	–	–
– Other	**210**	199	6%
Normalised EBIT	**943**	1,204	(22%)
Gross margin ($ per MT) – New Zealand Ingredients			
Reference products ($ per MT)	**232**	330	(30%)
Non-reference products ($ per MT)	**1,165**	1,348	(14%)
Return on capital[2]	**10.3%**	13.4%	–

1 China raw milk gross margin represents the net benefit / (loss) from the sale of milk produced by China Farms and sold to the Ingredients business in China at an internal raw milk price.

2 Return on capital is calculated as normalised EBIT, less equity-accounted investees' earnings, less a notional royalty charge for use of the Group's brands, less a notional tax charge, divided by capital employed. Capital employed excludes brands, goodwill and equity-accounted investments.

INGREDIENTS

NEW ZEALAND INGREDIENTS REVENUE AND VOLUME[1]	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016	CHANGE
Production volume ('000 MT)			
Reference products	**1,837**	1,873	(2%)
Non-reference products	**749**	746	0%
Sales volume ('000 MT)[2]			
Reference products	**1,841**	1,920	(4%)
Non-reference products	**696**	720	(3%)
Revenue per MT (NZD)[2]			
Reference products	**4,262**	3,276	30%
Non-reference products	**5,567**	4,972	12%

1 *Table excludes bulk liquid milk. The bulk liquid milk volume for the year ended 31 July 2017 was 76,000 MT of kgMS equivalent (year ended 31 July 2016 was 77,000 MT).*

2 *Revenue and sales volume exclude Foodservice volumes to China and Latin America. This volume for the year ended 31 July 2017 was 143,000 MT (year ended 31 July 2016 was 92,000 MT).*

Our product mix shifted towards fat-based products reflecting the strong global demand and high prices for these products, in particular butter. Our Ingredients business is the main supplier of our global Foodservice business, therefore we saw significant volume growth in products manufactured for this business such as UHT cream, mozzarella and butter – demonstrating the important role Ingredients plays in supporting our Consumer and Foodservice growth strategy.

NATURAL DEMAND

Global demand for butter is strong due to an increased recognition by consumers in the benefits of healthy and natural foods.

The Ingredients business has always had a focus on product innovation to meet exacting customer needs and open up new areas of demand. The products that serve these needs are called Advanced Ingredients, and generate premium pricing. They are differentiated from base ingredient offerings through their superior product performance, which is supported by Fonterra's own research and process innovation. Sales volumes of Advanced Ingredients, such as medical grade lactose, grew nine per cent this year and now make up 19 per cent of Fonterra's total external sales volume.

Strong customer demand and ongoing efforts to improve working capital meant that we closed the year with historically low inventory volume. Levels at our balance date of 31 July 2017 were 15 per cent lower than last year for Ingredients.

VALUE

Total normalised EBIT for the Ingredients business was $943 million, 22 per cent lower than last year's record level, primarily driven by lower gross margins in our New Zealand Ingredients business. The Ingredients business achieved manufacturing efficiencies, as well as reduced operating costs over the year. However, these benefits were more than offset by changes to the Farmgate Milk Price Manual, the impact of the natural lag in contracts with periodic pricing and the significant impact of stream returns.

Operationally our New Zealand sites delivered further improvements in yields and managed cost of quality to similar levels to last year despite tightening standards. The lower peak milk production, combined with additional processing capacity, ensured there were no costs associated with peak processing again this year. The unusual profile of milk collections over the season provided some challenges to operational planning, in particular the timing of late season production and sales.

The Farmgate Milk Price that informs our cost of milk for New Zealand production is calculated according to the Farmgate Milk Price Manual. The manual provides for Fonterra to retain an amount of earnings to generate a specified return on capital on an assumed asset base. These earnings are referred to as the regulated return. At the start of each season,

NEW PLANTS
Our Stanhope site in Australia reopened and Edgecumbe in New Zealand was expanded.

the manual is updated to reflect the latest revenue and cost assumptions. In 2017, lower assumed interest rates decreased the modelled return on capital, which lowered the regulated return across our New Zealand Ingredients portfolio. This negatively impacted gross margins in our Ingredients business.

In addition to this, the manual was amended to include prices from spot sales of WMP, SMP and AMF. This change was driven by Fonterra's constitutional requirement to pay the maximum sustainable milk price and regulatory requirements to pay an efficient, competitive milk price. This added an additional six cents per kgMS to the Farmgate Milk Price.

Our New Zealand Ingredients business manufactures five commodity products that inform the Farmgate Milk Price. These are called reference products, while all other products are non-reference products.

Gross margins for reference products were $428 million, $206 million lower than last year. This was a result of structural changes to the milk price model, a lower regulated return, lower margins from the natural lag in contracts with periodic pricing, which underperform in a rising commodity price environment, and lower sales of prior season inventories.

For non-reference products, gross margins were $811 million, $160 million down on last year. This was primarily due to significantly lower stream returns. Stream returns are the relative difference between reference product and non-reference product prices. This relative gap narrowed significantly, reflected in the 30 per cent increase in revenue per metric tonne for reference products versus a 12 per cent increase for non-reference products. This resulted in negative stream returns of $40 million, a decline of $180 million relative to last year. Non-reference product margins were also impacted by the structural changes to the milk price and a lower regulated return but these were offset by operational improvements.

The Australia Ingredients business delivered a strong performance. While normalised EBIT of $62 million was the same as last year, the quality of the earnings has improved.

INCREASED SHIPPING

With the introduction of a regular big-ship service from Tauranga, we now have weekly shipments on vessels with capacities of around 10,000 standard containers.

Last year's result included one-off gains such as the sale of Dairy Technical Services, whereas this year's result is largely sustainable earnings, and is on course to improve next year with the commissioning of the Stanhope cheese plant.

The Ingredients gross margin was also impacted by a $38 million loss representing the difference between the domestic milk price and the internal raw milk price paid to China Farms.

Our Global Operations team tightly managed capital expenditure through the year by focusing on value added products, efficiency gains and sustainability improvements. This year saw significant investment at our Edgecumbe site, the commissioning of Lichfield, and our $149 million rebuild of Stanhope.

CONSUMER AND **FOODSERVICE**

This comprises our Consumer brands and Foodservice businesses in Greater China, Latin America, Asia and Oceania.

$614M

NORMALISED EBIT

Despite significantly higher input costs earnings increased six per cent.

HIGHLIGHTS

- An additional 576 million LME moved into higher-value products
- Foodservice volume growth of 27 per cent and Consumer volumes up three per cent
- Normalised EBIT of $614 million, an increase of six per cent
- Return on capital of 47.2 per cent
- Successful product launches across every region

VOLUME

This year we continued to deliver on our strategy to move more volume into higher value Consumer and Foodservice products. We achieved volume growth of 12 per cent, selling 5.5 billion LME, an additional 576 million LME compared to last year. This increase was largely driven by strong Foodservice sales in Greater China, as well as strong growth out of Soprole and Sri Lanka. Overall volume growth for Foodservice was 27 per cent.

- **Greater China:** significant volume growth of 46 per cent, an additional 402 million LME this year, largely due to strong performance in China Foodservice.
- **Latin America:** strong growth of 18 per cent, due to another good performance by Soprole, with increased sales of yoghurts, liquid milk and desserts.
- **Asia:** volumes were up 153 million LME, a ten per cent increase, driven by double-digit growth in both Sri Lanka and Vietnam.
- **Oceania:** volumes were down five per cent, reflecting the sale of businesses in non-core categories in Australia.

FOODSERVICE GROWTH
Our Global Foodservice sales grew by 27 per cent this year.

NZD MILLION	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016	CHANGE
Volume (LME, billion)	**5.5**	4.9	12%
Consumer	**3.2**	3.1	3%
Foodservice	**2.3**	1.8	27%
Volume ('000 MT)	**1,783**	1,800	(1%)
Sales revenue	**6,517**	6,296	4%
Gross margin	**1,744**	1,808	(4%)
Gross margin (percentage)	**27%**	29%	–
Consumer	**29%**	29%	–
Foodservice	**22%**	27%	–
Normalised EBIT	**614**	580	6%
Return on capital[1]	**47.2%**	41.7%	–

1 *Return on capital is calculated as normalised EBIT, less equity-accounted investees' earnings, less a notional royalty charge for use of the Group's brands, less a notional tax charge, divided by capital employed. Capital employed excludes brands, goodwill and equity-accounted investments.*

NORMALISED EBIT: KEY PERFORMANCE DRIVERS NZD MILLION	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016
Normalised EBIT prior year	**580**	**408**
Volume	116	120
Price	64	(210)
Cost of goods sold	(176)	251
Operating expenses	53	(3)
Other	(23)	14
Normalised EBIT	**614**	**580**

CONSUMER AND **FOODSERVICE**

CONSUMER AND FOODSERVICE PERFORMANCE

	LME (BILLION)			NORMALISED EBIT ($M)		
	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016	CHANGE	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016	CHANGE
Consumer and foodservice	**5.5**	**4.9**	**12%**	**614**	**580**	**6%**
Greater China	1.3	0.9	46%	209	131	60%
Latin America	0.7	0.6	18%	103	108	(5%)
Asia	1.7	1.6	10%	201	244	(18%)
Oceania	1.7	1.8	(5%)	101	97	4%

VALUE

Our Consumer and Foodservice businesses delivered a solid result considering the pressure that was placed on margins by increased input costs this year. Normalised EBIT was $614 million, a six per cent increase compared to last year.

This increase was largely a result of higher volumes, improved pricing and reduced operating expenditure, partially offset by increased input costs as set out in the key performance drivers table. Overall our Consumer business maintained margins, with a gross margin of 29 per cent, the same as last year, reflecting a strong focus on strategic pricing and product range management. However, higher input costs were not able to be fully passed through in Foodservice, where gross margins compressed to 22 per cent from 27 per cent last year, due to a combination of competitive pressure and substitution risk.

- **Greater China:** delivered significant normalised EBIT growth of 60 per cent driven by increased volumes, particularly in Foodservice, and continued cost control.
- **Latin America:** strong earnings growth in Soprole driven by higher volumes through new product launches, however offset by the challenging economies of Brazil and Venezuela.
- **Asia:** normalised EBIT of $201 million, however higher input costs meant it was an 18 per cent decline.
- **Oceania:** normalised EBIT growth of four per cent, as our successful turnaround of the Australian business continues to deliver value.

REGIONAL UPDATE

Greater China

Greater China continues to deliver both volume and value growth, with an additional 402 million LME this year and normalised EBIT of $209 million, up 60 per cent on last year.

NEW UHT FLAVOURS

Our Anchor™ UHT range expanded, including a new 'Golden Kiwi' flavour.

The China Foodservice business delivered another strong performance, with sales volume growth of 48 per cent this year, as our Anchor™ Food Professionals™ model continues to build momentum in Mainland China. We increased our geographic reach, expanding into a further 20 cities, and enhanced our value proposition by operating in-market warehouses to enhance our service offering to customers and maximise cost-to-serve efficiencies.

SOPROLE BRAND
Our Soprole brand in Chile was relaunched this year.

Our Consumer brands businesses in Hong Kong and Taiwan performed well with both volume and value growth. Anchor™ has become the number one imported UHT brand in Mainland China for e-commerce sales this year, reflecting our strong commitment to this sales channel.

Our success in both the Consumer and Foodservice segments is in large part driven by ongoing development of innovative new products and solutions specifically tailored to Chinese consumer tastes, for example, the cream cheese tea macchiato in Foodservice and Anchor™ UHT milk in golden kiwi flavour.

The Greater China result has been normalised to exclude the $76 million impact of losses relating to, and an impairment on, our 18.8 per cent investment in Beingmate, our strategic partner in China. While these impacts are disappointing, it reflects the industry-wide disruption in the infant formula category in China leading up to the introduction of stricter regulation from 1 January 2018. Beingmate is well positioned for the new regulatory environment, having had 12 products approved in the first group of approvals from the Chinese regulatory body.

Latin America

Our Latin America business delivered a good result with volumes up 18 per cent on last year. However, normalised EBIT has declined, down five per cent for the year, due to the impact of weak economies in Brazil and Venezuela, offsetting strong earnings growth in Soprole.

MARKET LEADERSHIP

Six million servings of Soprole products are consumed every day in Chile.

Our Soprole business in Chile continues to perform strongly with total gross margin up 12 per cent on last year, as sales of desserts, liquid milk and yoghurt increased on the back of the successful relaunch of the Soprole brand, as well as the reformulation of products to meet higher nutritional standards introduced by the government. Although the business faced rising input costs, our pricing strategy and operational efficiencies allowed us to deliver both volume and revenue growth as well as increased market share.

FOODSERVICE
Our Foodservice business grew in all our four regions.

The economy in Brazil remains challenging, with overall market volumes in the chilled dairy category shrinking significantly this year. While total volumes in our business have decreased as well, continued focus on our cost base and product innovation has enabled us to gain market share, as well as increase revenue on last year. Despite this, high milk prices throughout most of the year, combined with high inflation, have put pressure on our gross margin. However, the business remains well positioned for when improved economic conditions return to Brazil.

In Venezuela, the adverse economic situation continues, however Fonterra's exposure to earnings risk is limited due to the relatively small scale of our business there and our local sourcing strategy.

Asia

We continued to grow volumes in our Asia Consumer and Foodservice business with significant volume growth of ten per cent, or 153 million LME. However, earnings were significantly impacted by increased input costs, which placed pressure on margins.

INNOVATIVE PARTNERSHIPS

In Thailand, we have a partnership with 7-11 to develop new food solutions for the leading convenience store chain.

Volume growth was driven largely by Sri Lanka where our 'Goodness Feeds Greatness' campaign and Ratthi festival promotions delivered successful results with increased sales of full cream milk powder, UHT and cream. Vietnam also performed well, with double-digit growth in Foodservice volumes as our chef-led approach expanded into cafes and bakeries across Vietnam. In the Foodservice business, we achieved volume growth across most of our markets, including Sri Lanka, Vietnam, Thailand, Indonesia and Malaysia.

Despite the growth in volumes, the $201 million of normalised EBIT was $43 million lower this year as increased milk prices had a significant impact on our input costs, particularly fat based products such as butter. Normalised EBIT was also impacted by an $18 million unfavourable currency translation movement from strengthening Asian currencies, and difficult trading conditions in the Middle East. Tight cost control led to savings in some markets, partially offsetting the higher costs.

AUSTRALIA MARKET LEADERSHIP

Fonterra products are number one by sales in the cheese and butter categories in Australia.

Oceania

Our Consumer and Foodservice businesses in Australia and New Zealand have delivered an increase in normalised EBIT, up four per cent to $101 million this year. Excluding the impact of businesses that are no longer part of ongoing operations in the region, sales growth was down one per cent and normalised EBIT was up six per cent.

STAR PERFORMER

One pack of Western Star™ butter, which turned 90 this year, is sold every second in Australia.

The turnaround in the Australian business has generated good results despite lower volumes and higher input costs. The business has focused on creating value in key product categories such as cheese and butter where consumer demand is strong and we have a competitive advantage with our strong brands. This year saw the completion of the transformation strategy by exiting less profitable product lines and businesses.

Our New Zealand business, including exports to the Pacific Islands, was impacted by poor summer weather, increased milk prices and strong competition in high value product categories such as ice cream and cheese. This put significant pressure on prices and margins, which were also impacted by higher short term operating costs associated with moving to new distribution facilities.

We have had a number of successful new product launches this year, with the release of eight different flavours of Kapiti™ ice cream tubs and Kapiti™ Single Farm Organic fresh white milk and cream, as well as our Anchor™ Protein+ range of high protein milk, yoghurts and smoothie boosters. Two of our key brands (Mainland™ and Tip Top™) were also voted within the top 20 most loved brands in New Zealand this year.

10x

GROWTH RATE

Our Anchor™ Food Professionals Foodservice™ business grew at 10 times the market growth rate for foodservice volume over the past 12 months.

$1 OUT OF EVERY $6 SPENT ON FOODSERVICE IS DAIRY RELATED.

We are on the ground in more than 50 markets, giving us a remarkable level of insight into our customers' needs. We sell to more than 10,000 bakeries each year, and this gives us a deep understanding of how that business operates and how to optimise it.

CHINA **FARMS**

This comprises our farming operations in China producing high quality fresh milk as part of our integrated China strategy.

335 M LME

COST REDUCTIONS
Operating costs reduced by six per cent or 0.21 RMB per litre.

HIGHLIGHTS

- Significant volume growth with both hubs fully operational
- Improved performance through on-farm efficiencies and cost management

VOLUME

Our farming operations in China comprise two completed hubs, which produce high quality fresh milk. Yutian, our most established hub, consists of three single farms and one double farm, with 19,200 milking cows. Our second hub, Ying, is now complete and consists of one single farm and two double farms, with 15,700 milking cows.

RAISED LOCALLY

All cows added to our operations going forward will be born and raised on our farms.

Sales volume increased by 47 per cent to 335 million LME this year. The significant increase in volume is largely a result of the Ying hub being operational for the full year, with fresh milk sales volume from Ying increasing more than 70 per cent this year. Production per cow has also improved, up five per cent year-on-year. Milk volume will continue to build as our herd progresses to full year-round production. When at full capacity our farms will be able to produce a combined volume of around 380–400 million LME.

DOWNSTREAM VALUE
Milk from our farms is now being used under the Anchor™ brand in cafés in China.

We are continuing our progress on the Joint Venture hub with Abbott, which leverages our expertise in dairy nutrition and farming, and Abbott's continued commitment to business development in China. Construction of the first farm was completed in late 2016 and the farm is now fully operational. Construction of the second farm began in early 2017 and is due for completion in late 2017.

VALUE

Our strategy for China Farms is to produce high quality fresh milk from scale, efficient and sustainable operations. From the start of this year, the responsibility for driving the greatest value from the raw milk produced in China now sits with the Ingredients team. This allows Fonterra to deliver value through integrating the sale of our milk into our Ingredients business and by developing high-value products for our Consumer and Foodservice businesses in Greater China. This year saw the first such product, with trial sales volumes of specially formulated Anchor™ barista milk for use in Chinese cafés.

This strategic focus enables China Farms to focus on production volumes and operational efficiency, without being impacted by fluctuations in milk price. The internal raw milk price between China Farms and our Ingredients business reflects the long-term milk price forecast for high quality milk in China. As a result, the China Farms financial result has improved significantly this year despite the on-going challenges of the low domestic milk price environment.

NZD MILLION	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016	CHANGE
Volume (LME, billion)	**0.3**	0.2	47%
Volume ('000 MT)[1]	**26**	16	55%
Sales revenue	**269**	183	47%
Normalised EBIT	**1**	(59)	–

1 China Farms volumes for the 2016 financial year have been restated to aid comparability between segments. Previously China Farms volumes were converted to metric tonnes based on the litres of raw milk sold. These volumes are now converted based on weight of milk solids (i.e. fat and protein content) in line with the Ingredients methodology, where 1 litre of milk converts to approximately 0.07 kg.

Normalised EBIT has improved from a $59 million loss last year to a $1 million profit this year, due to our ongoing efforts to reduce costs through operational efficiencies, milk volume growth and the impact of the market based internal raw milk price. We delivered a 0.21 RMB per litre or six per cent reduction in operating costs this year, largely due to more efficient fixed cost recoveries and a focus on efficient management of effluent. This enabled us to reduce effluent costs by 19 per cent despite the 17 per cent increase in production volumes.

With our own farm development programme now complete, capital expenditure for the year was significantly lower than last year. Costs incurred this year covered the completion of our effluent investments as well as business-as-usual maintenance and animal rearing costs.

50 FRESHWATER CATCHMENTS

THIS YEAR WE ANNOUNCED A BOLD NEW AMBITION.

We will lead the regeneration of 50 freshwater catchments across New Zealand.

SUSTAINABILITY AND **SOCIAL RESPONSIBILITY**

With the world's population expected to grow to an estimated 9.7 billion people by 2050[1], our Co-operative is well placed to play an important role in helping meet their nutritional needs in a sustainable way.

DAIRY DECLARATION
Dr Jeremy Hill, IDF and Dr Ren Wang, FAO sign the Dairy Declaration.

THE IMPORTANT CONTRIBUTION OF THE DAIRY SECTOR IN ACHIEVING A RANGE OF SUSTAINABLE DEVELOPMENT GOALS IS RECOGNISED IN THE DAIRY DECLARATION OF ROTTERDAM, SIGNED IN OCTOBER 2016 BY THE INTERNATIONAL DAIRY FEDERATION AND THE FOOD AND AGRICULTURE ORGANISATION.

OUR COMMITMENT

The dairy sector's contribution to achieving these sustainable development goals includes the role of dairy nutrition in balanced healthy diets, its contribution to employment, livelihoods and economies, and the improvements that are required in the management of the environment.

It links closely to our Sustainable Co-operative strategy framework and we have a strong commitment to build on our progress so far.

Operating sustainably includes listening to our stakeholders, taking ownership for the impacts of our decisions on society and the environment, and contributing to development within our communities.

As our products are delivered right around the world, we aim to make a difference to global health through dairy's natural goodness, providing nutritious, delicious and accessible food. At the same time, we are creating positive livelihoods for our farmers, our employees and their communities. By respecting human rights and providing good working conditions, we offer safe and meaningful employment, development opportunities and income generation which flows into the communities we operate in right around the world.

We know that to achieve long-term value we need to respect the environment and we achieve this through efficient and responsible farming, manufacturing and distribution.

1 *UN World Population Prospects (2015) - https://esa.un.org/unpd/wpp/publications/files/key_findings_wpp_2015.pdf*

HEART-PLUS™

Anlene Heart-Plus™ has been launched in Malaysia, helping to combat nutrition-related health issues.

PROTEIN+

Anchor™ Protein+ range launched to help consumers spread their protein intake across the day.

OUR APPROACH

Building on the core values of our people right throughout our farm to consumer supply chain, our approach is guided by best practice.

In 2014, we adopted ISO26000, the international guidance standard for operating in a socially responsible way, and established a process allowing us to analyse what is important to our stakeholders, assess our current performance and prioritise areas for improvement. This year we have also adopted the Global Reporting Initiative (GRI) standards and will be issuing a standalone sustainability report to complement this annual review later this year.

HEALTH AND NUTRITION

As a provider of dairy nutrition to the world, we are using the power of dairy to make a difference in the lives of two billion people by 2025. Through our scale and expertise, we have an opportunity and a responsibility to help address the complex challenge of malnutrition: under-nourishment, micro-nutrient deficiencies and over-nutrition.

We have launched Anlene Heart-Plus™ in Malaysia – a new formulation which adds vital nutrients to Anlene's 'nutrition for mobility' heritage, helping to combat nutrition-related health issues such as high cholesterol and diabetes. Anlene Heart-Plus™ was awarded the Healthier Choice logo by the Malaysian Ministry of Health, a trust mark showing consumers which products are healthier than others in the same category.

Improvements to our nutrition portfolio like this are developed based on sound science and are guided by our rigorous internal food and nutrition guidelines, which this year have been independently endorsed by the New Zealand Nutrition Foundation.

In New Zealand, Fonterra has committed to the Ministry of Health's Healthy Kids Industry Pledge which aims to reduce rates of obesity in Kiwi children. We recognise a big factor in making healthy eating choices is clarity of labelling and, in supporting the pledge, we are continuing to improve product labelling to help families make healthy choices for their children. As we refresh our packaging in New Zealand we are rolling out the health star rating on all of our everyday products, something we have already delivered on almost half of applicable products[2].

In a survey of New Zealand consumers on protein consumption, we found half of respondents say they get most of their protein in their evening meal while scientific evidence says that protein intake should be spread throughout the day to support optimal muscle health. To help Kiwis better balance their protein needs we have launched Anchor™ Protein+, a range of products designed to help spread protein intake across the day, supported by education material on the role of protein in healthy diets.

2 Applicable products are those intended for everyday consumption in New Zealand and where the packaging is not also used for export to regions where the health star rating is not accepted.

SUSTAINABILITY AND **SOCIAL RESPONSIBILITY**

FOR FUTURE GENERATIONS

Five years since Milk for Schools was launched, participation is still strong with more than 1,450 schools.

Nutrition programmes

We aim to demonstrate our co-operative spirit by making a difference for our communities through the way we conduct ourselves and by investing in specific nutrition programmes. For example, in New Zealand we are caring for Kiwi kids through our in-school nutrition programmes; Fonterra Milk for Schools and KickStart Breakfast (see page 23).

Food banks

Joining forces in 2007, our Australian business supports Foodbank, Australia's largest hunger relief organisation, who provide meals to charities and schools around Australia. To celebrate ten years of partnership, the relationship will now see Fonterra become the exclusive supplier of fresh milk for Foodbank's Milk Program in Victoria.

This programme distributes fresh milk to Australian families and individuals who need access to food. In 2016, Fonterra Australia donated fresh milk and other dairy foods equivalent to nearly 350,000 meals. Based largely on health and education outcomes, Foodbank has estimated a social return value of AU$4.4 million (NZ$4.66 million).

We also support other similar food bank initiatives throughout the world, including five food banks in the Auckland region, such as the Salvation Army and the Auckland City Mission; and also further afield with Red Alimentos in Chile.

TRUST IN SOURCE

Fonterra is committed to our promise of "Safe Food, Safe People, World Class Quality", delivering what matters most to our customers and consumers throughout our entire supply chain. This includes commitments to animal welfare, milk quality and on-farm management in New Zealand and all over the world.

Achieving benchmark standards

Two years ago, we set a target for all our manufacturing facilities to be certified to globally recognised benchmarks[3] by 2019; demonstrating they have robust Food Safety Management Systems. More than 80 per cent are now at this level. In addition, our own farming operations in China have also achieved this benchmark this year.

KICKSTART BREAKFAST

In partnership with Sanitarium, Kickstart Breakfast serves breakfast to more than 29,000 children and young people every week.

3 *Independent certification to standards recognised by the Global Food Safety Initiative.*

80%

BENCHMARK STANDARDS

In the last two years, 80 per cent of our manufacturing facilities have been certified to globally recognised benchmarks.

PRODUCT AUTHENTICATION

Our product authentication solution uses unique QR codes that allow consumers to check Anmum™ products are authentic.

Thinking and living food safety and quality

To ensure we deliver on our promise, we always focus on strengthening our food safety culture, knowing that with any improvement in the supply chain, everyone wins.

HELPING SET STANDARDS

Through participation in the GFSI's* Food Safety Culture Working Group we encourage new industry standards.

* GFSI = Global Food Safety Initiative

Independent research in 2017 shows the success of these efforts, with Fonterra employees better understanding their individual responsibilities as part of a food company. With this knowledge, they are empowered, encouraged and enabled to make decisions that ensure protecting food safety and quality is their first priority.

New and innovative thinking around food safety and quality has included turning procedural training activities into an interactive board game, customised to build engagement with its audience. The game has positively impacted food safety behaviours, and it won the New Zealand Association of Training and Documentation Learning Innovation of the Year 2016.

Global food defence – product authentication

We continue to deliver on our food traceability strategy, improving our capability to track all batches of product and the ingredients that went into them – from raw milk right through to the consumer. Our external traceability, or product authentication solution, uses a unique QR code that allows consumers to check the product is authentic, either pre or post purchase, as well as giving real time product status information.

This product authentication solution was launched in 2017 across our Anmum™ paediatric and maternal range in New Zealand.

OUR **PEOPLE**

DISRUPT
Our entrepreneurial programme involving 1,400 employees from 16 countries.

DIVERSITY AND INCLUSION

We believe having diverse and inclusive teams is hugely important to both our long-term success and to our communities. When we embrace different perspectives we know we are more innovative, make better decisions, and improve performance.

We have made good progress in this space, and we recognise there is more we can do to embed diversity and inclusion in our culture. To help achieve this we are engaging with our people to better understand what diversity means to them and supporting initiatives that foster diversity and inclusion across their networks.

Disrupt is an entrepreneurial programme enabling us to harness the diversity and talent of our people to create value, with cross-market and cross-functional teams developing and implementing new business models. Since launching last year, Disrupt has involved around 1,400 employees aged 21 to 60 from 16 countries.

As an example of our global activities, in Saudi Arabia we have worked with local government and developed our site facilities to meet the cultural requirements for female employees. Our manufacturing team in Saudi Arabia has gone from having no women in 2015, to women now making up eight per cent of the workforce.

Flexible working is a strategy we have adopted to promote a diverse and inclusive culture. By encouraging and supporting our staff when they need to work from different locations, or at different times, we can help with work-life balance and retain staff if circumstances change.

We don't do it alone – we also partner with organisations to further enhance diversity and inclusion. In New Zealand, these include the Whakaterehia Māori Leadership Programme, a partnership with ASB to develop Māori leaders for the future; Ngāti Whātua Ōrākei on leadership development and cultural elements of diversity and inclusion; First Foundation, which offers young people 'a hand up' irrespective of socio-economic status; and Global Women, with more than 35 of our female leaders taking part in their development programmes.

LEARNING AND DEVELOPMENT

Learning and development are essential building blocks of our Co-operative and, through a tiered development programme, we are offering our operators pathways to recognised[4] qualifications. DAIRYCRAFT is our entry-level technical training programme currently available for our processing and packing operators in New Zealand Powder, Cream and Cheese plants and delivered through a partnership with the Primary Industry Training Organisation. The programme is voluntary and self-paced, with coaching provided by a team of Fonterra staff. So far, 146 staff have completed the qualification and another 259 are in progress.

At the highest tier for operators, our Dairy Diploma programme is facilitated by a combination of staff from a local tertiary institute and our own experts. This year our second cohort started and we have 57 participants in total. Globally, we have continued to expand our Leadership

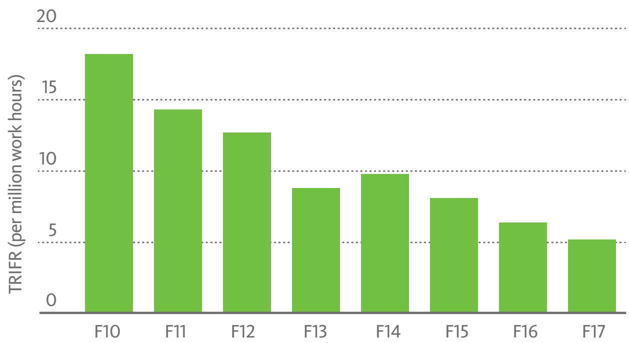
4 Recognised by New Zealand Qualifications Agency at level 3 and/or 4.

19%

KEEPING OUR PEOPLE SAFE

Our employee injury rate continues to improve, down 19 per cent on last year.

TOTAL RECORDABLE INJURY FREQUENCY RATE



Fundamentals programme, training 160 internal facilitators to deliver the face-to-face sessions in 16 countries.

This year we have also launched our new MYFONTERRA learning platform to give us increased ability to plan and record learning. As part of our annual policy compliance assessment, this enabled almost 2,000 staff around the world to complete 12 essential e-learning modules in their preferred language.

HEALTH, SAFETY AND WELLBEING

Health, safety and wellbeing are integral to how we operate because we want all of our people to go home from work healthy and safe every day.

WELLBEING CHALLENGE

Ninety per cent of those participating in this year's Eat, Move, Sleep Challenge said they'd keep the positive change going.

In Sri Lanka, the team was recognised by the Prime Minister and awarded silver at the National Occupational Safety and Health Excellence Awards.

Barry McColl, our General Manager of Transport and Logistics, was named the Road Risk Manager of the Year at the Australasian Fleet Safety Awards. This award recognises his role in maintaining the safety of more than 1,600 tanker drivers travelling more than 90 million kilometres per year.

There were no fatalities at any of our sites and serious harm injuries[5] have continued to decrease to 17, our lowest ever recorded level. We also reduced our employee injury rate to 5.2 total injuries per million hours worked, a reduction of more than 70 per cent since 2010. This is good progress, but we will never rest when it comes to having our people go home safely every day.

For the second year, our global wellbeing challenge was "Eat, Move, Sleep". Competing in teams, staff were encouraged to eat five servings of fruit and vegetables, move for more than 30 minutes and sleep for at least seven hours daily. Almost 20 per cent of all global staff participated and 85 per cent of staff surveyed afterwards felt it had a positive impact on their health.

Around the world our people have been significantly impacted by natural disasters such as the Kaikōura earthquakes, flooding in Edgecumbe and Sri Lanka; and by major civil unrest in Venezuela. Ensuring we protect the health and wellbeing of people is our first priority when any significant incident occurs. We are grateful to report that all our staff remained safe following these events and we have been able to provide assistance for them and the wider communities impacted.

5 Serious harm injuries are injuries that cause temporary or permanent loss of body function and include both employees and contractors.

SUSTAINABILITY AND **SOCIAL RESPONSIBILITY**

TUITION IN CHINA
Fonterra Scholarship students from Shanxi Agricultural University provide tuition to rural children.

AUSTRALIA GRASS ROOTS
We helped three pre-schools establish gardens, to learn about healthy eating.

LIVELIHOODS AND INCOME CREATION

We are committed to generating sustainable employment and income creation opportunities for our communities.

While international dairy prices were low, we sought creative ways to help alleviate the financial impact on our farmers, their employees and the wider communities they live in. Loans, which were interest free for two years have started to accrue interest but at a preferred rate. Our farmers benefited from discounts during FY17, both through our Farm Source™ stores and from our partnership vendors. They also earned Farm Source™ Rewards Dollars that can be used for on-farm purchases or for purchases for the family.

Approach to tax

Over the last few years there has been significant interest from regulators and politicians on how multi-nationals approach tax. We see our social responsibility commitments as extremely important and collecting and paying tax is part of that responsibility. We pay our fair share of tax in all jurisdictions, ensure legal compliance wherever we operate and do not avoid our tax responsibilities.

Co-operatives and corporates are very different and this is accommodated from a tax treatment perspective. Our tax law in New Zealand reflects this and, like most co-operatives, we pass income[6] directly to our farmer shareholders for them to pay tax rather than Fonterra paying tax directly and then passing those tax credits on to shareholders (the way a corporate would do).

COMMUNITY DEVELOPMENT

The Fonterra Grass Roots Fund

In New Zealand, Australia and Sri Lanka, our Grass Roots Fund financially supports initiatives that help to strengthen our dairy communities by bringing them together, caring for the environment and promoting safe and healthy lifestyles (see pages 22–23).

Greater China

In Greater China, our community care focusses on vulnerable or disadvantaged groups, both in the rural villages where we have farming operations and in some major cities. In addition to on-going activities, this year we introduced two new education programmes for primary-aged children from villages near our farms in the Ying county Shanxi Province.

Since 2010, nearly 900 university students have benefited from a Fonterra Scholarship and this year we established a summer holiday programme for them to return as teachers. Some students, from Shanxi Agricultural University, volunteered their time to provide extra tuition to around 70 children each day.

We have also funded lectures by influential NGO Girls' Protection to provide "protect your body" guidance to more than 100 children. The course seeks to help the children protect themselves against harassment.

6 Being approximately NZ$10 billion this year.

EMISSIONS EFFICIENT
Pasture-based dairying, is among the most emissions-efficient in the world.

LATAM

In Chile, in addition to supporting school sports and free education theatre for children, Soprole has backed the national Teletón since it started in 1978. Teletón is a charitable foundation committed to the rehabilitation and inclusion of disabled children in society. After almost 40 years, the annual Teletón event has become a flagship for national unity and collective community support for the development of these children and their families.

SUSTAINABLE DAIRYING

Supporting our farmers around the world

In all regions where we collect milk, we provide services specifically tailored to help our farmers build on existing good practices and make best use of on-farm innovations. In New Zealand, services are primarily provided through our Tiaki Sustainable Dairying Programme, in Australia it's through SupportCrew™ and in other countries support comes via our Supplier Relationship Officers.

Climate – carbon footprint

The main contributor to our overall carbon footprint is greenhouse gas (GHG) emissions from dairy production systems, primarily from our cows. We continue to invest in research and development[7] and improving productivity on-farm remains our priority. This is achieved by looking after cows so they stay healthy and produce high quality milk, supported by growing high quality feed and optimising other farm inputs.

This year, in addition to analysing our New Zealand milk supply for the full on-farm carbon lifecycle, we have also considered our Australian and China footprints for the 2015/2016[8] seasons using a similar approach.

Continuing a trend downwards over the past five years, our footprint in New Zealand has reduced and our milk is among the most climate efficient in the world - most of our raw milk supply is at less than half of the global estimated average. We are committed to continuing this progress through increased productivity and investment into research, science and technology.

Launched this year, Dairy Action for Climate Change was spearheaded by Dairy New Zealand in partnership with Fonterra and supported by the Ministry for Primary Industries. Among other activities, this will see farmers on 100 pilot farms given an indication of their specific footprint and how it changes over time. We will learn a lot through this pilot, which we can later apply at scale.

7 Our investment in research and development in this area is primarily through the Pastoral Greenhouse Gas Research Consortium (PGgRc).

8 Due to data availability lifecycle analysis to the farm gate can only be reported for the prior season and not that just completed.

SUSTAINABILITY AND **SOCIAL RESPONSIBILITY**

98.4%

CARING FOR OUR WATERWAYS

98.4 per cent of significant waterways on dairy farms across the country are fenced.

Water

We are fully committed to helping develop strong, sustainable ecosystems that can support profitable farms alongside healthy land and fresh water. This view has underpinned our farmers' active adoption of new farming practices, which both protect our waterways and support the production of high quality dairy products.

Our farmers have been working and investing in farming improvements for many years.

NUTRIENT MANAGEMENT

More than 95 per cent of farmers completed comprehensive nitrogen management assessments this year.

They have taken major steps to care for the land and their efforts to keep cows out of rivers and streams is a good example of this commitment. By fencing 98.4 per cent of significant waterways on dairy farms across the country and by ensuring that 99.8 per cent of regular water crossings now have a bridge or culvert, they are keeping their promise to care for the land.

Our next priority is for all New Zealand farmers to have a documented Riparian Management[9] plan in place by 2020. The launch of the new Tiaki Sustainable Dairying Programme in FY18 will support on-farm adoption rates, with a target of implementing 1,000 Farm Environment Plans over the next 12 months.

We know that science and technology will play a key role in meeting our commitment to swimmable waterways in New Zealand. Our farmers' investment in, and adoption of, new technology is accelerating our on-farm efforts to improve rivers, lakes and streams. Using the detailed information our farmers collect, our nutrient management service uses OVERSEER®[10], a nutrient software application, and our own systems to provide specialised reporting to our farmers. This information supports more informed decisions about nutrient management, helping to identify opportunities to reduce the risk of nitrogen leaching and improve efficiency. This year more than 95 per cent of our farmers completed an assessment for their farm.

Addressing water quality in New Zealand requires a localised approach. We are working proactively with Regional Councils to set environmental limits for water, looking at the land and water science, and determining the social, economic and environmental expectations of the communities they represent.

We have come a really long way, but of course we want to do more. Initiatives through our Innovative Co-operative strategy, tapping into the latest science and technology, will further help us make the transition to leading sustainable farming practices.

9 Management of the strip of land adjacent to the waterways including suitable planting to reduce erosion, capture nutrients and provide shade.

10 OVERSEER® is owned by the Ministry for Primary Industries, the Fertiliser Association and AgResearch.

LIVING WATER
Identifying solutions that can be adopted at scale.

PARTNERSHIPS IN ACTION

Living Water

Living Water is our 10-year partnership with the Department of Conservation (DOC) connecting our farmers with iwi, hapū, scientists, councils and community groups to demonstrate that sustainable dairying and healthy fresh water systems can thrive together. Combining DOC's conservation expertise with Fonterra's Sustainable Dairying Programme, we are trialling solutions that will scale to improve freshwater systems on farms across New Zealand. The following are examples of some solutions we've tested this year:

- An ecosystem services report commissioned by Living Water identified detention bunds, which slow down the release of flood and storm water. These are now seen as a potential solution for improving catchment resilience. Living Water is trialling two affordable detention bunds in the Wairua catchment to assess their ability to reduce peak flows and capture sediment.
- Following on-farm biodiversity assessments in Te Waihora, we started "re-battering" and planting banks. Re-battering of steep banks prevents slips and reduces sediment. With the inclusion of fast-growing native plants, it quickly provides shade to inhibit aquatic weed growth and cool the water which helps the development of beneficial aquatic organisms.

50 Catchments

We recognise we have an important role in addressing water quality and this year we announced a bold new ambition to restore 50 freshwater catchments across New Zealand. Our immediate focus will be on working with our farmers, communities, Government and other key partners to identify the catchments and develop a framework and improvement action plan.

SUSTAINABILITY AND **SOCIAL RESPONSIBILITY**

16%

REDUCING OUR IMPACT

We have achieved a reduction of more than 16 per cent in energy intensity since 2003.

SAVING WATER

The recently completed Lichfield powder plant expansion increased production 80 per cent while using 18 per cent less water.

SUSTAINABLE MANUFACTURING

This section focuses on our manufacturing footprint in New Zealand and Australia which together represent more than 95 per cent of our raw milk supply.

We have environmental management systems in place to ensure compliance with all relevant regulations and high standards of environmental performance.

For our sites, this means third party certification to the international standard ISO14001 and we are transitioning to the later 2015 version. In New Zealand, our five sites which make local consumer products such as fresh milk, yoghurt and ice cream have all achieved Enviro-Mark Diamond Status. This is the highest level of Enviro-Mark certification and equivalent to ISO14001:2015.

The Fonterra Brands team was recognised for its environmental performance at the Enviro-Mark Solutions' Environmental Excellence Awards this year.

Climate and energy in manufacturing

Fonterra has a number of commitments in place addressing intensity[11] of energy use and greenhouse gas emissions across our business operations, underpinned by our desire to move towards cleaner energy sources.

In our New Zealand operations we have achieved more than a 16 per cent reduction in energy intensity since 2003, against a target of 20 per cent by 2020.[12] With milk volumes down over the season, running plants as efficiently as in previous years has proved challenging and this has contributed to a flattening in progress this year. This applied across both countries increasing our overall energy use per tonne of production to 8.26 GJ/tonne.

An independent assessment of efficiency improvements made during the Pahiatua site upgrade identified significant benefits from the new dryer's heat recovery loop. Through energy conscious re-engineering, steam demand was reduced by 7.5 per cent.

Energy efficiency continues to be our main focus for greenhouse gas reduction but we are also committed to a transition to lower emission energy sources in our manufacturing activities. In 2016/17, we sought improvements in our greenhouse gas emission intensity by a shift in fuel mix quantity from coal to gas. At our Brightwater site we also completed a trial of co-firing coal with biomass and plans to develop this further are being progressed.

11 'Intensity' is the amount of energy used or greenhouse gas emissions produced per tonne of production.

12 Improvement is from a 2003 baseline and applies to New Zealand.

AOTEA MAERSK
One of a new generation of vessels that now regularly visits Port of Tauranga.

Water in manufacturing

Water use in manufacturing decreased for a second year to 14.4 cubic metres of water per tonne of production and reflects our increased focus in this area and investment in resource-efficient plants.

In its first full year of operation, our Pahiatua site increased production almost 90 per cent on FY15 while using almost 40 per cent less water. Expansion at the Lichfield site was commissioned this year and we have increased production by almost 80 per cent while using 18 per cent less water. In both cases we are capturing and cleaning the water evaporated from drying the milk so it can be re-used.

After using water we also need to dispose of it, with minimised impacts on the environment and working towards all manufacturing plants treating wastewater to a leading industry standard by 2026.

To help achieve this we are installing more biological treatment plants. These treatment plants also generate a waste product which is an excellent fertiliser for use on-farm. This fertiliser is an alternative to nitrogen and phosphorus fertilisers and contains matter which can also improve the water retention and structure of soil.

SUSTAINABLE DISTRIBUTION

Our land transport logistics partner, Coda, opened an intermodal freight hub at Savill Drive in Auckland this year and it's one of the largest in New Zealand.

Through the development of an end-to-end logistics model enabling visibility of broader import, export and domestic movements within the North Island's freight network, Coda is able to consolidate freight, reducing moves of empty space, by filling trucks and trains in both directions, saving fuel and reducing carbon emissions.

Innovative 25-foot curtain-sided containers have been created to support this strategy. These containers can be used on both road and rail, and are specifically designed with extra internal height to allow the double stacking of products.

Thermally-insulated curtain sides support efficient loading for fast moving consumer goods in the domestic market. Special features such as rivet-free internal surfaces help protect products from damage and reusable airbags secure the cargo while minimising waste.

The new era of larger ship visits, made possible through Kotahi's collaboration with export partners, Maersk Line and Port of Tauranga, is another key milestone. New generation vessels are more fuel efficient on a per-container basis and coupled with Coda's freight strategy we have more efficient and sustainable export logistics.

CORPORATE **GOVERNANCE**

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CORPORATE **GOVERNANCE**

The Board and Management of Fonterra consider that strong governance plays a critical role in the success of our Co-operative and are committed to achieving the highest standard of corporate governance and leadership.

To support this our Board has developed governance systems that reflect Fonterra's unique characteristics and requirements as a significant New Zealand based co-operative competing in the global dairy market.

Fonterra continuously reviews its Governance and Representation to ensure they reflect best practice for our Co-operative.

In October 2016, Fonterra's farmer shareholders voted to adopt a number of recommendations to enhance Fonterra's Governance and Representation including a reduction in the number of farmer elected Directors on Fonterra's Board and a change to the way Farmer Directors are elected.

CHANGES TO THE FONTERRA BOARD

There were a number of changes to the Fonterra Board during the financial year ending 31 July 2017:

- In August 2016, Mr John Waller, an Appointed Director, retired. In November 2016. Mr Scott St John was appointed by the Board to fill this vacancy.
- In December 2016, Mr Malcolm Bailey and Mr Ian Farrelly, both Farmer Directors, retired from the Board and Ms Donna Smit was elected to the Board as a Farmer Director.
- In January 2017, Mr Michael Spaans resigned from the Fonterra Board due to ill health. Mr Ian Farrelly was appointed by the Board to fill the vacancy created by Mr Spaans' resignation. Mr Farrelly's appointment is effective until the 2017 Annual Meeting on 2 November 2017.
- In June 2017, it was announced that Mr David Jackson, an Appointed Director, would be retiring from the Board in November 2017. Mr Bruce Hassall has been appointed by the Board to fill this vacancy with effect from 2 November 2017.

In line with the changes approved by farmer shareholders in October 2016, from 2 November 2017 the number of Directors elected by farmer shareholders (Farmer Directors) on the Board will be seven, with four Directors appointed by the Board (Appointed Directors).

COMPLIANCE WITH BEST PRACTICE GOVERNANCE STANDARDS

The Fonterra Board's governance framework takes into consideration contemporary standards in New Zealand and Australia, including the principles in the NZX Corporate Governance Code which comes into effect for reporting periods from 1 October 2017 (NZX Code). Fonterra has elected to report against the NZX Code. However, because it has elected to do this before it is required to do so, in certain instances Fonterra is not yet in compliance with all of the recommendations of the NZX Code.

We focus on governance in a way that promotes:

- the interests of our farmer shareholders, unitholders and other key stakeholders
- Fonterra's Co-operative philosophy, which is largely expressed through our Co-operative principles
- transparency, giving our farmer shareholders, unitholders and other stakeholders the information they need to assess our performance
- effective risk management and compliance to ensure that Fonterra meets its business objectives and all legal and reporting requirements
- an appropriate balance between the roles and responsibilities of the Board and Management
- communication with important stakeholder groups, including farmer shareholders, employees, customers, unitholders, debt investors, governments and the communities Fonterra works in.

CORPORATE GOVERNANCE

Principle 1: Code of Ethical Behaviour

Code of Ethics

A culture of honesty and integrity is integral to Fonterra's reputation and commitment to become the world's most trusted source of dairy nutrition. Fonterra expects its Directors, officers and employees to maintain high ethical standards and is committed to the use of global best management and business practices to ensure we operate ethically and legally in the countries where we do business.

Fonterra's Code of Business Conduct - The Way We Work, the Board Charter and the Group Ethical Behaviour Policy comprise Fonterra's code of ethics. These policies set clear expectations for our Directors and employees in matters relating to ethical behaviour which includes honesty and integrity, dealing with conflicts of interest, the use of corporate information and assets and property, giving and receiving gifts, procedures for whistle blowing and managing breaches. All three of these documents are required to be reviewed and approved annually.

Fonterra's values are at the core of Fonterra's commitment to acting ethically. These values are referenced in The Way We Work. This document provides straight forward, practical guidelines on how to apply Fonterra's values in everyday work situations and when working with customers, farmer shareholders, suppliers and the wider community.

The Group Ethical Behaviour Policy and The Way We Work are published in multiple languages and are available to all employees on Fonterra's internal website. As with other Fonterra Group Policies, employee training is included within Fonterra's global induction programme and annually refreshed. Individuals are assessed to ensure understanding of Group Policies and an annual certification process promotes compliance.

Fonterra has an established independently operated telephone, email, mail and web-based hotline. This provides individuals with a confidential channel to report concerns about unethical behaviour or any other action that they are concerned does not meet the standards of behaviour set in The Way We Work. This hotline is available in all regions that Fonterra operates within. In the 2017 financial year, 35 disclosures were made globally to the hotline. All were fully investigated, appropriate action taken and timely updates made available to the whistle-blower. An awareness campaign of the hotline was launched in 2017 and will be annually refreshed.

Fonterra operates a Conflict of Interest Register where employees must enter all actual or potential conflict of interests. Corporate gifts given or received, and hospitality and entertainment with third parties must also be reported in Fonterra's Gift & Entertainment Register.

The Way We Work, the Board Charter and the Group Ethical Behaviour Policy are available on www.fonterra.com.

Securities Trading Policy

Fonterra has adopted a Securities Trading Policy that details the rules for trading in shares, capital notes, retail bonds, units, milk price futures and options traded on the NZX and other listed securities of Fonterra or the Fonterra Shareholders Fund from time to time. The policy applies to Directors, officers, employees and contractors of the Fonterra Group (globally) and members of the Shareholders' Council and Milk Price Panel, and is additional to legislative requirements for trading securities in New Zealand and Australia.

The Securities Trading Policy is available, along with other key Group Policies on www.fonterra.com.

All Directors comply with the legislative requirements for disclosing interests in listed voting securities of Fonterra and its related companies.

Principle 2: Board Composition and Performance

Board Charter

The Board Charter includes details about the Board composition and procedures including the Chairman's election and role, the Board's relationship with Management and Incident Management engagement, training provided to Directors, and the process for assessing the Board's performance.

The Charter is reviewed annually and was last updated in June 2017. The Board Charter and the Charters of the Board Committees are available on www.fonterra.com.

Board Appointments

The Constitution of Fonterra provides for not more than 12 Directors until the conclusion of the 2017 Annual Meeting and not more than 11 Directors thereafter and sets out how they are appointed.

In accordance with the Constitution, presently not more than eight Directors are elected by farmer shareholders from the shareholder base (Farmer Directors), and not more than four Directors are appointed by the Board (Appointed Directors). Following the 2017 Annual Meeting this will change to not more than seven Farmer Directors, and not more than four Appointed Directors.

The Board is committed to building capabilities and maintaining the highest standards of governance. The Board also considers it important that there is a good balance of experience on the Board. A list of attributes that all Directors must be able to demonstrate has been developed by the Board and is reviewed annually. The Board has also developed a list of skills that the Board believes are required to effectively govern a complex, international co-operative, operating in multiple markets, answering to diverse stakeholders. The skills list is reviewed annually and, if required, updated. The Board then develops a 'Skills Matrix' by assessing the required weighting of each skill against the aggregate skills of the current Board.

The Skills Matrix is used to identify the skills to be targeted in each year, through the Farmer Director election process and the Appointed Director process. The list of attributes and skills, the Skills Matrix and the Board's targeted skills are published each year as part of the Farmer Director election process to assist potential candidates in assessing their suitability and to assist voting shareholders when assessing the candidates put forward for election.

The Nominations Committee appoints an 'Independent Selection Panel' to recommend to it appropriate candidates to be put to shareholders for their consideration to be elected as Farmer Directors. In addition to candidates recommended by the Nominations Committee, there is a 'self-nomination process' where candidates can propose themselves for election as Farmer Directors with the support of 35 shareholders. The Farmer Directors are elected by postal ballot by farmer shareholders. The elections are overseen by the Shareholders' Council.

The People, Culture and Safety Committee oversees the process for identifying and recommending potential Appointed Directors. Prior to appointment by the Board, the Fonterra Shareholders' Fund is consulted. The Appointed Directors are ratified by farmer shareholders at the next Annual Meeting.

Appointed Directors are selected to enable the Board to access a full complement of skills and competencies needed to lead an enterprise of Fonterra's size, global reach and complexity. They bring to the Board perspectives, experience and skills to augment the attributes and skills (including dairy industry knowledge) provided by the Farmer Directors.

Director Independence

The rules of the Fonterra Shareholders' Market (FSM Rules) require Fonterra to have a minimum of two Independent Directors or if there are eight or more Directors, three or one-third of the total number of Directors of Fonterra, whichever is greater. With Fonterra's current Board of twelve Directors, four must be Independent Directors.

In order to be an Independent Director, a Director must not be an executive officer of Fonterra, or have a 'disqualifying relationship'.

A Director has a disqualifying relationship where he or she has a direct or indirect interest or relationship that could reasonably influence, in a material way, the Director's decisions in relation to Fonterra. The FSM Rules contain specific examples of what may give rise to a disqualifying relationship. Appointed Directors cannot be shareholders and are expected to maintain independence for the length of their term.

Farmer Directors must be qualified as farmer shareholders under section 12.3 of the Constitution and are therefore not considered Independent Directors.

As at 31 July 2017, Clinton Dines, Simon Israel, David Jackson, and Scott St John each did not have (and continue not to have) any disqualifying relationship in relation to Fonterra and were therefore Independent Directors. John Waller was an Independent Director until his resignation with effect from 31 August 2016.

John Wilson, who is a Farmer Director, is the Board-elected Chairman.

Disclosure

Information about each Director (including experience, length of service, independence and ownership interests) is disclosed at the end of this section or in the statutory information section of this Annual Review, and is also available on www.fonterra.com.

Diversity Policy

We believe that a culture of diversity and inclusion better equips Fonterra to deliver its ambition. Respecting, leveraging and embracing the unique skills and diverse perspectives of our people is consistent with what we stand for to all our stakeholders, and reflects a core Fonterra value to 'Do What's Right'.

Fonterra's People Management Policy requires that all policies, standards and guidelines support the intent of diversity and inclusion. Over and above this, we have developed a Group Diversity and Inclusion Policy which sets out what people who work for and with Fonterra can expect around diversity and inclusion and how it will help Fonterra to deliver its ambition.

Fonterra develops and implements strategies and initiatives to build more diverse and inclusive teams. As part of Rautaki Māori (our Māori Strategy), we are active participants in the Whakaterehia programme which is identifying and developing Māori leaders for the future. We are a major partner of Global Women and are heavily involved in the New Zealand-based Champions for Change initiative. We also focus our attention on how to attract and select a more diverse group of graduates for both our business and technical graduate programmes.

Fonterra has committed to early adoption of the Champions for Change Reporting Framework to collect diversity data for New Zealand for the 1 April 2017 to 31 March 2018 reporting year. Although the framework specifically asks for age, ethnicity and gender data, subject to compliance with local laws, we will also look to use this as an opportunity to gather additional data over time that will enable us to have a more comprehensive view of our diversity globally.

As at 31 July 2017, the gender composition of the Board comprised 9 male Directors and 3 female Directors (2016: 11 male Directors and 2 female Directors). Of eight officers who reported directly to the Chief Executive at 31 July 2017, 6 were male and 2 were female (2016: 5 male and 3 female).

Ongoing Training

Following appointment to the Board, Directors undertake an induction programme to familiarise themselves with the Group. Areas covered include:

- business strategy and planning
- an overview of key financial metrics to monitor business performance
- an overview of material areas of the Fonterra business, including through meetings with key executives
- Fonterra's Constitution and other governance systems.

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Directors are expected to keep themselves abreast of changes and trends in the business and in Fonterra's environment and markets, and trends in the economic, political, social and legal climate generally. As a group, the Board holds several workshops on relevant subjects each year, and Directors are also expected to keep up to date with governance issues.

Assess Performance

Directors formally assess the performance of the Board each year. A regular programme of peer review of individual Directors also occurs as part of an ongoing Director development programme. The Shareholders' Council reviews the Board's Statement of Intentions against the performance and operation of the Group and reports on this to farmer shareholders annually. The Board is also responsible for reviewing the Chief Executive's performance.

Division of Roles

The Chairperson and Chief Executive roles at Fonterra are not exercised by the same individual.

Principle 3: Board Committees

Fonterra has a number of permanent Board Committees, as detailed in the table below. Additional Board Committees will be formed when it is efficient or necessary to facilitate efficient decision-making by providing for a sub-group of Directors to focus on particular areas or issues and to develop recommendations to the full Board.

The Board Committees have standard 'Terms of Reference' and each committee has a charter, which defines the scope and responsibilities of that committee and is approved by the Board annually. The minutes for each of the Board Committees' meetings are supplied to the Board for review.

COMMITTEE OR GROUP	MEMBERSHIP AS AT 31 JULY 2017		PURPOSE
Audit and Finance Committee	David Jackson (Chair and Independent) Ian Farrelly	Scott St John (Independent) Nicola Shadbolt Donna Smit	To assist the Board in fulfilling its governance responsibilities in relation to Fonterra's financial reporting, audit activities, treasury matters, financial risk management and internal control frameworks.
People, Culture and Safety Committee	John Wilson (Chair) Ashley Waugh John Monaghan Simon Israel (Independent)	Clinton Dines (Independent) David Jackson (observer)	To assist the Board in fulfilling its governance responsibilities in relation to the recruitment, retention, remuneration and development of Directors, executives and other employees, and to promote a safe and healthy working environment.
Co-operative Relations Committee	John Monaghan (Chair) David MacLeod Ian Farrelly	Leonie Guiney Ashley Waugh	To assist the Board in fulfilling its governance responsibilities in relation to the supply of milk from Fonterra suppliers, and to seek to resolve supplier complaints before reference to the Milk Commissioner.
Nominations Committee	David Jackson (Chair and Independent) Clinton Dines (Independent) Nicola Shadbolt	John Wilson Duncan Coull (SHC observer) Greg Kirkwood (SHC observer)	To recommend to the Board candidates for election as Farmer Directors.
Risk Committee	Nicola Shadbolt (Chair) David Jackson (Independent) David MacLeod	Leonie Guiney Clinton Dines (Independent)	To assist the Board in fulfilling its corporate governance responsibilities relating to Fonterra's management of key enterprise wide risks. This includes strategic and operational risks, through Fonterra's risk management framework, the behaviours required of its people and its guidelines, policies and processes for monitoring and mitigating enterprise-wide risks.

Board and Committee Attendance

	BOARD		AUDIT & FINANCE COMMITTEE		CO-OPERATIVE RELATIONS COMMITTEE		MILK PRICE PANEL		NOMINATIONS COMMITTEE		RISK COMMITTEE		PEOPLE, CULTURE & SAFETY COMMITTEE	
	Eligible to attend	Attendance	Eligible to attend	Attendance	Eligible to attend	Attendance	Eligible to attend	Attendance	Eligible to attend	Attendance	Eligible to attend	Attendance	Eligible to attend	Attendance
John Wilson	23	23	2	2	–	–	–	–	–	–	–	–	15	15
Malcolm Bailey	12	10	–	–	3	3	–	–	–	–	2	1	–	–
Clinton Dines	23	21	–	–	–	–	1	1	1	1	2	2	15	14
Ian Farrelly	21	21	5	5	2	1	–	–	–	–	–	–	8	8
Leonie Guiney	23	20	4	4	6	6	–	–	–	–	2	2	–	–
Simon Israel	23	16	–	–	–	–	–	–	–	–	–	–	15	15
David Jackson	23	22	6	6	–	–	7	7	1	1	4	4	15	15
David MacLeod	23	22	–	–	6	5	–	–	–	–	4	4	–	–
John Monaghan	23	22	–	–	6	6	–	–	1	1	–	–	15	14
Scott St John	14	14	5	5	–	–	5	5	–	–	–	–	–	–
Nicola Shadbolt	23	21	3	3	–	–	–	–	1	1	4	4	–	–
Donna Smit	11	11	3	3	–	–	–	–	–	–	–	–	–	–
Michael Spaans	14	10	3	2	3	2	2	2	–	–	–	–	–	–
John Waller	2	1	–	–	–	–	–	–	–	–	1	–	–	–
Ashley Waugh	23	22	3	3	6	5	5	4	–	–	–	–	6	6

Audit and Finance Committee

There is an established Audit and Finance Committee as described above.

The Audit and Finance Committee comprises two Appointed Directors and three Farmer Directors. The committee is chaired by David Jackson, who is an Independent Director and a Fellow of the New Zealand Institute of Chartered Accountants.

Employees attend Audit and Finance Committee meetings at the invitation of the Committee.

Takeover Offer

Given its co-operative structure and the thresholds on share ownership in the Constitution, the Board does not believe that it is necessary to establish protocols for a takeover offer.

Majority Independent Directors – Audit and Finance Committee, Nominations Committee and People, Culture and Safety Committee

The Audit and Finance Committee, Nominations Committee and People, Culture and Safety Committee committees do not comprise a majority of Independent Directors.

There is currently no 'headroom' for Fonterra, based on it having 12 Directors, to have more than 4 Independent Directors (as prescribed by the FSM Rules), as the Farmer Directors fill each of the 8 positions open to them (and as noted above, the Farmer Directors are not considered Independent Directors). Given this, it is very difficult for Fonterra to appoint a majority of Independent Directors to these committees without excluding Farmer Directors or significantly increasing the workload of the Independent Directors.

Fonterra does not consider that this is a significant issue, as both the Audit and Finance Committee and the Nominations Committee are chaired by Independent Directors, with the People, Culture and Safety Committee chaired by the Chair of the Board. In addition, under the FSM Rules, the Audit and Finance Committee is not required to comprise of a majority of Independent Directors.

Principle 4: Reporting and Disclosure

Disclosure Policy

Fonterra is committed to promoting a well-informed and efficient market in its shares, units issued by the Fonterra Shareholders' Fund and debt securities. The Board has approved a Group Disclosure Policy to ensure compliance with the FSM Rules regarding disclosure. The Group Disclosure Policy governs Fonterra's communications with investors and market participants, and the disclosure of information relevant to Fonterra.

Fonterra has established a Disclosure Committee that holds regular and ad hoc meetings to oversee Fonterra's continuous disclosure obligations. The members of the Disclosure Committee are the CEO, CFO, Managing Director Corporate Affairs, Director Capital Markets and the Company Secretary.

The Disclosure Committee has a Charter which states that the committee has responsibility for overseeing Fonterra's continuous disclosure obligations and reviewing, monitoring

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and implementing the Group Disclosure Policy. The Committee maintains a register of continuous disclosure matters and also ensures a consistent and high standard of communication with farmer shareholders, investors and market participants on a timely basis.

The Chairman of the Board, the Chairman of the Audit and Finance Committee and the Chairman of the Milk Price Panel attend the Committee's meetings to review and approve the release of the Interim and Annual Reports.

Fonterra and the Manager of the Fonterra Shareholders' Fund have entered into an arrangement to co-operate with each other and take all steps reasonably required to ensure that information to be disclosed by either of them under the FSM Rules and the listing rules of the NZX or the ASX (as the case may be) is disclosed simultaneously to the Fonterra Shareholders' Market, the NZX Main Board and the ASX. Fonterra simultaneously discloses relevant information on ASX on behalf of the Fonterra Shareholders Fund.

Website Disclosure

At present Fonterra has the following documents available on www.fonterra.com:

- Board Charter
- Co-operative Relations Committee Charter
- Risk Committee Charter
- Audit and Finance Committee Charter
- Environmental Policy
- Nominations Committee Charter
- People Culture and Safety Committee Charter
- The Way We Work (Code of Business Conduct)
- Group Disclosure Policy
- Group Ethical Behaviour Policy
- Group Securities Trading Policy
- Group Diversity and Inclusion Policy

Fonterra does not have a Director Remuneration Policy or a Management Remuneration Policy for the reasons noted under the heading 'Remuneration'.

Financial Reporting

The Audit and Finance Committee reviews the financial statements and recommends approval of the financial statements to the Board. The Committee considers whether the financial statements are complete, whether they reflect appropriate accounting policies, any major judgement areas, any legal matters that may significantly impact the financial statements and any complex transactions.

The CEO and CFO provide the Board with management representations that Fonterra's financial statements give a true and fair view, in all material respects, of Fonterra's financial position and financial performance for each financial reporting period.

Milk Price Panel

The Board has created the Milk Price Panel for the purpose of providing assurances as to the governance of the Farmgate Milk Price and the proper application of the Farmgate Milk Price Manual and the Milk Price Principles.

The Panel does not determine the Farmgate Milk Price, as this is a decision for the Board.

The Dairy Industry Restructuring Act 2001 (New Zealand) requires that the Chair and a majority of the members of the Panel (including the Chair) are independent. The Panel consists of two Appointed Directors, one Farmer Director and two appropriately qualified persons nominated by the Shareholders' Council, at least one of whom must be independent. The Chair must be one of the Appointed Director members. The Panel is currently chaired by Scott St John. Other Board members are David Jackson and Ashley Waugh. The Shareholders' Council appointees are Andrew Wallace and Bill Donaldson. The Board confirmed that at 31 July 2017, Scott St John, David Jackson and Andrew Wallace are considered to be Independent Members of this Panel.

Non-Financial Reporting

Fonterra is guided by international best practice and agrees that adoption of internationally recognised reporting frameworks is a good way of allowing users of our disclosure information to more easily compare it with others. For this reason we have adopted the Global Reporting Initiative (GRI) guidelines.

In this Annual Review, we provide coverage of both financial and non-financial matters. Non-financial reporting includes coverage of progress on strategy in the 'Our Potential' section. High-level consideration of material environmental, social and governance (ESG) factors and practices are included in the 'Sustainability and Social Responsibility' section.

Later this year we intend to issue our first separate Sustainability Report based upon GRI guidelines to further expand our non-financial disclosure for this financial year.

Principle 5: Remuneration

Director Remuneration

Fonterra's remuneration framework is designed to attract, retain and motivate high quality Directors and senior management.

The Constitution modifies the discretion of the Board to set remuneration of Directors. In accordance with the Constitution, farmer shareholders elect an independent committee of six farmer shareholders (the Directors' Remuneration Committee) to consider and make recommendations to the Annual Meeting on remuneration for Farmer Directors, which is approved by farmer shareholders.

The members of the Directors' Remuneration Committee as at 31 July 2017 were David Gasquoine (Chair), Murray Holdaway, Scott Montgomerie, Stephen Silcock, Philip Wilson and Gerard Wolvers.

The Board has full discretion over the remuneration of Appointed Directors with such remuneration not being approved at the Annual Meeting. The Board has historically remunerated

Appointed Directors at the same level as Farmer Directors in line with Directors' Remuneration Committee recommendations.

Given the arrangements outlined above, Fonterra does not have a specific policy for remuneration of Directors.

The details of the Directors' remuneration are contained on page 52 of the Annual Financial Results for the year ended 31 July 2017.

Management Remuneration

The People, Culture and Safety Committee governs the remuneration of management. There is no specific policy for management remuneration, but Fonterra has a framework which outlines relative weightings of remuneration components and relevant performance criteria.

Remuneration Framework

A well-designed remuneration framework helps the Co-operative attract and retain talent, and both motivates and recognises the role our people play in the success of the Co-operative.

Fonterra's remuneration framework for salaried staff is based on a 'total remuneration' approach, which is consistent with best practice globally. This includes fixed remuneration (salary), benefits (superannuation and insurance), and variable remuneration (incentives).

The amounts we pay to our employees are benchmarked against comparable companies in relevant markets, using information obtained from independent remuneration consultants. Adjustments to packages may occur on a cyclical basis, such as an annual salary review, or on an as-needed basis to recognise additional responsibilities.

The framework is designed to take into account budget targets and restraints, market conditions, internal equity, and governance factors such as local legislation, as well as taking into account individual performance.

Fonterra's incentive programmes are designed to drive the Co-operative's performance by:

- Focusing on the Co-operative's primary objective of maximising returns for its farmer shareholders;
- Promoting collaboration and a one team approach to achieve Fonterra's goals;
- Establishing targets which are challenging yet achievable; and linked to team (such as business unit) and group performance.

At the end of each financial year, performance is reviewed and incentive payments are approved by the People, Culture and Safety ("PCS") Committee at its discretion. The Committee retains absolute discretion in respect to payments for all incentive schemes.

Fixed Remuneration

Under our total remuneration approach for salaried positions, Fonterra aims to pay at the median rate in the markets in which we operate. Remuneration for employees who are on collective agreements is negotiated and agreed in partnership with Fonterra's employee representative organisations.

Fixed remuneration for salaried and waged employees who are not covered by a collective agreement is reviewed annually. Remuneration for employees on a collective agreement is reviewed in line with the schedules agreed with employee representative organisations.

Short Term Incentive Plans

The majority of permanent salaried employees in Fonterra participate in an annual short term incentive (STI) plan. In FY17 this incentive covered approximately 5,600 employees.

The STI plan encourages our people to focus on Fonterra's strategic objectives within each financial year. At the beginning of each financial year a series of Group and business unit key performance indicators (KPIs) are identified and approved by the Board's People, Culture and Safety ("PCS") Committee.

The KPIs are established every year, but normally include important financial measures (revenue and EBIT), capital efficiency (working capital), and measures centred on Safety and Quality.

Some employees eligible for the STI plan have a portion of their incentive aligned with their individual performance, and others are aligned fully to the relevant Group or business unit KPI scorecard.

Other Incentive Plans

Some business units, both in New Zealand and offshore, use sales incentive plans (SIP) for our market facing sales and support teams. These are targeted to achieve specific growth outcomes in key markets as well as aligning to our Group and business unit strategic objectives.

Employees in these plans do not, typically, participate in any other short term incentive plans.

Long Term Incentive Plans – Overview

Fonterra offers a Long Term Incentive (LTI) plan for certain senior executives. This plan is designed to reward and retain key senior executives based on longer-term objectives. The Fonterra Management Team (FMT) are eligible to participate, as well as a selected number of senior executives who lead large functions within our core business units, hold significant profit and loss responsibility, or head significant corporate functions.

Our LTI plan is based on achievement of specified long term outcomes for the Co-operative.

The nature of these Long Term Incentive plans means that payments are typically deferred over multiple time periods. This means that, in any given year, multiple payments may be made for incentives earned in prior years. For purposes of clarification, we have summarised the incentive plans that result in payments over multiple periods.

FY16 – Velocity Leadership Incentive

The LTI plan in place for FY16 and FY17 is our Velocity Leadership Incentive (VLI). The VLI was introduced in FY16

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as a targeted two-year plan to accelerate and reward the Fonterra business transformation, which the Co-operative refers to as 'Velocity'.

Velocity was designed to achieve significant improvement in business performance by re-setting our business. It encourages a focus on generating cash, operational efficiency and an owners' mindset to commercialise new ideas into additional revenue streams, faster than before.

Each of the first two years of Velocity required a significant step-change in every aspect of the Co-operative's business performance.

Organisation-wide business transformation goals were set and included specific delivery targets for FY16. During the course of the year, progress against these targets was monitored by the management team, and reported to the Board. All results were internally audited and validated.

The PCS Committee governs the VLI plan and approves all results and/or payments in respect of the VLI.

The business transformation in FY16 and FY17 delivered significant benefits across the Farmgate Milk Price, earnings and working capital. In FY17 it also supported a material uplift in Fonterra's organisational health and employee engagement. The FMT, selected senior management, and a small number of employees who led significant work streams in FY16 in support of Velocity were eligible to participate in the VLI.

The FY16 VLI was paid in cash with 70% paid following the end of FY16, and the remaining 30% deferred over two years in two payments of 15%.

On target performance under the FY16 VLI was set at 60% of fixed salary for the CEO and ranged from 25% to 50% of fixed salary for other participating employees.

In FY16, Velocity delivered significantly above expectations in terms of both financial performance arising from efficiency and value creation. This performance significantly exceeded global benchmarks for similar business transformations in our comparable industry and peer groups.

The Board retains overall discretion in relation to all aspects of the FY16 VLI.

FY17 Velocity Leadership Incentive

The FY17 VLI was the second year of the VLI programme, with certain changes. The payment schedule was changed to a 50% payment following the end of FY17, with the remaining 50% deferred over two years in two payments of 25%. The payment of the first deferral was dependent on achievement of a stipulated lift in organisational health* to recognise the importance of sustainable change.

On target performance under the FY17 VLI was set at 60% of fixed salary for the CEO and ranged from 25% to 50% of fixed salary for other participating employees.

The Board retains overall discretion in relation to all aspects of the FY17 VLI.

**Fonterra uses the McKinsey OHI measurement system to determine organisational health improvement (OHI), and Gallup Q12 to measure employee engagement. Both these surveys are globally benchmarked and well reputed in industry. Fonterra's FY17 OHI results are acknowledged to have demonstrated global best in class improvement over our FY16 performance.*

FY18–FY20 Long Term Incentive Overview

Fonterra has developed a new LTI plan for FY18 to FY20 and beyond to replace the VLI plan.

It marks a return to a more traditional LTI programme, as the Velocity programme moves into a sustained business focus. The new plan has been approved by the Board's PCS Committee. The FY18-FY20 LTI has been designed to incentivise the FMT and certain senior executives in relation to the achievement of the longer-term strategic objectives of the Co-operative.

This LTI uses two core financial metrics to measure achievement of the Co-operative's performance. The metrics are Return on Capital (ROC) and Earnings per Share (EPS), and are commonly used globally in long term incentive programmes. These metrics are important as they directly align to the Co-operative's performance, and therefore returns to its farmer shareholders, and are readily measurable.

The FY18-FY20 LTI targets for ROC and EPS have been set by reference to the FY20 business plan.

The FMT and selected senior executives are eligible to participate.

The Board retains overall discretion in relation to all aspects of the FY18-FY20 LTI.

Remuneration Changes for FY18

Given that the Velocity transformation activities from FY16-17 have been successful and the main elements of the transformation have been completed, Fonterra has adjusted the structure of our Short and Long Term Incentives.

The principle design features that have been applied in FY18 going forward are:

Link to long term outcomes for owners – our FY18-FY20 LTI program has been amended to focus on ROC and EPS. These measures are directly aligned to the performance of the Co-operative that flows through to our farmer owners, namely ROC and EPS. These outcomes sit alongside the achievement and delivery of a healthy and sustainable milk price.

Our short term incentive programmes now include a reward component that is based on the total farmer pay-out for a selected group of employees.

Safety and Quality incentives – Our approach in FY18 is to focus and measure on both actions we take, and the resultant outputs in respect of Safety and Quality. This approach is taken to ensure that we have a safe workplace and maintain the highest quality standards. Fonterra will therefore use both "lead" and "lag" measure to evaluate actions taken, and the outputs experienced, in respect of our Safety and Quality performance.

Benefits

As Fonterra operates a total remuneration approach, benefits are provided where required by legislation or where they represent typical market practice in that country or region.

Benchmarking

Fonterra adopts a "market median" positon on total compensation (base salary + short term + long term incentives).

For the CEO, FMT and certain senior roles, the pay benchmarking is conducted using independent third-party remuneration advisers appointed by the Board.

Given the Co-operative's size and global scale is unique to New Zealand, the peer group for these roles is comprised of 24 Australian listed companies that are more closely matched to the size and complexity and operational scope of Fonterra, allowing a more appropriate benchmarking of senior remuneration.

The benchmark also reflects that senior positions within Fonterra require global expertise, and are typically recruited from competitive global talent markets, particularly Australia and Asia.

For our wider employee population, benchmarking is conducted using independent third-party advisors as appropriate to the market in which our employees work. Currently, two principal advisory companies are used, selected based on their relative presence in these markets and global reach.

Chief Executive Officer – Total Remuneration FY17

The total remuneration of the Chief Executive Officer paid in FY17 was $8,320,406, made up as follows:

FY17		PAY FOR PERFORMANCE		TOTAL REMUNERATION
SALARY	BENEFITS[1]	STI[2]	LTI[3]	
$2,462,799	$170,036	$1,832,323	$3,855,248	$8,320,406

Notes and Explanations

1 Company Superannuation contribution

2 Payment of the FY16 STI in relation to performance in FY16

3 Total payments made in FY17 in relation to performance for:
FY16 VLI ($2,482,502)
FY16 VLI deferred payment ($664,956)
FY15 LTI deferred payment ($201,950)
FY14 LTI deferred payment ($505,840)

Principle 6: Risk Management

Risk Management Framework

Fonterra ensures its performance is optimised through the identification and management of the most material risks to the business. The Board Risk Committee has a broad mandate covering all aspects of risk and risk culture.

Fonterra's risk framework is based on the three lines of defence model with clear responsibilities for business risk management, enterprise risk oversight, building risk capability and risk assurance. Our risk management approach is aligned with international best practice and includes a consistent risk management process that:

- Considers our goals and relevant context
- Identifies any assumptions or uncertainties (risks) that could affect achieving our goals
- Prioritises control effort through assessing the potential consequences of a risk materialising, the likelihood of that occurrence
- Considers risk drivers
- Evaluates current controls, their effectiveness and outcome acceptability
- Introduces new controls or action plans to strengthen our position
- Regularly reviews control effectiveness, context changes and resulting exposure.

Fonterra's risk management policy is supported by a risk management standard that outlines our risk principles, accountabilities and the requirements for managing and reporting risk within the business. At the highest level, the most material risks to the business are grouped to reflect our focus on people, identity and strategy.

In the Sustainability and Social Responsibility section, we provide more detailed information on our risk management approach for Health and Safety, Food Safety and Quality, Environmental and Animal welfare risks.

These are reviewed regularly to consider any changes or need to adapt control strategies, and are reported to and reviewed by the Board Risk Committee at each meeting. We aim to deepen the understanding, management and reporting of key business risks through the roll out of a risk management technical product as part of programmed work. Increasingly we are reporting on emerging risk as part of our approach to strengthening organisational resilience.

Health and Safety

Fonterra seeks to provide a safe and healthy work environment to anyone who is affected by our operations. Continuous health and safety improvement is an integral part of everything we do. Achieving effective health and safety improvement is regarded as essential to our long-term success and an integral part of our corporate values and how we run our business. We have focussed programmes to address our critical risks and our injury reduction ambitions.

Fonterra's health and safety performance is measured using a number of reactive and preventive indicators. These include Total Recordable Injury Frequency Rate (TRIFR), number of serious harm injuries and status of self assurance and internal control Audits conducted throughout the business.

We have made a 19 per cent improvement to TRIFR compared to our performance in 2016 and we have achieved 19 per cent fewer serious harms in FY17 overall compared to FY16.

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We remain optimistic of achieving our longer term TRIFR goal of five which represents world class within our industry group.

Our focus is to continue to track our efforts on a broad range of health and wellbeing programmes to enhance our people care and actively prevent incidents from occurring.

Principle 7: Auditors

Auditor Framework

One of the roles of the Audit and Finance Committee is responsibility for making recommendations to the Board regarding the appointment of the external auditor. The auditor is appointed by the shareholders at the Annual Meeting.

The Audit and Finance Committee reviews the independence of the auditor and reviews the external audit fees, the terms of engagement and annual audit plan.

Fonterra encourages the rotation of the lead external audit partner in the relationship in accordance with best practice. Fonterra has a Group Audit Independence Policy, for certain activities the auditor may undertake for the Group. This policy is prescriptive as to the types of activities that the auditor may undertake, those the auditor may only undertake with the approval of the Audit and Finance Committee, and the types of activities that are not permitted. The Audit and Finance Committee will not approve the auditor performing any tasks that have the potential to create a conflict except in exceptional circumstances and then only if appropriate safeguards are in place. The Audit and Finance Committee monitor the performance of these additional activities undertaken by the auditor.

The Audit and Finance Committee Chairman communicates regularly with the external auditor and the Audit and Finance Committee meet with the external auditor without Management at least twice a year.

The Audit and Finance Committee is responsible for ensuring that the ability of the auditors to carry out their statutory audit role is not impaired, or could reasonably be perceived to be impaired.

The fees paid to Fonterra's auditor, PricewaterhouseCoopers are detailed in Note 4 to the Annual Financial Results for the year ended 31 July 2017.

Annual Meeting

The external auditor is required to attend Fonterra's Annual Meeting and be available to answer questions from shareholders in relation to the audit.

Internal Audit

Fonterra's Internal Audit function provides the Audit and Finance Committee and Management with objective and independent assurances on the design and effectiveness of internal controls.

Management through the CEO and CFO strongly support the need for Internal Audit. A close working relationship with Management is critical to ensure Internal Audit remains relevant and provides adequate audit coverage.

Internal Audit supports the achievement of Fonterra's Group business objectives by:

- Evaluating the effectiveness of risk management, controls and governance processes
- Delivering reasonable assurance over key business risks to the Audit and Finance Committee and Management
- Providing recommendations for control environment improvements
- Executing assignments in compliance with Institute of Internal Audit Standards

The approach to internal audit is based on the principle of line management responsibility for risk and controls.

- Management is responsible for implementing, operating and monitoring the system of internal controls to provide reasonable assurance of achieving business objectives.
- Internal Audit is responsible for:
  - Delivering a reasonable degree of assurance (as determined by the Audit and Finance Committee) over business risk
  - Assisting the business with special reviews or investigations where requested and approved by the Audit and Finance Committee
  - Complying with the Internal Audit methodology.

Principle 8: Shareholder Rights and Relations

Website

Fonterra has a website (www.fonterra.com) where investors and interested stakeholders can access financial and operational information and key corporate governance information about the issuer.

Shareholders' Council

One of the Board's most important relationships is with the Shareholders' Council. The Council, Fonterra's representative body, which is established under the Fonterra Constitution, is independent of the Board and as at 31 July 2017 comprised 35 farmer shareholders elected as councillors, representing 35 wards across New Zealand. However, with effect from the 2017 Annual Meeting the number of wards will be reduced to 25. The Shareholders' Council was created to be the guardian of the Co-operative Principles which apply to the cornerstone activities of the Co-operative. The functions of the Council are set out in the Constitution. The Council reviews the Board's Statement of Intentions for the performance and operations of the Group and publishes an annual report, commenting on these matters.

The Council, Board and Management have a working interface document which sets out the principles to facilitate the working partnership between the Board, the Council and Management and the way operational issues will be dealt with by the Board and the Council.

The working interface document is available on the Farm Source website.

The Council and the Board meet regularly, as do the Chairs of the Board and the Council and the Chairs of their respective Committees.

Farmer Communications

Fonterra is committed to maintaining and improving communication with its farmer shareholder base to ensure that the objectives of both the Group and farmer shareholders are understood. An extensive farmer shareholder and supplier relations programme is managed by the Chief Operating Officer, Farm Source. Channels for electronic communication are provided through the fonterra.com and Farm Source™ websites and the My Co-op phone application. In addition, Fonterra provides farmer shareholders with the ability to receive communications (such as the Annual Report) from Fonterra electronically.

Fonterra's communications with farmer shareholders include regular face-to-face meetings, Sky broadcasts, a regular Global Dairy Update, Farm Source™ magazine publication, My Co-op posts and regular emails from the Chairman and Regional Heads. As described above, Fonterra releases to the relevant stock exchanges all material information, and will comply with the listing rules of the Fonterra Shareholders' Market with respect to shareholder communications.

Farmer Meetings

A schedule of regular meetings with farmer shareholders, sharemilkers and farm workers is held across the country at least twice each year. Often these are run in conjunction with the Shareholders' Council and Farm Source™ regional teams.

Farmer Directors also regularly attend other farmer meetings during the year on specific topics.

In addition, the Board consults with farmer shareholders on specific issues as they arise.

Fonterra.com and Farm Source™ Digital Tools

Presentations on the development of the business are available on the fonterra.com website. The Group also uses email alerts, including regular updates from the Chairman and regular farmer shareholder updates.

The Farm Source™ website enables farmer shareholders, their employees and business partners to transact online with Fonterra and access information and tools on milk production and quality, online statements and up-to-the-minute news and weather. This site is also used to provide information on the business to farmer shareholders.

Fonterra's My Co-op provides constantly updated news and information from across the Co-op and the industry including milk price announcements, updates from the Chairman and CEO and rural and regional council news. The On Farm app provides daily milk production and quality information, comparisons against last season volumes, tanker ETA, and summary reports of key milk performance information for the last 30 days.

Annual Meeting

The Board views the Annual Meeting of farmer shareholders, which is held at a different venue around New Zealand each year, as an opportunity to communicate directly with farmer shareholders and also ensures that adequate time is provided at these meetings for farmer shareholders to raise issues or ask questions from the floor.

Notices of Meetings are sent to farmer shareholders at least 10 working days before the meeting.

The Constitution describes the process whereby a farmer shareholder can raise a proposal for discussion or resolution at the next meeting of farmer shareholders at which the farmer shareholder is entitled to vote.

Annual Report

The Group's Annual Report including financial statements and an annual review, together with the half-year reports and other material announcements, are designed to present a balanced and clear view of Fonterra's activities and prospects and are available on fonterra.com.

Other Disclosures

Information on the Group's performance, annual and half-year financial results, Director changes, and other significant matters, is advised to the market through the NZX and ASX in accordance with the Group Disclosure Policy. Farmer shareholders and other stakeholders receive regular updates on these and other issues relevant to them and all media and market releases are available on fonterra.com.

Voting

Shareholders have the right to vote on major transactions (as defined in the Companies Act 1993) as well as other major decisions that may change the nature of Fonterra as prescribed by the listing rules of the FSM. In particular, FSM Rule 8.1.1 restricts Fonterra from entering into any transaction (or series of linked or related transactions) which would change the essential nature of the business of Fonterra or in respect of which the gross value is in excess of 50% of the average market capitalisation of Fonterra without the prior approval of Fonterra's shareholders.

In accordance with the co-operative nature of Fonterra, voting is based on the quantity of milk solids supplied to Fonterra, backed by shares and is not on the principle of one vote per share.

BOARD OF **DIRECTORS**

1. **JOHN WILSON**
2. **CLINTON DINES**
3. **IAN FARRELLY**
4. **LEONIE GUINEY**
5. **SIMON ISRAEL**
6. **DAVID JACKSON**
7. **DAVID MACLEOD**
8. **JOHN MONAGHAN**
9. **NICOLA SHADBOLT**
10. **DONNA SMIT**
11. **SCOTT ST JOHN**
12. **ASHLEY WAUGH**

1. JOHN WILSON

BOARD RESPONSIBILITIES *Chairman, and Chair of the People, Culture and Safety Committee*

TERM OF OFFICE *Elected 2003, last re-elected 2015*

John Wilson was elected to the Fonterra Board in 2003 and became Chairman in 2012. Previously he served as the inaugural Chairman of the Fonterra Shareholders' Council. John is a director of Turners & Growers Limited and he serves on the Executive Board of the New Zealand China Council. He is a chartered member of the Institute of Directors in New Zealand. John lives on his dairy farm near Te Awamutu and jointly owns a dairy farming business based near Geraldine, South Canterbury.

B.Agr.Sc

2. CLINTON DINES

BOARD RESPONSIBILITIES *Appointed Director, Member of the People, Culture and Safety Committee and Board Risk Committee*

TERM OF OFFICE *Appointed 2015*

Clinton was appointed to the Fonterra Board in 2015. Clinton lived and worked in China for 36 years, 21 of which as President of BHP Billiton's China business. He has extensive experience as an executive in businesses in China and Asia and has had an active career as a Non-Executive Director, currently serving on the Boards of North Queensland Airports and Zanaga Iron Ore. He was Executive Chairman of Caledonia Asia from 2010 to 2013, a venture investment group in Asia, and is a Partner in Moreton Bay Partners, a strategic advisory firm based in Brisbane. He is an Adjunct Professor at Griffith University's Asia Institute and is a Member of the Griffith University Council.

BA (Modern Asian Studies, Griffith), CIM, INSEAD

3. IAN FARRELLY

BOARD RESPONSIBILITIES *Farmer-elected Director, Member of the Audit and Finance Committee and the Co-operative Relations Committee*

TERM OF OFFICE *Elected 2007, last re-elected 2013, retired November 2016, appointed January 2017*

Ian Farrelly was elected to the Fonterra Board in 2007. Ian had a 20-year career in the banking industry including 15 years as head of ASB's Rural Division. Ian serves on the Board of First Mortgage Managers Limited, Spectrum Dairies Limited, Fortuna Group Limited and Waikato Stud. He owns and runs a 500-hectare 10,000 animal calf rearing farm in Te Awamutu and has ownership interests in dairy farms in Canterbury and the Waikato.

B.Agr

4. LEONIE GUINEY

BOARD RESPONSIBILITIES *Farmer-elected Director, Member of the Board Risk Committee and the Co-operative Relations Committee*

TERM OF OFFICE *Elected 2014*

Leonie Guiney was elected to the Fonterra Board in 2014. Leonie has worked in the agriculture sector for 25 years in a number of positions including lecturer of Dairy Production at Lincoln University, consultant on the BNZ Growth Programme for farmers and has held roles with Golden Vale Dairy Co-operative in Ireland, LIC and FarmRight South Island. Leonie was the 2014 winner of the low input NZ Dairy Business of the Year and the 2006 Canterbury Sharemilker of the Year. Leonie began farming in Canterbury in 2002 and she is now a director and shareholder of five Canterbury farms and Bobby Square Limited.

B.Agr.Sc

5. SIMON ISRAEL

BOARD RESPONSIBILITIES *Appointed Director, Member of the People, Culture and Safety Committee*

TERM OF OFFICE *Appointed 2013*

Simon Israel was appointed to the Fonterra Board in 2013. Simon currently chairs Singapore Telecommunications Limited and Singapore Post Limited and is a member of the Westpac Asia Advisory Board. He was an Executive Director of Temasek Holdings for six years and President from 2010 to 2011. Simon was a director of Fraser & Neave, Neptune Orient Lines, Asia Pacific Breweries, Griffin Foods, CapitaLand and Frucor Beverage Group. He had ten years' experience in the dairy industry with Danone as a Senior Vice President and member of the Group Executive Committee. He was conferred Knight in the Legion of Honour by the French Government in 2007.

Diploma of Business Studies

6. DAVID JACKSON

BOARD RESPONSIBILITIES *Appointed Director, Chair of the Audit and Finance Committee and Nominations Committee, Member of the Board Risk Committee and Milk Price Panel, Observer of the People, Culture and Safety Committee*

TERM OF OFFICE *Appointed 2007*

David Jackson was appointed to the Fonterra Board in 2007. David is Chair of Tegel Group Holdings Limited and also serves on the board of Mitre 10 (New Zealand) Limited. He was previously Chairman of The New Zealand Refining Company Limited and served on the board of Nuplex Industries Limited. David spent more than 30 years with accounting firm Ernst & Young in a variety of roles, and served as Chairman of the board of management for the firm in New Zealand from 1999 to 2002.

M.Com(Hons), FCA, FInstD

7. DAVID MACLEOD

BOARD RESPONSIBILITIES *Farmer-elected Director, Member of the Co-operative Relations Committee and the Board Risk Committee*

TERM OF OFFICE *Elected 2011, last re-elected 2014*

David MacLeod was elected to the Fonterra Board in 2011. David also serves on the boards of Port Taranaki Limited, Predator Free 2050 Limited, Matau Technologies Limited and A.J. Greaves Electrical Limited. He is Chairman of the Taranaki Regional Council. David lives near Hawera in South Taranaki and is a director of P.K.W. Farms GP Limited, one of Fonterra's largest shareholders. He is a shareholder of Far South Farms Limited, which owns a dairy farm in Southland.

8. JOHN MONAGHAN

BOARD RESPONSIBILITIES *Farmer-elected Director, Chair of the Co-operative Relations Committee Chair of the Milk Supply Working Group and Member of the People, Culture and Safety Committee*

TERM OF OFFICE *Elected 2008, last re-elected 2014*

John Monaghan was elected to the Fonterra Board in 2008. Prior to joining the Fonterra Board John was Chairman of the Fonterra Shareholders' Council and the inaugural Chair of the Governance Development Programme.. He is also a director of Centre Port Limited and Centre Port Properties Limited. He holds a number of farming directorships and is a trustee of the Wairarapa Irrigation Trust. John has dairy farming interests in the Wairarapa and Otago regions.

9. NICOLA SHADBOLT

BOARD RESPONSIBILITIES *Farmer-elected Director, Chair of the Risk Committee, Member of the Audit and Finance Committee and Nominations Committee*

TERM OF OFFICE *Elected 2009, last re-elected 2015*

Nicola Shadbolt was elected to the Fonterra Board in 2009. Nicola is a Professor of Farm and Agribusiness Management at Massey University, serves on the Board of the Manager of the Fonterra Shareholders' Fund and represents New Zealand in the International Farm Comparison Network in Dairying. Nicola and her husband live in the Pohangina Valley in the Manawatu, which is the base for the five farming and forestry equity partnerships they run, which include two dairy farms.

B.Sc(Hons), M.AgrSc(Hons), DipBusStud (Accountancy), FNZIPIM (Reg), FAICD

10. DONNA SMIT

BOARD RESPONSIBILITIES *Farmer-elected Director, Member of the Audit and Finance Committee*

TERM OF OFFICE *Elected 2016*

Donna Smit was elected to the Fonterra board in December 2016. Donna lives and farms at Edgecumbe, and has built and owns seven dairy farms in Eastern Bay of Plenty and Oamaru. Donna is a Director of Ballance Agri Nutrients and Kiwifruit Equities Limited and a Trustee of Taratahi Agricultural Training Centre (Wairarapa) Trust Board and a Trustee of the Dairy Women's Network. Donna is a Chartered Accountant and was a company administrator at kiwifruit Co-operative EastPack for 24 years.

CA

11. SCOTT ST JOHN

BOARD RESPONSIBILITIES *Appointed Director, Chair of the Milk Price Panel and Member of the Audit and Finance Committee*

TERM OF OFFICE *Elected 2016*

Scott St John was appointed to the Fonterra Board in 2016 and serves on the Board of the Manager of the Fonterra Shareholders' Fund. He was the CEO of First NZ Capital (FNZC) for 15 years, stepping down from that role in early 2017. He is now a Non-Executive Director of the FNZC Board, and chairs its Audit and Risk Committee. Scott has served on the Council of the University of Auckland since 2009 and was appointed Chancellor in 2017. He is a director of Fisher and Paykel Healthcare and chairs that Board's Audit and Risk Committee, and was recently appointed to the Board of Mercury NZ Limited. He is also Director of NEXT Foundation. Previous roles have included Chairman of the Securities Industries Association, and membership of both the Capital Markets Development Taskforce, and the Financial Markets Authority Establishment Board.

B.Com, Diploma of Business

12. ASHLEY WAUGH

BOARD RESPONSIBILITIES *Farmer-elected Director, Member of the People Culture and Safety Committee, the Co-operative Relations Committee and Milk Price Panel*

TERM OF OFFICE *Elected 2015*

Ashley Waugh was elected in 2015. Ashley is Chairman of Moa Brewing Company Limited and serves on the Board of Seeka Limited and the Colonial Motor Company Limited. Ashley spent 10 years with The New Zealand Dairy Board followed by eight years with National Foods in Australia including the last four years as Chief Executive Officer. Ashley lives on his dairy farm near Te Awamutu and has shareholding interests in Puke Roha Limited in Pokuru.

BBS

FONTERRA **MANAGEMENT TEAM**

1. **THEO SPIERINGS**
2. **PAUL WASHER**
3. **LUKAS PARAVICINI**
4. **MILES HURRELL**
5. **ROBERT SPURWAY**
6. **JUDITH SWALES**
7. **KELVIN WICKHAM**

1. THEO SPIERINGS

Chief Executive Officer

Theo Spierings sets Fonterra's overall direction and leads the Fonterra Management Team. He is focused on building on Fonterra's strengths and securing future growth for the Co-operative. Theo joined Fonterra in 2011, bringing with him extensive experience from across the dairy industry, particularly in Asia, Latin America, Africa, the Middle East and Europe. Theo has over 30 years' experience in the global dairy industry in a variety of roles including general management, operations and supply chain, and sales and marketing positions. He was previously the acting CEO of Royal Friesland Foods, a Dutch dairy co-operative which, in 2008, he led through a merger with Campina. Before taking up his leadership role at Fonterra, Theo ran his own company in the Netherlands focusing on corporate strategy, and mergers and acquisitions, in fast-moving consumer goods (FMCG). Theo holds a Bachelor of Arts in Food Technology/Biotechnology and a Master of Business Administration.

2. PAUL WASHER

Acting Chief Financial Officer

Paul joined Fonterra in 2003. Prior to his current role he held a number of senior roles across the business including Director of Financial Performance and Planning, Commercial Manager of Global Sales and Marketing, and Commercial Manager of Optimisation.

Paul has been appointed to the role of Vice President, Commercial for Greater China, effective from 1st February 2018 and leads the office of the Chief Financial Officer (oCFO) in an interim capacity until this date. Paul has more than 25 years' experience in the functional areas of sales, planning and performance, treasury, IT and tax. Paul holds a Masters of Business Administration from the University of Otago, is a Chartered Accountant and a member of the New Zealand Institute of Directors.

3. LUKAS PARAVICINI

Chief Operating Officer, Global Consumer and Foodservice

Lukas Paravicini heads Fonterra's Global Consumer & Foodservice business whose 11,000 people are committed to bringing dairy nutrition to 80 countries across the world. He first joined Fonterra as CFO in 2013 after a long career with Nestlé where he held a number of senior positions including: General Manager for Nestlé Professional Europe, CFO of Nestlé Brazil, Vice President of Global Business Services and CFO of Nestlé Professional, and Nestlé's globally managed Out-of-Home business. Lukas' extensive experience in dairy provides him with an in-depth understanding of how dairy can deliver people's needs for delicious nutritious food. He has lived and worked in some of Fonterra's most strategically important markets. He holds a Business and Administration degree from the University of Zurich, Switzerland, and speaks five languages.

4. MILES HURRELL

Chief Operating Officer, Farm Source

Miles Hurrell heads Fonterra's global co-operative farming strategy which includes farmer services and engagement, milk sourcing and the chain of 71 Farm Source™ rural retail stores throughout New Zealand. Miles' 17 years' experience in the dairy industry has spanned four continents. In his previous role as General Manager Middle East, Africa and CIS he led a period of sustained growth during a time of political unrest across the region. He reset the African sales strategy and was a director of Fonterra's joint venture with Africa's largest dairy company, Clover Industries Limited. From 2006 to 2008 Miles oversaw the streamlining of the Co-operative's European operations before moving to the United States to establish new offshore partnerships. Miles has completed management programmes at INSEAD (International Executive Development), London Business School (Finance) and Kellogg's North Western University (Global Sales).

5. ROBERT SPURWAY

Chief Operating Officer, Global Operations

Robert Spurway joined Fonterra in 2011. As Chief Operating Officer, Global Operations, Robert leads Fonterra's global operations business and is responsible for the Co-operative's manufacturing and supply chain operations in New Zealand and around the world. In his previous role he was responsible for overseeing milk collection, manufacturing and logistics for the Co-operative's New Zealand milk supply. Prior to that, he was Fonterra's South Island Regional Operations Manager. In this role, he oversaw the greenfield development of the Co-operative's Darfield site. Robert has more than 20 years' experience in the food and dairy industries. After managing the Northland Dairy Company's Dargaville site, he moved to Australia in 1999, where he held various roles in Goodman Fielder Australia. From 2008 to 2011, Robert led two Australian food companies before returning to New Zealand. Robert holds a Bachelor of Engineering (Chemical and Materials).

6. JUDITH SWALES

Chief Operating Officer, Velocity and Innovation

Judith Swales has been with Fonterra since 2013 and was appointed Chief Operating Officer Velocity and Innovation in June 2016. She is responsible for driving efficiency across the Co-operative, bringing increased commercial focus to Fonterra's research, development and technology, and taking a strategic view on developing game changing business models. Prior to this appointment, Judith was the Managing Director of Fonterra Oceania, leading the successful turnaround of the Australian business and overseeing Fonterra Brands New Zealand.

She has extensive experience in senior management and business turnarounds, and prior to joining Fonterra, Judith was the Managing Director of Heinz Australia and CEO and Managing Director of Goodyear Dunlop, Australia and New Zealand. Before coming to Australia in 2001, Judith worked for a number of UK retailers which culminated in her move to Australia as the Managing Director of Angus and Robertson. She has served as a Non-Executive Director on the DuluxGroup Board since April 2011 and has a degree in microbiology and virology.

7. KELVIN WICKHAM

Chief Operating Officer, NZMP

Kelvin Wickham leads the sales and marketing of all Fonterra ingredients globally, delivering solutions to our global customers, ensuring optimisation of supply and demand, commodity price risk management, and championing the NZMP™ brand. Kelvin has more than 27 years' experience in the dairy industry and has played a key role in building markets, customer relationships and partnerships. His previous role of President Greater China and India focused on directing the development of Fonterra's business in these expanding markets, during which he oversaw a period of rapid growth. Prior to that, Kelvin led Fonterra's Supplier and External Relations team, and was Managing Director of Fonterra's Global Trade overseeing the launch of GlobalDairyTrade. From 2005 to 2007 he was the Director of Sales and Operations Planning. Kelvin holds a chemical and materials engineering degree, a Master of Management and a Diploma of Dairy Science and Technology.

SUMMARY **FINANCIAL STATEMENTS**

For the year ended 31 July 2017

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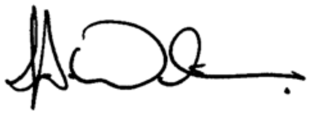
DIRECTORS' STATEMENT

FOR THE YEAR ENDED 31 JULY 2017

The Directors hereby approve and authorise for issue the summary financial statements for the year ended 31 July 2017 presented on pages 84 to 99. For and on behalf of the Board:



JOHN WILSON
CHAIRMAN
23 September 2017

DAVID JACKSON
DIRECTOR
23 September 2017

Fonterra Co-operative Group Limited (Fonterra or the Co-operative) is a co-operative company incorporated and domiciled in New Zealand. Fonterra is registered under the Companies Act 1993 and the Co-operative Companies Act 1996, and is an FMC Reporting Entity under the Financial Markets Conduct Act 2013. Fonterra is also required to comply with the Dairy Industry Restructuring Act 2001.

These summary financial statements comprise Fonterra and its subsidiaries (together referred to as the Group) and include the Group's interest in its equity accounted investees after adjustments to align to the accounting policies of the Group. They have been prepared in accordance with Financial Reporting Standard No. 43: Summary Financial Statements and have been extracted from the Group's full financial statements. The Group's full financial statements comply with International Financial Reporting Standards. They also comply with New Zealand Equivalents to International Financial Reporting Standards and have been prepared in accordance with Generally Accepted Accounting Practice applicable to for-profit entities.

The Board has elected to present summary financial statements for the year ended 31 July 2017 as part of the Annual Review sent to Shareholders. These summary financial statements include notes setting out key information.

These summary financial statements are presented for the year ended 31 July 2017. The comparative information is for the year ended 31 July 2016. These summary financial statements of the Group have been prepared using the same accounting policies and measurement basis as the Group's full financial statements for the year ended 31 July 2017.

The full financial statements for the year ended 31 July 2017, approved and authorised for issue by the Board on 23 September 2017, have been audited by PricewaterhouseCoopers and given an unqualified opinion.

The Group is primarily involved in the collection, manufacture and sale of milk and milk-derived products and in fast-moving consumer goods and foodservice businesses. These summary financial statements are presented in New Zealand Dollars ($ or NZD), which is Fonterra's functional and presentation currency, and rounded to the nearest million, except where otherwise stated.

The summary financial statements cannot be expected to provide as complete an understanding of the financial affairs of the Group as the full financial statements, which are available from Fonterra's registered office at 109 Fanshawe Street, Auckland, New Zealand or on Fonterra's website, www.fonterra.com.

INCOME STATEMENT

FOR THE YEAR ENDED 31 JULY 2017

		GROUP $ MILLION	
	NOTES	31 JULY 2017	31 JULY 2016
Revenue from sale of goods		19,232	17,199
Cost of goods sold	2	(15,968)	(13,567)
Gross profit		3,264	3,632
Other operating income		190	266
Selling and marketing expenses		(641)	(703)
Distribution expenses		(550)	(585)
Administrative expenses		(810)	(844)
Other operating expenses		(369)	(396)
Net foreign exchange gains		29	7
Share of profit of equity accounted investees		7	54
Profit before net finance costs and tax		1,120	1,431
Finance income		34	18
Finance costs		(389)	(517)
Net finance costs		(355)	(499)
Profit before tax		765	932
Tax expense	9	(20)	(98)
Profit after tax		745	834
Profit after tax is attributable to:			
Equity holders of the Co-operative		734	810
Non-controlling interests		11	24
Profit after tax		745	834

	GROUP $	
	31 JULY 2017	31 JULY 2016
Earnings per share:		
Basic and diluted earnings per share	0.46	0.51

The accompanying notes form part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 JULY 2017

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Profit after tax	**745**	834
Items that may be reclassified subsequently to profit or loss:		
Cash flow hedges and other costs of hedging, net of tax	**128**	601
Net investment hedges and translation of foreign operations, net of tax	**(124)**	(318)
Hyperinflation losses attributable to equity holders	**(1)**	(16)
Share of equity accounted investees' movements in reserves	**–**	5
Other reserve movements	**(2)**	5
Total items that may be reclassified subsequently to profit or loss	**1**	277
Items that will not be reclassified subsequently to profit or loss:		
Net fair value gains on investments in shares	**2**	–
Foreign currency translation losses attributable to non-controlling interests	**(3)**	(84)
Hyperinflation movements attributable to non-controlling interests	**–**	(10)
Non-controlling interest other movements	**(2)**	–
Total items that will not be reclassified subsequently to profit or loss	**(3)**	(94)
Total other comprehensive (expense)/income recognised directly in equity	**(2)**	183
Total comprehensive income	**743**	1,017
Total comprehensive income is attributable to:		
Equity holders of the Co-operative	**737**	1,087
Non-controlling interests	**6**	(70)
Total comprehensive income	**743**	1,017

The accompanying notes form part of these summary financial statements.

STATEMENT OF FINANCIAL POSITION

AS AT 31 JULY 2017

		GROUP $ MILLION	
	NOTES	**31 JULY 2017**	31 JULY 2016
ASSETS			
Current assets			
Cash and cash equivalents		**393**	369
Trade and other receivables		**2,303**	1,625
Inventories		**2,593**	2,401
Tax receivable		**32**	13
Derivative financial instruments		**580**	451
Assets held for sale		**–**	87
Other current assets		**181**	145
Total current assets		**6,082**	5,091
Non-current assets			
Property, plant and equipment		**6,391**	6,172
Equity accounted investments		**887**	960
Livestock		**319**	342
Intangible assets		**3,115**	3,142
Deferred tax assets		**363**	410
Derivative financial instruments		**239**	417
Other non-current assets		**446**	584
Total non-current assets		**11,760**	12,027
Total assets		**17,842**	17,118
LIABILITIES			
Current liabilities			
Bank overdraft		**11**	12
Borrowings`	5	**1,112**	955
Trade and other payables		**2,117**	2,169
Owing to suppliers	6	**1,330**	719
Tax payable		**34**	18
Derivative financial instruments		**43**	43
Provisions		**40**	47
Other current liabilities		**44**	35
Total current liabilities		**4,731**	3,998
Non-current liabilities			
Borrowings	5	**5,151**	5,397
Derivative financial instruments		**547**	569
Provisions		**148**	152
Deferred tax liabilities		**9**	44
Other non-current liabilities		**8**	11
Total non-current liabilities		**5,863**	6,173
Total liabilities		**10,594**	10,171
Net assets		**7,248**	6,947
EQUITY			
Subscribed equity		**5,858**	5,833
Retained earnings		**1,637**	1,384
Foreign currency translation reserve		**(552)**	(428)
Hedge reserves		**192**	64
Other reserves		**5**	6
Total equity attributable to equity holders of the Co-operative		**7,140**	6,859
Non-controlling interests		**108**	88
Total equity		**7,248**	6,947

The accompanying notes form part of these summary financial statements.

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 JULY 2017

GROUP $ MILLION	ATTRIBUTABLE TO EQUITY HOLDERS OF THE CO-OPERATIVE							
	SUBSCRIBED EQUITY	RETAINED EARNINGS	FOREIGN CURRENCY TRANSLATION RESERVE	HEDGE RESERVES	OTHER RESERVES	TOTAL	NON-CONTROLLING INTERESTS	TOTAL EQUITY
As at 1 August 2016	**5,833**	**1,384**	**(428)**	**64**	**6**	**6,859**	**88**	**6,947**
Profit after tax	**–**	**734**	**–**	**–**	**–**	**734**	**11**	**745**
Other comprehensive income/(expense)	**–**	**–**	**(124)**	**128**	**(1)**	**3**	**(5)**	**(2)**
Total comprehensive income/(expense)	**–**	**734**	**(124)**	**128**	**(1)**	**737**	**6**	**743**
Transactions with equity holders in their capacity as equity holders:								
Dividend paid to equity holders of the Co-operative	**–**	**(481)**	**–**	**–**	**–**	**(481)**	**–**	**(481)**
Equity instruments issued	**25**	**–**	**–**	**–**	**–**	**25**	**42**	**67**
Dividend paid to non-controlling interests	**–**	**–**	**–**	**–**	**–**	**–**	**(28)**	**(28)**
As at 31 July 2017	**5,858**	**1,637**	**(552)**	**192**	**5**	**7,140**	**108**	**7,248**
As at 1 August 2015	5,814	1,289	(110)	(537)	17	6,473	186	6,659
Profit after tax	–	810	–	–	–	810	24	834
Other comprehensive income/(expense)	–	5	(318)	601	(11)	277	(94)	183
Total comprehensive income/(expense)	–	815	(318)	601	(11)	1,087	(70)	1,017
Transactions with equity holders in their capacity as equity holders:								
Dividend paid to equity holders of the Co-operative	–	(720)	–	–	–	(720)	–	(720)
Equity instruments issued	19	–	–	–	–	19	–	19
Dividend paid to non-controlling interests	–	–	–	–	–	–	(28)	(28)
As at 31 July 2016	5,833	1,384	(428)	64	6	6,859	88	6,947

The accompanying notes form part of these summary financial statements.

CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 JULY 2017

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Cash flows from operating activities		
Profit before net finance costs and tax	**1,120**	1,431
Adjustments for:		
Foreign exchange gains	**(1)**	(365)
Depreciation and amortisation	**526**	570
Other	**15**	(44)
	540	161
Decrease/(increase) in working capital:		
Inventories	**(177)**	597
Trade and other receivables	**(634)**	485
Amounts owing to suppliers	**745**	560
Payables and accruals	**(100)**	171
Other movements	**(48)**	(42)
Total	**(214)**	1,771
Cash generated from operations	**1,446**	3,363
Net taxes paid	**(70)**	(85)
Net cash flows from operating activities	**1,376**	3,278
Cash flows from investing activities		
Cash was provided from:		
– Proceeds from sale of business operations	**–**	230
– Proceeds from disposal of property, plant and equipment	**105**	26
– Proceeds from sale of livestock	**62**	35
– Proceeds from sale of investments in shares	**–**	78
– Other cash inflows	**51**	26
Cash was applied to:		
– Acquisition of property, plant and equipment	**(690)**	(859)
– Acquisition of livestock	**(89)**	(95)
– Acquisition of intangible assets	**(103)**	(85)
– Co-operative support loans	**–**	(383)
– Advances to and investments in equity accounted investees	**(42)**	(41)
– Other cash outflows	**–**	(26)
Net cash flows from investing activities	**(706)**	(1,094)
Cash flows from financing activities		
Cash was provided from:		
– Proceeds from borrowings	**4,174**	4,909
– Interest received	**13**	7
– Other cash inflows	**38**	–
Cash was applied to:		
– Interest paid	**(393)**	(415)
– Repayment of borrowings	**(3,968)**	(5,815)
– Dividends paid to non-controlling interests	**(28)**	(28)
– Dividends paid to equity holders of the Co-operative	**(456)**	(701)
– Other cash outflows	**(2)**	(7)
Net cash flows from financing activities	**(622)**	(2,050)
Net increase in cash and cash equivalents	**48**	134
Cash and cash equivalents at the beginning of the year	**357**	303
Effect of exchange rate changes on cash balances	**(23)**	(80)
Cash and cash equivalents at the end of the year	**382**	357
Reconciliation of closing cash balances to the statement of financial position:		
Cash and cash equivalents	**393**	369
Bank overdraft	**(11)**	(12)
Closing cash balances	**382**	357

The accompanying notes form part of these summary financial statements.

NOTES TO THE SUMMARY FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 JULY 2017

PERFORMANCE

1 SEGMENT REPORTING

During the year, financial information was viewed by the Fonterra Management Team based on two different management reporting structures. The first, based on operating segments as presented in section (a); and the second, a strategic platform view as presented in section (b).

a) Operating segments

The Group has five reportable segments that reflect the Group's management and reporting structure as viewed by the Fonterra Management Team. Transactions between segments are based on estimated market prices.

REPORTABLE SEGMENT	DESCRIPTION
Global Ingredients and Operations	Represents the collection, processing and distribution of New Zealand milk, global sales and marketing of New Zealand and non-New Zealand milk products (including the Quick Service Restaurant businesses in Asia and Greater China), Global Brands and Nutrition, Co-operative Affairs, Fonterra Farm Source™ stores and Group Services.
Oceania	Represents fast-moving consumer goods (FMCG) businesses in New Zealand (including export to the Pacific Islands) and all FMCG and ingredients businesses in Australia (including Milk Supply and Manufacturing). It includes foodservice sales in Australia and New Zealand.
Asia	Represents FMCG and foodservice businesses (excluding the Quick Service Restaurant business) in Asia (excluding Greater China), Africa and the Middle East.
Greater China	Represents FMCG, foodservice (excluding the Quick Service Restaurant business) and farming businesses in Greater China.
Latin America	Represents FMCG and ingredients businesses in South America and the Caribbean.

NOTES TO THE SUMMARY FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

1 SEGMENT REPORTING CONTINUED

a) Operating segments continued

	GROUP $ MILLION						
	GLOBAL INGREDIENTS AND OPERATIONS	OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	ELIMINATIONS	TOTAL GROUP
Segment income statement							
Year ended 31 July 2017							
External revenue	12,510	2,458	1,509	1,183	1,572	–	19,232
Inter-segment revenue	1,949	458	142	275	8	(2,832)	–
Revenue from sale of goods	14,459	2,916	1,651	1,458	1,580	(2,832)	19,232
Cost of goods sold	(13,039)	(2,400)	(1,159)	(1,082)	(1,125)	2,837	(15,968)
Segment gross profit	1,420	516	492	376	455	5	3,264
Selling and marketing expenses	(170)	(100)	(155)	(99)	(117)	–	(641)
Distribution expenses	(204)	(143)	(35)	(11)	(157)	–	(550)
Administrative and other operating expenses	(738)	(154)	(106)	(108)	(88)	15	(1,179)
Segment operating expenses	(1,112)	(397)	(296)	(218)	(362)	15	(2,370)
Net other operating income	96	86	3	19	2	(16)	190
Net foreign exchange gains/(losses)	31	1	(5)	(1)	3	–	29
Share of profit/(loss) of equity accounted investees	49	–	–	(46)	4	–	7
Segment earnings before net finance costs and tax	484	206	194	130	102	4	1,120
Normalisation adjustments	1	(42)	–	76	–	–	35
Normalised segment earnings before net finance costs and tax	485	164	194	206	102	4	1,155
Normalisation adjustments							(35)
Finance income							34
Finance costs							(389)
Profit before tax							765
Profit before tax includes the following amounts:							
Depreciation	(307)	(51)	(11)	(27)	(39)	–	(435)
Amortisation	(68)	(18)	(3)	(1)	(1)	–	(91)
Normalisation adjustments consist of the following amounts:							
Gain on sale of Darnum manufacturing plant[1]	–	42	–	–	–	–	42
Reduction in the carrying value of investment in Beingmate[2]	–	–	–	(76)	–	–	(76)
Time value of options[3]	(1)	–	–	–	–	–	(1)
Total normalisation adjustments	(1)	42	–	(76)	–	–	(35)
Segment asset information:							
As at and for the year ended 31 July 2017							
Equity accounted investments	215	–	–	662	10	–	887
Capital expenditure[4]	553	188	23	38	49	–	851

1 The $42 million normalisation adjustment relates to other operating income.

2 Of the $76 million normalisation adjustment, $35 million relates to other operating expenses and $41 million to the share of profit/(loss) of equity accounted investees.

3 Of the $1 million normalisation adjustment, $18 million relates to revenue offset by $19 million of net foreign exchange losses.

4 Capital expenditure comprises purchases of property, plant and equipment and intangible assets, and net purchases of livestock.

a) Operating segments continued

	GROUP $ MILLION						
	GLOBAL INGREDIENTS AND OPERATIONS	OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	ELIMINATIONS	TOTAL GROUP
Segment income statement							
Year ended 31 July 2016							
External revenue	10,636	2,425	1,630	1,008	1,500	–	17,199
Inter-segment revenue	1,505	439	171	13	5	(2,133)	–
Revenue from sale of goods	12,141	2,864	1,801	1,021	1,505	(2,133)	17,199
Cost of goods sold	(10,343)	(2,362)	(1,213)	(742)	(1,042)	2,135	(13,567)
Segment gross profit	1,798	502	588	279	463	2	3,632
Selling and marketing expenses	(168)	(99)	(187)	(132)	(117)	–	(703)
Distribution expenses	(222)	(160)	(38)	(10)	(155)	–	(585)
Administrative and other operating expenses	(778)	(205)	(128)	(85)	(74)	30	(1,240)
Segment operating expenses	(1,168)	(464)	(353)	(227)	(346)	30	(2,528)
Net other operating income	145	97	3	27	20	(26)	266
Net foreign exchange gains/(losses)	30	1	(3)	(5)	(16)	–	7
Share of profit/(loss) of equity accounted investees	59	1	–	(10)	4	–	54
Segment earnings before net finance costs and tax	864	137	235	64	125	6	1,431
Normalisation adjustments	(96)	23	–	–	–	–	(73)
Normalised segment earnings before net finance costs and tax	768	160	235	64	125	6	1,358
Normalisation adjustments							73
Finance income							18
Finance costs							(517)
Profit before tax							932
Profit before tax includes the following amounts:							
Depreciation	(337)	(48)	(13)	(30)	(37)	–	(465)
Amortisation	(72)	(27)	(4)	(1)	(1)	–	(105)
Normalisation adjustments consist of the following amounts:							
Gain on sale of DairiConcepts investment[1]	68	–	–	–	–	–	68
Disposal and impairment of the Australian yoghurt and dairy desserts business[2]	–	(23)	–	–	–	–	(23)
Time value of options[3]	28	–	–	–	–	–	28
Total normalisation adjustments	96	(23)	–	–	–	–	73
Segment asset information:							
As at and for the year ended 31 July 2016							
Equity accounted investments	188	–	–	763	9	–	960
Capital expenditure[4]	632	114	21	131	46	–	944

1 The $68 million normalisation adjustment relates to other operating income.

2 Of the total $23 million, $4 million relates to cost of goods sold and $19 million to other operating expenses.

3 The $28 million normalisation adjustment relates to net foreign exchange gains.

4 Capital expenditure comprises purchases of property, plant and equipment and intangible assets, and net purchases of livestock.

NOTES TO THE SUMMARY FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

1 SEGMENT REPORTING CONTINUED

b) Strategic platforms

Strategic platforms are organised on a different basis than the Group's operating segments presented in section a) of this note. The basis of presentation is explained in the table below.

Fonterra considers this information to be useful as it provides more clarity on the financial performance of the ingredients, consumer and foodservice, and China Farms businesses.

PLATFORM	DESCRIPTION
Ingredients	Represents the Global Ingredients and Operations reportable segment, the ingredients businesses in Australia and South America, and excludes the Quick Service Restaurant businesses in Asia and Greater China and unallocated costs.
Consumer and foodservice	
– Oceania	Represents the Oceania reportable segment, excluding the ingredients business in Australia.
– Asia	Represents the Asia reportable segment and the Asia Quick Service Restaurant business reported in Global Ingredients and Operations.
– Greater China	Represents the Greater China reportable segment, excluding China Farms and including the Quick Service Restaurant business in Greater China reported in Global Ingredients and Operations.
– Latin America	Represents the Latin America reportable segment, excluding the ingredients businesses in South America.
China Farms	Represents farming operations in China.

	GROUP 31 JULY 2017								
	INGREDIENTS	CONSUMER AND FOODSERVICE					CHINA FARMS[1]	UNALLOCATED COSTS AND ELIMINATIONS	TOTAL
		OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	TOTAL			
Volume[2] (liquid milk equivalents, billion)	21.30	1.74	1.70	1.28	0.74	5.46	0.34	(4.16)	22.94
Volume[2] (metric tonnes, thousand)	3,019	636	310	237	600	1,783	26	(648)	4,180
Sales revenue[2] ($ million)	15,284	1,952	1,810	1,277	1,478	6,517	269	(2,838)	19,232
Normalised EBIT ($ million)	943	101	201	209	103	614	1	(403)	1,155
Capital employed[3] ($ million)	7,950	463	117	22	270	872	789	(518)	9,093
Return on capital[4]	10.3%	13.5%	118.4%	680.5%	23.3%	47.2%	NA		11.1%

For the year ended 31 July 2017 the Group's return on capital including intangible assets, goodwill and equity accounted investments, was 8.3 per cent.

	GROUP 31 JULY 2016								
	INGREDIENTS	CONSUMER AND FOODSERVICE					CHINA FARMS	UNALLOCATED COSTS AND ELIMINATIONS	TOTAL
		OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	TOTAL			
Volume[2] (liquid milk equivalents, billion)	22.39	1.83	1.55	0.87	0.62	4.87	0.23	(3.83)	23.66
Volume[2,5] (metric tonnes, thousand)	3,074	698	292	167	643	1,800	16	(577)	4,313
Sales revenue[2] ($ million)	13,005	2,051	1,944	916	1,385	6,296	183	(2,285)	17,199
Normalised EBIT ($ million)	1,204	97	244	131	108	580	(59)	(367)	1,358
Capital employed[3] ($ million)	7,724	489	127	22	284	922	873	(127)	9,392
Return on capital[4]	13.4%	10.9%	133.4%	429.9%	23.6%	41.7%	(6.5)%		12.4%

For the year ended 31 July 2016, the Group's return on capital including intangible assets, goodwill and equity accounted investments, was 9.2 per cent.

1 During the year ended 31 July 2017, the responsibility for the sale of China Farms' milk was transitioned to the Ingredients sales team in Greater China which has had an impact on year on year comparability. The transfer price is reflective of long-term milk price trends in China.

2 Includes sales to other strategic platforms. Total column represents total external sales.

3 Capital employed excludes brands, goodwill and equity accounted investments.

4 Return on capital is calculated as normalised EBIT, less equity accounted investees' earnings, less a notional royalty charge for use of the Group's brands, less a notional tax charge, divided by capital employed.

5 China Farms volumes for the year ended 31 July 2016 (metric tonnes, thousand), have been restated to align to the same product volume to weight conversion methodology as used by the Ingredients business to aid comparability between segments. Previously China Farms volumes were converted to metric tonnes based on the litres of raw milk sold.

c) Geographical revenue

	GROUP $ MILLION								
	CHINA	REST OF ASIA	AUSTRALIA	NEW ZEALAND	UNITED STATES	EUROPE	LATIN AMERICA	REST OF WORLD	TOTAL
Geographical segment external revenue:									
Year ended 31 July 2017	**3,383**	**5,165**	**1,592**	**2,056**	**1,254**	**838**	**2,162**	**2,782**	**19,232**
Year ended 31 July 2016	2,394	4,829	1,471	1,939	1,305	745	2,053	2,463	17,199

Revenue is allocated to geographical segments on the basis of the destination of the goods sold.

d) Non-current assets

	GROUP $ MILLION							
	GLOBAL INGREDIENTS AND OPERATIONS		OCEANIA		ASIA	GREATER CHINA	LATIN AMERICA	TOTAL GROUP
	NEW ZEALAND	REST OF WORLD	NEW ZEALAND	AUSTRALIA				
Geographical segment non-current assets:								
As at 31 July 2017	**5,479**	**347**	**1,285**	**840**	**738**	**1,481**	**988**	**11,158**
As at 31 July 2016	5,459	301	1,292	740	779	1,648	981	11,200

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Reconciliation of geographical segment's non-current assets to total non-current assets:		
Geographical segment non-current assets	**11,158**	11,200
Deferred tax assets	**363**	410
Derivative financial instruments	**239**	417
Total non-current assets	**11,760**	12,027

2 COST OF GOODS SOLD

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Opening inventory	**2,401**	3,025
Cost of milk:		
– New Zealand sourced	**9,471**	6,205
– Non-New Zealand sourced	**932**	944
Other purchases	**5,757**	5,794
Closing inventory	**(2,593)**	(2,401)
Total cost of goods sold	**15,968**	13,567

NOTES TO THE SUMMARY FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

DEBT AND EQUITY

3 SUBSCRIBED EQUITY INSTRUMENTS

Co-operative shares, including shares held within the Group

Co-operative shares may only be held by a shareholder supplying milk to the Company (farmer shareholder), by former farmer shareholders for up to three seasons after cessation of milk supply, or by Fonterra Farmer Custodian Limited (the Custodian). Voting rights in the Company are dependent on milk supply supported by Co-operative shares.[1]

	CO-OPERATIVE SHARES (THOUSANDS)
Balance at 1 August 2016	**1,602,703**
Shares issued under the dividend reinvestment plan[2]	4,230
Shares surrendered	–
Balance at 31 July 2017	**1,606,933**
Balance at 1 August 2015	1,599,094
Shares issued under the dividend reinvestment plan[2]	3,609
Shares surrendered	–
Balance at 31 July 2016	**1,602,703**

1 These rights are also attached to vouchers when backed by milk supply (subject to limits).

2 Total value of $25 million (31 July 2016:$19 million).

The rights attaching to Co-operative shares are set out in Fonterra's Constitution, available in the 'About Us/Our Governance' section of Fonterra's website.

Units in the Fonterra Shareholders' Fund

The Custodian holds legal title of Co-operative shares of which the Economic Rights have been sold to the Fund on trust for the benefit of the Fund. At 31 July 2017, 126,047,304 Co-operative shares (31 July 2016: 111,991,937) were legally owned by the Custodian, on trust for the benefit of the Fund.

	UNITS (THOUSANDS)
Balance at 1 August 2016	**111,992**
Units issued	**29,933**
Units surrendered	**(15,878)**
Balance at 31 July 2017	**126,047**
Balance at 1 August 2015	105,480
Units issued	27,137
Units surrendered	(20,625)
Balance at 31 July 2016	111,992

The rights attaching to units are set out in the Trust Deed constituting the Fonterra Shareholders' Fund, available in the 'Our Financials/Fonterra Shareholder's Fund' section of Fonterra's website.

Capital management and structure

The Board's objective is to maximise equity holder returns over time by maintaining an optimal capital structure. Trading Among Farmers (TAF) allows shares in Fonterra to be traded between shareholders, on the Fonterra Shareholders' Market (a private market operated by NZX Limited). The Fund supports this by allowing investors, including farmers, to trade in units backed by Economic Rights in Fonterra. The Fund also allows farmer shareholders to acquire units and exchange them for shares in Fonterra, and to exchange shares for units and dispose of those units on the NZX or ASX.

The Group provides returns to farmer shareholders through a milk price, and to equity holders through dividends and changes in the Company's share price.

The Fund is subject to the issue and redemption of units at the discretion of Fonterra and Fonterra's farmer shareholders. Fonterra has an interest in ensuring the stability of the Fund and has established a Fund Size Risk Management Policy, which requires that the number of units on issue remain within specified limits and that within these limits, the number of units is managed appropriately. Fonterra may use a range of measures to ensure the Fund size remains within the specified limits, including introducing or cancelling a dividend reinvestment plan, operating a unit and/or share repurchase programme and issuing new shares.

4 DIVIDENDS PAID

The Dividend Reinvestment Plan applied to all dividends in the table below.

	$ MILLION	
DIVIDENDS	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016
2017 Interim dividend – 20 cents per share[1]	321	–
2016 Final dividend – 10 cents per share[2]	160	–
2016 Interim dividend – 10 cents per share[3]	–	160
2016 Interim dividend – 20 cents per share[4]	–	320
2015 Final dividend – 15 cents per share[5]	–	240

1 Declared on 21 March 2017 and paid on 20 April 2017 to all Co-operative shares on issue at 5 April 2017.
2 Declared on 18 August 2016 and paid on 9 September 2016 to all Co-operative shares on issue at 1 September 2016.
3 Declared on 16 May 2016 and paid on 7 June 2016 to all Co-operative shares on issue at 30 May 2016.
4 Declared on 22 March 2016 and paid on 20 April 2016 to all Co-operative shares on issue at 8 April 2016.
5 Declared on 23 September 2015 and paid on 20 October 2015 to all Co-operative shares on issue at 8 October 2015.

Dividends declared after balance date

On 23 September 2017, the Board declared a final dividend of 20 cents per share, to be paid on 20 October 2017 to all Co-operative shares on issue as at 9 October 2017.

Fonterra has a Dividend Reinvestment Plan, where eligible shareholders can choose to reinvest all or part of their dividend in additional Co-operative shares. The Dividend Reinvestment Plan does apply to this dividend. Participation in the Dividend Reinvestment Plan requires shareholders to submit an election notice for participation by 9 October 2017. Full details of the Dividend Reinvestment Plan are available in the 'Our Dividends' section of Fonterra's website.

5 BORROWINGS

Economic net interest-bearing debt

Economic net interest-bearing debt reflects the effect of debt hedging in place at balance date.

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Net interest-bearing debt position		
Total borrowings	6,263	6,352
Cash and cash equivalents	(393)	(369)
Interest-bearing advances[1]	(435)	(464)
Bank overdraft	11	12
Net interest-bearing debt	5,446	5,531
Value of derivatives used to manage changes in hedged risks on debt instruments	155	(58)
Economic net interest-bearing debt	5,601	5,473

1 Includes $135 million of Fonterra Co-operative Support Loan repayments relating to the 2016/17 season (31 July 2016: nil).

NOTES TO THE SUMMARY FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

5 BORROWINGS CONTINUED

Total borrowings in the table above are represented by:

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Commercial paper	**164**	454
Bank loans	**854**	879
Finance leases[1]	**137**	143
Capital notes[2]	**35**	35
NZX-listed bonds	**500**	499
Medium-term notes	**4,573**	4,342
Total borrowings	**6,263**	6,352
Included within the statement of financial position as follows:		
Total current borrowings	**1,112**	955
Total non-current borrowings	**5,151**	5,397
Total borrowings	**6,263**	6,352

1 Finance leases are secured over the related item of property, plant and equipment.

2 Capital notes are unsecured subordinated borrowings.

3 All other borrowings are unsecured and unsubordinated.

Leverage ratios

The Board closely monitors the Group's leverage ratios, which include the gearing ratio and debt coverage ratios (debt payback and interest coverage ratios). The primary debt payback ratios comprise funds from operations divided by economic net interest-bearing debt, and economic net interest-bearing debt divided by EBITDA (Earnings Before Interest, Tax, Depreciation and Amortisation). Debt pay-back ratios are adjusted for the impact of operating leases. The gearing ratio is calculated as economic net interest-bearing debt divided by total capital. Economic net interest-bearing debt is calculated in the table above. Total capital is calculated as equity, as presented in the statement of financial position (excluding hedge reserves), plus economic net interest-bearing debt. The gearing ratio as at 31 July 2017 was 44.3 per cent (31 July 2016: 44.3 per cent). The Group is not subject to externally imposed capital requirements.

Liquidity risk

The Group manages its liquidity by retaining cash and marketable securities, the availability of funding from an adequate amount of committed credit facilities and the ability to close out market positions. Fonterra's funding facilities are reviewed at least annually, which is one of the key financial risk management activities undertaken by the Group to ensure an appropriate maturity profile given the nature of the Group's business. At balance date the Group had undrawn lines of credit totalling $3,811 million (31 July 2016: $3,723 million).

WORKING CAPITAL

6 OWING TO SUPPLIERS

The Board uses its discretion in establishing the rate at which Fonterra will pay suppliers for the milk supplied over the season. This is referred to as the advance rate. The following table provides a breakdown of the advance payments made to suppliers:

	GROUP	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Owing to suppliers ($ million)	**1,330**[1]	719
Farmgate Milk Price (per kgMS)	**$6.12**[2]	$3.90
Of this amount:		
– Total advance payments made during the year	**$5.21**	$3.48
– Total owing as at 31 July	**$0.91**	$0.42
Amount advanced during the year as a percentage of the milk price for the season ended 31 May	**85%**	89%

1 This amount is after offsetting $135 million Fonterra Co-operative Support Loan repayments relating to the 2016/17 season.

2 Represents the price for milk supplied on standard terms of supply. The Fonterra Farmgate Milk Price Statement sets out information about the Farmgate Milk Price as calculated in accordance with the Farmgate Milk Price Manual and the price for milk supplied on standard terms. It can be found in the 'Our Financials/Farmgate Milk Prices' section of the Fonterra website.

INVESTMENTS

7 EQUITY ACCOUNTED INVESTMENTS

The Group's significant equity accounted investments are listed below. The ownership interest in these entities is 51 per cent or less and the Group is not considered to exercise a controlling interest.

		OWNERSHIP INTERESTS (%)	
EQUITY ACCOUNTED INVESTEE NAME	COUNTRY OF INCORPORATION AND PRINCIPAL PLACE OF BUSINESS	AS AT 31 JULY 2017	AS AT 31 JULY 2016
DMV Fonterra Excipients GmbH & Co KG	Germany	**50**	50
Beingmate Baby & Child Food Co., Ltd	China	**18.8**	18.8
Falcon Dairy Holdings Limited	Hong Kong	**51**	51

All investees have balance dates of 31 December.

FINANCIAL RISK MANAGEMENT

8 FINANCIAL RISK MANAGEMENT

Overview

The Group's overall financial risk management programme focuses primarily on maintaining a prudent financial risk profile that provides flexibility to implement the Group's strategies, while ensuring optimisation of the return on assets. Financial risk management is centralised, which supports compliance with the financial risk management policies and procedures set by the Board.

KEY FINANCIAL RISK MANAGEMENT ACTIVITIES

Market risks

The Group uses various derivative financial instruments to manage its exposure to changes in foreign currency exchange rates, interest rates and commodity prices.

Liquidity risk

The Group actively manages its minimum on-hand cash facilities, access to committed funds and lines of credit, and the maturity profile of its financial obligations. For further detail refer to Note 5.

Capital management

The Group actively manages its capital structure through leverage and coverage ratios. The Fonterra Shareholders' Fund removes the redemption risk associated with Co-operative shares. For further detail refer to Note 3.

HEDGE ACCOUNTING

The Group applies hedge accounting to derivatives that are designated into effective hedge relationships. The hedge accounting rules in NZ IFRS 9 Financial Instruments align hedge accounting more closely with Fonterra's risk management activities than the previous accounting standard applied. Therefore, Fonterra elected to adopt NZ IFRS 9 from 1 August 2016. This means that:

- Hedge accounting is now able to be achieved for certain interest rate swaps, which was not possible under the accounting standards previously applied.
- Option premium costs and the time value of options are now recognised in other comprehensive income as 'costs of hedging reserve', until the sales transaction is recognised. Under the accounting standards previously applied these costs were recorded in the income statement when they were incurred.

The adoption of NZ IFRS 9 did not result in any changes to the comparative numbers presented.

NOTES TO THE SUMMARY FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

OTHER

9 TAXATION

Taxation – income statement

The total taxation expense in the income statement is summarised as follows:

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Current tax expense	97	108
Prior period adjustments to current tax	(25)	5
Deferred tax movements:		
– Origination and reversal of temporary differences	(52)	(15)
Tax expense	**20**	98

The taxation charge that would arise at the standard rate of corporation tax in New Zealand is reconciled to the tax expense as follows:

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Profit before tax	**765**	932
Prima facie tax expense at 28%	214	261
Add/(deduct) tax effect of:		
– Effect of tax rates in foreign jurisdictions	(33)	(24)
– Non-deductible expenses/additional assessable income	54	90
– Non-assessable income/additional deductible expenses	(30)	(66)
– Prior year under provision	(25)	5
Tax expense before distributions and deferred tax	**180**	266
Effective tax rate before distributions and deferred tax[1]	**23.5%**	28.5%
Tax effect of distributions to farmer shareholders	(163)	(170)
Tax expense before deferred tax	**17**	96
Effective tax rate before deferred tax[1]	**2.2%**	10.3%
Add/(deduct) tax effect of:		
– Origination and reversal of other temporary differences	2	(1)
– Losses of overseas Group entities not recognised	1	3
Tax expense	**20**	98
Effective tax rate[1]	**2.6%**	10.5%

Imputation credits

Imputation credits available for use in subsequent reporting periods	20	20

Tax losses

Gross tax losses available for which no deferred tax asset has been recognised	52	48

1 The effective tax rate is the tax charge on the face of the income statement expressed as a percentage of the profit before tax.

10 CONTINGENT LIABILITIES, PROVISIONS AND COMMITMENTS

Contingent liabilities

In the normal course of business, Fonterra, its subsidiaries and equity accounted investees, are exposed to claims and legal proceedings that may in some cases result in costs to the Group.

In early August 2013, Fonterra publicly announced a potential food safety issue with three batches of Whey Protein Concentrate (WPC80) produced at the Hautapu manufacturing site and initiated a precautionary product recall.

In late August 2013, the New Zealand Government confirmed that the *Clostridium* samples found in WPC80 were not *Clostridium botulinum* and were not toxigenic, meaning the consumers of products containing the relevant batches of WPC80 were never in danger from *Clostridium botulinum*.

In January 2014, Danone formally initiated legal proceedings against Fonterra in the High Court of New Zealand and separate Singapore arbitration proceedings against Fonterra in relation to the WPC80 precautionary recall. The New Zealand High Court proceedings have been stayed pending completion of the Singapore arbitration. An initial hearing of the arbitration took place in February 2016 and a final hearing of the arbitration took place in June 2016. A decision of the arbitration panel is pending.

Based on current information available and the claims made to date in both proceedings, Fonterra will vigorously defend its position in these proceedings. Uncertainty exists regarding the outcome of the proceedings. Fonterra has provided $11 million (31 July 2016: $11 million) in respect of the Danone claims, which represents the maximum contractual liability to Danone.

The Directors believe that these proceedings have been adequately provided for and disclosed by the Group and that there are no additional claims or legal proceedings in respect of this matter that are pending at the date of these financial statements that require provision or disclosure.

The Group has no other contingent liabilities as at 31 July 2017 (31 July 2016: nil).

11 NET TANGIBLE ASSETS PER SECURITY

	GROUP	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Net tangible assets per security[1]		
$ per listed debt security on issue	**6.86**	6.32
$ per equity instrument on issue	**2.57**	2.37
Listed debt securities on issue (million)	**603**	603
Equity instruments on issue (million)	**1,607**	1,603

1 Net tangible assets represents total assets less total liabilities less intangible assets.

INDEPENDENT AUDITOR'S REPORT

FOR THE YEAR ENDED 31 JULY 2017

REPORT OF THE INDEPENDENT AUDITOR ON THE SUMMARY FINANCIAL STATEMENTS

TO THE SHAREHOLDERS OF FONTERRA CO-OPERATIVE GROUP LIMITED

The summary financial statements comprise:

- the statement of financial position as at 31 July 2017;
- the income statement for the year then ended;
- the statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the cash flow statement for the year then ended; and
- the notes to the summary financial statements.

OUR OPINION

The summary financial statements are derived from the audited financial statements of Fonterra Co-operative Group Limited, including its controlled entities (the Group) for the year ended 31 July 2017.

In our opinion, the accompanying summary financial statements are consistent, in all material respects, with the audited financial statements, in accordance with FRS-43: *Summary Financial Statements* issued by the New Zealand Accounting Standards Board.

SUMMARY FINANCIAL STATEMENTS

The summary financial statements do not contain all the disclosures required by New Zealand equivalents to International Financial Reporting Standards (NZ IFRS). Reading the summary financial statements and the auditor's report thereon, therefore, is not a substitute for reading the audited financial statements and the auditor's report thereon. The summary financial statements and the audited financial statements do not reflect the effects of events that occurred subsequent to the date of our report on the audited financial statements.

THE AUDITED FINANCIAL STATEMENTS AND OUR REPORT THEREON

We expressed an unmodified audit opinion on the audited financial statements in our report dated 23 September 2017.

That report also includes the communication of key audit matters. Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current year.

RESPONSIBILITIES OF THE DIRECTORS FOR THE SUMMARY FINANCIAL STATEMENTS

The Directors are responsible, on behalf of the Company, for the preparation of the summary financial statements in accordance with FRS-43: *Summary Financial Statements*.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on whether the summary financial statements are consistent, in all material respects, with the audited financial statements based on our procedures, which were conducted in accordance with International Standard on Auditing (New Zealand) 810 (Revised), *Engagements to Report on Summary Financial Statements*.

Our firm carries out other services for the Group in relation to advisory, other assurance and attestation services. Partners and employees of our firm may deal with the Group on normal terms within the ordinary course of trading activities of the Group. These matters have not impaired our independence as auditor of the Group.

WHO WE REPORT TO

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

PricewaterhouseCoopers

Chartered Accountants
Auckland
23 September 2017

STATUTORY INFORMATION

FOR THE YEAR ENDED 31 JULY 2017

CURRENT CREDIT RATING STATUS

Standard & Poor's long term rating for Fonterra is A- with a rating outlook of stable. Fitch's long and short term default rating is A with a rating outlook of stable. Retail Bonds have been rated the same as the Company's long term rating by both Standard & Poor's and Fitch. Capital Notes which are subordinate to other Fonterra debt issued are rated BBB+ by Standard & Poor's and A- by Fitch.

EXCHANGE RULINGS AND WAIVERS

NZX Limited (NZX) has ruled that Capital Notes do not constitute 'equity securities' under the NZX Main Board/Debt Market Listing Rules ('Rules'). This means that where Capital Notes are quoted on NZX's Debt Market ('NZDX'), the Company is not required to comply with certain Rules which apply to an issuer of quoted equity securities.

The Company was issued with a waiver of Rule 11.1.1 to enable it to decline to accept or register transfers of Capital Notes (NZDX listed debt securities FCGHA) if such transfer would result in the transferor holding or continuing to hold Capital Notes with a face value or principal amount of less than $5,000 or if such transfer is for an amount of less than $1,000 or not a multiple thereof. The effect of this waiver is that the minimum holding amount in respect of the Capital Notes will at all times be $5,000 in aggregate and can only be transferred in multiples of $1,000.

The Company was issued with a waiver of Rule 5.2.3 by NZX on 10 April 2015 (for a period of one year from 21 April 2015) in respect of the Company's issuance of $350 million of unsecured, unsubordinated, fixed rate bonds maturing on 20 October 2021 ('FCG030 Bonds'), to the extent that that rule would otherwise require the FCG030 Bonds to be held by at least 500 members of the public holding at least 25% of the FCG030 Bonds.

The Company was also issued with a waiver of Rule 5.2.3, as modified by NZX's ruling on Rule 5.2.3, by NZX on 18 February 2016 (for a period of six months from 8 March 2016) in respect of the Company's issuance of $150 million of unsecured, unsubordinated, fixed rate bonds maturing on 7 March 2023 ('FCG040 Bonds'), to the extent that the rule (as modified) would otherwise require the FCG040 Bonds to be held by at least 100 members of the public holding at least 25% of the FCG040 Bonds.

The effect of these waivers from Rule 5.2.3 is that the FCG030 Bonds and the FCG040 Bonds may not be widely held and there may be reduced liquidity in those bonds.

The Company was issued with a waiver of Rule 7.11.1 by NZX on 18 February 2016 in respect of the Company's issuance of the FCG040 Bonds, to the extent that the rule would have otherwise required the Company to allot the FCG040 Bonds within five business days after the latest date on which applications for the FCG040 Bonds closed.

Fonterra Co-operative Group Limited (Fonterra) was issued with a ruling in respect of Rule 1.7.1(d) of the Fonterra Shareholders' Market Rules (Rules) on 27 June 2017 by NZX Limited (NZX). The effect of this ruling was to not preclude the appointment of Mr Bruce Hassall to the position of an independent director of Fonterra by virtue of a child of Mr Hassall being employed in a non-decision making and non-senior role at Fonterra.

Fonterra was issued with a ruling in respect of Rule 5.1.2(c) on 22 November 2016 by NZX. The effect of this ruling is that Fonterra's internal governance resolutions are considered to be matters that do not require the NZX to approve a notice of meeting under Rule 5.1.1.

Fonterra was issued with a waiver of Rule 3.2.1(c) on 31 August 2016 by the NZX, to the extent that such Rule requires Fonterra to have a minimum of two independent directors or, if Fonterra has eight or more directors, three or one-third of the total number of directors, whichever is greater. This waiver was granted in connection with the resignation of Mr John Waller and applied for a period ending on the earlier of the appointment of a new independent director or three months from the date of the waiver.

NZX TRADING HALTS

No trading halts were placed on Fonterra securities by NZX Regulation in the financial year ended 31 July 2017.

FIVE YEAR SUMMARY

FOR THE YEAR ENDED 31 JULY 2017

	JULY 2017	JULY 2016	JULY 2015	JULY 2014	JULY 2013
SHAREHOLDER SUPPLIER RETURNS					
Payout					
Farmgate Milk Price (per kgMS)[1]	**6.12**	3.90	4.40	8.40	5.84
Dividend (per share)	**0.40**	0.40	0.25	0.10	0.32
Cash payout[2]	**6.52**	4.30	4.65	8.50	6.16
Retentions (per share)[3]	**0.06**	0.11	0.04	–	0.14
OPERATING PERFORMANCE					
Average commodity prices (US$ per MT FOB)					
Whole Milk Powder[4]	**2,855**	2,111	2,639	4,824	3,394
Skim Milk Powder[4]	**2,216**	1,803	2,552	4,504	3,625
Butter[4]	**4,221**	2,830	3,027	3,920	3,550
Cheese[5]	**3,763**	2,766	3,477	4,706	4,124
Average NZD/USD spot exchange rate applying throughout the year[6]	**0.71**	0.67	0.76	0.84	0.82
Fonterra's average NZD/USD conversion rate[7]	**0.70**	0.71	0.79	0.81	0.80
Revenue ($ million)					
Ingredients and other revenue	**12,715**	10,903	12,144	17,748	13,926
Consumer revenue	**6,517**	6,296	6,701	4,527	4,717
Total revenue	**19,232**	17,199	18,845	22,275	18,643
Dairy ingredients manufactured in New Zealand (000s MT)	**2,379**	2,466	2,753	2,519	2,312
Total ingredients sales volume (000s MT)[8]	**3,018**	3,074	2,982	3,052	2,765
Segment earnings ($ million)[9]					
Global Ingredients and Operations	**484**	864	673	280	480
Oceania	**206**	137	(156)	31	93
Asia	**194**	235	192	50	207
Greater China	**130**	64	(5)	30	–
Latin America	**102**	125	256	111	137
Eliminations	**4**	6	(18)	1	20
Segment earnings	**1,120**	1,431	942	503	937
Normalisation adjustments	**35**	(73)	32	–	65
Normalised segment earnings	**1,155**	1,358	974	503	1,002
Profit after tax attributable to shareholders ($ million)	**734**	810	466	157	718
Earnings per share	**0.46**	0.51	0.29	0.10	0.44

1 From the beginning of the 2009 season the Farmgate Milk Price has been determined by the Board. In making that determination, the Board takes into account the Farmgate Milk Price calculated in accordance with the principles set out in the Farmgate Milk Price Manual.

2 Average Payout for a 100 per cent share-backed supplier.

3 Retentions are calculated as net profit after tax attributable to Co-operative shareholders at 31 July divided by the number of shares at 31 May, less dividend per share.

4 Source: Fonterra Farmgate Milk Price Statement representing the weighted-average United States Dollar (USD) contract prices of Reference Commodity Products.

5 Source: Oceania Export Series, Agricultural Marketing Service, US Department of Agriculture.

6 Average spot exchange rate is the average of the daily spot rates for the financial period.

7 Fonterra's average conversion rate is the rate that Fonterra has converted net United States Dollar receipts into New Zealand Dollars based on the hedge cover in place.

8 For the year ended 31 July 2014 the total ingredients sales volume has been restated to reflect Fonterra's strategic platforms. Figures for the year ended 31 July 2013 have not been restated.

9 Represents segment earnings before unallocated finance income, finance costs and tax. For the years ended 31 July 2016, 2015 and 2014, Greater China has been disclosed separately in alignment with the disclosures in the segment note. For the years ended 31 July 2013 and earlier, Greater China was part of Asia. The year ended 31 July 2015 has been restated to reflect changes to the organisation of business units that occurred in the year ended 31 July 2016. The year ended 31 July 2014 has been restated to reflect changes to the organisation of business units that occurred in the year ended 31 July 2015.

	JULY 2017	JULY 2016	JULY 2015	JULY 2014	JULY 2013
KEY CAPITAL MEASURES ($ million)					
Equity excluding hedge reserve	**7,056**	6,883	7,196	6,452	6,830
Economic net interest-bearing debt[10]	**5,601**	5,473	7,120	4,732	4,467
Economic debt to debt plus equity ratio[11]	**44.3%**	44.3%	49.7%	42.3%	39.6%
Capital employed[12]	**9,093**	9,392	9,487	8,493	8,249
Return on capital[13]	**11.1%**	12.4%	8.9%	4.7%	10.5%
STAFF EMPLOYED					
Total staff employed (000s, permanent full time equivalents)	**21.4**	21.3	22.0	18.2	17.5
New Zealand	**11.7**	11.4	11.9	11.4	11.2
Overseas	**9.7**	9.9	10.1	6.8	6.3
SEASON STATISTICS[14]					
Total NZ milk collected (million litres)	**17,051**	17,585	18,143	17,932	16,673
Highest daily volume collected (million litres)	**80.1**	86.9	89.7	87.1	84.8
NZ shareholder supply milk solids collected (million kgMS)	**1,417**	1,453	1,520	1,533	1,424
NZ contract supply milk solids collected (million kgMS)	**109**	113	94	51	39
NZ milk solids collected (million kgMS)	**1,526**	1,566	1,614	1,584	1,463
Total number of shareholders at 31 May	**10,267**	10,579	10,753	10,721	10,668
Total number of sharemilkers at 31 May	**2,722**	3,098	3,379	3,398	3,449
Total number of shares at 31 May (million)	**1,607**	1,602	1,599	1,598	1,598

10 Economic net interest-bearing debt reflects total borrowings less cash and cash equivalents and non-current interest-bearing advances adjusted for derivatives used to manage changes in hedged risks.

11 Economic debt to debt plus equity ratio is calculated as economic net interest-bearing debt divided by economic net interest-bearing debt plus equity excluding hedge reserves.

12 Capital employed excludes brands, goodwill and equity accounted investments.

13 Return on capital is calculated as normalised EBIT, less equity accounted investees' earnings, divided by capital employed.

14 All season statistics are based on the 12 month milk season of 1 June–31 May.

NON-GAAP MEASURES

Fonterra uses several non-GAAP measures when discussing financial performance. For further details and definitions of non-GAAP measures used by Fonterra, refer to the glossary on page 105. These are non-GAAP measures and are not prepared in accordance with NZ IFRS.

Management believes that these measures provide useful information as they provide valuable insight on the underlying performance of the business. They may be used internally to evaluate the underlying performance of business units and to analyse trends. These measures are not uniformly defined or utilised by all companies. Accordingly, these measures may not be comparable with similarly titled measures used by other companies. Non-GAAP financial measures should not be viewed in isolation nor considered as a substitute for measures reported in accordance with NZ IFRS.

Reconciliations for the NZ IFRS measures to certain non-GAAP measures referred to by Fonterra are detailed below.

Reconciliation from the NZ IFRS measure of profit for the period to Fonterra's normalised EBITDA

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Profit for the period	745	834
Add: Depreciation	435	465
Add: Amortisation	91	105
Add: Net finance costs	355	499
Add/(Less): Taxation expense/(credit)	20	98
Total EBITDA	1,646	2,001
Add: Reduction in the carrying value of investment in Beingmate	76	–
Add: Disposal and impairment of the Australian yoghurt and dairy desserts business	–	23
Add: Restructuring and redundancy provisions	–	–
Add/(Less): Time value of options	1	(28)
Less: Gain on sale of Darnum manufacturing plant	(42)	–
Less: Gain on DairiConcepts sale	–	(68)
Less: Gain on Latin America realignment	–	–
Total normalisation adjustments	35	(73)
Normalised EBITDA	1,681	1,928

Reconciliation from the NZ IFRS measure of profit for the period to Fonterra's normalised EBIT

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Profit for the period	745	834
Add: Net finance costs	355	499
Add/(Less): Taxation expense/(credit)	20	98
Total EBIT	1,120	1,431
(Less)/Add: Normalisation adjustments (as detailed above)	35	(73)
Total normalised EBIT	1,155	1,358

Reconciliation from the NZ IFRS measure of profit for the period to Fonterra's normalised earnings per share

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Profit for the period	745	834
(Less)/Add: Normalisation adjustments (as detailed above)	35	(73)
Add/(Less): Tax on normalisation adjustments	12	52
Total normalised earnings	792	813
Less: Share attributable to non-controlling interests	(11)	(24)
Net normalised earnings attributable to equity holders of the Parent	781	789
Weighted average number of shares (thousands of shares)	1,604,744	1,600,825
Normalised earnings per share ($)	0.49	0.49

GLOSSARY

NON-GAAP MEASURES

Fonterra refers to non-GAAP financial measures throughout the Annual Review, and these measures are not prepared in accordance with NZ IFRS. The definitions below explain how Fonterra calculates the non-GAAP measures referred to throughout the Annul Review.

EBIT	means earnings before interest and tax and is calculated as profit for the period before net finance costs and tax.
EBITDA	means earnings before interest, tax, depreciation and amortisation and is calculated as profit for the period before net finance costs, tax, depreciation and amortisation.
Economic net interest bearing debt	means net interest bearing debt including the effect of debt hedging.
Farmgate Milk Price	means the base price that Fonterra pays for milk supplied to it in New Zealand for a season. The season refers to the 12 month milk season of 1 June to 31 May.
Gearing ratio	is calculated as economic net interest bearing debt divided by total capital. Total capital is equity excluding the hedge reserves, plus economic net interest bearing debt.
Normalisation adjustments	means transactions that are unusual by nature and size. Excluding these transactions can assist users with forming a view of the underlying performance of the business. Unusual transactions by nature are the result of specific events or circumstances that are outside the control of the business, or relate to major acquisitions, disposals or divestments, or are not expected to occur frequently. It also includes fair value movements if they are non-cash and have no impact on profit over time. Unusual transactions by size are those that are unusually large in a particular accounting period.
Normalised EBIT	means profit for the period before net finance costs and tax, and after normalisation adjustments.
Normalised segment earnings	means segmental profit for the period before net finance costs and tax, and after normalisation adjustments.
Payout	means the total cash payment to farmer shareholders. It is the sum of the Farmgate Milk Price (kg/MS) and the dividend per share. Both of these components have established policies and procedures in place on how they are determined.
Retentions	means net profit after tax attributable to farmer shareholders divided by the number of shares at 31 May, less dividend per share.
Return on capital	is calculated as normalised EBIT less equity accounted investees' earnings divided by capital employed. Capital employed is calculated as the average for the period of: net assets excluding net interest-bearing debt, deferred tax balances and brands, goodwill and equity accounted investments.
Segment earnings	means segmental profit for the period before net finance costs and tax.
Working capital	is calculated as current trade receivables plus inventories, less current trade payables and accruals. It excludes amounts owing to suppliers and employee entitlements.
Working capital days	is calculated as average period to date working capital divided by external revenue, multiplied by the number of days in the period.

DIRECTORY

FONTERRA BOARD OF DIRECTORS

John Wilson

Clinton Dines

Ian Farrelly

Leonie Guiney

Simon Israel

David Jackson

David MacLeod

John Monaghan

Nicola Shadbolt

Donna Smit

Scott St John

Ashley Waugh

FONTERRA MANAGEMENT TEAM

Theo Spierings

Lukas Paravicini

Miles Hurrell

Robert Spurway

Judith Swales

Paul Washer

Kelvin Wickham

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ANNUAL **FINANCIAL RESULTS**

FOR THE YEAR ENDED
31 JULY 2017

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DIRECTORS' STATEMENT

FOR THE YEAR ENDED 31 JULY 2017

The Directors of Fonterra Co-operative Group Limited (Fonterra) are pleased to present to Shareholders the Annual Report[1] and financial statements for Fonterra and its subsidiaries (together the Group) and the Group's interest in its equity accounted investments for the year ended 31 July 2017.

The Directors present financial statements for each financial year which fairly present the financial position of the Group and its financial performance and cash flows for that period.

The Directors consider the financial statements of the Group have been prepared using accounting policies which have been consistently applied and supported by reasonable judgements and estimates, and that all relevant financial reporting and accounting standards have been followed.

The Directors believe that proper accounting records have been kept which enable, with reasonable accuracy, the determination of the financial position of the Group and facilitate compliance of the financial statements with the Financial Markets Conduct Act 2013.

The Directors consider that they have taken adequate steps to safeguard the assets of the Group, and to prevent and detect fraud and other irregularities.

The Directors hereby approve and authorise for issue the Annual Report for the year ended 31 July 2017. For and on behalf of the Board:

JOHN WILSON
CHAIRMAN
23 September 2017

DAVID JACKSON
DIRECTOR
23 September 2017

1 This document, in conjunction with the Fonterra Annual Review 2017, constitutes the 2017 Annual Report to Shareholders of Fonterra Co-operative Group Limited.

INCOME STATEMENT

FOR THE YEAR ENDED 31 JULY 2017

		GROUP $ MILLION	
	NOTES	31 JULY 2017	31 JULY 2016
Revenue from sale of goods		19,232	17,199
Cost of goods sold	2	(15,968)	(13,567)
Gross profit		3,264	3,632
Other operating income		190	266
Selling and marketing expenses		(641)	(703)
Distribution expenses		(550)	(585)
Administrative expenses		(810)	(844)
Other operating expenses		(369)	(396)
Net foreign exchange gains		29	7
Share of profit of equity accounted investees	16	7	54
Profit before net finance costs and tax	4	1,120	1,431
Finance income	8	34	18
Finance costs	8	(389)	(517)
Net finance costs		(355)	(499)
Profit before tax		765	932
Tax expense	18	(20)	(98)
Profit after tax		745	834
Profit after tax is attributable to:			
Equity holders of the Co-operative		734	810
Non-controlling interests		11	24
Profit after tax		745	834

		GROUP $	
		31 JULY 2017	31 JULY 2016
Earnings per share:			
Basic and diluted earnings per share	3	0.46	0.51

The accompanying notes form part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 JULY 2017

	NOTES	GROUP $ MILLION 31 JULY 2017	GROUP $ MILLION 31 JULY 2016
Profit after tax		**745**	834
Items that may be reclassified subsequently to profit or loss:			
Cash flow hedges and other costs of hedging, net of tax		**128**	601
Net investment hedges and translation of foreign operations, net of tax		**(124)**	(318)
Hyperinflation losses attributable to equity holders		**(1)**	(16)
Share of equity accounted investees' movements in reserves	16	**–**	5
Other reserve movements		**(2)**	5
Total items that may be reclassified subsequently to profit or loss		**1**	277
Items that will not be reclassified subsequently to profit or loss:			
Net fair value gains on investments in shares		**2**	–
Foreign currency translation losses attributable to non-controlling interests		**(3)**	(84)
Hyperinflation movements attributable to non-controlling interests		**–**	(10)
Non-controlling interests other movements		**(2)**	–
Total items that will not be reclassified subsequently to profit or loss		**(3)**	(94)
Total other comprehensive (expense)/income recognised directly in equity		**(2)**	183
Total comprehensive income		**743**	1,017
Total comprehensive income is attributable to:			
Equity holders of the Co-operative		**737**	1,087
Non-controlling interests		**6**	(70)
Total comprehensive income		**743**	1,017

The accompanying notes form part of these financial statements.

STATEMENT OF FINANCIAL POSITION

AS AT 31 JULY 2017

		GROUP $ MILLION	
	NOTES	**31 JULY 2017**	31 JULY 2016
ASSETS			
Current assets			
Cash and cash equivalents		**393**	369
Trade and other receivables	9	**2,303**	1,625
Inventories	10	**2,593**	2,401
Tax receivable		**32**	13
Derivative financial instruments		**580**	451
Assets held for sale		**–**	87
Other current assets		**181**	145
Total current assets		**6,082**	5,091
Non-current assets			
Property, plant and equipment	13	**6,391**	6,172
Equity accounted investments	16	**887**	960
Livestock	14	**319**	342
Intangible assets	15	**3,115**	3,142
Deferred tax assets	18	**363**	410
Derivative financial instruments		**239**	417
Other non-current assets		**446**	584
Total non-current assets		**11,760**	12,027
Total assets		**17,842**	17,118
LIABILITIES			
Current liabilities			
Bank overdraft		**11**	12
Borrowings	7	**1,112**	955
Trade and other payables	11	**2,117**	2,169
Owing to suppliers	12	**1,330**	719
Tax payable		**34**	18
Derivative financial instruments		**43**	43
Provisions	19	**40**	47
Other current liabilities		**44**	35
Total current liabilities		**4,731**	3,998
Non-current liabilities			
Borrowings	7	**5,151**	5,397
Derivative financial instruments		**547**	569
Provisions	19	**148**	152
Deferred tax liabilities	18	**9**	44
Other non-current liabilities		**8**	11
Total non-current liabilities		**5,863**	6,173
Total liabilities		**10,594**	10,171
Net assets		**7,248**	6,947
EQUITY			
Subscribed equity		**5,858**	5,833
Retained earnings		**1,637**	1,384
Foreign currency translation reserve	17	**(552)**	(428)
Hedge reserves	17	**192**	64
Other reserves		**5**	6
Total equity attributable to equity holders of the Co-operative		**7,140**	6,859
Non-controlling interests		**108**	88
Total equity		**7,248**	6,947

The accompanying notes form part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 JULY 2017

	ATTRIBUTABLE TO EQUITY HOLDERS OF THE CO-OPERATIVE							
GROUP $ MILLION	SUBSCRIBED EQUITY	RETAINED EARNINGS	FOREIGN CURRENCY TRANSLATION RESERVE	HEDGE RESERVES	OTHER RESERVES	TOTAL	NON-CONTROLLING INTERESTS	TOTAL EQUITY
As at 1 August 2016	**5,833**	**1,384**	**(428)**	**64**	**6**	**6,859**	**88**	**6,947**
Profit after tax	**–**	**734**	**–**	**–**	**–**	**734**	**11**	**745**
Other comprehensive income/(expense)	**–**	**–**	**(124)**	**128**	**(1)**	**3**	**(5)**	**(2)**
Total comprehensive income/(expense)	**–**	**734**	**(124)**	**128**	**(1)**	**737**	**6**	**743**
Transactions with equity holders in their capacity as equity holders:								
Dividend paid to equity holders of the Co-operative	**–**	**(481)**	**–**	**–**	**–**	**(481)**	**–**	**(481)**
Equity instruments issued	**25**	**–**	**–**	**–**	**–**	**25**	**42**	**67**
Dividend paid to non-controlling interests	**–**	**–**	**–**	**–**	**–**	**–**	**(28)**	**(28)**
As at 31 July 2017	**5,858**	**1,637**	**(552)**	**192**	**5**	**7,140**	**108**	**7,248**
As at 1 August 2015	5,814	1,289	(110)	(537)	17	6,473	186	6,659
Profit after tax	–	810	–	–	–	810	24	834
Other comprehensive income/(expense)	–	5	(318)	601	(11)	277	(94)	183
Total comprehensive income/(expense)	–	815	(318)	601	(11)	1,087	(70)	1,017
Transactions with equity holders in their capacity as equity holders:								
Dividend paid to equity holders of the Co-operative	–	(720)	–	–	–	(720)	–	(720)
Equity instruments issued	19	–	–	–	–	19	–	19
Dividend paid to non-controlling interests	–	–	–	–	–	–	(28)	(28)
As at 31 July 2016	5,833	1,384	(428)	64	6	6,859	88	6,947

The accompanying notes form part of these financial statements.

CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 JULY 2017

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Cash flows from operating activities		
Profit before net finance costs and tax	1,120	1,431
Adjustments for:		
Foreign exchange gains	(1)	(365)
Depreciation and amortisation	526	570
Other	15	(44)
	540	161
Decrease/(increase) in working capital:		
Inventories	(177)	597
Trade and other receivables	(634)	485
Amounts owing to suppliers	745	560
Payables and accruals	(100)	171
Other movements	(48)	(42)
Total	(214)	1,771
Cash generated from operations	1,446	3,363
Net taxes paid	(70)	(85)
Net cash flows from operating activities	1,376	3,278
Cash flows from investing activities		
Cash was provided from:		
– Proceeds from sale of business operations	–	230
– Proceeds from disposal of property, plant and equipment	105	26
– Proceeds from sale of livestock	62	35
– Proceeds from sale of investments in shares	–	78
– Other cash inflows	51	26
Cash was applied to:		
– Acquisition of property, plant and equipment	(690)	(859)
– Acquisition of livestock	(89)	(95)
– Acquisition of intangible assets	(103)	(85)
– Co-operative support loans	–	(383)
– Advances to and investments in equity accounted investees	(42)	(41)
– Other cash outflows	–	(26)
Net cash flows from investing activities	(706)	(1,094)
Cash flows from financing activities		
Cash was provided from:		
– Proceeds from borrowings	4,174	4,909
– Interest received	13	7
– Other cash inflows	38	–
Cash was applied to:		
– Interest paid	(393)	(415)
– Repayment of borrowings	(3,968)	(5,815)
– Dividends paid to non-controlling interests	(28)	(28)
– Dividends paid to equity holders of the Co-operative	(456)	(701)
– Other cash outflows	(2)	(7)
Net cash flows from financing activities	(622)	(2,050)
Net increase in cash and cash equivalents	48	134
Cash and cash equivalents at the beginning of the year	357	303
Effect of exchange rate changes on cash balances	(23)	(80)
Cash and cash equivalents at the end of the year	382	357
Reconciliation of closing cash balances to the statement of financial position:		
Cash and cash equivalents	393	369
Bank overdraft	(11)	(12)
Closing cash balances	382	357

The accompanying notes form part of these financial statements.

BASIS OF PREPARATION

FOR THE YEAR ENDED 31 JULY 2017

A) GENERAL INFORMATION

Fonterra Co-operative Group Limited (Fonterra, the Company or the Co-operative) is a co-operative company incorporated and domiciled in New Zealand. Fonterra is registered under the Companies Act 1993 and the Co-operative Companies Act 1996, and is an FMC Reporting Entity under the Financial Markets Conduct Act 2013. Fonterra is also required to comply with the Dairy Industry Restructuring Act 2001.

These financial statements comprise Fonterra and its subsidiaries (together referred to as the Group) and the Group's interest in its equity accounted investees after adjustments to align to the accounting policies of the Group.

The Group operates predominantly in the international dairy industry. The Group is primarily involved in the collection, manufacture and sale of milk and milk-derived products and in fast-moving consumer goods and foodservice businesses.

B) BASIS OF PREPARATION

These financial statements comply with International Financial Reporting Standards (IFRS). These financial statements also comply with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and have been prepared in accordance with Generally Accepted Accounting Practice (GAAP) applicable to for-profit entities.

These financial statements are prepared on a historical cost basis, except for derivative financial instruments, the investment in Beingmate Baby & Child Food Co., Ltd., livestock and the hedged risks on certain debt instruments, which are recognised at their fair values.

These financial statements are presented in New Zealand dollars ($ or NZD), which is Fonterra's functional currency, and rounded to the nearest million, except where otherwise stated.

Significant accounting policies which are relevant to an understanding of the financial statements and summarise the measurement basis used are provided throughout the Notes in blue frames.

In the process of applying the Group's accounting policies, management make a number of judgements, estimates of future events, and assumptions. These are all believed to be reasonable based on the most current set of circumstances available to the Group. Judgements and estimates that have the most significant effect on the amounts recognised in the financial statements are described below and in the following notes:

Intangible assets (Note 15)

The recoverability of the carrying value of goodwill and indefinite life brands is assessed at least annually to ensure they are not impaired. Performing this assessment requires management to estimate future cash flows, pre-tax discount rates and terminal growth rates.

Investment in Beingmate Baby & Child Food Co., Ltd. (Beingmate) (Note 16)

Throughout the year, Beingmate's shares traded significantly below the share price at the time Fonterra acquired its investment. In addition, Beingmate reported losses for the full year ended December 2016 and the half year ended 30 June 2017. As a result the carrying value of the investment has been assessed for impairment. In previous periods a discounted cash flow forecast was used to perform this assessment. However, the short-term uncertainty associated with the market's response to regulatory changes, which has had an adverse impact on Beingmate's financial performance, means that as at 31 July 2017 a fair value methodology has been applied. The fair value applied is an estimate of what a market participant would pay for a similar stake in Beingmate under current market conditions. The market fundamentals remain strong and the changes to the regulatory regime, anticipated to be effective from 1 January 2018, are expected to have a positive impact on Beingmate's financial performance. However, the value of the investment calculated on a fair value basis supports a carrying value of $617 million, therefore an impairment loss of $35 million has been recognised in the financial year.

Provisions and contingent liabilities (Note 19)

Legal counsel or other experts are consulted on matters that may give rise to a provision or a contingent liability. Estimates and assumptions are made in determining the likelihood, amount and timing of cash outflows when the outcome is uncertain.

Deferred tax assets (Note 18)

Deferred tax assets relating to tax losses carried forward can only be recognised if it is probable that they can be used. In assessing the amount of tax losses that can be recognised management has estimated the forecast future taxable profits against which the tax losses carried forward can be utilised.

C) BASIS OF CONSOLIDATION

In preparing these financial statements, subsidiaries are consolidated from the date the Group gains control until the date on which control ceases. The Group's share of results of equity accounted investments is included in the consolidated financial statements from the date that significant influence or joint control commences, until the date that significant influence or joint control ceases. All intercompany transactions are eliminated.

Translation of the financial statements into NZD

The assets and liabilities of Group companies whose functional currency is not NZD are translated into NZD at the year end exchange rate. The revenue and expenses of these companies are translated into NZD at rates approximating those at the dates of the transactions. Exchange differences arising on this translation are recognised in the foreign currency translation reserve. On disposal or partial disposal of an entity, the related exchange differences that were recorded in equity are recognised in the income statement as part of the gain or loss on sale. The financial statements of a subsidiary in a hyperinflationary economy are translated into NZD at the year end exchange rate. The government in Venezuela has established multiple foreign currency systems. For consolidation, Fonterra translates its operations in Venezuela using the rate most representative of the entity's economic circumstances.

D) NEW AND AMENDED INTERNATIONAL FINANCIAL REPORTING STANDARDS

i) New and amended standards adopted by the Group: Impact of adopting NZ IFRS 9 Financial Instruments

NZ IFRS 9 Financial Instruments addresses the classification, measurement and de-recognition of financial assets, financial liabilities, impairment of financial assets and hedge accounting. The hedge accounting rules in NZ IFRS 9 align hedge accounting more closely with Fonterra's risk management activities. Therefore, Fonterra elected to adopt NZ IFRS 9 from 1 August 2016. The impact of adopting NZ IFRS 9 is summarised below:

- Fonterra is now able to achieve hedge accounting for certain interest rate swaps, which was not possible under the accounting standards previously applied.
- For interest rate swaps in place on transition to NZ IFRS 9, the hedging relationship for accounting purposes can only commence on 1 August 2016. This means that these interest rate swaps will not be perfectly matched to the underlying exposure. Any hedge ineffectiveness will continue to be reflected in finance costs.
- Option premium costs and the time value of options are now recognised in other comprehensive income as 'costs of hedging reserve', until the hedged sales transaction is recognised. Under the accounting standards previously applied, these costs were recorded in the income statement when they were incurred. This change is required to be recognised retrospectively, however as it did not have a material impact on Fonterra's financial statements for the year ended 31 July 2016, no change has been made to the comparative numbers.

NZ IFRS 9 required changes in classification, measurement and impairment requirements, none of which were material to Fonterra's financial statements.

ii) New and amended standards issued but not yet effective

New and amended standards that could be expected to have a material impact on the Group's financial statements, which were available for early adoption but have not been adopted, are stated below.

- NZ IFRS 15 Revenue from Contracts with Customers replaces the current guidance on revenue recognition. It requires revenue to be recognised when a customer obtains control of the goods or service, and has the ability to direct the use and obtain the benefits from those goods or services.

  Fonterra has reviewed its main types of contracts with customers. As a result of this review, Fonterra's preliminary assessment is that the application of NZ IFRS 15 will not have a material impact on its financial position or performance.
- NZ IFRS 16 Leases replaces the current guidance on lease accounting. It requires a lease liability, reflecting future lease payments, and a 'right of use asset' to be recognised for most lease contracts. This includes many of the leases currently classified as operating leases for which no asset or liability is reflected on the balance sheet under existing accounting rules. Entities can choose to retain the current accounting treatment for certain short-term leases and leases of low value assets.

  Fonterra has commenced its assessment of the impact of NZ IFRS 16. The policy choices and transition options available in the Standard are currently being evaluated. Therefore the impact of adoption has not yet been fully assessed. Fonterra's operating lease commitments as at reporting date are disclosed in Note 19.

There are no other new or amended standards that are issued but not yet effective that would be expected to have a material impact on the Group.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 JULY 2017

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

PERFORMANCE

This section focuses on Fonterra's financial performance and the returns provided to equity holders.

This section includes the following Notes:

Note 1: Segment reporting

Note 2: Cost of goods sold

Note 3: Earnings per share

Note 4: Profit before net finance costs and tax

1 SEGMENT REPORTING

During the year financial information was viewed by the Fonterra Management Team based on two different management reporting structures. The first, based on operating segments as presented in section (a), the second, a strategic platform view as presented in section (b).

a) Operating segments

The Group has five reportable segments that reflect the Group's management and reporting structure as viewed by the Fonterra Management Team. Transactions between segments are based on estimated market prices.

REPORTABLE SEGMENT	DESCRIPTION
Global Ingredients and Operations	Represents the collection, processing and distribution of New Zealand milk, global sales and marketing of New Zealand and non-New Zealand milk products (including the Quick Service Restaurant businesses in Asia and Greater China), Global Brands and Nutrition, Co-operative Affairs, Fonterra Farm Source™ stores and Group Services.
Oceania	Represents fast-moving consumer goods (FMCG) businesses in New Zealand (including export to the Pacific Islands) and all FMCG and ingredients businesses in Australia (including Milk Supply and Manufacturing). It includes foodservice sales in Australia and New Zealand.
Asia	Represents FMCG and foodservice businesses (excluding the Quick Service Restaurant business) in Asia (excluding Greater China), Africa and the Middle East.
Greater China	Represents FMCG, foodservice (excluding the Quick Service Restaurant business) and farming businesses in Greater China.
Latin America	Represents FMCG and ingredients businesses in South America and the Caribbean.

a) **Operating segments** continued

	GROUP $ MILLION						
	GLOBAL INGREDIENTS AND OPERATIONS	OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	ELIMINATIONS	TOTAL GROUP
Segment income statement							
Year ended 31 July 2017							
External revenue	12,510	2,458	1,509	1,183	1,572	–	19,232
Inter-segment revenue	1,949	458	142	275	8	(2,832)	–
Revenue from sale of goods	14,459	2,916	1,651	1,458	1,580	(2,832)	19,232
Cost of goods sold	(13,039)	(2,400)	(1,159)	(1,082)	(1,125)	2,837	(15,968)
Segment gross profit	1,420	516	492	376	455	5	3,264
Selling and marketing expenses	(170)	(100)	(155)	(99)	(117)	–	(641)
Distribution expenses	(204)	(143)	(35)	(11)	(157)	–	(550)
Administrative and other operating expenses	(738)	(154)	(106)	(108)	(88)	15	(1,179)
Segment operating expenses	(1,112)	(397)	(296)	(218)	(362)	15	(2,370)
Net other operating income	96	86	3	19	2	(16)	190
Net foreign exchange gains/(losses)	31	1	(5)	(1)	3	–	29
Share of profit/(loss) of equity accounted investees	49	–	–	(46)	4	–	7
Segment earnings before net finance costs and tax	484	206	194	130	102	4	1,120
Normalisation adjustments	1	(42)	–	76	–	–	35
Normalised segment earnings before net finance costs and tax	485	164	194	206	102	4	1,155
Normalisation adjustments							(35)
Finance income							34
Finance costs							(389)
Profit before tax							765
Profit before tax includes the following amounts:							
Depreciation	(307)	(51)	(11)	(27)	(39)	–	(435)
Amortisation	(68)	(18)	(3)	(1)	(1)	–	(91)
Normalisation adjustments consist of the following amounts:							
Gain on sale of Darnum manufacturing plant[1]	–	42	–	–	–	–	42
Reduction in the carrying value of investment in Beingmate[2]	–	–	–	(76)	–	–	(76)
Time value of options[3]	(1)	–	–	–	–	–	(1)
Total normalisation adjustments	(1)	42	–	(76)	–	–	(35)
Segment asset information:							
As at and for the year ended 31 July 2017							
Equity accounted investments	215	–	–	662	10	–	887
Capital expenditure[4]	553	188	23	38	49	–	851

1 The $42 million normalisation adjustment relates to other operating income.

2 Of the $76 million normalisation adjustment, $35 million relates to other operating expenses and $41 million to the share of profit/(loss) of equity accounted investees.

3 Of the $1 million normalisation adjustment, $18 million relates to revenue offset by $19 million of net foreign exchange losses.

4 Capital expenditure comprises purchases of property, plant and equipment and intangible assets, and net purchases of livestock.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

a) Operating segments continued

	GROUP $ MILLION						
	GLOBAL INGREDIENTS AND OPERATIONS	OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	ELIMINATIONS	TOTAL GROUP
Segment income statement							
Year ended 31 July 2016							
External revenue	10,636	2,425	1,630	1,008	1,500	–	17,199
Inter-segment revenue	1,505	439	171	13	5	(2,133)	–
Revenue from sale of goods	12,141	2,864	1,801	1,021	1,505	(2,133)	17,199
Cost of goods sold	(10,343)	(2,362)	(1,213)	(742)	(1,042)	2,135	(13,567)
Segment gross profit	1,798	502	588	279	463	2	3,632
Selling and marketing expenses	(168)	(99)	(187)	(132)	(117)	–	(703)
Distribution expenses	(222)	(160)	(38)	(10)	(155)	–	(585)
Administrative and other operating expenses	(778)	(205)	(128)	(85)	(74)	30	(1,240)
Segment operating expenses	(1,168)	(464)	(353)	(227)	(346)	30	(2,528)
Net other operating income	145	97	3	27	20	(26)	266
Net foreign exchange gains/(losses)	30	1	(3)	(5)	(16)	–	7
Share of profit/(loss) of equity accounted investees	59	1	–	(10)	4	–	54
Segment earnings before net finance costs and tax	864	137	235	64	125	6	1,431
Normalisation adjustments	(96)	23	–	–	–	–	(73)
Normalised segment earnings before net finance costs and tax	768	160	235	64	125	6	1,358
Normalisation adjustments							73
Finance income							18
Finance costs							(517)
Profit before tax							932
Profit before tax includes the following amounts:							
Depreciation	(337)	(48)	(13)	(30)	(37)	–	(465)
Amortisation	(72)	(27)	(4)	(1)	(1)	–	(105)
Normalisation adjustments consist of the following amounts:							
Gain on sale of DairiConcepts investment[1]	68	–	–	–	–	–	68
Disposal and impairment of the Australian yoghurt and dairy desserts business[2]	–	(23)	–	–	–	–	(23)
Time value of options[3]	28	–	–	–	–	–	28
Total normalisation adjustments	96	(23)	–	–	–	–	73
Segment asset information:							
As at and for the year ended 31 July 2016							
Equity accounted investments	188	–	–	763	9	–	960
Capital expenditure[4]	632	114	21	131	46	–	944

1 The $68 million normalisation adjustment relates to other operating income.

2 Of the total $23 million, $4 million relates to cost of goods sold and $19 million to other operating expenses.

3 The $28 million normalisation adjustment relates to net foreign exchange gains.

4 Capital expenditure comprises purchases of property, plant and equipment and intangible assets, and net purchases of livestock.

b) Strategic platforms

Strategic platforms are organised on a different basis than the Group's operating segments presented in section a) of this note. The basis of presentation is explained in the table below.

Fonterra considers this information to be useful as it provides more clarity on the financial performance of the ingredients, consumer and foodservice, and China Farms businesses.

PLATFORM	DESCRIPTION
Ingredients	Represents the Global Ingredients and Operations reportable segment, the ingredients businesses in Australia and South America, and excludes the Quick Service Restaurant businesses in Asia and Greater China and unallocated costs.
Consumer and foodservice	
– Oceania	Represents the Oceania reportable segment, excluding the ingredients business in Australia.
– Asia	Represents the Asia reportable segment and the Asia Quick Service Restaurant business reported in Global Ingredients and Operations.
– Greater China	Represents the Greater China reportable segment, excluding China Farms and including the Quick Service Restaurant business in Greater China reported in Global Ingredients and Operations.
– Latin America	Represents the Latin America reportable segment, excluding the ingredients businesses in South America.
China Farms	Represents farming operations in China.

	GROUP 31 JULY 2017								
	INGREDIENTS	CONSUMER AND FOODSERVICE					CHINA FARMS[1]	UNALLOCATED COSTS AND ELIMINATIONS	TOTAL
		OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	TOTAL			
Volume[2] (liquid milk equivalents, billion)	**21.30**	**1.74**	**1.70**	**1.28**	**0.74**	**5.46**	**0.34**	**(4.16)**	**22.94**
Volume[2] (metric tonnes, thousand)	**3,019**	**636**	**310**	**237**	**600**	**1,783**	**26**	**(648)**	**4,180**
Sales revenue[2] ($ million)	**15,284**	**1,952**	**1,810**	**1,277**	**1,478**	**6,517**	**269**	**(2,838)**	**19,232**
Normalised EBIT ($ million)	**943**	**101**	**201**	**209**	**103**	**614**	**1**	**(403)**	**1,155**
Capital employed[3] ($ million)	**7,950**	**463**	**117**	**22**	**270**	**872**	**789**	**(518)**	**9,093**
Return on capital[4]	**10.3%**	**13.5%**	**118.4%**	**680.5%**	**23.3%**	**47.2%**	**NA**		**11.1%**

For the year ended 31 July 2017 the Group's return on capital including intangible assets, goodwill and equity accounted investments, was 8.3 per cent.

	GROUP 31 JULY 2016								
	INGREDIENTS	CONSUMER AND FOODSERVICE					CHINA FARMS	UNALLOCATED COSTS AND ELIMINATIONS	TOTAL
		OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	TOTAL			
Volume[2] (liquid milk equivalents, billion)	22.39	1.83	1.55	0.87	0.62	4.87	0.23	(3.83)	23.66
Volume[2,5] (metric tonnes, thousand)	3,074	698	292	167	643	1,800	16	(577)	4,313
Sales revenue[2] ($ million)	13,005	2,051	1,944	916	1,385	6,296	183	(2,285)	17,199
Normalised EBIT ($ million)	1,204	97	244	131	108	580	(59)	(367)	1,358
Capital employed[3] ($ million)	7,724	489	127	22	284	922	873	(127)	9,392
Return on capital[4]	13.4%	10.9%	133.4%	429.9%	23.6%	41.7%	(6.5)%		12.4%

For the year ended 31 July 2016 the Group's return on capital including intangible assets, goodwill and equity accounted investments, was 9.2 per cent.

1 During the year ended 31 July 2017 the responsibility for the sale of China Farm's milk was transitioned to the Ingredients sales team in Greater China which has had an impact on year on year comparability. The transfer price is reflective of long-term milk price trends in China.

2 Includes sales to other strategic platforms. Total column represents total external sales.

3 Capital employed excludes brands, goodwill and equity accounted investments.

4 Return on capital is calculated as normalised EBIT, less equity accounted investees' earnings, less a notional royalty charge for use of the Group's brands, less a notional tax charge, divided by capital employed.

5 China Farms volumes for the year ended 31 July 2016 (metric tonnes, thousand), have been restated to align to the same product volume to weight conversion methodology as used by the Ingredients business to aid comparability between segments. Previously China Farms volumes were converted to metric tonnes based on the litres of raw milk sold.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

c) Geographical revenue

	GROUP $ MILLION								
	CHINA	REST OF ASIA	AUSTRALIA	NEW ZEALAND	UNITED STATES	EUROPE	LATIN AMERICA	REST OF WORLD	TOTAL
Geographical segment external revenue:									
Year ended 31 July 2017	**3,383**	**5,165**	**1,592**	**2,056**	**1,254**	**838**	**2,162**	**2,782**	**19,232**
Year ended 31 July 2016	2,394	4,829	1,471	1,939	1,305	745	2,053	2,463	17,199

Revenue is allocated to geographical segments on the basis of the destination of the goods sold.

d) Non-current assets

	GROUP $ MILLION							
	GLOBAL INGREDIENTS AND OPERATIONS		OCEANIA		ASIA	GREATER CHINA	LATIN AMERICA	TOTAL GROUP
	NEW ZEALAND	REST OF WORLD	NEW ZEALAND	AUSTRALIA				
Geographical segment non-current assets:								
As at 31 July 2017	**5,479**	**347**	**1,285**	**840**	**738**	**1,481**	**988**	**11,158**
As at 31 July 2016	5,459	301	1,292	740	779	1,648	981	11,200

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Reconciliation of geographical segment's non-current assets to total non-current assets:		
Geographical segment non-current assets	**11,158**	11,200
Deferred tax assets	**363**	410
Derivative financial instruments	**239**	417
Total non-current assets	**11,760**	12,027

2 COST OF GOODS SOLD

Cost of goods sold is primarily made up of New Zealand sourced cost of milk.

New Zealand sourced cost of milk includes the cost of milk supplied by farmer shareholders, supplier premiums paid, and the cost of milk purchased from contract milk suppliers during the financial year.

New Zealand sourced cost of milk supplied by farmer shareholders comprises the volume of milk solids supplied at the Farmgate Milk Price as determined by the Board for the relevant season. In making that determination the Board takes into account the Farmgate Milk Price calculated in accordance with the Farmgate Milk Price Manual, which is independently audited. The Fonterra Farmgate Milk Price Statement sets out information about the Farmgate Milk Price, and how it is calculated by Fonterra. It can be found in the 'Our Financials/Farmgate Milk Prices' section of the Fonterra website.

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Opening inventory	**2,401**	3,025
Cost of milk:		
– New Zealand sourced	**9,471**	6,205
– Non-New Zealand sourced	**932**	944
Other costs	**5,757**	5,794
Closing inventory	**(2,593)**	(2,401)
Total cost of goods sold	**15,968**	13,567

3 EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the profit or loss attributable to equity holders of the Co-operative by the weighted average number of Co-operative shares outstanding during the period.

Diluted earnings per share is determined by adjusting the profit or loss attributable to equity holders of the Co-operative and the weighted average number of Co-operative shares outstanding for the effects of all Co-operative shares with dilutive potential. There were no Co-operative shares with dilutive potential for either of the years presented.

	GROUP	
	31 JULY 2017	31 JULY 2016
Basic and diluted earnings per share attributable to equity holders of the Co-operative ($)	0.46	0.51
Earnings attributable to equity holders of the Co-operative ($ million)	734	810
Weighted average number of shares (thousands of shares)	1,604,744	1,600,825

4 PROFIT BEFORE NET FINANCE COSTS AND TAX

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
The following items have been included in profit before net finance costs and tax:		
Auditors' remuneration:		
– Fees paid for the audit of the financial statements	6	5
– Fees paid for other services[1]	–	–
Operating lease expense	84	94
Research and development costs	81	88
Donations	1	1
Research and development grants received from government	(4)	(4)
Total employee benefits expense	1,966	2,019
Contributions to defined contribution plans included in employee benefits expense	68	69

1 The Group uses the services of PricewaterhouseCoopers on assignments additional to their statutory audit duties where their expertise and experience with the Group are important and auditor independence is not impaired. Other services include other assurance and attestation services $0.1 million (31 July 2016: $0.1 million) and advisory services of $0.1 million (31 July 2016: nil).

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

DEBT AND EQUITY

This section outlines Fonterra's capital structure and the related financing costs. It also provides details on how the funds that finance current and future activities are raised and on how the Group manages liquidity risk and interest rate risk.

This section includes the following Notes:

Note 5: Subscribed equity instruments

Note 6: Dividends paid

Note 7: Borrowings

Note 8: Net finance costs

5 SUBSCRIBED EQUITY INSTRUMENTS

Subscribed equity instruments comprise Co-operative shares and units in the Fonterra Shareholders' Fund (the Fund). Incremental costs directly attributable to equity transactions are recognised as a deduction from subscribed equity.

Co-operative shares, including shares held within the Group

Co-operative shares may only be held by a shareholder supplying milk to the Company (farmer shareholder), by former farmer shareholders for up to three seasons after cessation of milk supply, or by Fonterra Farmer Custodian Limited (the Custodian). Voting rights in the Company are dependent on milk supply supported by Co-operative shares.[1]

	CO-OPERATIVE SHARES (THOUSANDS)
Balance at 1 August 2016	**1,602,703**
Shares issued under the dividend reinvestment plan[2]	**4,230**
Shares surrendered	**–**
Balance at 31 July 2017	**1,606,933**
Balance at 1 August 2015	1,599,094
Shares issued under the dividend reinvestment plan[2]	3,609
Shares surrendered	–
Balance at 31 July 2016	1,602,703

1 These rights are also attached to vouchers when backed by milk supply (subject to limits).

2 Total value of $25 million (31 July 2016:$19 million).

The rights attaching to Co-operative shares are set out in Fonterra's Constitution, available in the 'About Us/Our Governance' section of Fonterra's website.

Units in the Fonterra Shareholders' Fund

The Custodian holds legal title of Co-operative shares of which the Economic Rights have been sold to the Fund on trust for the benefit of the Fund. At 31 July 2017, 126,047,304 Co-operative shares (31 July 2016: 111,991,937) were legally owned by the Custodian, on trust for the benefit of the Fund.

	UNITS (THOUSANDS)
Balance at 1 August 2016	**111,992**
Units issued	**29,933**
Units surrendered	**(15,878)**
Balance at 31 July 2017	**126,047**
Balance at 1 August 2015	105,480
Units issued	27,137
Units surrendered	(20,625)
Balance at 31 July 2016	111,992

The rights attaching to units are set out in the Trust Deed constituting the Fonterra Shareholders' Fund, available in the 'Our Financials/Fonterra Shareolders' Fund' section of Fonterra's website.

Capital management and structure

The Board's objective is to maximise equity holder returns over time by maintaining an optimal capital structure. Trading Among Farmers (TAF) allows shares in Fonterra to be traded between shareholders, on the Fonterra Shareholders' Market (a private market operated by NZX Limited). The Fund supports this by allowing investors, including farmers, to trade in units backed by Economic Rights in Fonterra. The Fund also allows farmer shareholders to acquire units and exchange them for shares in Fonterra, and to exchange shares for units and dispose of those units on the NZX or ASX.

5 SUBSCRIBED EQUITY INSTRUMENTS CONTINUED

The Group provides returns to farmer shareholders through a milk price, and to equity holders through dividends and changes in the Company's share price.

The Fund is subject to the issue and redemption of units at the discretion of Fonterra and Fonterra's farmer shareholders. Fonterra has an interest in ensuring the stability of the Fund and has established a Fund Size Risk Management Policy, which requires that the number of units on issue remain within specified limits and that within these limits, the number of units is managed appropriately. Fonterra may use a range of measures to ensure the Fund size remains within the specified limits, including introducing or cancelling a dividend reinvestment plan, operating a unit and/or share repurchase programme and issuing new shares.

6 DIVIDENDS PAID

All Co-operative shares, including those held by the Custodian on trust for the benefit of the Fund, are eligible to receive dividends if declared by the Board. Dividends paid to the Custodian are passed on to unit holders by the FSF Management Company Limited (the Manager).

Dividends are recognised as a liability in the Group's financial statements in the period in which they are declared by the Board.

The Dividend Reinvestment Plan applied to all dividends in the table below.

	$ MILLION	
DIVIDENDS	YEAR ENDED 31 JULY 2017	YEAR ENDED 31 JULY 2016
2017 Interim dividend – 20 cents per share[1]	321	–
2016 Final dividend – 10 cents per share[2]	160	–
2016 Interim dividend – 10 cents per share[3]	–	160
2016 Interim dividend – 20 cents per share[4]	–	320
2015 Final dividend – 15 cents per share[5]	–	240

1 Declared on 21 March 2017 and paid on 20 April 2017 to all Co-operative shares on issue at 5 April 2017.
2 Declared on 18 August 2016 and paid on 9 September 2016 to all Co-operative shares on issue at 1 September 2016.
3 Declared on 16 May 2016 and paid on 7 June 2016 to all Co-operative shares on issue at 30 May 2016.
4 Declared on 22 March 2016 and paid on 20 April 2016 to all Co-operative shares on issue at 8 April 2016.
5 Declared on 23 September 2015 and paid on 20 October 2015 to all Co-operative shares on issue at 8 October 2015.

Dividend declared after balance date

On 23 September 2017, the Board declared a final dividend of 20 cents per share, to be paid on 20 October 2017 to all Co-operative shares on issue as at 9 October 2017.

Fonterra has a Dividend Reinvestment Plan, where eligible shareholders can choose to reinvest all or part of their dividend in additional Co-operative shares. The Dividend Reinvestment Plan does apply to this dividend. Participation in the Dividend Reinvestment Plan requires shareholders to submit an election notice for participation by 9 October 2017. Full details of the Dividend Reinvestment Plan are available in the 'Dividends' section of Fonterra's website.

7 BORROWINGS

The Group borrows in the form of bonds, bank facilities and other financial instruments. The interest expense incurred on Fonterra's borrowings is shown in Note 8.

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost using the effective interest method, with the hedged risks on certain debt instruments measured at fair value. Details of the Group's hedge accounting policies are included in Note 17 Financial Risk Management.

Economic net interest-bearing debt

Economic net interest-bearing debt reflects the effect of debt hedging in place at balance date.

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Net interest-bearing debt position		
Total borrowings	6,263	6,352
Cash and cash equivalents	(393)	(369)
Interest-bearing advances[1]	(435)	(464)
Bank overdraft	11	12
Net interest-bearing debt	5,446	5,531
Value of derivatives used to manage changes in hedged risks on debt instruments	155	(58)
Economic net interest-bearing debt	5,601	5,473

1 Includes $135 million of Fonterra Co-operative Support Loan repayments relating to the 2016/17 season (31 July 2016: nil).

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

7 BORROWINGS CONTINUED

Total borrowings in the table above are represented by:

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Commercial paper	**164**	454
Bank loans	**854**	879
Finance leases[1]	**137**	143
Capital notes[2]	**35**	35
NZX-listed bonds	**500**	499
Medium-term notes	**4,573**	4,342
Total borrowings	**6,263**	6,352
Included within the statement of financial position as follows:		
Total current borrowings	**1,112**	955
Total non-current borrowings	**5,151**	5,397
Total borrowings	**6,263**	6,352

1 Finance leases are secured over the related item of property, plant and equipment (Note 13).

2 Capital notes are unsecured subordinated borrowings.

3 All other borrowings are unsecured and unsubordinated.

Leverage ratios

The Board closely monitors the Group's leverage ratios, which include the gearing ratio and debt coverage ratios (debt payback and interest coverage ratios). The primary debt payback ratios comprise funds from operations divided by economic net interest-bearing debt, and economic net interest-bearing debt divided by EBITDA (Earnings Before Interest, Tax, Depreciation and Amortisation). Debt pay-back ratios are adjusted for the impact of operating leases. The gearing ratio is calculated as economic net interest-bearing debt divided by total capital. Economic net interest-bearing debt is calculated in the table above. Total capital is calculated as equity, as presented in the statement of financial position (excluding hedge reserves), plus economic net interest-bearing debt. The gearing ratio as at 31 July 2017 was 44.3 per cent (31 July 2016: 44.3 per cent). The Group is not subject to externally imposed capital requirements.

Finance leases included in total borrowings are represented by:

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Finance leases – minimum lease payments		
Not later than one year	**17**	17
Later than one year and not later than five years	**144**	161
Later than five years	**5**	6
	166	184
Future finance charges on finance leases	**(29)**	(41)
Present value of finance leases	**137**	143
The present value of finance leases is as follows:		
Not later than one year	**6**	6
Later than one year and not later than five years	**126**	131
Later than five years	**5**	6
Total present value of finance leases	**137**	143

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity risk is to ensure that it will always have sufficient funds to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group has a policy in place to ensure that it has sufficient cash or facilities on demand to meet expected operational expenses for a period of at least 80 days, including the servicing of financial obligations. This excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters. In such situations back-up funding lines are maintained and as set out in the Company's constitution, the Company can defer payments to farmer shareholders if necessary.

The Group manages its liquidity by retaining cash and marketable securities, the availability of funding from an adequate amount of committed credit facilities and the ability to close out market positions. Fonterra's funding facilities are reviewed at least annually, which is one of the key financial risk management activities undertaken by the Group to ensure an appropriate maturity profile given the nature of the Group's business. At balance date the Group had undrawn lines of credit totalling $3,811 million (31 July 2016: $3,723 million).

7 BORROWINGS CONTINUED

Liquidity and refinancing risks are also managed by ensuring that Fonterra can maintain access to funding markets throughout the world. To that end, Fonterra maintains debt issuance programmes in a number of key markets and manages relationships with international investors.

Exposure to liquidity risk

The following tables show the timing of the gross contractual cash flows of the Group's financial instruments.

	GROUP $ MILLION					
	AS AT 31 JULY 2017					
	CARRYING AMOUNT	CONTRACTUAL CASH FLOWS	3 MONTHS OR LESS	3–12 MONTHS	1–5 YEARS	MORE THAN 5 YEARS
Non-derivative financial liabilities						
Borrowings						
– Commercial paper	(164)	(165)	(165)	–	–	–
– Bank loans	(854)	(904)	(218)	(189)	(497)	–
– Finance leases	(137)	(166)	(4)	(13)	(144)	(5)
– Capital notes	(35)	(42)	–	(1)	(6)	(35)
– NZX-listed bonds	(500)	(609)	(11)	(11)	(430)	(157)
– Medium-term notes	(4,573)	(5,806)	(232)	(537)	(2,168)	(2,869)
Bank overdraft	(11)	(12)	(12)	–	–	–
Owing to suppliers	(1,330)	(1,330)	(1,330)	–	–	–
Trade and other payables (excluding employee entitlements)	(1,841)	(1,841)	(1,841)	–	–	–
Financial guarantees issued[1]	–	(1)	(1)	–	–	–
Total non-derivative financial liabilities	(9,445)	(10,876)	(3,814)	(751)	(3,245)	(3,066)
Derivative financial instruments						
Gross settled derivatives						
– Inflow		22,210	10,964	7,921	1,364	1,961
– Outflow		(22,052)	(10,838)	(7,579)	(1,451)	(2,184)
Total gross settled derivative financial instruments	312	158	126	342	(87)	(223)
Net settled derivatives	(83)	(122)	(5)	9	(130)	4
Total financial instruments	(9,216)	(10,840)	(3,693)	(400)	(3,462)	(3,285)

1 Maximum cash flows under guarantees provided by the Group.

	GROUP $ MILLION					
	AS AT 31 JULY 2016					
	CARRYING AMOUNT	CONTRACTUAL CASH FLOWS	3 MONTHS OR LESS	3–12 MONTHS	1–5 YEARS	MORE THAN 5 YEARS
Non-derivative financial liabilities						
Borrowings						
– Commercial paper	(454)	(456)	(365)	(91)	–	–
– Bank loans	(879)	(911)	(368)	(135)	(408)	–
– Finance leases	(143)	(184)	(4)	(13)	(161)	(6)
– Capital notes	(35)	(42)	–	(1)	(6)	(35)
– NZX-listed bonds	(499)	(630)	(11)	(11)	(87)	(521)
– Medium-term notes	(4,342)	(5,653)	(33)	(175)	(2,643)	(2,802)
Bank overdraft	(12)	(12)	(12)	–	–	–
Owing to suppliers	(719)	(719)	(719)	–	–	–
Trade and other payables (excluding employee entitlements)	(1,867)	(1,867)	(1,867)	–	–	–
Financial guarantees issued[1]	–	(6)	(6)	–	–	–
Total non-derivative financial liabilities	(8,950)	(10,480)	(3,385)	(426)	(3,305)	(3,364)
Derivative financial instruments						
Gross settled derivatives						
– Inflow		24,524	13,975	7,236	1,601	1,712
– Outflow		(24,332)	(13,837)	(6,975)	(1,647)	(1,873)
Total gross settled derivative financial instruments	461	192	138	261	(46)	(161)
Net settled derivatives	(205)	(106)	(28)	1	(98)	19
Total financial instruments	(8,694)	(10,394)	(3,275)	(164)	(3,449)	(3,506)

1 Maximum cash flows under guarantees provided by the Group.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

8 NET FINANCE COSTS

Interest income and expense is recognised on an accrual basis in profit or loss, using the effective interest method.

Finance costs also include the changes in fair value relating to derivatives used to manage interest rate risk, and the associated changes in fair value of the borrowings designated in a hedge relationship. Details of the Group's hedge accounting policies are included in Note 17 Financial Risk Management.

Fonterra Co-operative Support Loans
Fonterra Co-operative Support Loans are initially recorded at fair value. As the loans have interest rates that are below market rates, there is a difference between the cash advanced and the loans' fair value. This difference is recorded within finance costs at the date Fonterra is contractually committed to advance the funds. Finance income is recognised using the notional interest rate implicit in the loans, over the periods until the loans are repaid.

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Finance income[1]	**34**	18
Total interest expense at amortised cost[2]	**(427)**	(434)
Changes in fair value relating to:		
– Borrowings designated in a hedge relationship	**157**	(111)
– Derivatives designated in a hedge relationship	**(123)**	129
– Derivatives where hedge accounting has not been applied	**4**	(101)
Total interest income/(expense) from fair value movements	**38**	(83)
Finance costs	**(389)**	(517)
Net finance costs	**(355)**	(499)

1 Finance income includes $24 million of fair value adjustments relating to the Fonterra Co-operative Support Loans. For the year ended 31 July 2016, $36 milliion of fair value adjustments are included within interest expense at amortised cost.

2 Includes interest expense of $22 million (31 July 2016: $22 million) relating to derivatives where hedge accounting has not been applied, and cash flow hedge effectiveness reclassified to profit or loss.

Interest rate risk

Details of how the Group manages interest rate risk is included in Note 17 Financial Risk Management.

WORKING CAPITAL

This section provides information about the primary elements of Fonterra's working capital. Working capital represents the short term operating assets and liabilities generated by Fonterra. Movements in these items have a direct impact on the net cash flows generated from operating activities.

This section includes the following Notes:

Note 9: Trade and other receivables

Note 10: Inventories

Note 11: Trade and other payables

Note 12: Owing to suppliers

9 TRADE AND OTHER RECEIVABLES

Revenue from sale of goods is recognised at the fair value of the consideration received or receivable, net of returns, discounts and allowances. Revenue is recognised when the amount can be reliably measured, significant risks and rewards of ownership of the inventory have passed to the buyer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, and there is no continuing management involvement with the goods.

Trade receivables are amounts due from customers for goods sold. Trade receivables are recognised initially at their fair value, which is represented by their face value, and subsequently measured at the amount expected to be collected.

Estimates are used in determining the level of receivables that may not be collected. A provision for impairment is established when there is evidence that the Group will not be able to collect all amounts due.

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Trade receivables	**2,015**	1,302
Less: provision for impairment of trade receivables	**(23)**	(20)
Trade receivables net of provision for impairment	**1,992**	1,282
Receivables from related parties[1]	**32**	18
Other receivables	**162**	201
Total receivables	**2,186**	1,501
Prepayments	**117**	124
Total trade and other receivables	**2,303**	1,625

1 There were no provisions for impairment of receivables from related parties.

Credit risk

Details of how the Group manages credit risk is included in Note 17 Financial Risk Management.

The aging profile of the Group's trade and other receivables (excluding prepayments) is as follows:

GROUP $ MILLION	CURRENT	LESS THAN 1 MONTH PAST DUE	MORE THAN 1 MONTH BUT LESS THAN 3 MONTHS PAST DUE	MORE THAN 3 MONTHS PAST DUE	TOTAL
As at 31 July 2017	**1,941**	**168**	**46**	**31**	**2,186**
As at 31 July 2016	1,303	130	38	30	1,501

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

10 INVENTORIES

Inventories are stated at the lower of cost or net realisable value on a first-in-first-out basis.

In the case of manufactured inventories, cost includes all direct costs plus the portion of fixed and variable production overheads incurred in bringing inventories into their present location and condition.

Net realisable value is the estimated selling price, less the costs of completion and selling expenses.

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Raw materials	**680**	647
Finished goods	**1,950**	1,793
Impairment of finished goods	**(37)**	(39)
Total inventories	**2,593**	2,401

11 TRADE AND OTHER PAYABLES

Trade and other payables, excluding amounts owing to farmer shareholders and New Zealand contract milk suppliers, are recognised at the amount invoiced by the supplier. Due to their short-term nature, they are not discounted.

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Trade payables	**1,683**	1,640
Amounts due to related parties	**21**	16
Other payables	**137**	211
Total trade and other payables (excluding employee entitlements)	**1,841**	1,867
Employee entitlements	**276**	302
Total trade and other payables	**2,117**	2,169

12 OWING TO SUPPLIERS

Amounts owing to suppliers are amounts Fonterra owes to farmer shareholders and New Zealand contract milk suppliers for the collection of milk, which includes end of season adjustments, offset by amounts owing from farmer shareholders for goods and services provided to them by Fonterra.

These amounts are recognised at the amount due to the supplier for the milk provided. Due to their short-term nature, they are not discounted.

The Board uses its discretion in establishing the rate at which Fonterra will pay suppliers for the milk supplied over the season. This is referred to as the advance rate. The following table provides a breakdown of the advance payments made to suppliers:

	GROUP	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Owing to suppliers ($ million)	**1,330**[1]	719
Farmgate Milk Price (per kgMS)	**$6.12**[2]	$3.90
Of this amount:		
– Total advance payments made during the year	**$5.21**	$3.48
– Total owing as at 31 July	**$0.91**	$0.42
Amount advanced during the year as a percentage of the milk price for the season ended 31 May	**85%**	89%

1 This amount is after offsetting $135 million Fonterra Co-operative Support Loan repayments relating to the 2016/17 season (31 July 2016: nil).

2 Represents the price for milk supplied on standard terms of supply. The Fonterra Farmgate Milk Price Statement sets out information about the Farmgate Milk Price as calculated in accordance with the Farmgate Milk Price Manual and the price for milk supplied on standard terms. It can be found in the 'Our Financials/Farmgate Milk Prices' section of the Fonterra website.

LONG-TERM ASSETS

This section provides information about the investments Fonterra has made in long-term assets to operate the business and generate returns to equity holders. These assets include physical assets such as land and buildings and livestock, and non-physical assets such as brands and goodwill. This section also explains the estimates and judgements applied in the measurement of these assets.

This section includes the following Notes:

Note 13: Property, plant and equipment

Note 14: Livestock

Note 15: Intangible assets

13 PROPERTY, PLANT AND EQUIPMENT

Items of property, plant and equipment are measured at cost less accumulated depreciation and impairment losses. Cost includes the purchase consideration and those costs directly attributable to bringing the asset to the location and condition necessary for its intended use. It also includes financing costs directly attributable to the acquisition, production or construction of the asset. Subsequent costs are capitalised only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of any replaced part is derecognised. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

The assets' residual values and useful lives are reviewed and adjusted, where required, each financial year.

Gains and losses on disposals are determined by comparing the disposal proceeds with the carrying amount, and are recognised in the income statement.

Depreciation

Depreciation is calculated on a straight line basis to allocate the cost of the asset, less any residual value, over its estimated useful life. The range of estimated useful lives for each class of property, plant and equipment is as follows:

– Land	Indefinite
– Buildings and leasehold improvements	15–60 years
– Plant, vehicles and equipment	3–55 years

	GROUP $ MILLION				
	LAND	BUILDINGS AND LEASEHOLD IMPROVEMENTS	PLANT, VEHICLES AND EQUIPMENT	CAPITAL WORK IN PROGRESS	TOTAL
As at 31 July 2017					
Cost	**348**	**2,644**	**7,740**	**535**	**11,267**
Accumulated depreciation and impairment	**–**	**(953)**	**(3,923)**	**–**	**(4,876)**
Net book value at 31 July 2017	**348**	**1,691**	**3,817**	**535**	**6,391**
As at 31 July 2016					
Cost	339	2,479	7,231	718	10,767
Accumulated depreciation and impairment	–	(883)	(3,712)	–	(4,595)
Net book value at 31 July 2016	339	1,596	3,519	718	6,172

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

13 PROPERTY, PLANT AND EQUIPMENT CONTINUED

	GROUP $ MILLION				
	LAND	BUILDINGS AND LEASEHOLD IMPROVEMENTS	PLANT, VEHICLES AND EQUIPMENT	CAPITAL WORK IN PROGRESS	TOTAL
Net book value					
As at 1 August 2016	**339**	**1,596**	**3,519**	**718**	**6,172**
Additions[1]	**3**	**13**	**53**	**685**	**754**
Transfer from capital work in progress	**15**	**205**	**644**	**(864)**	**–**
Hyperinflationary movements	**2**	**4**	**2**	**2**	**10**
Depreciation charge	**–**	**(92)**	**(343)**	**–**	**(435)**
Impairment reversal/(losses)	**–**	**2**	**–**	**–**	**2**
Disposals	**(8)**	**(9)**	**(29)**	**(2)**	**(48)**
Foreign currency translation	**(3)**	**(28)**	**(29)**	**(4)**	**(64)**
As at 31 July 2017	**348**	**1,691**	**3,817**	**535**	**6,391**
Net book value					
As at 1 August 2015	366	1,505	3,185	1,103	6,159
Additions[1]	1	6	21	769	797
Transfer from capital work in progress	11	313	794	(1,118)	–
Hyperinflationary movements	2	4	3	1	10
Depreciation charge	–	(108)	(357)	–	(465)
Impairment losses	–	(2)	(16)	–	(18)
Disposals	(5)	(6)	(24)	(3)	(38)
Foreign currency translation	(36)	(116)	(87)	(34)	(273)
As at 31 July 2016	339	1,596	3,519	718	6,172

1 Additions include borrowing costs of $10 million (2016: $19 million) capitalised using a weighted average interest rate of 5.85 per cent (2016: 6.00 per cent).

Leased assets

Leases of property, plant and equipment where the Group assumes substantially all the risks and rewards of ownership are classified as finance leases.

Assets under finance leases are recognised as property, plant and equipment in the statement of financial position. They are recognised initially at their fair value or, if lower, at the present value of the minimum lease payments. A corresponding liability is established and each lease payment allocated between the liability and interest expense using the effective interest method. The assets recognised are depreciated on the same basis as equivalent property, plant and equipment.

Leases that are not finance leases are classified as operating leases and the leased assets are not recognised on the Group's statement of financial position. Operating lease payments are recognised as an expense on a straight line basis over the lease term.

The net book value of property, plant and equipment subject to finance leases is as follows:

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Land	**5**	5
Building and leasehold improvements	**93**	97
Plant and equipment	**22**	25
Net book value of property, plant and equipment subject to finance leases	**120**	127

14 LIVESTOCK

The Group's livestock balance primarily comprises dairy cows, which provide Fonterra with a quality milk source in China.

Livestock is measured at fair value less costs to sell, with any resulting gain or loss recognised in the income statement. The Group's dairy cow herd comprises both immature and mature livestock.

Immature livestock comprises dairy cows that are intended to be reared to maturity. These cows are held to produce milk or offspring, but have not yet produced their first calf and begun milk production. Costs incurred in rearing immature livestock are capitalised to the statement of financial position. The fair value of immature livestock is determined using a market approach, adjusted to reflect the age of the herd.

Mature livestock includes dairy cows that have produced their first calf and begun milk production. Costs incurred in relation to mature livestock are recognised in the income statement. The fair value of mature dairy cows is determined using a discounted cash flow methodology. The Group also holds immaterial quantities of other livestock.

The quantity of livestock owned by the Group is presented below:

	HEADCOUNT	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Immature dairy cows	**46,269**	58,055
Mature dairy cows	**39,280**	36,516
Other livestock	**3,664**	2,802
Total livestock headcount	**89,213**	97,373

During the year the Group collected 371 million litres of milk (31 July 2016: 279 million litres) from its dairy cows.

The value of livestock at 31 July is as follows:

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Opening balance	**342**	331
Purchase of livestock	**7**	17
Rearing costs of immature livestock	**82**	77
Change in fair value – birth and growth	**(5)**	20
Change in fair value – price changes	**10**	1
Sale of livestock	**(98)**	(68)
Effect of movements in exchange rates	**(19)**	(36)
Closing balance	**319**	342
Represented by:		
Immature dairy cows	**160**	197
Mature dairy cows	**158**	144
Other livestock	**1**	1
Total livestock at 31 July	**319**	342

Valuation techniques and significant unobservable inputs

The following table shows the relationship between the significant unobservable inputs and fair value measurement for mature livestock:

TYPE	VALUATION TECHNIQUE	SIGNIFICANT UNOBSERVABLE INPUTS	RELATIONSHIP BETWEEN KEY UNOBSERVABLE INPUTS AND FAIR VALUE MEASUREMENT
Mature livestock	Discounted cash flows	Raw milk yield	A 5% increase/(decrease) in the raw milk yield would result in a $11 million (31 July 2016: $10 million) increase/(decrease) in fair value.
		Milk price	A 5% increase/(decrease) in the selling price of milk would result in a $22 million (31 July 2016: $19 million) increase/(decrease) in fair value.

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FOR THE YEAR ENDED 31 JULY 2017

15 INTANGIBLE ASSETS

The significant intangible assets recognised by the Group are goodwill, brands and software assets.

Goodwill

Goodwill represents the premium paid by the Group over the fair value of the Group's share of the net identifiable assets of an acquired subsidiary at the date of acquisition. It is initially recognised at cost and is subsequently measured at cost less accumulated impairment losses.

Goodwill is not amortised but is instead tested for impairment annually, or more frequently if there is an indicator of impairment.

Brands and other identifiable intangible assets

Brands that are purchased by the Group are initially recognised at cost, or at their fair value if acquired as part of a business combination. They are subsequently measured at cost less amortisation, if they are finite life brands, and accumulated impairment losses.

Indefinite life brands are not amortised but are instead tested for impairment annually, or more frequently if there is an indicator of impairment. A brand is determined to have an indefinite life where there is an intention to maintain and support the brand for an indefinite period.

Finite life brands are amortised on a straight line basis over the shorter of their contractual or useful economic life, being three to 25 years. They are tested for impairment when an indicator of impairment exists.

Software assets

Software assets, both purchased and internally developed, are capitalised provided there is an identifiable asset that will generate future economic benefits through cost savings or supporting revenue generation. Subsequent costs are capitalised if they extend the useful life or enhance the functionality of the asset.

Software assets amortised on a straight line basis over their estimated useful lives, being three to 10 years. They are tested for impairment when an indicator of impairment exists.

	GROUP $ MILLION					
	GOODWILL	BRANDS	SOFTWARE	SOFTWARE WIP	OTHER	TOTAL INTANGIBLES
As at 31 July 2017						
Cost	**1,076**	**1,690**	**1,223**	**134**	**73**	**4,196**
Accumulated amortisation and impairment	**(3)**	**(114)**	**(910)**	**–**	**(54)**	**(1,081)**
Net book value at 31 July 2017	**1,073**	**1,576**	**313**	**134**	**19**	**3,115**
As at 31 July 2016						
Cost	1,082	1,733	1,192	67	77	4,151
Accumulated amortisation and impairment	(3)	(111)	(838)	–	(57)	(1,009)
Net book value at 31 July 2016	1,079	1,622	354	67	20	3,142

15 INTANGIBLE ASSETS CONTINUED

	GROUP $ MILLION					
	GOODWILL	BRANDS	SOFTWARE	SOFTWARE WIP	OTHER	TOTAL INTANGIBLES
Net book value						
As at 1 August 2016	**1,079**	**1,622**	**354**	**67**	**20**	**3,142**
Additions	**–**	**–**	**6**	**107**	**–**	**113**
Transfer from work in progress	**–**	**–**	**40**	**(40)**	**–**	**–**
Amortisation	**–**	**(3)**	**(87)**	**–**	**(1)**	**(91)**
Foreign currency translation	**(6)**	**(43)**	**–**	**–**	**–**	**(49)**
As at 31 July 2017	**1,073**	**1,576**	**313**	**134**	**19**	**3,115**
Net book value						
As at 1 August 2015	1,099	1,699	350	92	33	3,273
Additions	–	–	2	83	1	86
Transfer from work in progress	–	–	108	(108)	–	–
Amortisation	–	(3)	(101)	–	(1)	(105)
Impairment loss	–	(7)	–	–	–	(7)
Disposals	–	(8)	–	–	(13)	(21)
Foreign currency translation	(20)	(59)	(5)	–	–	(84)
As at 31 July 2016	1,079	1,622	354	67	20	3,142

Amortisation is recognised in other operating expenses in the income statement.

Impairment testing of goodwill and indefinite life brands

Impairment testing is performed annually at the same time each year. In completing the impairment testing, the recoverable amounts are determined on a value in use basis, using a discounted cash flow methodology. The cash flows are based on the Group's three-year strategic business plan which has been prepared taking into account past performance as well as forecast future performance supported by strategic initiatives. Other key assumptions are based on external data where possible.

Brazil consumer and foodservice business

The consumer and foodservice business in Brazil includes goodwill of $143 million (31 July 2016: $145 million) and brands of $266 million (31 July 2016: $270 million).

The long term growth rate applied to the future cash flows at year 10 of the forecast is 4.5 per cent (31 July 2016: 5.3 per cent). The discount rate applied is within the market range of 11.7 per cent to 12.4 per cent (31 July 2016: 12.9 per cent to 13.6 per cent).

Notwithstanding the challenging economic environment in Brazil, the cash flow forecast used to support the carrying value of the consumer and foodservice business in Brazil shows significant growth in each year of the extended five-year forecast period. This growth is supported by the strategic business plan and associated initiatives, and reflects the expected improvement in economic conditions in Brazil. The forecast growth rate used in the following five years is aligned to the expected economic recovery in Brazil.

Using these key assumptions the recoverable amount is equivalent to the carrying value of the consumer and foodservice business in Brazil.

Significant goodwill balance

The consumer and foodservice business in New Zealand includes goodwill of $611 million (31 July 2016: $650 million) and brands of $391 million (31 July 2016: $389 million).

The long-term growth rate applied to the future cash flows is 2.1 per cent (31 July 2016: 2.2 per cent). The discount rate applied is within the market range of 7.7 per cent to 8.3 per cent (31 July 2016: 7.7 per cent to 8.3 per cent).

Significant indefinite life brands balances

The consumer and foodservice businesses in Asia include brands of $624 million (31 July 2016: $662 million).

The average long-term growth rate applied to the future cash flows is 3.1 per cent (31 July 2016: 3.1 per cent). The average discount rate applied is 9.2 per cent (31 July 2016: 9.2 per cent).

Of the total brands held by the Group, 99 per cent (31 July 2016: 99 per cent) have indefinite lives.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

INVESTMENTS

This section provides information about Fonterra's interest in other entities. These investments include subsidiaries and equity accounted investments.

This section includes the following Note:

Note 16: Equity accounted investments

16 EQUITY ACCOUNTED INVESTMENTS

Associates and joint ventures

Associates are those entities in which the Group has significant influence, but not control or joint control, over the financial and operating policies. Joint ventures are those arrangements in which the Group has contractually agreed to share control and where the Group has rights to the net assets rather than rights to the assets and obligations for the liabilities.

For joint ventures and associates the Group applies the equity method of accounting. Under the equity method, the Group recognises its initial investment at cost (including any goodwill identified on acquisition) and subsequently adjusts this for its share of the entities' profits or losses. The Group's share of profits and losses are recognised in the income statement and its share of movements in other comprehensive income is recognised in other comprehensive income. Dividends received from equity accounted investees reduce the carrying amount of the investment.

When the Group's share of losses exceeds its interest in an equity accounted investee, the carrying amount of that interest is reduced to nil and no further losses are recognised except to the extent the Group has an obligation or has made payments on behalf of the investee.

The Group determines at each reporting date whether there is any objective evidence that its investments in equity accounted investees are impaired. If this is the case, the Group recognises any impairment in the income statement.

The Group's significant equity accounted investments are listed below. The ownership interest in these entities is 51 per cent or less and the Group is not considered to exercise a controlling interest.

		OWNERSHIP INTERESTS (%)	
EQUITY ACCOUNTED INVESTEE NAME	COUNTRY OF INCORPORATION AND PRINCIPAL PLACE OF BUSINESS	**AS AT 31 JULY 2017**	AS AT 31 JULY 2016
DMV Fonterra Excipients GmbH & Co KG	Germany	**50**	50
Beingmate Baby & Child Food Co., Ltd[1]	China	**18.8**	18.8
Falcon Dairy Holdings Limited	Hong Kong	**51**	51

1 Carrying value reflectsthe fair value of the investment.

All investees have balance dates of 31 December.

The Group holds investments in a number of joint ventures and associates. The aggregate amount of the Group's share of these equity accounted investments is included in the table below:

	GROUP $ MILLION					
	ASSOCIATES		JOINT VENTURES		TOTAL	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016	**AS AT 31 JULY 2017**	AS AT 31 JULY 2016	**AS AT 31 JULY 2017**	AS AT 31 JULY 2016
Carrying amount of investment	**617**[1]	739	**270**	221	**887**	960
Profit/(loss) from continuing operations	**(42)**	(7)	**49**	61	**7**	54
Other comprehensive income	**–**	–	**–**	5	**–**	5
Total comprehensive income	**(42)**	(7)	**49**	66	**7**	59

1 The carrying value of the Group's investment in Beingmate Baby & Child Food Co., Ltd. includes an impairment of $35 million and a decrease of $47 million from the impacts of foreign exchange.

The Group has provided financial guarantees to certain equity accounted investees as set out in Note 20.

There are no contingent liabilities relating to the Group's interests in joint ventures or equity accounted investees.

FINANCIAL RISK MANAGEMENT

This section outlines the key risk management activities undertaken to manage the Group's exposure to financial risk.

This section includes the following Note:

Note 17: Financial risk management

17 FINANCIAL RISK MANAGEMENT

Financial risks faced by the Group

The Group's overall financial risk management programme focuses primarily on maintaining a prudent financial risk profile that provides flexibility to implement the Group's strategies, while ensuring optimisation of the return on assets. Financial risk management is centralised, which supports compliance with the financial risk management policies and procedures set by the Board.

A summary of the financial risks that impact the Group, how these risks are managed, and other disclosures included in the financial risk management note is presented below.

FINANCIAL RISK/DISCLOSURE ITEM	DESCRIPTION	MANAGEMENT OF RISK
Market Risks		
Foreign exchange risk (Section a)	Impact from changes in foreign exchange rates	*Foreign currency transactions* For foreign currency transactions the Group uses foreign currency forward contracts and foreign currency options to manage foreign exchange risk. *Foreign operations* For investments in foreign operations the Group uses foreign currency denominated borrowings and foreign currency swaps to manage foreign exchange risk. *Foreign denominated borrowings* For foreign denominated borrowings the Group uses cross-currency interest rate swaps to manage foreign exchange and interest rate risk combined.
Interest rate risk (Section b)	Impact from changes in interest rates	The Group uses interest rate swaps to achieve a target ratio of fixed and floating rate exposure on its borrowings.
Commodity price risk (Section c)	Impact from changes in commodity prices	The Group uses commodity derivatives to manage its exposure to commodity price risk. The Group also uses its product mix and sales contract terms to manage the impact of changes in dairy commodity prices on its earnings.
Sensitivity analysis of changes in market risks (Section d)	Sensitivity of the Group's reported profit and equity to changes in market risks	
Impact to reserves in equity (Section e)	Movements in the Group's hedge reserves and foreign currency translation reserve	
Other Risks		
Credit risk (Section f)	Risk of loss to the Group due to customer and counterparty default	The Group sets minimum credit quality requirements, credit limits and uses other credit mitigation tools to manage its credit risk.
Liquidity risk (Note 7)	Risk that the Group will be unable to meet its financial obligations as they fall due	The Group actively manages its minimum on-hand cash facilities, access to committed funds and lines of credit and the maturity profile of its financial obligations.
Fair value measurement (Section g)	Assets and liabilities measured or disclosed at fair value	
Offsetting of financial assets and liabilities (Section h)	Financial asset and financial liability balances that are offset in the balance sheet	
Capital management and structure (Note 5)	The Group's capital structure	The Group actively manages its capital structure through leverage and coverage ratios. The Fonterra Shareholders' Fund removes the redemption risk associated with Co-operative shares.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

17 FINANCIAL RISK MANAGEMENT CONTINUED

Derivative financial instruments and hedge accounting

Derivatives are measured at fair value. Refer to Section g) Fair value measurement for details on how fair value is determined.

The resulting gain or loss on re-measurement is recognised in the income statement immediately, unless the derivative is designated into an effective hedge relationship as a hedging instrument, in which case the timing of recognition in the income statement depends on the nature of the designated hedge relationship.

The Group may designate derivatives as:

- Fair value hedges (where the derivative is used to manage the variability in the fair value of recognised assets and liabilities);
- Cash flow hedges (where the derivative is used to manage the variability in cash flows relating to recognised liabilities or forecast transactions); or
- Net investment hedges (where borrowings or derivatives are used to manage the risk of fluctuation in the translated value of its foreign operations).

Hedge accounting is discontinued when the hedging instrument expires, is terminated, is exercised, or no longer qualifies for hedge accounting.

Fair value hedges

For fair value hedges the following are recognised in the income statement:

- the change in fair value of the hedging instruments; and
- the change in the fair value of the underlying hedged item attributable to the hedged risk.

If the hedge no longer meets the criteria for hedge accounting, hedge accounting is discontinued. The fair value adjustment to the carrying amount of the hedged item upon discontinuance is amortised and recognised in the income statement over the remaining term of the original hedge.

Cash flow hedges

The effective portion of changes in the fair value of the hedging instruments are recognised in other comprehensive income and accumulated in a separate reserve in equity. Subsequently the cumulative amount is transferred to the income statement when the underlying transactions are recognised in the income statement.

The ineffective portion of changes in the fair value of the hedging instruments are recognised immediately in the income statement.

If the hedge no longer meets the criteria for hedge accounting, hedge accounting is discontinued. The cumulative gain or loss previously recognised in other comprehensive income remains there until the forecast transaction occurs, or is immediately recognised in the income statement if the transaction is no longer expected to occur.

Net investment hedges

The effective portion of changes in the fair value of the hedging instruments are recognised in other comprehensive income and transferred to ‘Net foreign exchange gains’ in the income statement when the foreign operation is disposed of, or sold.

The ineffective portion of changes in the fair value of the hedging instruments are recognised immediately in ‘Net foreign exchange gains’ in the income statement.

Costs of hedging

The change in fair value of a hedging instrument relating to the time-value of foreign currency options, and the foreign currency basis component of cross-currency interest rate swaps are recognised in other comprehensive income and accumulated in a separate reserve in equity. Subsequently, the cumulative amount is transferred to the income statement at the same time as the hedged item impacts the income statement.

a) Foreign exchange risk

Nature and exposure of foreign exchange risk

Net foreign exchange gains or losses

Foreign currency transactions are translated using the exchange rate at the dates of transactions. Monetary assets and liabilities denominated in foreign currencies are translated using the exchange rate at balance date.

Any resulting foreign exchange gains and losses are recognised in the income statement, except when they relate to hedged items or hedging instruments designated in a cash flow hedge or net investment hedge relationship.

The Group is exposed to foreign exchange risk through transactions denominated in foreign currencies and the translation of foreign currency denominated balances. The amounts shown below represent the Group’s exposure to foreign currency before applying the risk management strategies:

- The Group’s foreign currency transactions are predominantly denominated in United States Dollars.
- The Group has net investments in foreign operations of $5,518 million (31 July 2016: $5,321 million). This amount is before considering borrowings held by the Group in the same currency as the investment.
- The Group has borrowings denominated in foreign currency of $4,672 million (31 July 2016: $4,489 million).

17 FINANCIAL RISK MANAGEMENT CONTINUED

How foreign exchange risk is managed

Forecast foreign currency transactions

The Group enters into foreign currency forward contracts and foreign currency option contracts for the following items:

- forecast cash receipts from sales for a period of up to 18 months within limits approved by the Board; and
- up to 100 per cent of other forecast foreign currency transactions.

The Group applies cash flow hedge accounting where derivatives are used to manage foreign exchange risk on forecast foreign currency transactions. The amount and maturity of the derivative and the forecast transaction is aligned to ensure that hedge relationship remains effective, with any undesignated costs of hedging accounted for separately.

The effect of the Group's application of hedge accounting in managing foreign exchange risk related to forecast foreign currency transactions is presented in the table below.

	GROUP $ MILLION						
	AS AT 31 JULY 2017[1]					YEAR ENDED 31 JULY 2017[2]	
		CARRYING AMOUNT				HEDGE EFFECTIVENESS IN RESERVES	
HEDGING INSTRUMENT USED	NOMINAL AMOUNT[3]	DERIVATIVE ASSETS	DERIVATIVE LIABILITIES	ACCUMULATED COST OF HEDGING	CHANGE IN VALUE USED TO CALCULATE HEDGE EFFECTIVENESS	RECOGNISED IN OTHER COMPREHENSIVE INCOME	RECLASSIFIED TO THE INCOME STATEMENT[4]
Cash flow hedging							
Foreign currency forwards and options							
Maturity: 0-18 months Weighted average NZD:USD rate: 0.7122	7,896	426	(3)	11	388	465	(330)
Total	7,896	426	(3)	11	388	465	(330)

1 Life-to-date amounts as at balance date.
2 Year-to-date amounts recognised during the year.
3 Nominal amount represents forecast foreign currency transactions in cash flow hedge relationships, translated into New Zealand Dollars using the exchange rate at balance date.
4 Recognised in revenue.

Net investments in foreign operations

The Group's net investments are designated in hedge relationships to the extent of:

- borrowings denominated in the same foreign currency; and
- foreign currency swaps directly attributed to the net investment.

Hedge ineffectiveness arises if the carrying amount of the net investment falls below the amount of the designated hedging instruments.

The effect of the Group's hedge accounting policy in managing foreign exchange risk related to the Group's net investments in foreign operations is presented in the table below:

	GROUP $ MILLION				
	AS AT 31 JULY 2017			YEAR ENDED 31 JULY 2017	
	CARRYING AMOUNT		NOMINAL AMOUNT	HEDGE EFFECTIVENESS	
HEDGED NET INVESTMENTS AND HEDGING INSTRUMENTS USED	AMOUNT OF NET INVESTMENT HEDGED[1]	FOREIGN CURRENCY BORROWINGS	FOREIGN CURRENCY SWAPS[2]	NET INVESTMENT GAIN/(LOSS) RECOGNISED IN OTHER COMPREHENSIVE INCOME	BORROWING/ SWAPS GAIN/(LOSS) RECOGNISED IN OTHER COMPREHENSIVE INCOME
Net investment hedging					
United States Dollar-denominated Maturity of borrowings: 34-47 months	123	(123)	–	(7)	7
Australian Dollar-denominated Maturity of borrowings: 48 months	425	(425)	–	1	(1)
Euro-denominated Maturity of borrowings: 89 months	151	(151)	–	–	–
Chinese Renminbi-denominated Maturity of borrowings: 18 months Maturity of swaps: 1-4 months	341	(247)	(94)	(24)	24
Hong Kong Dollar-denominated Maturity of borrowings: 10 months	36	(36)	–	–	–
Total	1,076	(982)	(94)	(30)	30

1 The carrying amount of the net investment designated into a net investment hedge relationship.
2 The carrying amount of foreign currency swaps at balance date is $3 million, and is presented within derivative assets.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

17 FINANCIAL RISK MANAGEMENT CONTINUED

Borrowings denominated in foreign currency

The Group's policy is to maintain its net exposure to a foreign currency within predefined limits.

To the extent the Group has monetary assets in the same foreign currency as the borrowing, the Group has a reduced exposure to foreign exchange risk. The foreign currency gains and losses relating to these balances is off-set in net foreign exchange gains/(losses) in the income statement.

To manage the net exposure to foreign currency borrowings, the Group enters into cross currency interest rate swaps (CCIRS). CCIRS are used to manage the combined foreign exchange risk and interest rate risk as they swap fixed rate foreign currency borrowings and interest payments into equivalent New Zealand Dollar-denominated amounts of principal with floating interest rates.

The Group applies hedge accounting to foreign currency denominated borrowings that are managed by CCIRS. The hedge relationship may be designated into separate cash flow hedges and fair value hedges to manage the different components of foreign currency and interest rate risk:

- fair value hedge relationship where CCIRS are used to manage the interest rate and foreign currency risk in relation to foreign currency denominated borrowings with fixed interest rates.
- cash flow hedge relationship where CCIRS are used to manage the variability in cash flows arising from interest rate movements on floating interest rate payments and foreign exchange movements on payments of principal and interest.

Hedge ineffectiveness arises predominantly from changes in counterparty credit risk and cross currency basis spreads.

The effect of the Group's hedge accounting policies in managing both its foreign exchange risk and interest rate risk related to borrowings denominated in foreign currency is presented in the table below.

	GROUP $ MILLION								
	AS AT 31 JULY 2017[1]					YEAR ENDED 31 JULY 2017[2]			
		CARRYING AMOUNT				HEDGE EFFECTIVENESS IN RESERVES		HEDGE EFFECTIVENESS	HEDGE INEFFECTIVENESS
HEDGING INSTRUMENTS USED	NOMINAL AMOUNT[3]	DERIVATIVE ASSETS	DERIVATIVE LIABILITIES	ACCUMULATED COST OF HEDGING	CHANGE IN VALUE USED TO CALCULATE HEDGE EFFECTIVENESS	CASH FLOW HEDGE (OCI)	CASH FLOW HEDGE RECLASSIFIED TO THE INCOME STATEMENT[4]	FAIR VALUE HEDGE (INCOME STATEMENT) GAIN/(LOSS)[4]	RECOGNISED IN THE INCOME STATEMENT GAIN/(LOSS)[4]
Cash flow hedging and fair value hedging									
Cross-currency interest rate swaps									
USD Maturity: 111-159 months Weighted average interest rate: floating Weighted average NZD:USD rate: 0.7841	893	83	(18)	–	44	2	3	(87)	6
GBP Maturity: 77 months Weighted average interest rate: floating Weighted average NZD:GBP rate: 0.3610	623	79	(319)	–	(260)	(19)	20	(27)	(8)
EUR Maturity: 89 months Weighted average interest rate: floating Weighted average NZD:EUR rate: 0.6559	386	–	(16)	(5)	(8)	1	(11)	(9)	(3)
Fair value hedging Maturity: 10-47 months Weighted average interest rate: floating Weighted average NZD:USD rate: 0.7733	356	19	–	–	19	NA	NA	(19)	6
Total		181	(353)	(5)	(205)	(16)	12	(142)	1

1 Life-to-date amounts as at balance date.

2 Year-to-date amounts recognised during the year.

3 Nominal amount is the face value, converted using the weighted average foreign exchange rate, of foreign denominated borrowings in hedge relationships. For those borrowings in fair value hedges, the carrying amount includes the life-to-date fair value hedge adjustment of $82 million.

4 Recognised in net finance costs.

Receivables and payables denominated in foreign currency

The Group enters into foreign currency forward contracts and foreign currency option contracts for 100 per cent of the net foreign currency receivables and payables.

Derivatives used to hedge the changes in the value of foreign currency receivables and payables are not hedge accounted. Changes in the fair value of these derivatives provide an off-set to the change in the value of foreign currency receivables and payables recognised in the income statement. These are recognised within foreign exchange gains and losses in the income statement.

17 FINANCIAL RISK MANAGEMENT CONTINUED

Foreign exchange gains and losses in the income statement

The table below provides a breakdown of the net foreign exchange gains or losses recognised in the income statement.

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Relationships where fair value hedge accounting has been applied		
Net foreign exchange gains/(losses) attributable to:		
– Foreign currency-denominated borrowings	91	193
– Derivatives	(94)	(195)
Relationships where fair value hedge accounting has not been applied		
Net foreign exchange gains/(losses) attributable to:		
– Foreign currency denominated receivables	(229)	(271)
– Foreign currency denominated payables and borrowings	125	135
– Derivatives	135	138
– Other net foreign exchange gains	1	7
Net foreign exchange gains	29	7

b) Interest rate risk

Nature and exposure of interest rate risk to the Group

The Group is exposed to interest rate risk on its interest-bearing borrowings, included within economic net interest-bearing debt (refer Note 7).

Changes in market interest rates expose the Group to:

- changes in the fair value of borrowings subject to fixed interest rates (fair value risk); and
- changes in future interest payments on borrowings subject to floating interest rates (cash flow risk).

How the Group manages its exposure to interest rate risk

The Group's policy is to maintain a target ratio of fixed and floating interest rate exposure. To achieve this the Group considers its forecast debt over a specified time horizon and manages the interest rate exposure by:

- issuing fixed rate debt; and
- entering into interest rate swaps (IRS).

The Group applies hedge accounting to the borrowings and the associated IRS, for movements in benchmark market interest rates (i.e. excluding any margin component).

Hedge ineffectiveness arises in relation to IRS that have been designated to hedge relationships after their initial recognition. The ineffectiveness for these hedges will continue until maturity.

In specific situations, where changes in the fair value of fixed-to-floating IRS provide an off-set to the changes in the fair value of other associated floating-to-fixed IRS, hedge accounting is not applied. The changes in fair values of these IRS off-set each other and are recognised within net finance costs in the income statement.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

17 FINANCIAL RISK MANAGEMENT CONTINUED

The effect of the Group's hedge accounting policies in managing interest rate risk is presented in the table below.

	GROUP $ MILLION							
	AS AT 31 JULY 2017[1]				YEAR ENDED 31 JULY 2017[2]			
		CARRYING AMOUNT			HEDGE EFFECTIVENESS IN RESERVES		HEDGE EFFECTIVENESS	HEDGE INEFFECTIVENESS
HEDGING INSTRUMENTS USED	NOMINAL AMOUNT[3]	DERIVATIVE ASSETS	DERIVATIVE LIABILITIES	CHANGE IN VALUE USED TO CALCULATE HEDGE EFFECTIVENESS	CASH FLOW HEDGE (OCI)	CASH FLOW HEDGE RECLASSIFIED TO THE INCOME STATEMENT[4]	FAIR VALUE HEDGE (INCOME STATEMENT) GAIN/(LOSS)[4]	RECOGNISED IN THE INCOME STATEMENT GAIN/(LOSS)[4]
Cash flow hedging								
Interest rate swaps								
Maturity: 4-87 months Weighted average interest rate: 4.36%	3,935	1	(178)	38	1	41	NA	37
Fair value hedging								
Interest rate swaps on NZD borrowings								
Maturity: 3-68 months Weighted average interest rate: floating	575	4	–	(9)	NA	NA	(5)	(4)
Interest rate swaps on AUD borrowings								
Maturity: 108 months Weighted average interest rate: floating	191	–	(12)	(12)	NA	NA	(10)	–
Total		5	(190)	17	1	41	(15)	33

1 Life-to-date amounts as at balance date.
2 Year-to-date amounts recognised during the year.
3 The nominal amount represents the principal amount of outstanding or forecast borrowings designated in hedge relationships. For those borrowings in fair value hedges, the carrying amount includes the life-to-date fair value hedge adjustment of $15 million.
4 Recognised in net finance costs.

c) Commodity price risk

Nature and exposure of commodity price risk to the Group

The Group is exposed to dairy commodity price risk through changes in selling prices and the cost of milk. In addition, the Group is a large purchaser of electricity, diesel and sugar and is exposed to changes in the cost of these commodities.

How the Group manages its exposure to commodity price risk

Dairy commodity price risk

The Group manages its exposure to dairy commodity price risk by:

- determining the most appropriate mix of products to manufacture based on the supply curve and global demand for dairy products;
- governing the length and terms of sales contracts so that sales revenue is reflective of current market prices and is, where possible, linked to GlobalDairyTrade (GDT) prices; and
- using dairy commodity derivative contracts to obtain an optimal price for future sales. The markets for dairy commodity derivatives are relatively limited, which reduces the ability to manage earnings volatility. As markets for these derivatives grow the use of dairy commodity derivatives to manage dairy commodity price risk may increase.

Other commodity price risk

The Group manages its exposure to other commodity price risk through the use of derivative contracts to hedge the cost of electricity, diesel and sugar.

Hedge accounting

Hedge accounting is not applied to commodity derivatives. Changes in the fair value of commodity derivative contracts are recognised within other operating income in the income statement.

17 FINANCIAL RISK MANAGEMENT CONTINUED

d) Sensitivity analysis of changes in market risks

The table below presents the effect on profit for the year and equity at the reporting date if various market rates had been higher or lower with all other variables held constant.

The sensitivity thresholds used represent reasonably possible changes in market rates.

	GROUP $ MILLION			
	31 JULY 2017		31 JULY 2016	
	EQUITY	PROFIT	EQUITY	PROFIT
Foreign currency rates				
10% strengthening of the NZD	138	4	(28)	4
10% weakening of the NZD	(115)	8	96	(5)
Interest rates				
100 basis point increase	68	5	11	40
100 basis point decrease	(66)	(21)	(14)	(46)
Dairy commodity prices				
10% increase	–	15	–	(3)
10% decrease	–	(15)	–	3

Interest rate cash flow sensitivity analysis

A change in interest rate would also impact floating rate interest payments and receipts on the Group's borrowings and derivatives.

The impact of a change in interest rate on the one year forecast cash flows is shown below:

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
100 basis point increase in interest rates	(3)	(3)
100 basis point decrease in interest rates	3	3

e) Impact to reserves in equity

The impact of the Group's hedge accounting policies on the reserves in equity is presented in the table below:

	GROUP $ MILLION	
	HEDGE RESERVES	FOREIGN CURRENCY TRANSLATION RESERVES
As at 1 August 2016	64	(428)
Movements attributable to cash flow hedges		
Change in value of effective derivative hedging instruments	450	NA
Reclassifications to the income statement:		
– As hedged transactions occurred	(277)	NA
Movements attributable to net investments in foreign operations and net investment hedges		
Net translation gain/(loss) on:		
– Borrowings and derivative hedging instruments	NA	30
– Net investments in foreign operations	NA	(143)
Reclassifications to the income statement:		
– Upon disposal of foreign operations	NA	(2)
Net change in the cost of hedging reserve	6	NA
Tax expense	(51)	(9)
Total movement	128	(124)
As at 31 July 2017	192[1]	(552)[2]

1 Included in the closing balance of the hedge reserves is $32 million relating to hedge relationships for which hedge accounting is no longer applied.

2 Included in the closing balance of the foreign currency translation reserve is $35 million relating to hedge relationships for which hedge accounting is no longer applied.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

17 FINANCIAL RISK MANAGEMENT CONTINUED

f) Credit risk

Nature and exposure of credit risk to the Group

Credit risk is the risk of loss to the Group due to customer and counterparty default on the Group's receivable balances. The Group's maximum exposure to credit risk is represented by the carrying amounts of cash and cash equivalents, trade and other receivables, derivative assets, and other investments and receivables.

The Group has no undue concentrations of credit risk.

How the Group manages its exposure to credit risk

The Group's policy is to actively manage its exposure to credit risk by:

- using financial counterparties that have a credit rating of at least 'A-' from Standard & Poor's (or equivalent) for derivative contracts, cash and cash equivalents and other investment balances;
- using commodity counterparties that have a credit rating of at least 'BBB-' from Standard & Poor's (or equivalent) for derivative contracts; and
- applying credit limits, and credit mitigation tools, such as letters of credit.

Trade and other receivable balances are included in Note 9 Trade and other receivables.

g) Fair value measurement

Valuation techniques for determining fair values

The fair value is the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date.

The fair values of financial assets and liabilities are calculated by reference to quoted market prices where that is possible. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis.

If quoted market prices are not available, the methodology used to calculate the fair values of financial assets and liabilities is to identify the expected cash flows under the terms of each specific contract and then discount these values back to the present value. These models use as their basis independently sourced market data where it is available and rely as little as possible on entity-specific estimates.

The calculation of the fair value of financial instruments reflects the impact of credit risk where applicable.

Specific valuation techniques used to value financial instruments include:

- the fair value of foreign exchange contracts is determined using observable currency exchange rates, option volatilities and interest rate yield curves;
- the fair value of interest rate contracts is calculated as the present value of the estimated future cash flows based on observable interest rate yield curves;
- the fair value of commodity contracts that are not exchange traded is determined by calculating the present value of estimated future cash flows based on observable quoted prices for similar instruments; and
- the fair value on the hedged risks of borrowings and long-term advances that are not exchange traded is calculated as the present value of the estimated future cash flows based on observable interest rate yield curves.

17 FINANCIAL RISK MANAGEMENT CONTINUED

Fair value hierarchy

All financial instruments for which a fair value is recognised are categorised within level 1 or level 2 of the fair value hierarchy. These categories are described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices included within level 1 that are observable for the asset or liability either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: Inputs for the assets or liabilities that are not based on observable market data (unobservable inputs).

The following table shows the fair value hierarchy for assets measured at fair value on the statement of financial position:

	GROUP $ MILLION					
	LEVEL 1		LEVEL 2		LEVEL 3	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016	AS AT 31 JULY 2017	AS AT 31 JULY 2016	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Derivative assets						
– Commodity derivatives	30	5	1	1	–	–
– Foreign exchange derivatives	–	–	595	473	–	–
– Interest rate derivatives[1]	–	–	193	389	–	–
Derivative liabilities						
– Commodity derivatives	(7)	(16)	(2)	(3)	–	–
– Foreign exchange derivatives	–	–	(24)	(25)	–	–
– Interest rate derivatives[1]	–	–	(557)	(568)	–	–
Investments in shares	10	6	–	–	9	–
Investement in Beingmate[2]	–	–	–	–	617	–
Livestock	–	–	–	–	319	342
Fair value	33	(5)	206	267	945	342

1 Includes cross-currency interest rate swaps.

2 The key assumption used in determining the fair value of the investment in Beingmate is the premium above share price that would be paid for a long term strategic investment of a similar size.

The following table shows the fair value hierarchy for each class of financial asset and liability where the carrying value in the statement of financial position differs from the fair value:

	GROUP $ MILLION					
	CARRYING VALUE		LEVEL 1		LEVEL 2	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016	AS AT 31 JULY 2017	AS AT 31 JULY 2016	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Financial assets						
Long-term advances	300	464	–	–	289	466
Financial liabilities						
Borrowings						
– NZX-listed bonds	(500)	(499)	(510)	(510)	–	–
– Capital notes	(35)	(35)	(33)	(33)	–	–
– Medium-term notes	(4,573)	(4,342)	–	–	(4,829)	(4,665)
– Finance leases	(137)	(143)	–	–	(155)	(167)

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

17 FINANCIAL RISK MANAGEMENT CONTINUED

h) Offsetting of financial assets and liabilities

Financial assets and liabilities are offset and the net amount reported in the statement of financial position where there currently is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

The Group enters into various master netting arrangements or similar agreements that do not meet the criteria for offsetting in the statement of financial position but still allow for the related amounts to be offset in certain circumstances. These principally relate to derivative transactions under ISDA (International Swap and Derivative Association) agreements where each party has the option to settle amounts on a net basis in the event of default of the other party.

The table below sets out the financial assets and financial liabilities subject to offsetting, enforceable master netting arrangements and other agreements.

	GROUP $ MILLION				
	AMOUNTS OFFSET IN THE STATEMENT OF FINANCIAL POSITION				
	GROSS FINANCIAL ASSETS/ (LIABILITIES)	GROSS FINANCIAL ASSETS/ (LIABILITIES) SET OFF	NET FINANCIAL ASSETS/ (LIABILITIES) PRESENTED	AMOUNTS NOT OFFSET	NET
Derivative financial assets	**963**	**(144)**	**819**	**(411)**	**408**
Trade and other receivables (excluding prepayments)	**2,900**	**(714)**	**2,186**	**–**	**2,186**
	3,863	**(858)**	**3,005**	**(411)**	**2,594**
Derivative financial liabilities	**(734)**	**144**	**(590)**	**292**	**(298)**
Trade and other payables (excluding employee entitlements)	**(2,340)**	**499**	**(1,841)**	**–**	**(1,841)**
Owing to suppliers	**(1,545)**	**215**	**(1,330)**	**–**	**(1,330)**
Borrowings	**(6,263)**	**–**	**(6,263)**	**119**	**(6,144)**
	(10,882)	**858**	**(10,024)**	**411**	**(9,613)**
31 July 2017	**(7,019)**	**–**	**(7,019)**	**–**	**(7,019)**
Derivative financial assets	1,037	(169)	868	(510)	358
Trade and other receivables (excluding prepayments)	1,964	(463)	1,501	–	1,501
	3,001	(632)	2,369	(510)	1,859
Derivative financial liabilities	(781)	169	(612)	373	(239)
Trade and other payables (excluding employee entitlements)	(2,257)	390	(1,867)	–	(1,867)
Owing to suppliers	(792)	73	(719)	–	(719)
Borrowings	(6,352)	–	(6,352)	137	(6,215)
	(10,182)	632	(9,550)	510	(9,040)
31 July 2016	(7,181)	–	(7,181)	–	(7,181)

OTHER

This section contains additional notes and disclosures that aid in understanding Fonterra's position and performance but do not form part of the primary sections.

This section includes the following Notes:

Note 18: Taxation

Note 19: Contingent liabilities, provisions and commitments

Note 20: Related party transactions

Note 21: Group entities

Note 22: Net tangible assets per security

18 TAXATION

Tax expense comprises current and deferred tax. Tax expense, including the tax consequences of distributions to farmer shareholders, is recognised in the income statement. The tax consequences of distributions to farmer shareholders are recognised in the year to which the distribution relates. Other than distributions to farmer shareholders, tax consequences of items recognised directly in equity are also recognised in equity.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the balance date, and any adjustment to tax payable or receivable in respect of previous years.

Deferred tax arises due to certain temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and those for taxation purposes. Deferred tax is measured at the tax rate that is expected to apply to the temporary differences when they reverse, based on laws that have been enacted or substantively enacted by the balance date.

Deferred tax is not recognised on the following temporary differences:

- the initial recognition of goodwill;
- the initial recognition of assets and liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit; and
- differences relating to investments in subsidiaries and equity accounted investees to the extent that the timing of the reversal is controlled by the Group and it is probable that they will not reverse in the foreseeable future.

Deferred tax assets are recognised to the extent it is probable that future taxable profits will be available against which the temporary differences can be utilised.

a) Taxation – income statement

The total taxation expense in the income statement is summarised as follows:

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Current tax expense	**97**	108
Prior period adjustments to current tax	**(25)**	5
Deferred tax movements:		
– Origination and reversal of temporary differences	**(52)**	(15)
Tax expense	**20**	98

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

18 TAXATION CONTINUED

The taxation charge that would arise at the standard rate of corporation tax in New Zealand is reconciled to the tax expense as follows:

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Profit before tax	**765**	932
Prima facie tax expense at 28%	**214**	261
Add/(deduct) tax effect of:		
– Effect of tax rates in foreign jurisdictions	**(33)**	(24)
– Non-deductible expenses/additional assessable income	**54**	90
– Non-assessable income/additional deductible expenses	**(30)**	(66)
– Prior year under provision	**(25)**	5
Tax expense before distributions and deferred tax	**180**	266
Effective tax rate before distributions and deferred tax[1]	**23.5%**	28.5%
Tax effect of distributions to farmer shareholders	**(163)**	(170)
Tax expense before deferred tax	**17**	96
Effective tax rate before deferred tax[1]	**2.2%**	10.3%
Add/(deduct) tax effect of:		
– Origination and reversal of other temporary differences	**2**	(1)
– Losses of overseas Group entities not recognised	**1**	3
Tax expense	**20**	98
Effective tax rate[1]	**2.6%**	10.5%
Imputation credits		
Imputation credits available for use in subsequent reporting periods	**20**	20
Tax losses		
Gross tax losses available for which no deferred tax asset has been recognised	**52**	48

1 The effective tax rate is the tax charge on the face of the income statement expressed as a percentage of the profit before tax.

b) Taxation – statement of financial position

The table below outlines the deferred tax assets and liabilities that are recognised in the statement of financial position, together with movements in the year:

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Deferred tax		
Property, plant and equipment	(3)	(53)
Intangible assets	(519)	(522)
Derivative financial instruments	(84)	(30)
Employee entitlements	75	75
Inventories	31	52
Receivables, payables and provisions	58	71
New Zealand tax losses	486	480
Offshore tax losses	289	287
Other	21	6
Total deferred tax	354	366
Movements for the year		
Opening balance	366	623
Recognised in the income statement	52	15
Recognised directly in other comprehensive income	(60)	(262)
Foreign currency translation	(4)	(10)
Closing balance	354	366
Included within the statement of financial position as follows:		
Deferred tax assets	363	410
Deferred tax liabilities	(9)	(44)
Total deferred tax	354	366

Deferred tax assets relating to tax losses carried forward of $540 million (31 July 2016: $471 million) are recognised by Group entities that reported a taxable loss in either the current or prior year. The forecast utilisation of the carried forward tax losses of these entities reflect their strategic business plans.

The Group has not recognised deferred tax liabilities in respect of unremitted earnings that are considered indefinitely reinvested in foreign subsidiaries. As at 31 July 2017, these earnings amount to $893 million (31 July 2016: $675 million). These could be subject to withholding and other taxes on remittance.

19 CONTINGENT LIABILITIES, PROVISIONS AND COMMITMENTS

Contingent liabilities

In the normal course of business, Fonterra, its subsidiaries and equity accounted investees, are exposed to claims and legal proceedings that may in some cases result in costs to the Group.

In early August 2013, Fonterra publicly announced a potential food safety issue with three batches of Whey Protein Concentrate (WPC80) produced at the Hautapu manufacturing site and initiated a precautionary product recall.

In late August 2013, the New Zealand Government confirmed that the *Clostridium* samples found in WPC80 were not *Clostridium botulinum* and were not toxigenic, meaning the consumers of products containing the relevant batches of WPC80 were never in danger from *Clostridium botulinum*.

In January 2014, Danone formally initiated legal proceedings against Fonterra in the High Court of New Zealand and separate Singapore arbitration proceedings against Fonterra in relation to the WPC80 precautionary recall. The New Zealand High Court proceedings have been stayed pending completion of the Singapore arbitration. An initial hearing of the arbitration took place in February 2016 and a final hearing of the arbitration took place in June 2016. A decision of the arbitration panel is pending.

Based on current information available and the claims made to date in both proceedings, Fonterra will vigorously defend its position in these proceedings. Uncertainty exists regarding the outcome of the proceedings. Fonterra has provided $11 million (31 July 2016: $11 million) in respect of the Danone claims, which represents the maximum contractual liability to Danone.

The Directors believe that these proceedings have been adequately provided for and disclosed by the Group and that there are no additional claims or legal proceedings in respect of this matter that are pending at the date of these financial statements that require provision or disclosure.

The Group has no other contingent liabilities as at 31 July 2017 (31 July 2016: nil).

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

19 CONTINGENT LIABILITIES, PROVISIONS AND COMMITMENTS CONTINUED

Provisions

Provisions are recognised in the statement of financial position only where the Group has a present legal or constructive obligation as a result of a past event, when it is probable, being more likely than not, that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made.

	GROUP $ MILLION			
	RESTRUCTURING AND RATIONALISATION PROVISIONS	LEGAL CLAIMS PROVISIONS	OTHER PROVISIONS	TOTAL PROVISIONS
As at 1 August 2016	5	80	114	199
Additional provisions	1	–	22	23
Unused amounts reversed	(2)	(7)	(4)	(13)
Charged to income statement	(1)	(7)	18	10
Utilised during the year	(2)	(1)	(18)	(21)
As at 31 July 2017	2	72	114	188
Included within the statement of financial position as follows:				
Current liabilities				40
Non-current liabilities				148
Total provisions				188

	GROUP $ MILLION			
	RESTRUCTURING AND RATIONALISATION PROVISIONS	LEGAL CLAIMS PROVISIONS	OTHER PROVISIONS	TOTAL
As at 1 August 2015	39	99	125	263
Additional provisions	5	–	22	27
Unused amounts reversed	(5)	(13)	(4)	(22)
Charged to income statement	–	(13)	18	5
Utilised during the year	(34)	–	(9)	(43)
Foreign currency translation	–	(6)	(20)	(26)
As at 31 July 2016	5	80	114	199
Included within the statement of financial position as follows:				
Current liabilities				47
Non-current liabilities				152
Total provisions				199

The nature of the provisions are:

- the provision for restructuring and rationalisation includes obligations relating to planned changes throughout the business to improve efficiencies and reduce costs. The provisions are expected to be utilised in the next year;
- the legal claims provisions include obligations relating to tax, customs and duties and legal matters arising in the normal course of business. The timing and amount of the future obligations are uncertain, as they are contingent on the outcome of a number of judicial proceedings. The outcome of most of the obligations is not expected to be determined within the next year and therefore most of these provisions are classified as non-current; and
- other provisions include defined benefit pension schemes obligations and other employee related provisions.

19 CONTINGENT LIABILITIES, PROVISIONS AND COMMITMENTS CONTINUED

Commitments

a) Capital commitments

Capital expenditure contracted for at balance date but not recognised in the financial statements are as follows:

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Buildings	63	79
Plant, vehicles and equipment	172	48
Software	20	8
Livestock	–	3
Total commitments	**255**	**138**

b) Operating lease commitments

The Group leases premises, plant and equipment. The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Less than one year	116	109
One to five years	224	227
Greater than five years	170	177
Total operating lease commitments	**510**	**513**

20 RELATED PARTY TRANSACTIONS

Equity accounted investees (refer to Note 16 for a list) and key management personnel are related parties of the Group. Key management personnel comprises the Board and the Fonterra Management Team.

The transactions with related parties that were entered into during the year, and the year end balances that arose from those transactions are shown below:

Key management personnel remuneration

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Short-term employee benefits	11	16
Long-term employee benefits	10	3
Termination benefits	–	1
Directors' remuneration	3	3
Total key management personnel remuneration	**24**	**23**

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

20 RELATED PARTY TRANSACTIONS CONTINUED

Transactions with related parties during the year

Transactions with related parties are under normal trade terms.

	GROUP $ MILLION	
	31 JULY 2017	31 JULY 2016
Equity accounted investees		
Revenue from the sale of goods[1]	90	73
Sale of services[2]	7	5
Royalty and other income	2	2
Dividends received	22	77
Interest income from financing arrangements	–	1
Purchases of goods[3]	(5)	(10)
Purchases of services[4]	(158)	(44)
Key management personnel		
Purchases of goods[5]	(121)	(78)
Co-operative support loans	–	(6)
Dividends paid	(6)	(9)

1 Goods sold are primarily commodity products.
2 Services provided include management fees.
3 Goods purchased are primarily commodity products.
4 Services provided are primarily freight services.
5 Purchases from key management personnel primarily relate to milk supplied by farmer shareholder Directors.

Outstanding balances with related parties

	GROUP $ MILLION	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Equity accounted investees		
Total receivables arising from the sale or purchase of goods or services[6]	22	18
Total receivables arising from financing arrangements[7]	61	50
Total payables arising from the sale or purchase of goods or services	(21)	(15)
Total payables arising from financing arrangements	(2)	–
Key management personnel		
Total payables arising from the sale or purchase of goods or services[8]	(17)	(9)
Total receivables arising from Co-operative support loans	5	6

6 There were no material provisions for impairment on the receivables from related parties.
7 Loans to related parties other than equity accounted investees are unsecured and repayable in cash on demand. Loans to equity accounted investees are unsecured and repayable over varying terms of between four years and nine years.
8 Payables to key management personnel relate to amounts owing for milk supplied by farmer shareholder Directors.

Financial guarantees

The Group has provided financial guarantees for several equity accounted investees. The aggregate drawn down amount of equity accounted investees' liabilities for which the Group is jointly and severally liable is nil (31 July 2016: nil).

Transactions with related entities

As part of the administration of Trading Among Farmers, Fonterra entered into an Authorised Fund Contract to provide administrative services in relation to the Fund and meet the operating expenses of the Fund. In addition, Fonterra has agreed to provide corporate facilities, support functions and other services at no cost to the Fund.

Commitments

In addition to the transactions disclosed above, the Group has prospective commitments with related parties including contracts with equity accounted investees for the supply of dairy products and energy, and the provision of various management services.

21 GROUP ENTITIES

Subsidiaries are entities controlled by the Group. Subsidiaries are consolidated from the date the Group gains control until the date on which control ceases.

Non-controlling interests are allocated their share of profit after tax in the income statement and are presented within equity in the statement of financial position separately from equity attributable to equity holders. The effect of all transactions with non-controlling interests that change the Group's ownership interest but do not result in a change in control are recorded in equity. Where control is lost, the remaining interest in the investment is remeasured to fair value and any surplus or deficit arising from that remeasurement is recognised in the income statement.

Equity accounted investments are discussed in further detail in Note 16.

The Group's subsidiaries and equity accounted investees are involved in the marketing, distribution, processing, technology or financing of dairy products. All Group entities have a balance date of 31 July unless otherwise indicated. Subsidiaries and equity accounted investees with different balance dates from that of the Group are due to legislative requirements in the country the entities are domiciled. Equity accounted investees may also have a different balance date due to alignment with their other investors' balance dates or to align with the milk season.

The Group holds investments in certain countries that have some limited restrictions on the repatriation of funds back to New Zealand. This does not result in any significant restriction on the flow of funds for the Group.

The significant subsidiaries of the Group are listed below:

		OWNERSHIP INTERESTS (%)	
SUBSIDIARY NAME	COUNTRY OF INCORPORATION AND PRINCIPAL PLACE OF BUSINESS	**AS AT 31 JULY 2017**	AS AT 31 JULY 2016
Fonterra Australia Pty Limited	Australia	**100**	100
Fonterra Brands (Australia) Pty Limited	Australia	**100**	100
Dairy Partners Americas Brasil Limitada[1]	Brazil	**51**	51
Comercial Santa Elena S.A.[1]	Chile	**99.9**	99.9
Soprole S.A.[1]	Chile	**99.9**	99.9
Prolesur S.A.[1]	Chile	**86.18**	86.26
Fonterra Commercial Trading (Shanghai) Company Limited[1]	China	**100**	100
Fonterra (Yutian) Dairy Farm Co. Limited[1]	China	**100**	100
Fonterra (Ying) Dairy Company Limited[1]	China	**100**	100
PT Fonterra Brands Indonesia	Indonesia	**100**	100
Fonterra Brands (Hong Kong) Limited	Hong Kong	**100**	100
Fonterra Brands (Malaysia) Sdn Bhd	Malaysia	**100**	100
Fonterra (Europe) Coöperatie U.A.	Netherlands	**100**	100
Fonterra Europe Manufacturing B.V.	Netherlands	**100**	100
Fonterra Brands (Singapore) Pte Limited	Singapore	**100**	100
Fonterra (SEA) Pte Limited	Singapore	**100**	100
Fonterra Brands Lanka (Private) Limited	Sri Lanka	**100**	100
Fonterra (USA) Inc.	United States	**100**	100
Corporación Inlaca CA	Venezuela	**60**	60
Canpac International Limited	New Zealand	**100**	100
Fonterra Brands (New Zealand) Limited	New Zealand	**100**	100
Fonterra Brands (Tip Top) Limited	New Zealand	**100**	100
Fonterra Dairy Solutions Limited	New Zealand	**100**	100
Fonterra Ingredients Limited	New Zealand	**100**	100
Fonterra Limited	New Zealand	**100**	100
Fonterra (New Zealand) Limited	New Zealand	**100**	100
RD1 Limited	New Zealand	**100**	100
Kotahi Logistics LP	New Zealand	**91**	91

1 Balance date 31 December.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

21 GROUP ENTITIES CONTINUED

The Group's ownership interest of the following entities is 50 per cent or less. However they have been consolidated on the basis that the Group controls them through its exposure or rights to variable returns and the power to affect those returns.

		OWNERSHIP INTERESTS (%)	
OVERSEAS SUBSIDIARIES 50% OR LESS OWNERSHIP	COUNTRY OF INCORPORATION AND PRINCIPAL PLACE OF BUSINESS	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Fonterra (Japan) Limited	Japan	**50**	50
Fonterra Brands (Middle East) L.L.C.	UAE	**49**	49

In addition to the entities above, Fonterra controls the Fonterra Shareholders' Fund and Fonterra Farmer Custodian Limited and consolidates these two entities. The trustees of the Fonterra Farmer Custodian Trust own the legal title to all of the shares of the Custodian. The Fund is a unit trust with an independent trustee. In concluding that the Group controls the Fund and the Custodian, the Directors took into consideration that they form an integral part of the structure and operation of Trading Among Farmers.

22 NET TANGIBLE ASSETS PER SECURITY

	GROUP	
	AS AT 31 JULY 2017	AS AT 31 JULY 2016
Net tangible assets per security[1]		
$ per listed debt security on issue	**6.86**	6.32
$ per equity instrument on issue	**2.57**	2.37
Listed debt securities on issue (million)	**603**	603
Equity instruments on issue (million)	**1,607**	1,603

1 Net tangible assets represents total assets less total liabilities less intangible assets.

INDEPENDENT AUDITOR'S REPORT

FOR THE YEAR ENDED 31 JULY 2017

TO THE SHAREHOLDERS OF FONTERRA CO-OPERATIVE GROUP LIMITED

We have audited the financial statements which comprise:

- the statement of financial position as at 31 July 2017;
- the income statement for the year then ended;
- the statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the cash flow statement for the year then ended; and
- the notes to the financial statements, which include significant accounting policies.

OUR OPINION

In our opinion, the financial statements of Fonterra Co-operative Group Limited (the Company), including its controlled entities (the Group), present fairly, in all material respects, the financial position of the Group as at 31 July 2017, its financial performance and its cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards (IFRS).

BASIS FOR OPINION

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs NZ) and International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

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

We are independent of the Group in accordance with Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* (PES 1) issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Our firm carries out other services for the Group in relation to advisory, other assurance and attestation services. Partners and employees of our firm may deal with the Group on normal terms within the ordinary course of trading activities of the Group. These matters have not impaired our independence as auditor of the Group.

OUR AUDIT APPROACH

Overview

An audit is designed to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

Overall Group materiality: $32 million, which represents 5% of the Group's three-year weighted average net profit before tax.

We chose to use the Group's net profit before tax because, in our view, it is the benchmark against which the performance of the Group is most commonly measured. However, the Group's net profit before tax is subject to volatility due to fluctuations in the Farmgate Milk Price, commodity prices, and foreign exchange rates. Therefore using a three-year weighted average net profit before tax provides a more stable basis for establishing our materiality.

We have determined that there are two key audit matters:

- Impairment assessment of goodwill and brands for the Brazil consumer and foodservice business; and
- Impairment assessment of the Group's investment in Beingmate.

Materiality

The scope of our audit was influenced by our application of materiality.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall Group materiality for the financial statements as a whole as set out above. These, together with qualitative considerations, helped us to determine the scope of our audit, the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Audit scope

We designed our audit by assessing the risks of material misstatement in the financial statements and our application of materiality. As in all of our audits, we also addressed the risk of management override of internal controls including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

INDEPENDENT AUDITOR'S REPORT CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry and strategic markets in which the Group operates. The Group has five reportable segments that reflect the Group's management and reporting structure as viewed by the Company's Management Team. The financial statements are a consolidation of 163 subsidiaries, comprising the Group's collection, processing and distribution of New Zealand milk, global sales and marketing of New Zealand and non-New Zealand milk products, Quick Service Restaurant businesses, Global Brands and Nutrition, Co-operative Affairs, Fonterra Farm Source stores, Group Services, fast-moving consumer goods businesses, ingredients businesses, foodservice businesses, and farming businesses.

Of the Group's 163 subsidiaries we identified 11 subsidiaries that, due to their financially significant contribution as well as strategic importance to the Group's overall results, required a full-scope audit. In addition, we also performed specific audit procedures on certain balances and transactions of other subsidiaries. Audits of each location are performed at a materiality level calculated with reference to a proportion of Group materiality relative to the financial scale of the business concerned.

In establishing the overall approach to the Group audit, we determined the type of work to be performed at the subsidiaries by us, as the Group engagement team, or by component auditors from other PwC network firms operating under our instruction. Where the work was performed by component auditors, we determined the level of involvement we needed to have in the audit work at those subsidiaries to be able to conclude whether sufficient appropriate audit evidence had been obtained to provide a basis for our opinion on the financial statements as a whole. This, together with additional procedures performed at the Group level, provided us with the audit evidence we needed for our opinion on the financial statements as a whole.

New Zealand sourced cost of milk supplied by farmer shareholders comprises the volume of milk solids supplied at the Farmgate Milk Price as determined by the Board of Directors for the relevant season. In making that determination the Board takes into account the Farmgate Milk Price calculated in accordance with the Farmgate Milk Price Manual, which is independently audited. The Fonterra Farmgate Milk Price Statement sets out information about the Farmgate Milk Price, and how it is calculated by Fonterra. It can be found in the 'Our Financials/Farmgate Milk Prices' section of Fonterra Co-operative Group Limited's website.

KEY AUDIT MATTERS

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current year. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How our audit addressed the key audit matter
1. Impairment assessment of goodwill and brands for the Brazil consumer and foodservice business	
Indefinite life intangible assets (goodwill and brands) are disclosed within note 15 (pages 26 and 27) of the financial statements. These assets are required to be tested for impairment on an annual basis. Management tests for impairment of intangible assets by performing a value-in-use assessment using a discounted cash flow model based on forecast future performance. The recoverability of these assets are therefore dependent on achieving sufficient future cash flows. Forecast cash flows are judgemental and influenced by factors such as regulatory and economic environments. As these assets are spread across a broad range of economic markets, there are a number of different factors and judgements that can influence the impairment assessment. Due to a general deterioration in the macroeconomic environment in Brazil, the impact on the current performance of the business and the potential impact on future cash flows, our audit focused on the Brazil cash generating unit (CGU) impairment assessment. The preparation of forecast cash flows requires the application of significant judgement over key assumptions such as earnings growth, discount rates and long-term growth rates. The carrying values of the indefinite lived intangible assets held in the Brazil CGU amounts to $409 million, which represents approximately 15% of the Group's indefinite life intangible assets.	We performed the following audit procedures in relation to the Brazil CGU impairment assessment: • held discussions with management and understood the processes undertaken and basis for determining key assumptions in preparing the forecast cash flows; • engaged our auditor's valuation experts to assist us in evaluating the assumptions and methodologies used; and • challenged management on key assumptions, including earnings growth, discount rates and long-term growth rates as described below. The Brazil CGU impairment assessment is the most sensitive to forecast cash flows from key strategic and go-to-market growth initiatives. In relation to these forecast cash flows we performed the following procedures: • compared forecast cash flows to the three year Board approved business plan and understood the processes undertaken by the Directors to approve the plan; • understood and assessed growth rates applied to the forecast cash flows beyond the business plan, a combination of continued growth from strategic initiatives and industry forecasts; • understood the difference between historical and budgeted performance to assess the accuracy of the budgeting process in previous years and considered the impact on forecast earnings; and • understood and assessed the commercial prospects of achieving key strategic and go-to-market growth initiatives, by agreeing these to detailed supporting analyses prepared by management and corroborating these to independent market analyses (where relevant).

Key audit matter	How our audit addressed the key audit matter
1. Impairment assessment of goodwill and brands for the Brazil consumer and foodservice business (continued)	
The recoverable amount of these assets are equivalent to their carrying values.	In relation to discount rates and long-term growth rates, we assessed the economic and industry forecasts in Brazil and cost of capital and other inputs to comparable organisations both in Brazil and globally. We also considered the appropriateness of disclosures in relation to intangible assets.
2. Impairment assessment of the Group's investment in Beingmate	
As disclosed in the basis of preparation (page 7) and within note 16 (page 28) of the financial statements, the Group holds an 18.8% share in Beingmate Baby and Child Food Co., Ltd., (Beingmate) a Chinese listed entity. The entity is accounted for as an equity accounted investment. Beingmate reported losses for the financial year ended 31 December 2016 and further losses for the half year ended 30 June 2017. The Group accounted for its share of Beingmate's losses for the period 1 August 2016 through to 31 July 2017 as a reduction in the carrying amount of the investment of $41 million. Beingmate's share price has also traded significantly below the share price at the time the Group acquired its investment. As a result of these factors, the carrying value of the investment has been assessed for impairment, using a fair value less cost to sell methodology. The fair value has been determined using an estimate of what a market participant would pay for a similar long-term strategic equity stake in Beingmate under current market conditions. This resulted in an impairment charge of $35 million. Our audit focused on this area as there are a number of judgements and assumptions applied in determining the fair value.	Our audit procedures in relation to the Group's investment in Beingmate, and specifically our audit of management's impairment assessment, focused on the key input to which the fair value is most sensitive, in particular, the determination of the premium above share price which a market participant might pay to acquire a long-term strategic investment of a similar size to Beingmate (the acquisition premium). In relation to the acquisition premium, we performed the following audit procedures: • conducted meetings with management responsible for overseeing the strategic relationships with Beingmate and understood the processes management undertook to derive the acquisition premium; • understood and assessed the impact on the acquisition premium of: the infant milk formula market fundamentals in China; Beingmate's market share; potential growth opportunities due to imminent changes in the Chinese regulatory regime for both food safety laws and cross border e-commerce regulations; Fonterra's access to Beingmate's distribution network and other key strategic benefits; • considered the impact of Beingmate's reported losses for the financial year ended 31 December 2016, and further losses for the half year ended 30 June 2017 on the acquisition premium; • through the engagement of our auditor's valuation experts, we challenged the appropriateness of the acquisition premium with reference to comparable market acquisition premia where strategic market penetration and synergies were evidenced; and • considered the appropriateness of disclosures in relation to the impairment. Based on our work, the impairment charge fell within the range of reasonable outcomes we considered.

INFORMATION OTHER THAN THE FINANCIAL STATEMENTS AND AUDITOR'S REPORT

The Directors are responsible for the Annual Report. Our opinion on the financial statements does not cover the other information included in the Annual Report and we do not and will not express any form of assurance conclusion on the other information.

In connection with our audit of the financial statements, our responsibility is to read the other information included in the Annual Report and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

RESPONSIBILITIES OF THE DIRECTORS FOR THE FINANCIAL STATEMENTS

The Directors are responsible, on behalf of the Company, for the preparation and fair presentation of the financial statements in accordance with NZ IFRS and IFRS, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

INDEPENDENT AUDITOR'S REPORT CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE FINANCIAL STATEMENTS

Our objectives are to obtain reasonable assurance about whether the financial statements, as a whole, are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs NZ and ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located at the External Reporting Board's website at: https://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-1/

This description forms part of our auditor's report.

WHO WE REPORT TO

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

The engagement partner on the audit resulting in this independent auditor's report is Jonathan Skilton.

For and on behalf of:

PricewaterhouseCoopers

Chartered Accountants

Auckland
23 September 2017

STATUTORY INFORMATION

FOR THE YEAR ENDED 31 JULY 2017

EQUITY SECURITIES HELD AT BALANCE DATE

In accordance with Rules of the Fonterra Shareholders' Market (FSM) Rule 9.4.4(c), the following table identifies the Equity Securities in which each Director has a Relevant Interest as at 31 July 2017.

	UNITS ISSUED BY THE FONTERRA SHAREHOLDERS' FUND[1]	CO-OPERATIVE SHARES
Leonie Guiney	–	878,824
John Monaghan	–	140,179
Nicola Shadbolt	–	366,705
Donna Smit	–	1,457,589
Ashley Waugh	–	115,812
John Wilson	–	4,523,700

1 Units issued by the Fonterra Shareholders' Fund may be converted to Co-operative shares.

A 'Relevant Interest' in Fonterra securities which is required to be disclosed is explicitly defined in the Financial Markets Conduct Act 2013.

To qualify as a Farmer Elected Director under the Fonterra Constitution a person must be a shareholder, a shareholder of a company that is a shareholder, a member of a partnership that is a shareholder, or have a legal or beneficial interest in, or a right or entitlement to participate directly in the distributions of, a body corporate that is a shareholder of Fonterra.

Given the variety of ways that farmer shareholders can organise their interests, it is possible for Fonterra Elected Directors to have an interest in Fonterra shares without this being a 'Relevant Interest' as defined in the Financial Markets Conduct Act 2013.

The interests of Mr Ian Farrelly and Mr David MacLeod in Fonterra shares at balance date did not meet the 'Relevant Interest' definition applicable to the disclosure above. However, their respective interests in Fonterra shares qualify them as Elected Directors under the Fonterra Constitution. Other Fonterra Elected Directors also have interests in Fonterra shares which are not within the definition of 'Relevant Interest' in the Financial Markets Conduct Act 2013 and those interests are not disclosed above.

CO-OPERATIVE STATUS

In accordance with section 10 of the Co-operative Companies Act 1996, the Directors of Fonterra unanimously resolved on 23 August 2017 that the Company was, for the year ended 31 July 2017, a co-operative company. The opinion was based upon the fact that:

- Throughout that period the principal activities of the Company have been the activities stated in clause 1.3 of the Company's constitution:
  - the manufacture and sale of butter, cheese, dried milk, casein, or any other product derived from milk or milk solids supplied to the Company by its shareholders;
  - the sale to any person of milk or milk solids supplied to the Company by its shareholders;
  - the collection, treatment, and distribution for human consumption of milk or cream supplied to the Company by its shareholders.
- Each of the Company's principal activities are co-operative activities (as defined in section 3 of the Co-operative Companies Act 1996).
- Throughout that period not less than 60 per cent of the voting rights attaching to shares in the Company have been held by transacting shareholders (as defined in section 4 of the Co-operative Companies Act 1996).

STATUTORY INFORMATION CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

REMUNERATION OF DIRECTORS

The total remuneration and value of other benefits received by each Director in the 12 month period from 1 August 2016 to 31 July 2017 are scheduled below:

	BOARD FEES	COMMITTEE CHAIR FEES	TRAVEL ALLOWANCE	TOTAL REMUNERATION ($)
Malcolm Bailey	58,808	–	–	58,808
Clinton Dines	165,000	–	–	165,000
Ian Farrelly	138,154	–	–	138,154
Leonie Guiney	165,000	–	–	165,000
Simon Israel	165,000	–	80,000[1]	245,000
David Jackson (Chair of the Audit and Finance Committee and Chair of the Milk Price Panel, part year)	165,000	31,000	–	196,000
David MacLeod	165,000	–	–	165,000
John Monaghan (Chair of the Co-operative Relations Committee)	165,000	31,000	–	196,000
Nicola Shadbolt (Chair of the Risk Committee)	165,000	31,000	–	196,000
Donna Smit	110,032	–	–	110,032
Michael Spaans	82,500	–	–	82,500
Scott St John (Chair of the Milk Price Panel, part year)	126,500	8,250	–	134,750
John Waller (Chair of the Milk Price Panel, part year)	13,750	2,583	–	16,333
Ashley Waugh	165,000	–	–	165,000
John Wilson (Chairman of the Board of Directors)	405,000	–	–	405,000

1 The Board has approved the payment to Mr Israel of a travel allowance of $10,000 per meeting to travel to and from New Zealand to attend Board meetings.

SUBSIDIARY COMPANY DIRECTORS

The following companies were subsidiaries of Fonterra as at 31 July 2017. Directors as at that date are listed; those who resigned during the year are denoted with an R. Alternate Directors are denoted with an A.

Anchor Ethanol Limited:
G A Duncan, P D Washer

Canpac International Limited:
G A Duncan, M R Spiers

Civil Whey Distributors Limited:
G A Duncan, M R Spiers

Dairy Industry Superannuation Scheme Trustee Limited:
M A Apiata-Wade, B J Kerr, D M Marshall (R), T P McGuinness, D W C Scott, A K Williams, P D Wynen, K Duffy (R)

Fonterra (Delegated Compliance Trading Services) Limited:
G A Duncan, S D T Till

Fonterra (International) Limited:
G A Duncan, C E Rowe

Fonterra (Kotahi) Limited:
M E Leslie, R J Spurway

Fonterra (Middle East) Limited:
G A Duncan, P D Washer

Fonterra (New Zealand) Limited:
G A Duncan, C E Rowe

Fonterra (North Asia) Limited:
G A Duncan, K A Wickham (R), S D T Till

Fonterra Brands (New Zealand) Limited:
M R Cronin, L M Clement

Fonterra Brands (Tip Top Investments) Limited:
G A Duncan, K M Turner

Fonterra Brands (Tip Top) Limited:
M R Cronin, L M Clement

Fonterra Commodities Limited:
G A Duncan, B M Turner

Fonterra Dairy Solutions Limited:
G A Duncan, R McNickle

Fonterra Equities Limited:
G A Duncan, S D T Till

Fonterra Farming Ventures Limited:
G A Duncan, J P Minkhorst

Fonterra Finance Corporation Limited:
G A Duncan, S D T Till

Fonterra Holdings (Americas) Limited:
G A Duncan, R M Kennerley

Fonterra Holdings (Brazil) Limited:
G A Duncan, R M Kennerley

Fonterra Holdings (Venezuela) Limited:
G A Duncan, R M Kennerley

Fonterra Ingredients Limited:
G A Duncan, L J Paravicini

Fonterra Limited:
K A Wickham, R J Spurway

Fonterra PGGRC Limited:
G A Duncan, J P Minkhorst

Fonterra TM Limited:
G A Duncan, S D T Till

Glencoal Energy Limited:
G A Duncan, M R Spiers

GlobalDairyTrade Holdings Limited:
G A Duncan, L J Paravicini

Kotahi GP Limited:
M E Leslie, K G Winders (R), R J Spurway, R M Kennerley, G P Howie

MIH Limited:
G A Duncan, J P Minkhorst

Milktest GP Limited:
P G Brown, B Greaney (R), M E Leslie, R G Townshend, T A Winter, P D S Grave, J T Powell

MyMilk Limited:
M W Hurrell, R M Kennerley

New Zealand Dairy Board:
G A Duncan, C E Rowe

New Zealand Milk (International) Limited:
G A Duncan, L J Paravicini

New Zealand Milk Brands Limited:
G A Duncan, S D T Till

NZAgbiz Limited:
G A Duncan, J P Minkhorst

RD1 Limited:
J P Minkhorst, K M Turner

SAITL Limited:
B Greaney, M E Leslie

Tangshan Dairy Farm (NZ) Limited:
G A Duncan, K A Wickham

Whareroa Co-Generation Limited:
G A Duncan, M R Spiers

A.C.N. 113 345 430 Pty Ltd [Australia]:
G A Duncan, A Maharaj

Anchor Insurance Pte. Limited [Singapore]:
L J Paravicini, S S Herbert, M W Smith (R), C L Khoon (A), R M Kennerley

Anmum (Malaysia) Sdn. Bhd. [Malaysia]:
M W Smith (R), J M Porraz, J Ling, F Spinelli

Auckland Limited [Barbados]:
M F Maldonado, A Turnbull, L Hartmann, F Spinelli, L J Paravicini

Australasian Food Holdings Pty Limited [Australia]:
G A Duncan, A Maharaj

Bonlac Finance Pty Limited [Australia]:
G A Duncan, A Maharaj

Bonland Cheese Trading Pty Ltd [Australia]:
G A Duncan, A Maharaj

Comercial Dos Alamos S.A. [Chile]:
J C Petersen, R Waldspurger, M Kunstmann

Comercial Santa Elena S.A. [Chile]:
H Covarrubias Lalanne, J Barria, E Aldunate

Corporación Inlaca C.A [Venezuela]:
M F Maldonado, M M Perez, J R Odon, F C Ortega

Dairy Enterprises (Chile) Limitada [Chile]:
R Sepúlveda Seminario, J P Egaña Bertoglia (A), F Spinelli, G A Duncan, R Lavados (A), P L Linhares (A)

Dairy Enterprises International (Chile) Limited [Cayman Islands]:
M P Campbell, G A Duncan

Dairymas (Malaysia) Sdn Bhd [Malaysia]:
M W Smith (R), J M Porraz, J Ling, F Spinelli

Dairy Partners Americas Brasil Limitada [Brazil]:
O C L Faccina (R), M J L Barros, L P L Rivero, D G Cano (R), F A Sporques, L Medeiros, F Goncalves, D S Oliveira

Dairy Partners Americas Nordeste-Productos Alimenticios Ltda [Brazil]:
O C L Faccina (R), M J L Barros, D G Cano (R), F A Sporques, L P L Rivero, L Medeiros, F Goncalves, D S Oliveira

Darnum Park Pty Ltd [Australia]:
J Swales (R), G A Duncan, R Dedoncker

Falcon Dairy Holdings Limited [Hong Kong]:
R M Kennerley, G A Duncan (R), J F Ginascol, R O Frey, M P Campbell

Fast Forward FFW Limited [United Kingdom]:
M P Campbell, H Huistra, M Gallagher, A Waugh, K Baine

Fazenda MIH Ltda [Brazil]:
R Santos (R), R Carneiro (R), M P Bueno, G Nascimento

Fonterra (Brasil) Ltda [Brazil]:
F Spinelli (R), R Carneiro (R), M P Bueno, G Nascimento, M J L Barros

Fonterra (Canada), Inc. [Canada]:
G A Duncan, B Kipping,B M Ryan, J P Coote

Fonterra (China) Limited [Hong Kong]:
G A Duncan, C Zhu, M Namboodiri

Fonterra (CIS) Limited Liability Company [Russian Federation]:
M Bates

Fonterra (Europe) Coöperatie U.A. [Netherlands]:
G A Duncan, H Huistra, A Wright

Fonterra (Europe) GmbH [Germany]:
A Wright

Fonterra (France) SAS [France]:
H Huistra

Fonterra (Ing.) Limited [Mauritius]:
G Lee, B M Ryan

Fonterra (Japan) Limited [Japan]:
K Kumagai, H Ono, Y Saito, K Ueta, B M Ryan, K A Wickham

Fonterra (Korea) Limited [Korea]:
G A Duncan, Y Saito (R), J Murney

Fonterra (Logistics) Ltd [United Kingdom]:
G R Sharma, A Wright

Fonterra (Mexico) S.A. de C.V. [Mexico]:
G A Duncan, M M Pérez Ortiz (R), P D Washer (R), L Barona Mariscal (A), F R Camacho (A), G A Castro Palafox (A) (R), J P Coote, J A Del Rio, E P G R Gil (A)

Fonterra (SEA) Pte. Ltd. [Singapore]:
B Connolly (R), J C M Fair (R), H Gowans, A Aggarwal

Fonterra (Thailand) Limited [Thailand]:
K Vunthanadit, B Connolly (R), A Aggarwal

Fonterra (USA) Inc. [United States]:
G A Duncan, B M Ryan, J P Coote, N R Christiansen

Fonterra (Ying) Dairy Farm Company Limited [China]:
R M Kennerley, A van der Nagel (R), G A Duncan, H Berghorst

Fonterra (Yutian) Dairy Farm Company Limited [China]:
R M Kennerley, A van der Nagel (R), G A Duncan, H Berghorst

Fonterra Argentina S.R.L. [Argentina]:
L P Wiener

Fonterra Australia Pty Ltd [Australia]:
G A Duncan, J Swales (R), R Dedoncker

Fonterra Beijing Farm Management Consulting Company Limited [China]:
R M Kennerley, A van der Nagel, L O'Neil

Fonterra Brands (Asia Holdings) Pte. Ltd [Singapore]:
M W Smith (R), M R Cronin, S I Ahmed, A Dasgupta

Fonterra Brands (Australia) Pty Ltd [Australia]:
G A Duncan, J Swales (R), R Dedoncker

Fonterra Brands (Far East) Limited [Hong Kong]:
G A Duncan, M Namboodiri, S C Deschamps

Fonterra Brands (Guangzhou) Ltd [China]:
K A Wickham, A R R Kasireddy, R M Kennerley

Fonterra Brands (Guatemala), S.A. [Guatemala]:
A J Cordner, G A Duncan, K J Murray (R)

Fonterra Brands (Hong Kong) Limited [Hong Kong]:
G A Duncan, M Namboodiri, S C Deschamps

Fonterra Brands (Malaysia) Sdn Bhd [Malaysia]:
M W Smith (R), J M Porraz, J Ling, F Spinelli

Fonterra Brands (New Young) Pte. Ltd. [Singapore]:
Y Lin, C Lin, J Ling, M W Smith (R), S C Deschamps, Y Li, A Dasgupta

Fonterra Brands (Singapore) Pte. Ltd [Singapore]:
M W Smith (R), M R Cronin, A Dasgupta

Fonterra Brands (Thailand) Ltd [Thailand]:
C Phaonimmongkol (R), M W Smith (R), P A Richards, P Oh, F Spinelli

Fonterra Brands (Viet Nam) Company Limited [Vietnam]:
A M Fitzsimmons (R), M W Smith (R), A Renard, F Spinelli

Fonterra Brands Indonesia, PT [Indonesia]:
M W Smith (R), A Afiffudin, M Namjoshi, A R R Kasireddy (R), J H Priem (R), J Chow, F Spinelli

Fonterra Brands Lanka (Private) Limited [Sri Lanka]:
J H P Gallage, M W Smith (R), S Sethi, F Spinelli

Fonterra Brands Manufacturing Indonesia, PT [Indonesia]:
M W Smith (R), M A Nasution, T A Siswanto, A R R Kasireddy (R), M Namjoshi, J H Priem (R), J Chow, F Spinelli

Fonterra Brands Myanmar Co Ltd [Myanmar]:
G A Duncan, M W Smith (R), P Richards

Fonterra Brands Phils. Inc. [Philippines]:
L T Barin, R A Mendoza, E T Ogsimer, M W Smith (R), S Choo, M T Boness, F Spinelli

Fonterra Commercial Trading (Shanghai) Company Limited [China]:
W F Chu (R), G A Duncan, A R R Kasireddy (R), R M Kennerley (R), K A Wickham (R), R Allen, J Ruan, S C R Deschamps, C Zhu

Fonterra Egypt Limited [Egypt]:
G A Duncan, A Anwar

Fonterra Europe Manufacturing B.V. [Netherlands]:
H Berghorst, C E Rowe

Fonterra Europe Manufacturing Holding B.V. [Netherlands]:
G A Duncan, H Huistra

Fonterra Farming Ventures (Australia) Pty Ltd [Australia]:
G A Duncan, A Maharaj

STATUTORY INFORMATION CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

Fonterra Foodservices (USA), Inc. [United States]:
G A Duncan, R J Pedersen (R), J P Coote, N R Christiansen

Fonterra Global Business Services Asia Sdn Bhd [Malaysia]:
J Ling, J M Porraz

Fonterra India Private Limited [India]:
G N Kane (R), K M Turner, H D Gowans, S G Matthews

Fonterra Ingredients Australia Pty Ltd [Australia]:
G A Duncan, J Swales (R), A Maharaj

Fonterra Investments Netherlands Coöperatie U.A. [Netherlands]:
H Huistra, B M Ryan, G A Duncan

Fonterra Middle East FZE [United Arab Emirates]:
G A Duncan, A M Fitzsimmons

Fonterra MIH Holdings Brasil Ltda [Brazil]:
R Carneiro (R), F Spinelli (R), M P Bueno, G Nascimento

Fonterra Milk Australia Pty Ltd [Australia]:
G A Duncan, A Maharaj

Fonterra Tangshan Dairy Farm (HK) Limited [Hong Kong]:
A van der Nagel (R), R M Kennerley, H Berghorst

Fonterra Venezuela, S.A. [Venezuela]:
F C Ortega Becea, G A Duncan, M M Perez

Inversiones Dairy Enterprises S.A. [Chile]:
J P Egaña Bertoglia (A), R Sepúlveda Seminario, F Spinelli, R Lavados (A), P L Linhares (A), G A Duncan

Key Ingredients, Inc. [United States]:
G A Duncan, B M Ryan, J P Coote, N R Christiansen

Lactaid Holdings Ltd [Barbados]:
M F Maldonado, A D Turnbull, L Hartmann, F Spinelli, L J Paravicini

Lacven Corp [Barbados]:
M F Maldonado, A Turnbull, L Hartmann, L J Paravicini, F Spinelli

Milk Products Holdings (Middle East) EC [Bahrain]:
M W Smith (R), G A Duncan, A Fitzsimmons, F Spinelli

Milk Products Holdings (North America) Inc. [United States]:
G A Duncan (R), B M Ryan, R Pedersen (R), J P Coote, N R Christiansen

New Tai Milk Products Co Ltd [Taiwan]:
G N Kane (R), C Lee, G Lee, M Lee, B M Ryan, J H Priem, K Lee, K A Wickham

New Zealand Milk (Australasia) Pty Ltd [Australia]:
G A Duncan, A Maharaj

New Zealand Milk (Barbados) Ltd [Barbados]:
G A Duncan, F Spinelli

New Zealand Milk (LATAM) Ltd [Bermuda]:
G A Duncan, F Spinelli

New Zealand Milk Products (Ethiopia) SC [Ethiopia]:
A Fitzsimmons, M Woodward, M W Smith (R), M Smith (R), A B Abubeker, M B Abubeker

Newdale Dairies (Private) Limited [Sri Lanka]:
J H P Gallage, M W Smith (R), S Sethi, F Spinelli

NZMP (AEM) Ltd [United Kingdom]:
G R Sharma, A Wright

NZMP Fonterra Nigeria Limited [Nigeria]:
G A Duncan, H Huistra

Pure Source Dairy Farm Company Limited [Hong Kong]:
R M Kennerley, A van der Nagel (R), J F Ginascol, Y Chen, H Berghorst

Sociedad Agrícola y Lechera Praderas Australes S.A. ("Pradesur") [Chile]:
J C Petersen, R Waldspurger, M Kunstmann

Sociedad Procesadora de Leche Del Sur S.A. [Chile]:
E Alcalde Undurraga, A Cussen Mackenna (R), J Milic Barros, A J R Valente Vias, G Varela, J M Alcalde Undurraga (A), G Jiménez Barahona (A), J P Matus Pickering (A), S Oddo Gómez (A), C Perez-Cotapos Subercaseaux (A), J P Egana Bertoglia (A), F Spinelli (R), T Walker Prieto, R Lavados McKenzie (A), M W Hurrell

Solid Fresh Food & Beverage (M) Sdn. Bhd. [Malaysia]:
M W Smith (R), J M Porraz, J Ling, F Spinelli

Soprole Inversiones SA [Chile]:
A D Turnbull (R), J R Valente Vias, G Varela Alfonso, S Diez Arriagada (A), C Herrera Barriga (A), R Sepúlveda Seminario (A), M Somarriva Labra (A) (R), R Tisi Lanchares (A), L J Paravicini, F Spinelli, P L Linhares (A), R Carneiro

Soprole S.A. [Chile]:
J R Valente Vias, G Varela Alfonso, C Herrera Barriga (A), R Sepúlveda Seminario (A), R A Tisi Lanchares (A), A D Turnbull (R), S Diez Arriagada (A), L J Paravicini, R Carneiro, F Spinelli, P L Linhares (A)

Tangshan Fonterra Dairy Farm Ltd [China]:
R M Kennerley, J L Zhang (R), A van der Nagel (R), G A Duncan, H Berghorst, Q Jiang

Unilac Australia Pty Ltd [Australia]:
G A Duncan, A Maharaj

United Milk Tasmania Pty Limited [Australia]:
G A Duncan, A Maharaj

REMUNERATION FRAMEWORK

A well-designed remuneration framework helps the Co-operative attract and retain talent, and both motivates and recognises the role our people play in the success of the Co-operative.

Fonterra's remuneration framework for salaried staff is based on a 'total remuneration' approach, which is consistent with best practice globally. This includes fixed remuneration (salary), benefits (superannuation and insurance), and variable remuneration (Incentives).

The amounts we pay to our employees are benchmarked against comparable companies in relevant markets, using information obtained from independent remuneration consultants. Adjustments to packages may occur on a cyclical basis, such as an annual salary review, or on an as-needed basis to recognise additional responsibilities.

The framework is designed to take into account budget targets and restraints, market conditions, internal equity, and governance factors such as local legislation, as well as taking into account individual performance.

Fonterra's incentive programmes are designed to drive the Co-operative's performance by:

- Focusing on the Co-operative's primary objective of maximising returns for its farmer shareholders;
- Promoting collaboration and a one team approach to achieve Fonterra's goals;
- Establishing targets which are challenging yet achievable; and linked to team (such as business unit) and group performance.

At the end of each financial year, performance is reviewed and incentive payments are approved by the People, Culture and Safety ("PCS") Committee at its discretion. The Committee retains absolute discretion in respect to payments for all incentive schemes.

Further detail on Fontera's remuneration framework can be found in the Corporate Governance section of the Annual Review on page 73.

EMPLOYEE REMUNERATION

The Group operates in a number of countries where remuneration market levels differ widely. During the year ended 31 July 2017, the number of employees, not being Directors of Fonterra, who received remuneration and the value of other benefits exceeding $100,000 was as follows:

REMUNERATION RANGE ($)		NEW ZEALAND[1]	OFFSHORE[2]	CESSATIONS[3]	TOTAL
100,000	110,000	917	193	58	**1,168**
110,001	120,000	797	233	29	**1,059**
120,001	130,000	444	188	24	**656**
130,001	140,000	234	161	23	**418**
140,001	150,000	183	110	13	**306**
150,001	160,000	140	90	12	**242**
160,001	170,000	119	57	11	**187**
170,001	180,000	86	63	8	**157**
180,001	190,000	74	39	8	**121**
190,001	200,000	61	32	7	**100**
200,001	210,000	57	27	7	**91**
210,001	220,000	46	31	2	**79**
220,001	230,000	30	21	4	**55**
230,001	240,000	33	22	2	**57**
240,001	250,000	29	14	4	**47**
250,001	260,000	14	14	2	**30**
260,001	270,000	17	9	3	**29**
270,001	280,000	22	14	2	**38**
280,001	290,000	19	16	2	**37**
290,001	300,000	11	13	2	**26**
300,001	310,000	15	12	1	**28**
310,001	320,000	8	10	–	**18**
320,001	330,000	6	9	1	**16**
330,001	340,000	9	12	1	**22**
340,001	350,000	7	7	2	**16**
350,001	360,000	3	5	1	**9**
360,001	370,000	2	7	2	**11**
370,001	380,000	2	3	1	**6**
380,001	390,000	4	6	–	**10**
390,001	400,000	3	4	–	**7**
400,001	410,000	4	2	–	**6**
410,001	420,000	5	5	1	**11**
420,001	430,000	5	4	–	**9**
430,001	440,000	5	1	1	**7**
440,001	450,000	1	5	–	**6**
450,001	460,000	4	3	2	**9**
460,001	470,000	4	1	1	**6**
470,001	480,000	6	2	–	**8**
480,001	490,000	–	3	1	**4**
490,001	500,000	2	4	–	**6**
500,001	510,000	1	4	1	**6**
510,001	520,000	1	3	–	**4**
520,001	530,000	1	4	1	**6**
530,001	540,000	–	3	–	**3**
540,001	550,000	2	–	–	**2**
550,001	560,000	–	1	–	**1**
560,001	570,000	2	–	–	**2**
570,001	580,000	2	2	1	**5**
580,001	590,000	–	2	1	**3**

REMUNERATION RANGE ($)		NEW ZEALAND[1]	OFFSHORE[2]	CESSATIONS[3]	TOTAL
590,001	600,000	2	–	–	**2**
610,001	620,000	3	1	–	**4**
620,001	630,000	–	2	–	**2**
630,001	640,000	4	3	–	**7**
640,001	650,000	2	–	–	**2**
650,001	660,000	2	1	–	**3**
660,001	670,000	2	1	–	**3**
670,001	680,000	–	2	–	**2**
680,001	690,000	1	–	–	**1**
690,001	700,000	2	–	–	**2**
700,001	710,000	1	3	1	**5**
710,001	720,000	1	1	–	**2**
720,001	730,000	1	1	–	**2**
730,001	740,000	2	1	–	**3**
740,001	750,000	1	1	–	**2**
760,001	770,000	–	1	1	**2**
780,001	790,000	2	1	1	**4**
790,001	800,000	–	2	–	**2**
800,001	810,000	–	1	–	**1**
810,001	820,000	1	–	–	**1**
820,001	830,000	–	1	–	**1**
840,001	850,000	–	1	–	**1**
850,001	860,000	–	1	–	**1**
880,001	890,000	1	–	–	**1**
890,001	900,000	–	1	–	**1**
910,001	920,000	1	1	–	**2**
930,001	940,000	–	–	1	**1**
940,001	950,000	–	2	–	**2**
950,001	960,000	–	1	–	**1**
960,001	970,000	–	1	–	**1**
970,001	980,000	1	1	–	**2**
990,001	1,000,000	–	2	–	**2**
1,020,001	1,030,000	–	–	1	**1**
1,040,001	1,050,000	1	–	–	**1**
1,060,001	1,070,000	1	–	–	**1**
1,080,001	1,090,000	–	–	1	**1**
1,090,001	1,100,000	–	1	–	**1**
1,110,001	1,120,000	1	–	–	**1**
1,150,001	1,160,000	1	–	–	**1**
1,180,001	1,190,000	1	1	–	**2**
1,260,001	1,270,000	1	–	–	**1**
1,300,001	1,310,000	–	1	–	**1**
1,370,001	1,380,000	–	1	–	**1**
1,380,001	1,390,000	1	1	–	**2**
1,490,001	1,500,000	–	–	1	**1**
1,610,001	1,620,000	–	–	1	**1**
1,710,001	1,720,000	–	1	–	**1**
1,750,001	1,760,000	–	1	–	**1**
2,050,001	2,060,000	1	–	–	**1**
2,070,001	2,080,000	1	–	–	**1**
2,660,001	2,670,000	1	–	–	**1**
2,870,001	2,880,000	1	–	–	**1**
2,980,001	2,990,000	–	–	1	**1**
3,250,001	3,260,000	1	–	–	**1**
8,320,001	8,330,000	1	–	–	**1**
Total		**3,481**	**1,513**	**251**	**5,245**

1 Includes employees employed in New Zealand during the reporting period.

2 Includes employees employed in an offshore operation during the reporting period. Amounts paid in foreign currency have been translated at the average conversion rate for the period. As Fonterra has a significant offshore population, the number of offshore employees exceeding the fixed figure of $100,000 increases if the New Zealand dollar currency weakens significantly. Should the New Zealand dollar strengthen against those markets' currencies, these same individuals may not be reported in future lists.

3 Cessations include employees that have been terminated or retired during the period. The amounts paid to former employees include salary and bonuses for the current period, prior period bonuses that have been paid in the current period (which were accrued at 31 July 2016) and termination entitlements including those arising from employment arrangements entered into by legacy companies prior to the formation of Fonterra.

STATUTORY INFORMATION CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

CURRENT CREDIT RATING STATUS

Standard & Poor's long term rating for Fonterra is A- with a rating outlook of stable. Fitch's long and short term default rating is A with a rating outlook of stable. Retail Bonds have been rated the same as the Company's long term rating by both Standard & Poor's and Fitch. Capital Notes which are subordinate to other Fonterra debt issued are rated BBB+ by Standard & Poor's and A- by Fitch.

EXCHANGE RULINGS AND WAIVERS

NZX Limited (NZX) has ruled that Capital Notes do not constitute 'equity securities' under the NZX Main Board/Debt Market Listing Rules ('Rules'). This means that where Capital Notes are quoted on NZX's Debt Market ('NZDX'), the Company is not required to comply with certain Rules which apply to an issuer of quoted equity securities.

The Company was issued with a waiver of Rule 11.1.1 to enable it to decline to accept or register transfers of Capital Notes (NZDX listed debt securities FCGHA) if such transfer would result in the transferor holding or continuing to hold Capital Notes with a face value or principal amount of less than $5,000 or if such transfer is for an amount of less than $1,000 or not a multiple thereof. The effect of this waiver is that the minimum holding amount in respect of the Capital Notes will at all times be $5,000 in aggregate and can only be transferred in multiples of $1,000.

The Company was issued with a waiver of Rule 5.2.3 by NZX on 10 April 2015 (for a period of one year from 21 April 2015) in respect of the Company's issuance of $350 million of unsecured, unsubordinated, fixed rate bonds maturing on 20 October 2021 ('FCG030 Bonds'), to the extent that that rule would otherwise require the FCG030 Bonds to be held by at least 500 members of the public holding at least 25% of the FCG030 Bonds.

The Company was also issued with a waiver of Rule 5.2.3, as modified by NZX's ruling on Rule 5.2.3, by NZX on 18 February 2016 (for a period of six months from 8 March 2016) in respect of the Company's issuance of $150 million of unsecured, unsubordinated, fixed rate bonds maturing on 7 March 2023 ('FCG040 Bonds'), to the extent that the rule (as modified) would otherwise require the FCG040 Bonds to be held by at least 100 members of the public holding at least 25% of the FCG040 Bonds.

The effect of these waivers from Rule 5.2.3 is that the FCG030 Bonds and the FCG040 Bonds may not be widely held and there may be reduced liquidity in those bonds.

The Company was issued with a waiver of Rule 7.11.1 by NZX on 18 February 2016 in respect of the Company's issuance of the FCG040 Bonds, to the extent that the rule would have otherwise required the Company to allot the FCG040 Bonds within five business days after the latest date on which applications for the FCG040 Bonds closed.

Fonterra Co-operative Group Limited (Fonterra) was issued with a ruling in respect of Rule 1.7.1(d) of the Fonterra Shareholders' Market Rules on 27 June 2017 by NZX. The effect of this ruling was to not preclude the appointment of Mr Bruce Hassall to the position of an independent director of Fonterra by virtue of a child of Mr Hassall being employed in a non-decision making and non-senior role at Fonterra.

Fonterra was issued with a ruling in respect of Rule 5.1.2(c) on 22 November 2016 by NZX. The effect of this ruling is that Fonterra's internal governance resolutions are considered to be matters that do not require the NZX to approve a notice of meeting under Rule 5.1.1.

Fonterra was issued with a waiver of Rule 3.2.1(c) on 31 August 2016 by the NZX, to the extent that such Rule requires Fonterra to have a minimum of two independent directors or, if Fonterra has eight or more directors, three or one-third of the total number of directors, whichever is greater. This waiver was granted in connection with the resignation of Mr John Waller and applied for a period ending on the earlier of the appointment of a new independent director or three months from the date of the waiver.

NZX TRADING HALTS

No trading halts were placed on Fonterra securities by NZX Regulation in the financial year ended 31 July 2017.

STOCK EXCHANGE LISTINGS

Fonterra's co-operative shares are listed and quoted on the Fonterra Shareholders' Market (operated by NZX Limited for Fonterra) under the code 'FCG'. Fonterra has two issues of retail bonds listed and quoted on the NZDX under the codes 'FCG030' and 'FCG040'. Fonterra also has an issue of capital notes listed and quoted on NZDX under the code 'FCGHA' and a Euro Medium Term Note Programme listed on the Singapore Stock Exchange.

As at 14 August 2017 there were 1,606,932,511 Fonterra Co-operative shares on issue.

ANALYSIS OF SHAREHOLDING

Analysis of Fonterra's shareholding as at 14 August 2017:

FCG Largest Recorded Share Holdings[1]

NAME	NUMBER OF SHARES	% OF SHARES
Fonterra Farmer Custodian Limited	127,307,140	7.92
Ellis-Lea Farms (2000) Ltd – Lamorna	1,032,996	0.06
Singletree Dairies 2013 Limited	1,001,077	0.06
Stewart Partnership Ltd	922,500	0.06
Theland Tahi Farm Group Limited – Pureora	898,786	0.06
Moffitt Dairy Ltd	873,433	0.05
McBain Farms Ltd	867,790	0.05
Arlanda Limited	863,479	0.05
Poplar Partnership Ltd	843,970	0.05
Bishopdale Farm Limited	833,858	0.05
McIntyre Williamson Partnership	819,888	0.05
Van'T Klooster Farms Ltd – Waihao Valley Farm	817,500	0.05
Coringa Park Dairies Ltd	810,666	0.05
Plantation Road Dairies Ltd	794,170	0.05
Van'T Klooster Farms Ltd – Tawai Farm	785,190	0.05
Theland Tahi Farm Group Limited – Ngaherenga	761,354	0.05
Feather Holdings Limited – Wairango	744,898	0.05
Twin Terraces Ltd	742,768	0.05
Elderslie Holdings Limited	742,383	0.05
Ellis-Lea Farms (2000) Ltd – Grandview	736,844	0.05

1 The FSM Rules, which reflect the rules of the NZX Main Board, require that Fonterra's annual report contain the names and holdings of persons having the 20 largest holdings of Fonterra shares on the register of Fonterra as at a date not earlier than two months before the date of the publication of the annual report. The list above complies with the FSM Rules and sets out the list of the 20 largest shareholders on the register as at the appropriate date. There is a separate requirement in the FSM Rules to disclose in the annual report those persons who have a 'Relevant Interest' (as defined in the Financial Markets Conduct Act 2013) in Fonterra shares in excess of five per cent, where this information has been provided to Fonterra. Accordingly, the list of the 20 largest holdings of Fonterra shares is not required to show, and does not purport to show, the top 20 holdings of 'Relevant Interests' in Fonterra shares which may be owned or controlled by a person or entity and their associated entities. Other people or entities may have 'Relevant Interests' in a greater number of Fonterra shares than those listed above. However, it is not possible for Fonterra to accurately determine those interests, nor is it a requirement of the FSM Rules for those interests to be reported in the annual report, except where Fonterra has been advised that a person has a 'Relevant Interest' in excess of the five per cent threshold.

Substantial Product Holders

According to notices given to the Company under the Financial Markets Conduct Act 2013, as at 31 July 2017, the substantial product holders in the Company and their relevant interests are noted below. The total number of Co-operative shares on issue as at 14 August 2017 was 1,606,932,511.

SUBSTANTIAL PRODUCT HOLDERS	NUMBER OF VOTING SECURITIES	DATE OF MOST RECENT NOTICE
Fonterra Farmer Custodian Limited	111,308,130	25 July 2016
FSF Management Company Limited	111,180,848	25 July 2016

More than one 'Relevant Interest' can exist in the same voting financial products. Fonterra Farmer Custodian Limited holds Fonterra shares for the Fonterra Shareholders' Fund, of which FSF Management Company Limited is the manager. These two notices therefore refer to substantially the same Fonterra shares. The Custodian also holds some Fonterra shares for the Registered Volume Provider in respect of the Fonterra Shareholders' Fund.

STATUTORY INFORMATION CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

FCG Fonterra Co-operative Shares

Analysis of Fonterra Co-operative Shares as at 14 August 2017:

FROM–TO	HOLDER COUNT	%	HOLDING QUANTITY	%
1–50,000	1,517	14.84	39,659,088	2.47
50,001–100,000	2,882	28.19	218,982,854	13.63
100,001–200,000	3,477	34.02	488,956,495	30.43
200,001–400,000	1,946	19.04	527,955,956	32.85
400,001 and over	400	3.91	331,378,118	20.62

ANALYSIS OF CAPITAL NOTE AND RETAIL BOND HOLDING

Analysis of Fonterra's Capital Note Holding as at 9 August 2017:

FCGHA Capital Notes

FROM–TO	HOLDER COUNT	%	HOLDING QUANTITY	%
1–1,000	10	1.35	4,358	0.01
1,001–5,000	27	3.65	70,236	0.07
5,001–10,000	247	33.38	1,754,038	1.71
10,001–100,000	423	57.16	12,160,604	11.86
100,001 and over	33	4.46	88,530,018	86.35

100,001 and over includes Fonterra Co-operative Group Limited's holding of 67,435,575.

Analysis of Fonterra's Retail Bond Holding as at 9 August 2017:

FCG030 $350 million Retail Bond issue

FROM–TO	HOLDER COUNT	%	HOLDING QUANTITY	%
5,000–9,999	42	6.68	243,000	0.07
10,000–49,999	319	50.71	7,108,000	2.03
50,000–99,999	83	13.19	5,018,000	1.43
100,000–999,999	161	25.60	52,186,000	14.91
1,000,000 and over	24	3.82	285,445,000	81.56

FCG040 $150 million Retail Bond issue

FROM–TO	HOLDER COUNT	%	HOLDING QUANTITY	%
5,000–9,999	60	9.13	344,000	0.23
10,000–49,999	424	64.54	8,823,000	5.88
50,000–99,999	82	12.48	4,929,000	3.29
100,000–999,999	76	11.57	16,345,000	10.90
1,000,000 and over	15	2.28	119,559,000	79.70

ENTRIES IN THE INTERESTS REGISTER

Directors' interests in transactions

General disclosures of interest

The following general disclosures of interest were made in the period from 1 August 2016 to 31 July 2017:

Clinton Dines	Director of Freedom Road Travel
Ian Farrelly	Chair of Fortuna Group Limited; Director and Shareholder of F.D. Lands Limited, Jamieson Dairies Limited, Kahuterawa Farms Limited; Director of FMM Holdings Limited, Island Glen Dairies Limited, Tower Peak Station Limited, Hinewai Holdings Limited, Spectrum Dairies GP Limited, Totman Dairies Limited and Waikato Stud Limited; ceased as a Director of FSF Management Company Limited
Simon Israel	Director of Stewardship Asia Centre CLG Limited; Member of Westpac Advisory Board; ceased to be a Director of Stewardship Asia Centre Pte Limited, CapitaLand Limited
David Jackson	Chair of Tegel Group Holdings Limited; ceased as a Director of Nuplex Industries Limited
David MacLeod	Director of Predator Free 2050 Limited
Donna Smit	Director of KEL Woodlands Orchard Limited, Director of KEL Rangiuru Orchard Limited and Primary ITO; Director and Shareholder of Corona Farms Limited, Seven Mile Farms Limited, Ballance Agri Nutrients Limited, Kiwifruit Equities Limited and Corona Kiwi Limited; Shareholder of Ravensdown Limited, Eastpack Limited, Farmlands Co-operative Society Limited and Livestock Improvement Corporation Limited; Trustee of Eastern Bay Energy Trust, Taratahi Agricultural Training Centre (Wairarapa) Trust Board and Dairy Women's Network; ceased as Director of Primary ITO; ceased as a Trustee of Eastern Bay Energy Trust
Scott St John	Director of FSF Management Company Limited, Te Awanga Terraces Limited, Hutton Wilson Nominees Limited, Fisher and Paykel Healthcare Corporation Limited, NEXT Foundation, Captain Cook Nominees Limited and First NZ Capital Limited; Trustee of Butland Medical Foundation; Chancellor of the University of Auckland

During the financial year there were no notices from Directors requesting to disclose or use information received in their capacity as Directors which would not otherwise have been available to them.

Securities dealings of Directors

The following entries were made in the Interests Register during the year.

New disclosures

Directors disclosed the following holdings of Co-operative shares during the year:

	RELEVANT INTERESTS IN CO-OPERATIVE SHARES
Donna Smit (on appointment 8 December 2016)	1,457,589

During the year, Directors disclosed in respect of section 148(2) of the Companies Act 1993 and/or section 297 of the Financial Markets Conduct Act 2013 that they (or their associated persons) acquired or disposed of a relevant interest in financial products as follows:

Co-operative share transactions

DIRECTOR	NUMBER OF SECURITIES ACQUIRED	NUMBER OF SECURITIES DISPOSED	CONSIDERATION $	DATE
John Wilson[1]	25,182[1]	25,182[1]	–	10 November 2016
John Wilson	–	31,614	–	30 November 2016

1 Transfers between related entities.

Unit transactions

There were no transactions by Directors (or their associated persons) in Units reported during the period from 1 August 2016 to 31 July 2017.

Retail Bond transactions

There were no transactions by Directors (or their associated persons) in Retail Bonds reported during the period from 1 August 2016 to 31 July 2017. No current holdings of Retail Bonds have been advised by Directors (or their associated persons).

Capital Note transactions

There were no transactions by Directors (or their associated persons) in Capital Notes reported during the period from 1 August 2016 to 31 July 2017. No current holdings of Capital Notes have been advised by Directors (or their associated persons).

STATUTORY INFORMATION CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

Directors' remuneration

The Directors' Remuneration Committee, comprising six shareholders elected in accordance with the Constitution, makes recommendations for shareholder approval as to the level of Directors' fees.

At the Annual Meeting of shareholders held on 8 December 2016, shareholders approved, on the recommendation of the Directors' Remuneration Committee, the following amounts of remuneration to apply to Elected Directors from the date of that Annual Meeting of shareholders.

Chairman	$405,000 p.a.
Directors	$165,000 p.a.
Discretionary additional payments to the Chair of permanent Board Committees (except if the Chair is the Fonterra Chairman)	$31,000 p.a.

The Board has approved payment of the discretionary additional payment, at the prevailing approved rate, to the Chair of permanent Board Committees.

The Board has discretion to set the fees for Directors appointed under clause 12.4 of the Constitution (Appointed Directors). In the period to 31 July 2017 the Board applied the same remuneration levels as above to the Appointed Directors.

The Board has approved the payment to Mr Israel of a travel allowance of $10,000 per meeting for travel to and from New Zealand to attend Board meetings.

Fees paid by subsidiary or associate companies in respect of Fonterra Directors or employees appointed by Fonterra as Directors of those companies are payable directly to Fonterra.

Directors' indemnity and insurance

Fonterra has given indemnities to, and has effected insurance for, Directors and executives of the Company and its related companies, in accordance with section 162 of the Companies Act 1993, and clause 35 of Fonterra's Constitution, which, except for specific matters that are expressly excluded, indemnify and insure Directors and executives against monetary losses as a result of actions undertaken by them in the course of their duties. Among the matters specifically excluded are penalties and fines that may be imposed for breaches of law.

FIVE YEAR SUMMARY

FOR THE YEAR ENDED 31 JULY 2017

	JULY 2017	JULY 2016	JULY 2015	JULY 2014	JULY 2013
SHAREHOLDER SUPPLIER RETURNS					
Payout					
Farmgate Milk Price (per kgMS)[1]	**6.12**	3.90	4.40	8.40	5.84
Dividend (per share)	**0.40**	0.40	0.25	0.10	0.32
Cash payout[2]	**6.52**	4.30	4.65	8.50	6.16
Retentions (per share)[3]	**0.06**	0.11	0.04	–	0.14
OPERATING PERFORMANCE					
Average commodity prices (US$ per MT FOB)					
Whole Milk Powder[4]	**2,855**	2,111	2,639	4,824	3,394
Skim Milk Powder[4]	**2,216**	1,803	2,552	4,504	3,625
Butter[4]	**4,221**	2,830	3,027	3,920	3,550
Cheese[5]	**3,763**	2,766	3,477	4,706	4,124
Average NZD/USD spot exchange rate applying throughout the year[6]	**0.71**	0.67	0.76	0.84	0.82
Fonterra's average NZD/USD conversion rate[7]	**0.70**	0.71	0.79	0.81	0.80
Revenue ($ million)					
Ingredients and other revenue	**12,715**	10,903	12,144	17,748	13,926
Consumer revenue	**6,517**	6,296	6,701	4,527	4,717
Total revenue	**19,232**	17,199	18,845	22,275	18,643
Dairy ingredients manufactured in New Zealand (000s MT)	**2,379**	2,466	2,753	2,519	2,312
Total ingredients sales volume (000s MT)[8]	**3,018**	3,074	2,982	3,052	2,765
Segment earnings ($ million)[9]					
Global Ingredients and Operations	**484**	864	673	280	480
Oceania	**206**	137	(156)	31	93
Asia	**194**	235	192	50	207
Greater China	**130**	64	(5)	30	–
Latin America	**102**	125	256	111	137
Eliminations	**4**	6	(18)	1	20
Segment earnings	**1,120**	1,431	942	503	937
Normalisation adjustments	**35**	(73)	32	–	65
Normalised segment earnings	**1,155**	1,358	974	503	1,002
Profit after tax attributable to shareholders ($ million)	**734**	810	466	157	718
Earnings per share[10]	**0.46**	0.51	0.29	0.10	0.44

1 From the beginning of the 2009 season the Farmgate Milk Price has been determined by the Board. In making that determination, the Board takes into account the Farmgate Milk Price calculated in accordance with the principles set out in the Farmgate Milk Price Manual.

2 Average payout for a 100 per cent share-backed supplier.

3 Retentions are calculated as net profit after tax attributable to Co-operative shareholders at 31 July divided by the number of shares at 31 May, less dividend per share.

4 Source: Fonterra Farmgate Milk Price Statement representing the weighted-average United States Dollar (USD) contract prices of Reference Commodity Products.

5 Source: Oceania Export Series, Agricultural Marketing Service, US Department of Agriculture.

6 Average spot exchange rate is the average of the daily spot rates for the financial period.

7 Fonterra's average conversion rate is the rate that Fonterra has converted net United States Dollar receipts into New Zealand Dollars based on the hedge cover in place.

8 For the year ended 31 July 2014 the total ingredients sales volume has been restated to reflect Fonterra's strategic platforms. Figures for the year ended 31 July 2013 have not been restated.

9 Represents segment earnings before unallocated finance income, finance costs and tax. For the years ended 31 July 2016, 2015 and 2014, Greater China has been disclosed separately in alignment with the disclosures in the segment note. For the years ended 31 July 2013 and earlier, Greater China was part of Asia. The year ended 31 July 2015 has been restated to reflect changes to the organisation of business units that occurred in the year ended 31 July 2016. The year ended 31 July 2014 has been restated to reflect changes to the organisation of business units that occurred in the year ended 31 July 2015.

FIVE YEAR SUMMARY CONTINUED

FOR THE YEAR ENDED 31 JULY 2017

	JULY 2017	JULY 2016	JULY 2015	JULY 2014	JULY 2013
KEY CAPITAL MEASURES ($ million)					
Equity excluding hedge reserve	**7,056**	6,883	7,196	6,452	6,830
Economic net interest-bearing debt[10]	**5,601**	5,473	7,120	4,732	4,467
Economic debt to debt plus equity ratio[11]	**44.3%**	44.3%	49.7%	42.3%	39.6%
Capital employed[12]	**9,093**	9,392	9,487	8,493	8,249
Return on capital[13]	**11.1%**	12.4%	8.9%	4.7%	10.5%
STAFF EMPLOYED					
Total staff employed (000s, permanent full time equivalents)	**21.4**	21.3	22.0	18.2	17.5
New Zealand	**11.7**	11.4	11.9	11.4	11.2
Overseas	**9.7**	9.9	10.1	6.8	6.3
SEASON STATISTICS[14]					
Total NZ milk collected (million litres)	**17,051**	17,585	18,143	17,932	16,673
Highest daily volume collected (million litres)	**80.1**	86.9	89.7	87.1	84.8
NZ shareholder supply milk solids collected (million kgMS)	**1,417**	1,453	1,520	1,533	1,424
NZ contract supply milk solids collected (million kgMS)	**109**	113	94	51	39
NZ milk solids collected (million kgMS)	**1,526**	1,566	1,614	1,584	1,463
Total number of shareholders at 31 May	**10,267**	10,579	10,753	10,721	10,668
Total number of sharemilkers at 31 May	**2,722**	3,098	3,379	3,398	3,449
Total number of shares at 31 May (million)	**1,607**	1,602	1,599	1,598	1,598

10 Economic net interest-bearing debt reflects total borrowings less cash and cash equivalents and non-current interest-bearing advances adjusted for derivatives used to manage changes in hedged risks.

11 Economic debt to debt plus equity ratio is calculated as economic net interest-bearing debt divided by economic net interest-bearing debt plus equity excluding hedge reserves.

12 Capital employed excludes brands, goodwill and equity accounted investments.

13 Return on capital is calculated as normalised EBIT, less equity accounted investees' earnings, divided by capital employed.

14 All season statistics are based on the 12 month milk season of 1 June–31 May.

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Fonterra

Dairy for life

PERFORMANCE REVIEW

Annual Results 2017

25 SEPTEMBER 2017

OUR CO-OPERATIVE
OUR POTENTIAL
OUR PERFORMANCE

Disclaimer

This presentation may contain forward-looking statements and projections. There can be no certainty of outcome in relation to the matters to which the forward-looking statements and projections relate. These forward-looking statements and projections involve known and unknown risks, uncertainties, assumptions and other important factors that could cause the actual outcomes to be materially different from the events or results expressed or implied by such statements and projections. Those risks, uncertainties, assumptions and other important factors are not all within the control of Fonterra Co-operative Group Limited (Fonterra) and its subsidiaries (the Fonterra Group) and cannot be predicted by the Fonterra Group.

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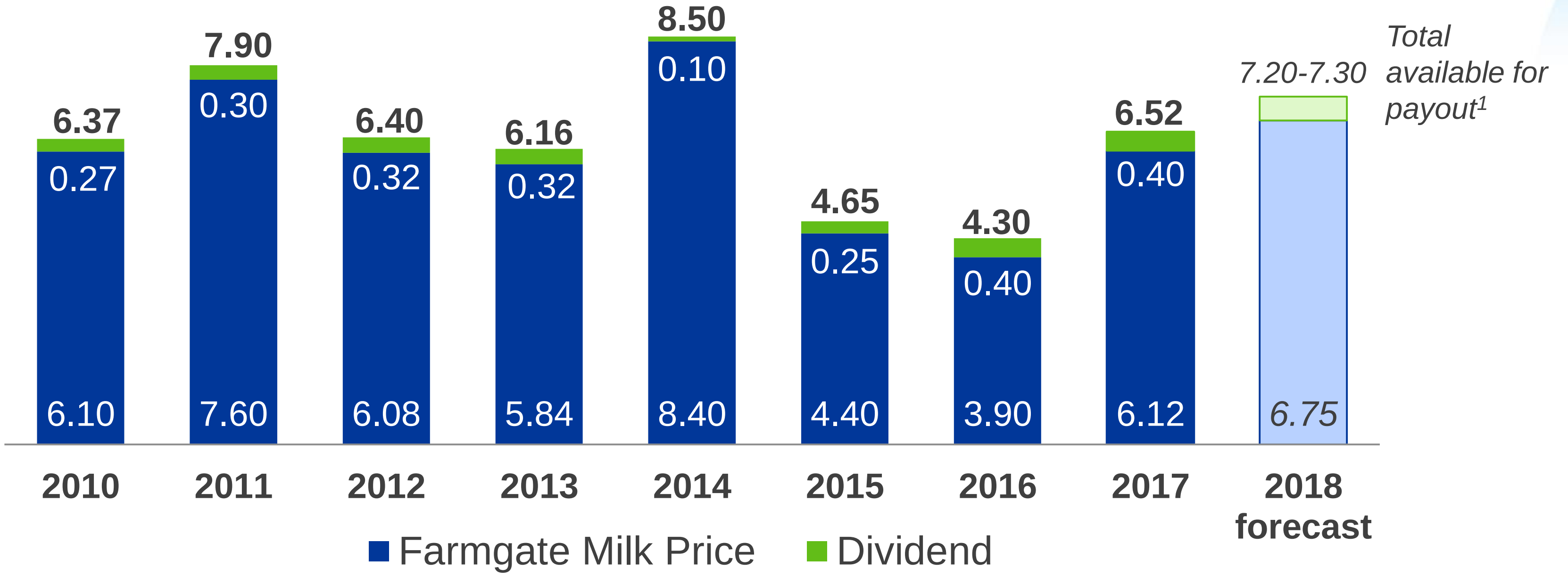
Our Co-Operative

Good season for our farmers

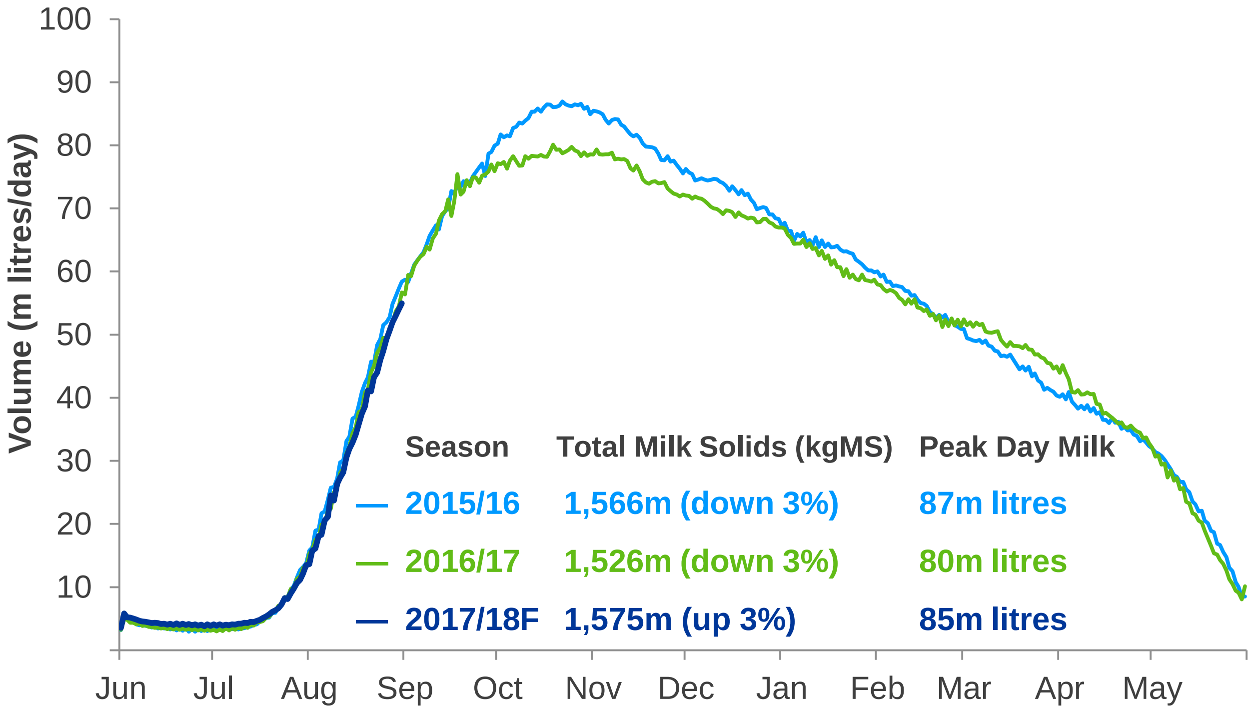
Return to solid results after two seasons of unusually low milk prices



1. Total available for payout = Forecast Farmgate Milk Price + Forecast Earnings Per Share (EPS) of 45-55 cents; For farm budgeting purposes the likely dividend will be calculated in accordance with Fonterra policy of paying out 65-75 per cent of adjusted net profit after tax over time

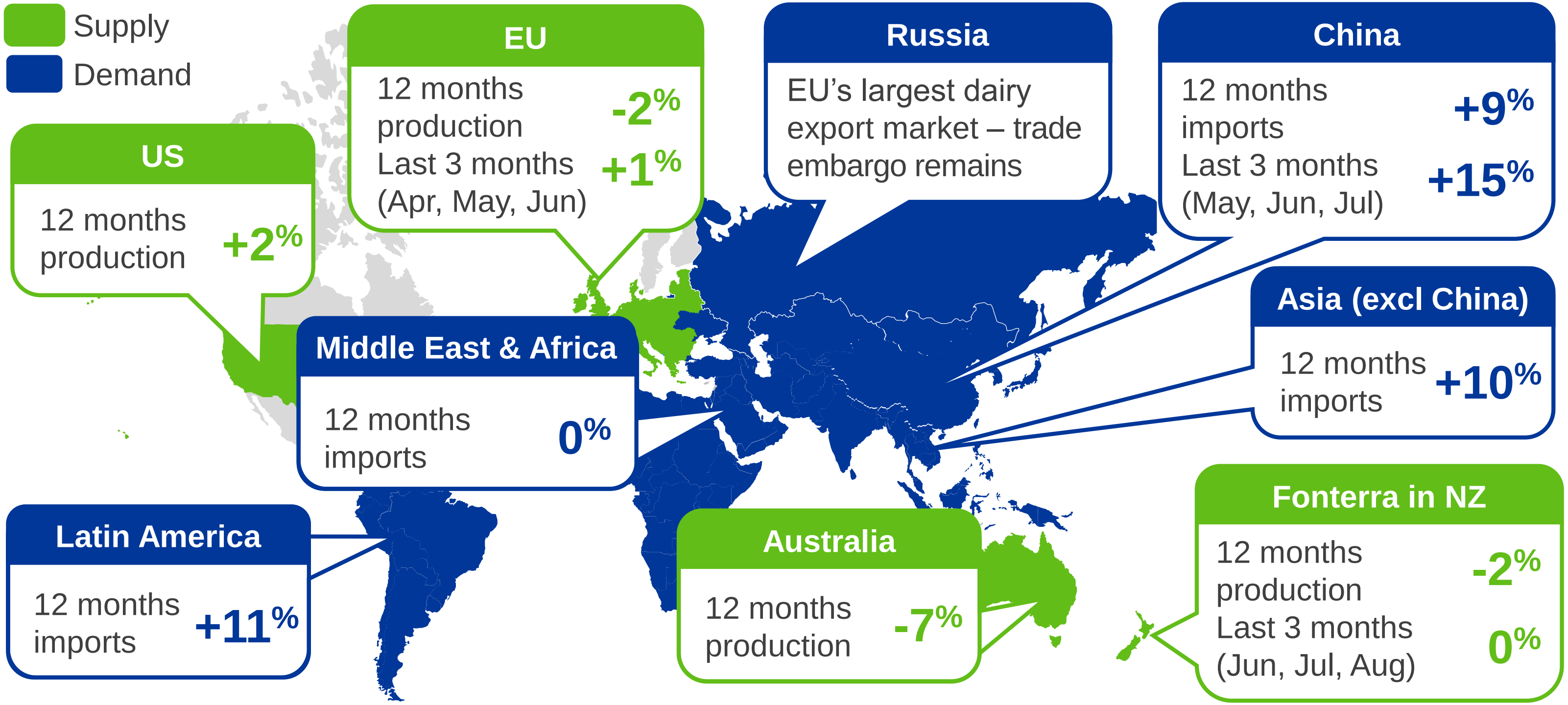
Note: Farmgate Milk Price: $ per kgMS; Dividend: $ per share

Milk supply recovering to 2015/16 season levels



- 2016/17 season ended at 1,526m kgMS
- Wet spring conditions offset by stronger autumn production
- 2017/18 season forecast volumes of 1,575m kgMS, back to more normal levels
- Strong winter milk production but wet conditions impacting recent production

Global dairy market – positive outlook with continued balancing of supply and demand



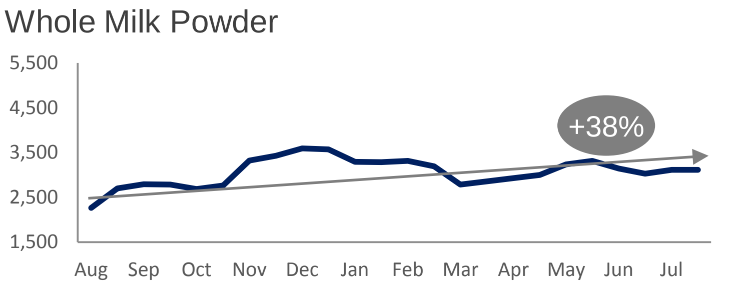
Note: All 12 month figures are rolling 12 months compared to previous comparable period: Australia (Jun), EU (Jun), United States (Jul), China (Jul), Asia (May), Middle East & Africa (May), Latin America (May)

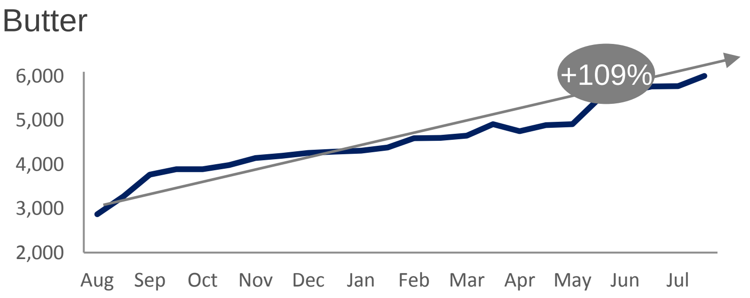
Source: Government milk production statistics; GTIS trade data; Fonterra analysis]

Dairy prices rose strongly in response over the year

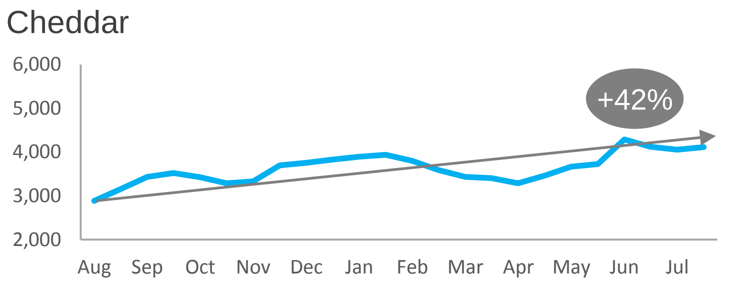
Improved Farmgate Milk Price put pressure on margins

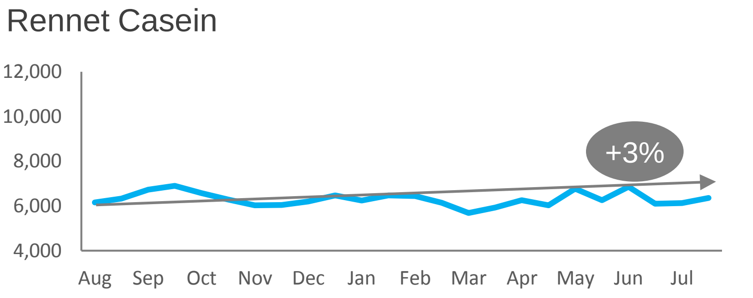
Products informing milk price up significantly





Other products up but to a lower degree



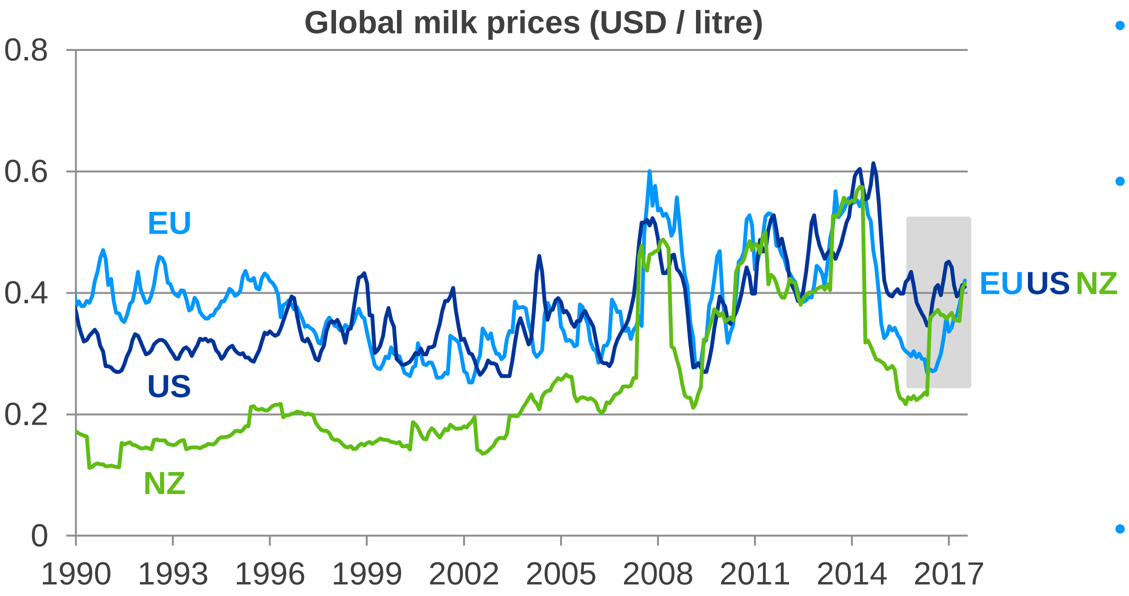


Note: All prices in US dollars per MT

Source: GDT data

Globally competitive cash payout

Driven by strong Co-op and world-class strategy



- 2016/17 $6.12 milk price added additional $3 billion into the NZ economy
- Farmgate Milk Price Manual reinforces competitive milk price
  - FY17: added six cents from manual change plus three cents through efficiencies[1]
  - Since 2009: added 45 cents per kgMS in total
- Transparent Farmgate Milk Price and demand-led strategy strengthened cash payout

1. Refer Farmgate Milk Price Statement for detailed explanation of changes in assumptions for season 2016/17

Note: All prices are adjusted to a milk composition of 3.5% protein and 4.2% fat and for spot exchange rates

Source: DairyNZ (NZ to May 2014); Fonterra announced payout (milk price and dividend) (NZ from June 2014); USDA; European Milk Market Observatory (Netherlands milk price)

Our Potential

Global Context	• Outlook for dairy remains strong • Improved prices with positive outlook but volatility will continue • Opportunities despite continued geopolitical uncertainty
Value Creation	• Strategy delivering – higher milk price and solid profit • Demand led-strategy to optimise NZ milk, supported by our offshore milk • Investing in technology and people for the future
Trust	• Step-change in engagement with our people • Ongoing involvement in our communities • Creating sustainable long-term value

Solid business performance

VOLUME

22.9B LME

↓ 3%

REVENUE

$19.2B

↑ 12%

NORMALISED EBIT

$1,155M

↓ 15%

RETURN ON CAPITAL[1]

11.1%

↓ Down from 12.4%

NPAT

$745M

↓ 11%

EPS

46c

ANNUAL DIVIDEND

40CPS

Stable

YIELD[2]

6.7%

Ingredients

Volume (LME)[3]	↓	21.3 B
Gross Margin (%)	↓	9.7%
Normalised EBIT	↓	$943M
Return on Capital[1]	↓	10.3%

Consumer and Foodservice

Volume (LME)[3]	↑	5.5 B
Gross Margin (%)	↓	26.8%
Normalised EBIT	↑	$614M
Return on Capital[1]	↑	47.2%

China Farms

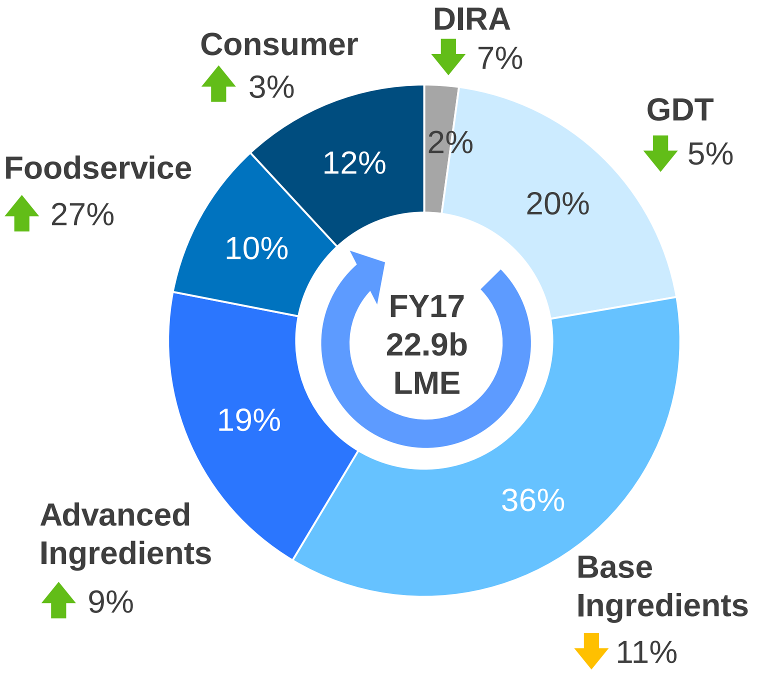
Volume (LME)[3]	↑	0.3B
Gross Margin (%)	↑	8.6%
Normalised EBIT	↑	$1M

1. Return on Capital (ROC) excludes goodwill, brands and equity accounted investments; Group ROC including these items was 8.3% in FY17 (FY16: 9.2%)
2. FY17 dividend over volume weighted average FCG price of $5.96 across the year; 3. Includes sales to other strategic platforms.

More volume to higher value

1 billion LMEs shifted to Consumer, Foodservice and Advanced Ingredients

1. **Optimise** NZ milk
2. **Build and grow** beyond our current consumer positions
3. **Deliver** on Foodservice potential
4. **Grow** our active living business
5. **Develop** leading positions in paediatric & maternal nutrition
6. **Selectively invest** in milk pools
7. **Align** our business and organisation



- **GDT**
  - Volumes aligned with lower production
- **Ingredients**
  - Lower NZ milk collections and record low closing inventory
  - 473m LMEs shifted to higher margin Advanced Ingredients
- **Consumer & Foodservice**
  - Added 576m more LMEs
  - Normalised EBIT up 6%

%	*FY17 sales volume growth over FY16*

Note: Wheel shows percentage of total FY17 external sales (LME); Consumer, Foodservice and Ingredients growth rates include intercompany sales

Delivery of FY17 strategic priorities

Priority		Achievements
1 **Optimise** NZ milk	▪ Optimise Global Operations ▪ Deliver sustainable price achievement	Production costs lower Advanced Ingredients up 9%
2 **Build and grow** beyond our current consumer positions 3 **Deliver** on Foodservice potential 4 **Grow** our active living business 5 **Develop** leading positions in paediatric & maternal nutrition	▪ Drive Consumer growth strategy ▪ Deliver double-digit Foodservice growth ▪ Transform Brazil ▪ Enhance and grow the Beingmate partnership	Successful Anlene re-launch 27% volume growth Solid progress in difficult market Responding to structural market challenges
6 **Selectively invest** in milk pools	▪ Unlock value of China Farms ▪ Complete Australian transformation	Low local milk prices, but progress on costs and downstream initiatives $200m+ turnaround
7 **Align** our business and organisation	▪ Embed Velocity into BAU ▪ Embed disruptive innovation mindset	3-year targets hit in Year 2 New ventures launched

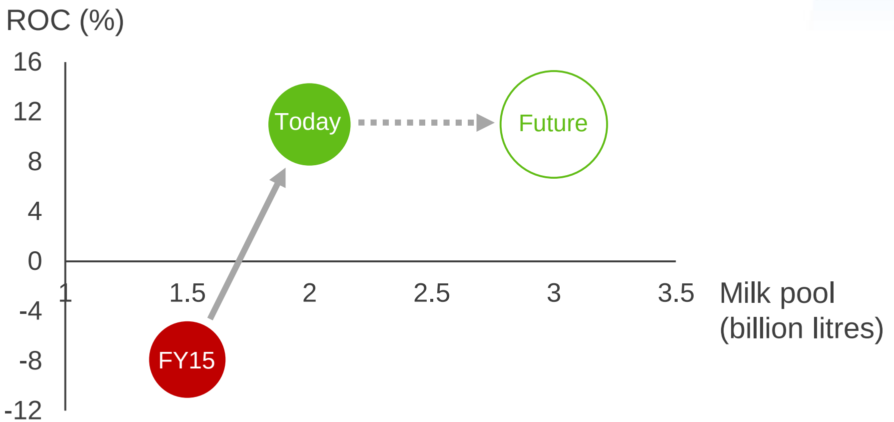
Australia – delivering on our offshore milk strategy

Vertically integrated cheese / whey / nutritionals milk pool

$200m plus turnaround over two years

- Right assets
  - Optimal asset footprint now in place
  - 50% expansion in Stanhope capacity
  - Hi-tech distribution centre opening in October
- Right product mix
  - Mix centred around cheese / whey / nutritionals
  - Exited unprofitable contracts and product portfolios
  - Strong growth in dairy ingredient exports
- Right cost-base
  - Overheads reduced by 22%[1]
  - Owners mindset well embedded in business
  - Continued focus on cost leadership in operations

Growing volume and value in Australia



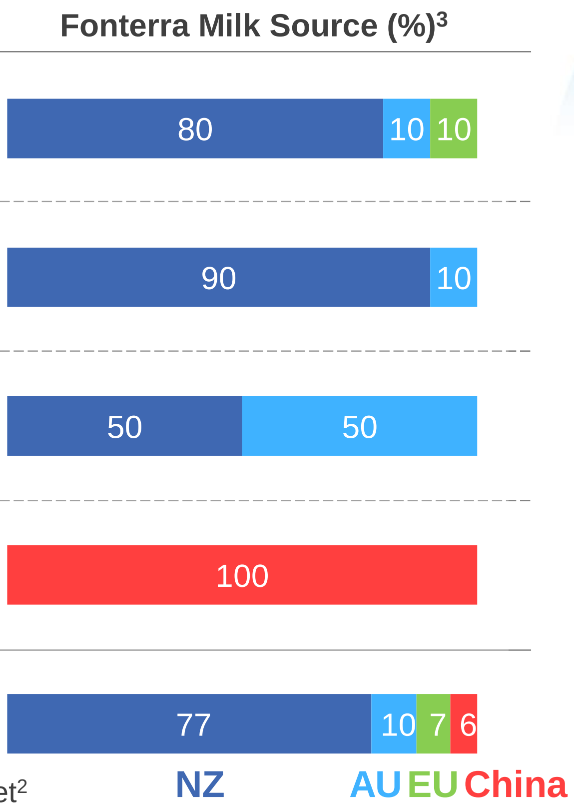
1. FY17 compared with FY15

China opportunity

Fonterra well positioned in every segment

1. **Optimise** NZ milk
2. **Build and grow** beyond our current consumer positions
3. **Deliver** on Foodservice potential
4. **Grow** our active living business
5. **Develop** leading positions in paed & maternal nutrition
6. **Selectively invest** in milk pools
7. **Align** our business and organisation

LME b	2013	TODAY
nzmp — **Ingredients**		
China market	8b	8b
Fonterra	3.5b	3.7b
Anchor — **Consumer & Foodservice**		
China market	28b	31b
Fonterra	0.4b	1.3b
Anlene, Anmum, Beingmate — **Advanced Nutrition**		
China market	2b	3b
Fonterra	0.02b	0.2b[1]
New Zealand Farm Source — **Domestic Milk Pool**		
China market	30-35b[2]	
Fonterra	0.06b	0.34b
Total Fonterra China		
Fonterra	4b	5.5b



b LME Fonterra **b LME** China market[2]

1. Based on April-2017 external data and analysis
2. Includes Beingmate sales of ~180m LME
3. Indicative share of sourcing
Source: Euromonitor; Fonterra analysis

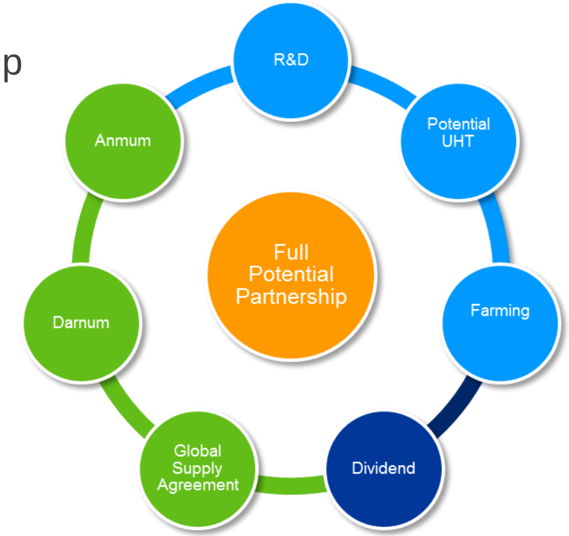
Beingmate is a key investment

Challenging last 12 months

- Regulatory changes
  - Long-term, brand rationalisation will benefit major domestic players
  - New regulations in place on 1 January 2018
  - Beingmate in first wave of approvals
- Competitive environment
  - Over-supply from non-approved players
  - Price competition and de-stocking
  - Impacted Beingmate sales and profitability
- Financial impact
  - Recognised share of one-off losses
  - Impairment in carrying value

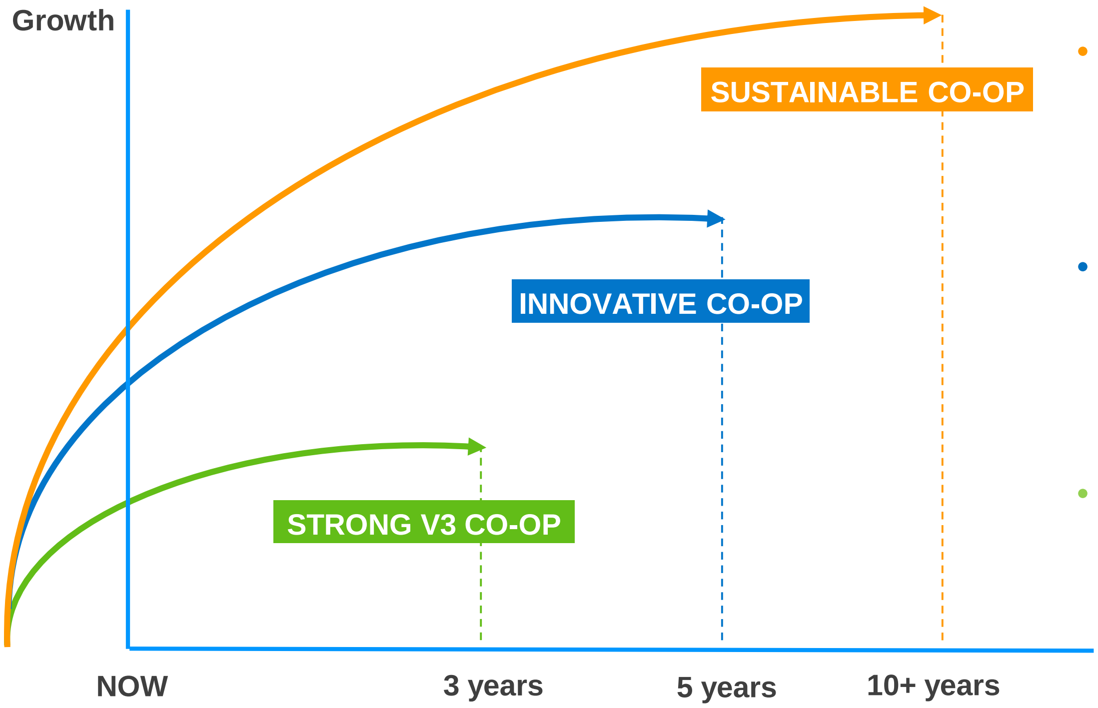
Strong strategic rationale remains

1. Market fundamentals are strong
2. Partnership with Beingmate part of a larger, profitable Greater China business
3. Strategic partnership value extends beyond direct investment



Strategy focused on achieving our ambition

Three strategic horizons



- Creating sustainable value for all stakeholders
- Investing in technology and people for the future
- Demand-led strategy to optimise NZ milk, supported by milk pools

Competitive advantage of **Cost Leadership through Scale Efficiency**

We are embracing tomorrow's innovation in what we do today

AGTECH

ENERGY & CLEAN TECH

PRECISION FARMING

SUSTAINABLE FARMS

ENERGY & WATER EFFICIENCY

SOIL & CROP TECH

FOOD SAFETY & TRACEABILITY

ROBOTICS

BLOCKCHAIN

SUSTAINABLE OPERATIONS

DIGITAL MANUFACTURING

3D PRINTING

SHARING ECONOMY

DIGITAL LIVING

CONSUMERS OF THE FUTURE

HYPER-PERSONALISATION

NEW RETAIL

FUTURE CONSUMERS

GAMIFICATION

CONNECTED LIFE

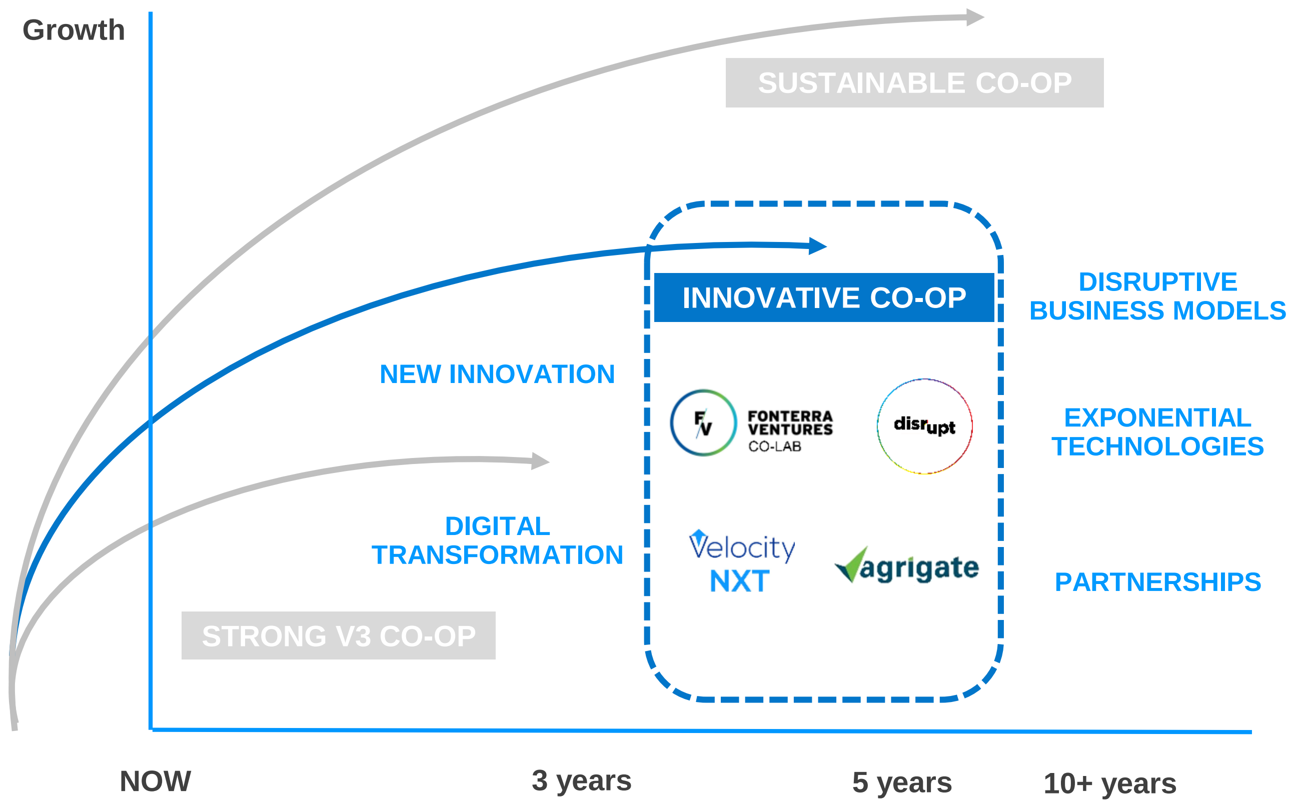
AR/VR

GENOMICS

ENABLERS

DIGITAL | ARTIFICIAL INTELLIGENCE | BIG DATA | BEHAVIOUR ECONOMICS

We have already begun the innovation journey



Velocity and VelocityNXT are very actively adding to our culture and performance

	Velocity	VelocityNXT
New Mindset	Accountability Bias to action Cash is king	Entrepreneurship Growth Innovation
Performance	Tangible financial recurring benefits 3,600+ initiatives completed >4,000 employees involved Over last 2 years	Launched in May this year Hundreds of ideas generated Dozens of concepts refined Six initiatives into incubation

Our Performance

Value creation

Solid profit with ongoing financial discipline

RETURN ON CAPITAL

11.1%

Down from 12.4%

GROSS MARGIN

17.0%

Down from 21.1%

CAPEX

$851M

10%

OPEX

$2,370M

6%

WORKING CAPITAL

75 DAYS

2 days

NORMALISED EBIT

$1,155M

15%

NPAT

$745M

11%

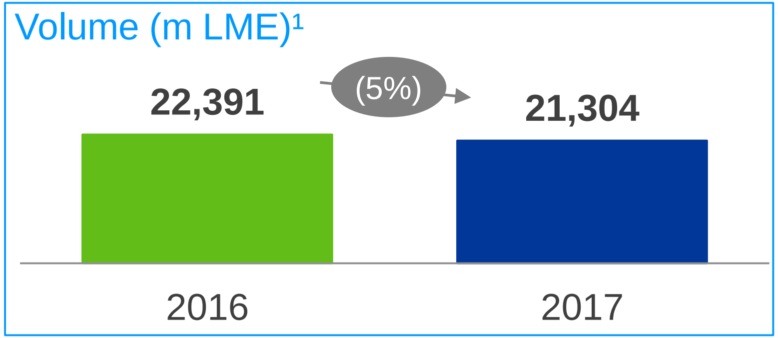
EPS

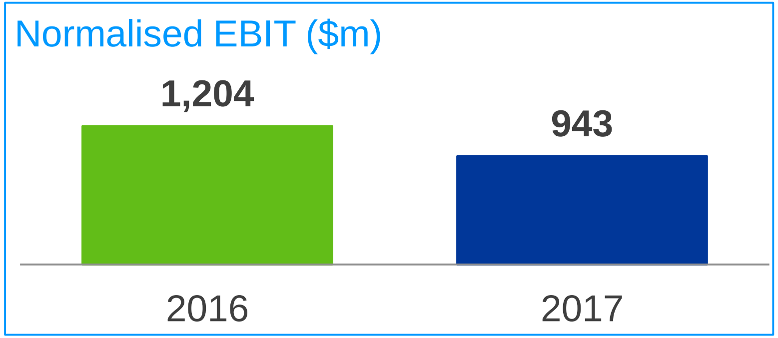
46C

Note: Return on Capital (ROC) excludes goodwill, brands and equity accounted investments; Group ROC including these items was 8.3% (2016: 9.2%)

Ingredients

Return on capital of 10.3%





Volume

- Challenging NZ milk collection profile
- Lower closing inventory carried into this year
- Growth in Advanced Ingredients of 9% (473m LME)

Value

- NZ Ingredients margins impacted by rising reference product prices relative to non-reference
  - Stream returns down significantly from last year
- Australia: $62m normalised EBIT from recurring business
- China milk: ($38m) impact of ongoing lower domestic prices

Velocity

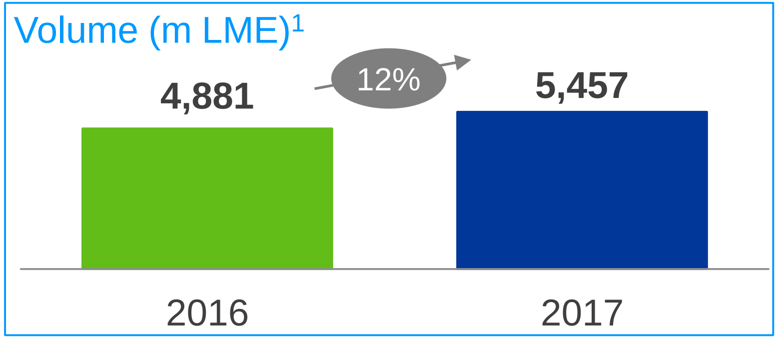
- Targeted capex with Foodservice focus and Stanhope rebuild
- Optionality used to prioritise higher value production
- Yield improvements and efficient peak management

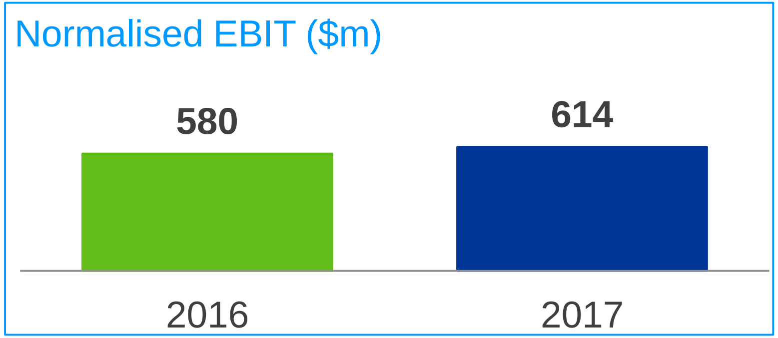
1. Includes sales to other strategic platforms

Note: Return on Capital (ROC) excludes goodwill, brands and equity accounted investments

Consumer & Foodservice

Return on capital of 47.2%





Volume

- 576m more LME into higher-value, exceeded 400m target
- Foodservice growth of 27%

Value

- Normalised EBIT growth of 6% – an increase of $34m
  - Significantly higher earnings in Greater China
  - Strong sales and earnings growth by Soprole in Chile
- Significant increases in input costs put pressure on gross margins, partially offset by revenue growth
  - Particularly for Foodservice butter, UHT and mozzarella

Velocity

- Australia turnaround delivering strong earnings
- Well positioned in Brazil for when economy recovers

1. Includes sales to other strategic platforms

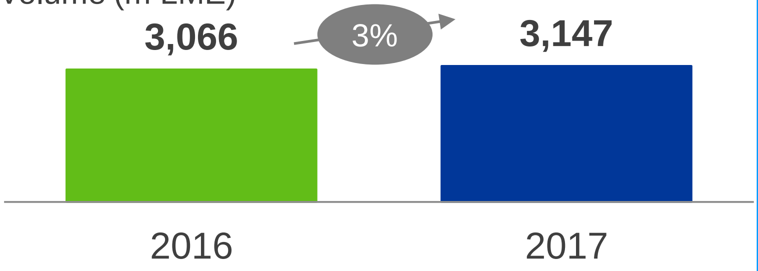
Note: Return on Capital (ROC) excludes goodwill, brands and equity accounted investments

Consumer and Foodservice

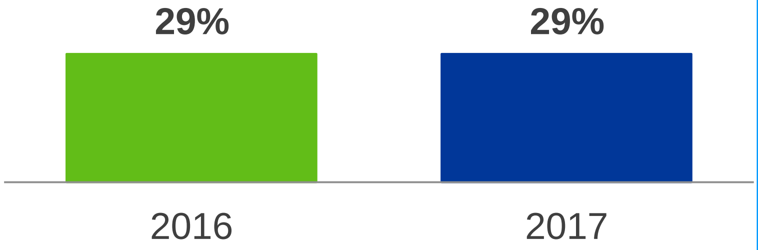
Significant growth but higher input costs created margin pressure

Consumer

Volume (m LME)[1]

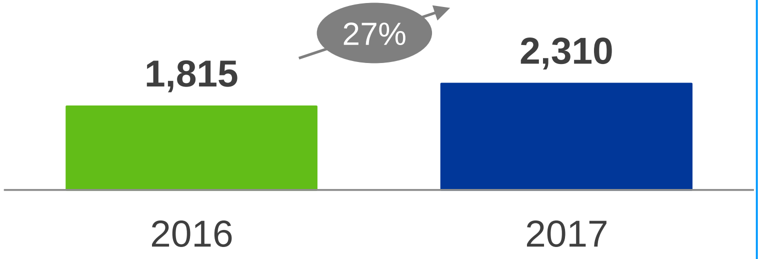


Gross Margin (%)

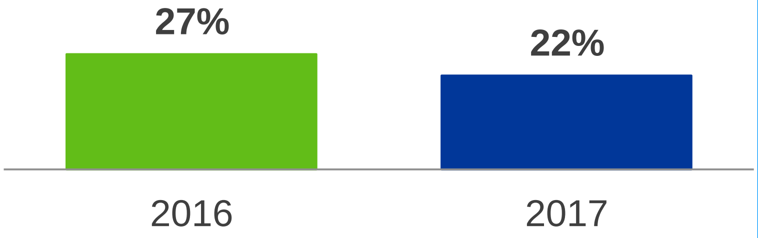


Foodservice

Volume (m LME)[1]



Gross Margin (%)

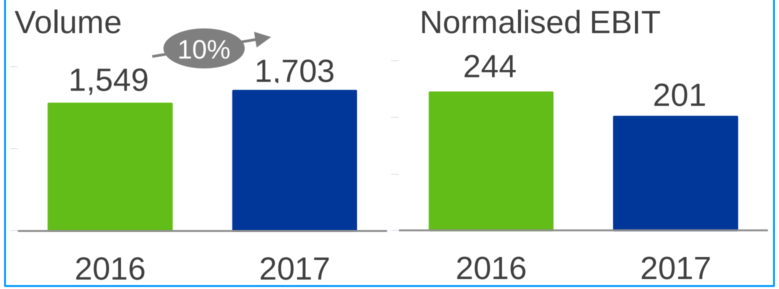


1. *Includes sales to other strategic platforms*

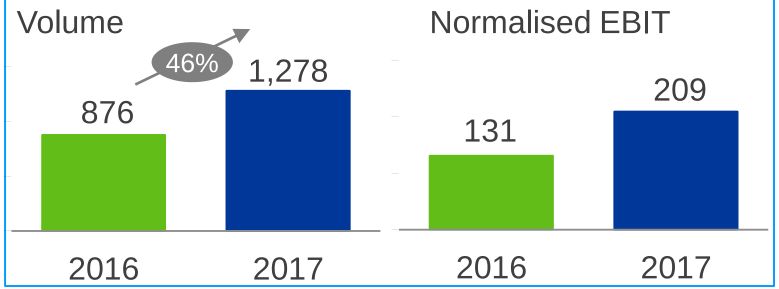
Consumer and Foodservice

Solid performance led by Greater China

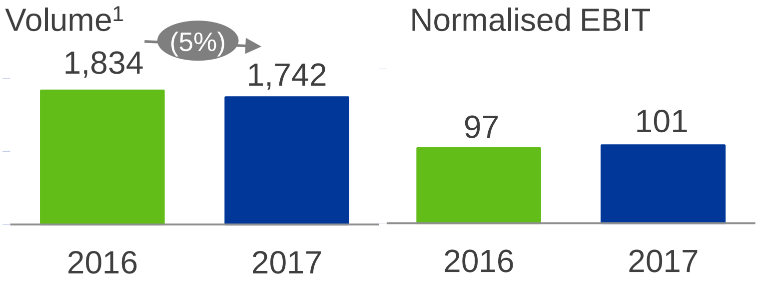
Asia



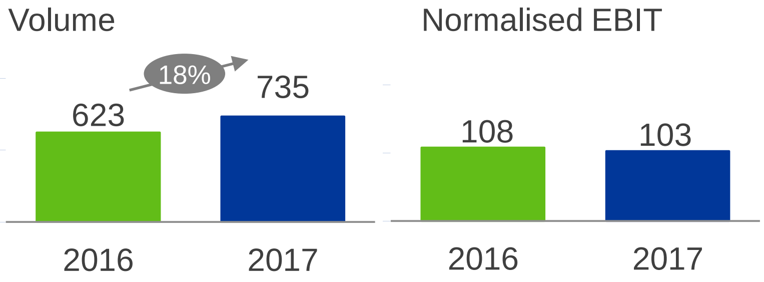
Greater China



Oceania



Latin America



1. Sales volume growth of (1%) when excluding impact of discontinued businesses

Note: All volumes include intercompany sales

Financial discipline

Strength of the balance sheet underpins our Co-op

GEARING[1]

44.3%

= Stable

NET DEBT[2]

$5.6B

Up 2%

DEBT / EARNINGS[3]

3.5

Up from 2.8x

TOTAL EQUITY

$7.2B

Up 4%

CREDIT RATING

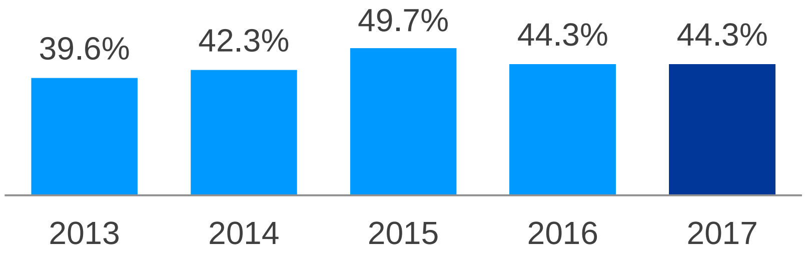
A	A-
STABLE	STABLE
Fitch	S&P

1. *Gearing ratio is economic net interest bearing debt divided by economic net interest bearing debt plus total equity excluding hedge reserves*
2. *Economic net interest-bearing debt*
3. *Debt payback ratio is economic net interest bearing debt divided by EBITDA. Both debt and EBITDA are adjusted for the impact of operating leases*

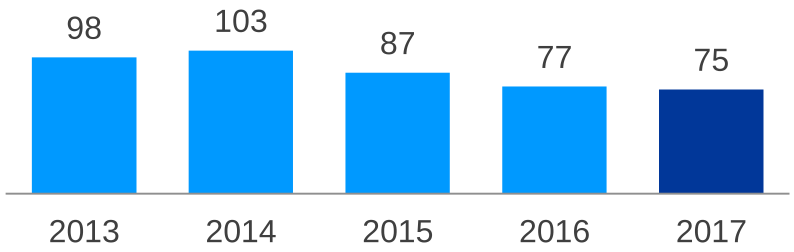
Financial strength of the Co-op

Continued strong balance sheet supports solid credit rating

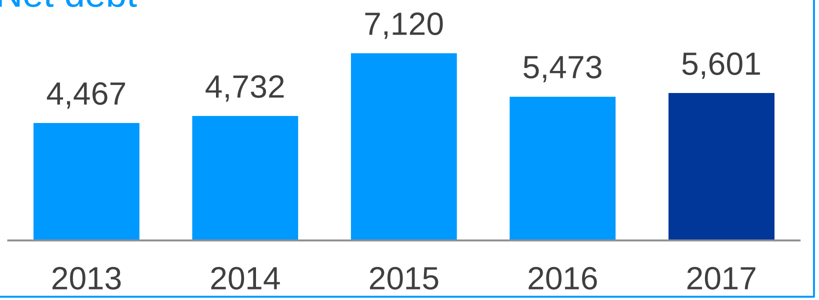
Gearing[1]



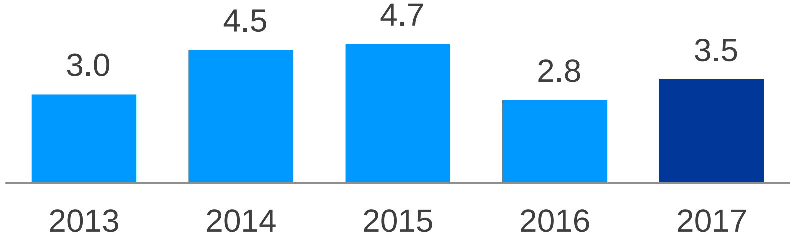
Working capital days[2]



Net debt[3]



Debt / EBITDA ratio[4]



1. Gearing ratio is economic interest bearing debt divided by economic net interest bearing debt plus equity excluding hedge reserves; 2. Working capital days excludes amounts owing to farmer suppliers; 3. Economic net interest-bearing debt ($ million); 4. Ratio is economic net interest bearing debt divided by EBITDA. Both debt and EBITDA are adjusted for the impact of operating leases

Return on capital

Comparison to competitors[1]

	Revenue Mix		Total EBIT %	Asset Efficiency Ratio	Return on Capital[3 4]		
	Ingredients[2]	Consumer			2015	2016	2017
Fonterra Dairy for life	66%	34%	6.0%	2.5	8.9%	12.4%	11.1%
FrieslandCampina	43%	57%	5.1%	3.2	10.4%	9.9%	8.8%
Arla	19%	81%	5.3%	3.0	7.9%	7.5%	7.4%

1. *Arla and FrieslandCampina based on FY16 results (Dec year end); Fonterra based on normalised FY17 results (Jul year end)*
2. *Ingredients includes Ingredients and other revenue streams*
3. *Fonterra ROC excludes goodwill, brands and equity accounted investments – including these items ROC was 8.3% in FY17 (FY16: 9.2% and FY15: 6.9%)*
4. *ROC for competitors is based on Fonterra's estimates and may not be an accurate reflection of the competitors actual returns; Calculated as NOPAT divided by Invested Capital; NOPAT defined as reported NPAT plus finance costs less one-off gains in sale; Invested Capital defined as two-year average closing balance of debt + equity – deferred tax*

Outlook

FY18 strategic priorities driving value

1 **Optimise** NZ milk	▪ Protect market share of NZ milk ▪ Deliver sustainable value creation in NZMP
2 **Build and grow** beyond our current consumer positions	▪ Deliver Everyday Nutrition focused growth path ▪ Target positions in Affordable Nutrition
3 **Deliver** on Foodservice potential	▪ Deliver double-digit Foodservice diversified growth
4 **Grow** our active living business	▪ Revitalise the Anlene brand (Healthy Living) ▪ Build an Active Living portfolio
5 **Develop** leading positions in paediatric & maternal nutrition	▪ Deliver China and Beingmate partnership at full potential
6 **Selectively invest** in milk pools	▪ Develop cheese / whey supply options ▪ Grow Australian milk pool share
7 **Align** our business and organisation	▪ Invest to deliver future-oriented capabilities

Our ambition is on track

	From (2015)	2016	2017	Ambition
Revenue[1]	Ingredients $0.7 / LME Consumer & Foodservice $1.5 / LME	Ingredients $0.6 / LME Consumer & Foodservice $1.3 / LME	Ingredients $0.7 / LME Consumer & Foodservice $1.2 / LME	$1.2 / LME
Gross Margin	17%	21%	17%	20%+
Normalised EBIT	$1.0b	+39%	+19%	50-100% uplift
Return on Capital[2]	8.9%	12.4%	11.1%	11-13%
Gearing[3]	45-50%	44.3%	44.3%	40-45%

1. Includes sales to other strategic platforms; 2. Return on Capital (ROC) excludes goodwill, brands and equity accounted investments; Group ROC including these items was 8.3% in FY17 (FY16: 9.2%); 3. Fonterra's target is to maintain its strong investment grade credit rating and debt payback & cash flow coverage metrics that support this

Strong outlook for 2018

- Forecast for 2017/18:
  - A forecast Farmgate Milk Price of $6.75 per kgMS
  - A forecast earnings performance of 45-55 cents per share
  - Solid performance, strong Co-op, future-focused strategy

- Global supply and demand
  - Strong global demand – renewed interest in dairy nutrition
  - Dairy market in balance with NZ supply back to more normal levels and pressures in some key offshore producing regions

Supplementary Information

Normalised EBIT reconciliation

$ million	Year ended 31 July 2017	Year ended 31 July 2016
Profit after tax	745	834
Add: Net finance costs	355	499
Add: Taxation expense	20	98
Total reported EBIT	1,120	1,431
Add: Impairment of assets in Australia	-	23
Add: Impairment of Investment in Beingmate	35	-
Add: Share of Beingmate losses	41	-
Less: Gain on DairiConcepts sale	-	(68)
Less: Gain on Darnum sale[1]	(42)	-
Add / Less: Time value of options	1	(28)
Total normalisation adjustments	35	(73)
Total normalised EBIT	1,155	1,358

1. Proceeds from the sale of 51% of the Darnum site in Australia to Beingmate

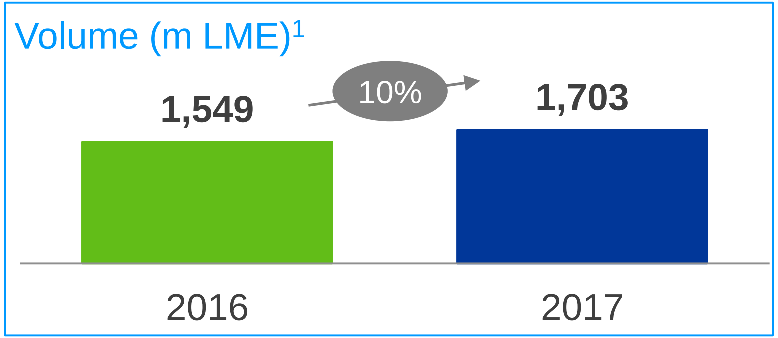
NZ Ingredients product mix

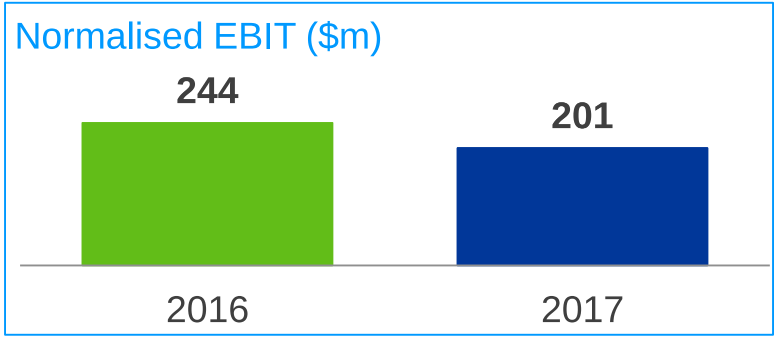
	Full Year ended 31 July 2017	Full Year ended 31 July 2017	Full Year ended 31 July 2016	Full Year ended 31 July 2016
		$ per MT		$ per MT
Sales volume (000 MT)				
Reference products	**1,841**	**-**	1,920	-
Non-reference products	**696**	**-**	720	-
Revenue ($ million)				
Reference products	**7,846**	**4,262**	6,290	3,276
Non-reference products	**3,875**	**5,567**	3,580	4,972
Cost of milk ($ million)				
Reference products	**6,147**	**3,339**	4,163	2,168
Non-reference products	**2,337**	**3,359**	1,708	2,371
Gross margin ($ million)				
Reference products	**428**	**232**	634	330
Non-reference products	**811**	**1,165**	971	1,348

Note: Reference products are products used in the calculation of the Farmgate Milk Price – WMP, SMP, BMP, Butter, AMF; Milk solids used in the products sold were 1,061m kgMS reference and 441m kgMS non-reference (year ended 31 July 2016 was 1,083m kgMS reference and 423m non-reference); Excludes bulk liquid milk volumes of 76,000 MT of kgMS equivalent (year ended 31 July 2016 was 77,000 MT); Excludes Foodservice volumes to China and Latin America of 143,000 MT (year ended 31 July 2016 was 92,000 MT)

Asia – Consumer & Foodservice

Tough year due to significantly higher input costs





Volume

- Growth in Foodservice volumes across region
- Successful product launches and campaigns in Sri Lanka

Value

- Lower profit but in line with expectations due to increase in input costs
- Product mix-shift in key markets as we respond to changing customer preferences
- Adversely impacted by strengthening Asian currencies and challenging Middle East market

Velocity

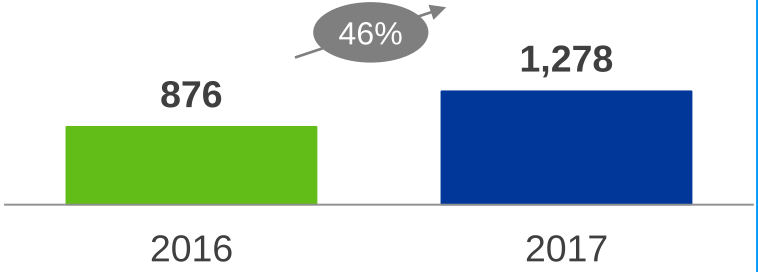
- Strategic relaunch of Anlene brand

1. *Includes sales to other strategic platforms*

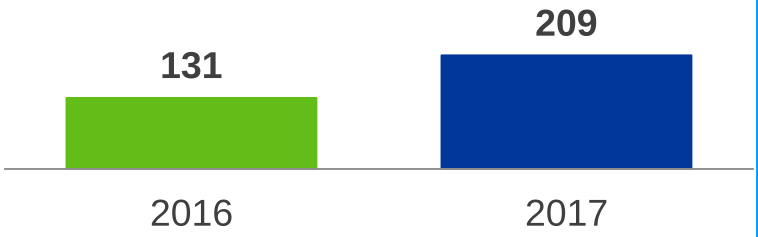
Greater China – Consumer & Foodservice

Ongoing growth and profitability with strong Foodservice contribution

Volume (m LME)[1]



Normalised EBIT ($m)



Volume

- Volume growth driven by Foodservice
- Category and range expansion in Consumer
- Anmum sales volumes up 91% in China

Value

- Profit up 60% even with higher input costs and mix shift to Foodservice
- Anchor now #1 imported UHT milk in online market

Velocity

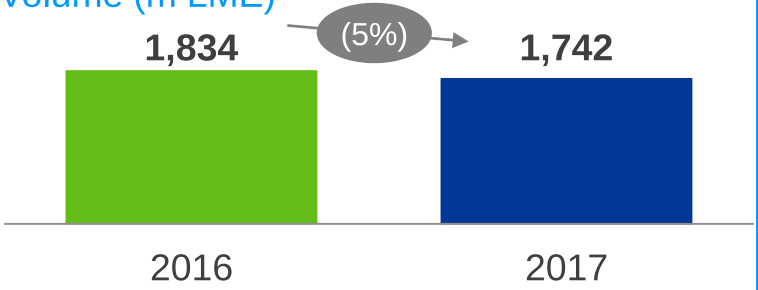
- Beingmate products in first wave of infant formula product approvals
- Successful roll-out of new route-to-market model

1. *Includes sales to other strategic platforms*

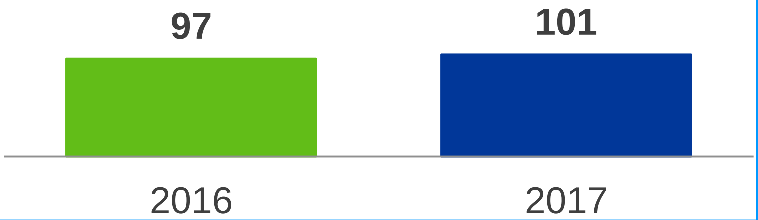
Oceania – Consumer & Foodservice

Overall higher earnings driven by Australia turnaround

Volume (m LME)[1]



Normalised EBIT ($m)



Volume

- Lower volumes due to sale of businesses and transfer of UHT volumes to Ingredients

Value

- Australia turnaround now delivering stable, strong earnings
- NZ impacted by wet summer and higher short-term costs associated with transition to a new distribution centre

Velocity

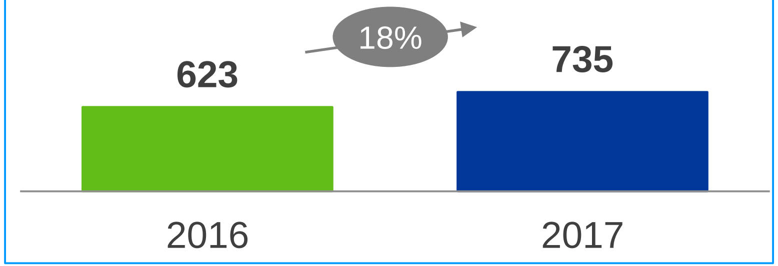
- Stanhope cheese plant operational

1. *Includes sales to other strategic platforms*

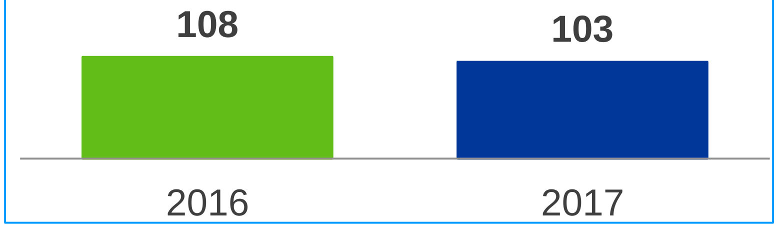
Latin America – Consumer & Foodservice

Good result in challenging environment

Volume (m LME)[1]



Normalised EBIT ($m)



Volume

- Strong growth by Soprole in Chile supported by successful product launches and new branding
- Overall volumes impacted by adverse economic situations in Brazil and Venezuela

Value

- Strong Soprole result but overall slight decline
- Brazil impacted by 15% decline in overall category value
- Venezuelan business impacted by extremely difficult operating environment

Velocity

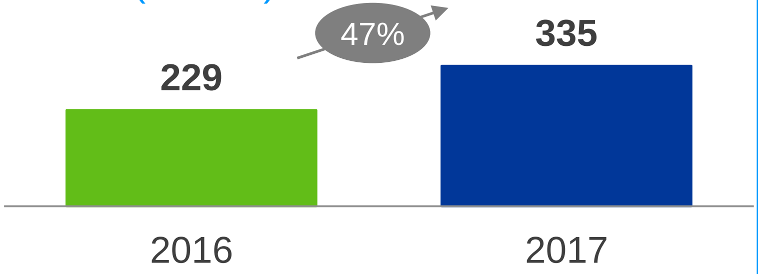
- Now strong #2 market position in Brazil – well positioned for market recovery

1. *Includes sales to other strategic platforms*

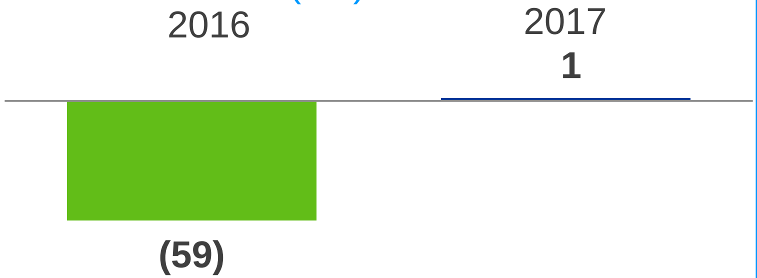
China Farms

Significantly improved operating performance

Volume (m LME)[1]



Normalised EBIT ($m)



Volume

- Increased sales volumes by 47%
- First full year of mature operations for both hubs

Value

- Cash costs reduced by a further 0.21 RMB per litre – a 6% reduction
- Improved performance reflects adoption of internal fixed raw milk price with Ingredients team managing sales opportunities
  - Ingredients gross margin impact of $38 million

Velocity

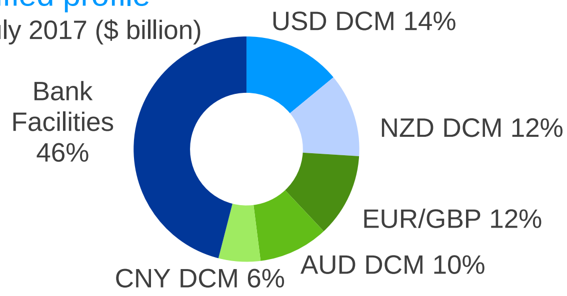
- Greatly improved operating performance
- First sale of China Farms milk as Anchor branded product by foodservice

1. *Includes sales to other strategic platforms*

Diversified and prudent funding position

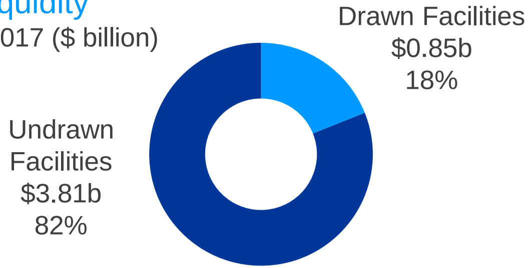
Diversified profile[1]

At 31 July 2017 ($ billion)



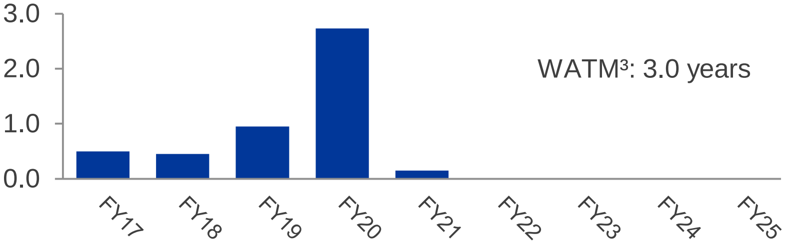
Prudent liquidity

At 31 July 2017 ($ billion)



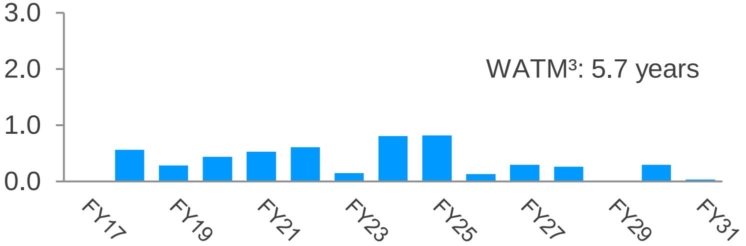
Bank facility maturity profile

At 31 July 2017 ($ billion)



DCM maturity profile[2]

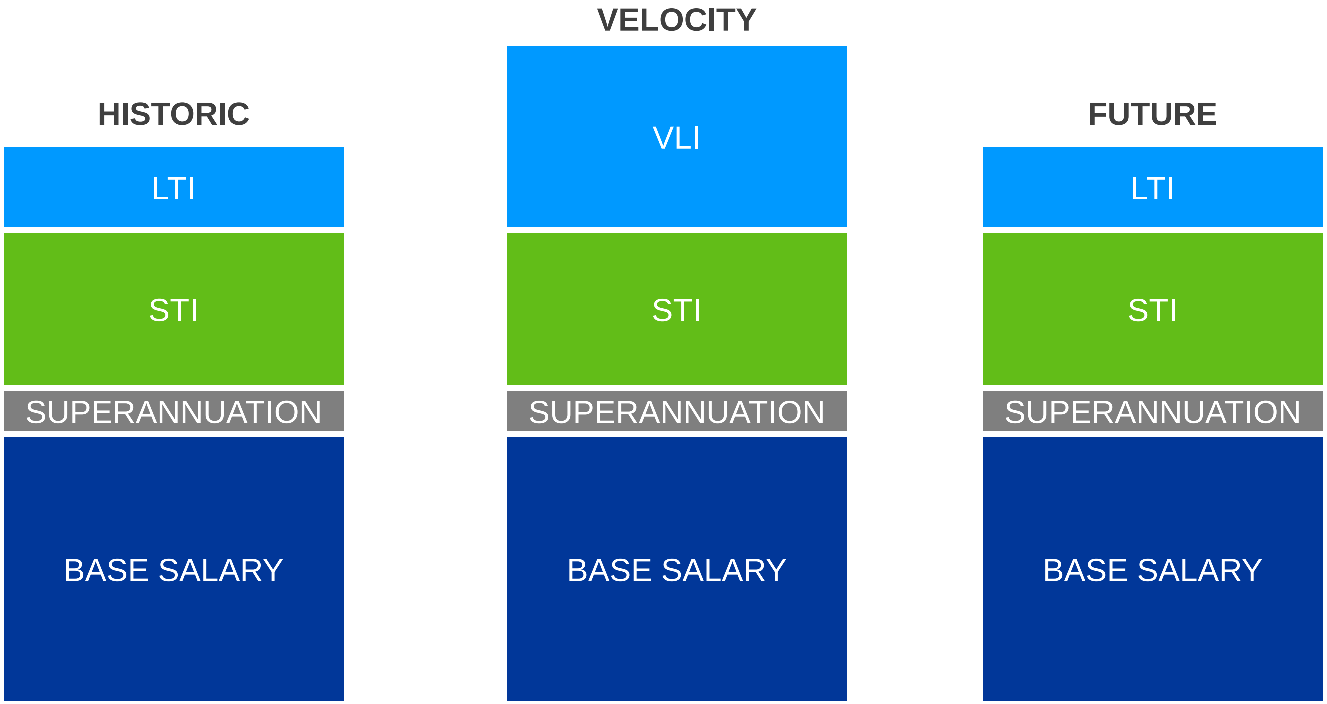
At 31 July 2017 ($ billion)



1. *Includes undrawn facilities and commercial paper*
2. *Excluding commercial paper*
3. *WATM is weighted average term to maturity*

Executive rewards

How senior executives’ remuneration packages work



- LTI is linked to EPS and ROC
- VLI was a targeted two-year plan to accelerate and reward the Fonterra business transformation – replacing the LTI plan for FY16 and FY17
- From FY18 our FMT and sales staff incentives will be subject to modification +/- based on total available for payout

Note: STI = Short-Term Incentive; LTI = Long-Term Incentive; VLI = Velocity Leadership Incentive; EPS = Earnings Per Share; ROC = Return on Capital; FMT = Fonterra Management Team

Glossary

Acronyms and Definitions

AMF
Anhydrous Milk Fat

BMP
Butter Milk Powder

Base Price
Prices used by Fonterra's sales team as referenced against GDT prices and other relevant benchmarks

DIRA
Dairy Industry Restructuring Act 2001 (New Zealand)

GDT
GlobalDairyTrade, the online provider of the twice monthly global auctions of dairy ingredients

Gearing Ratio
Economic net interest bearing debt divided by economic net interest bearing debt plus equity excluding cash-flow hedge reserves

Farmgate Milk Price
The price for milk supplied in New Zealand to Fonterra by farmer shareholders

Fluid and Fresh Dairy
The Fonterra grouping of skim milk, whole milk and cream – pasteurised or UHT processed, concentrated milk products and yoghurt

LME (Liquid Milk Equivalent)
A standard measure of the amount of milk (in litres) allocated to each product based on the amount of fat and protein in the product relative to the amount of fat and protein in standardised raw milk

kgMS
Kilogram of milk solids, the measure of the amount of fat and protein in the milk supplied to Fonterra

Non-Reference Products
All dairy products, except for Reference, produced by the NZ Ingredients business

Price Achievement
Revenue achieved over the base price less incremental supply chain costs above those set out in the Milk Price model

Reference Products
The dairy products used in the calculation of the Farmgate Milk Price, which are currently WMP, SMP, BMP, butter and AMF

Regulated Return
The earnings component of Milk Price generated from a WACC return on an assumed asset base

Season
New Zealand: A period of 12 months to 31 May in each year

Australia: A period of 12 months to 30 June in each year

SMP
Skim Milk Powder

Stream Returns
The gross margin differential between Non-Reference Product streams and the WMP stream (based on base prices)

WACC
Weighted Average Cost of Capital

WMP
Whole Milk Powder

Glossary

Fonterra Strategic Platforms

Ingredients

The Ingredients platform comprises bulk and specialty dairy products such as milk powders, dairy fats, cheese and proteins manufactured in New Zealand, Australia, Europe and Latin America, or sourced through our global network, and sold to food producers and distributors in over 140 countries. It also includes Fonterra Farm Source™ retail stores.

Consumer

The Consumer platform comprises branded consumer products, such as powders, yoghurts, milk, butter, and cheese. Base products are sourced from the ingredients business and manufactured into higher-value consumer dairy products.

Foodservice

The Foodservice platform comprises a range of branded products and solutions for commercial kitchens, including bakery butter, culinary creams, and cheeses.

China Farms

The China Farms platform comprises the farming operations in China, which produce high quality fresh milk for the Chinese market.

FARMGATE
MILK PRICE STATEMENT

FONTERRA FARMGATE MILK PRICE STATEMENT 2017
FOR THE SEASON ENDED 31 MAY 2017

Dairy for life

INTRODUCTION

The primary purpose of this Statement is to help Fonterra farmer shareholders, unit holders in the Fonterra Shareholders' Fund, and other interested parties better understand the Farmgate Milk Price.

This Farmgate Milk Price Statement sets out information about the Farmgate Milk Price and outlines the way that Fonterra Co-operative Group Limited (Fonterra) has calculated the Farmgate Milk Price for the milk season that ended on 31 May 2017 (2017 Season).

The appendices provide an overview of the Farmgate Milk Price and a report by Fonterra's external auditors that confirms that the Farmgate Milk Price for the 2017 Season has been derived in accordance with the Principles, Methodologies and Detailed Rules in Fonterra's Farmgate Milk Price Manual, dated 1 August 2016. Five attachments provide further detail for the past three seasons on the most significant factors that affect the Farmgate Milk Price. A glossary of the terms used completes the report[1].

Fonterra has also released as an adjunct to this Statement an unaudited Microsoft Excel-based financial model that shows how the information set out in the Statement has been used to calculate the Farmgate Milk Price for the 2017 Season.

Numbers in this Statement have been rounded and, as a result, some tables may not exactly total or sum to 100 per cent.[2] The information on the Farmgate Milk Price presented in this Statement is based on data used within the Milk Price Model, not Fonterra's actual data.

A Farmgate Milk Price Statement is made available each year with Fonterra's annual results on www.fonterra.com.

1 Capitalised terms in this Statement are defined in the glossary.

2 Percentage changes shown in tables in this Statement have been calculated by reference to the underlying data, and may differ from percentage movements between the rounded data presented in the tables.

FARMGATE MILK PRICE **FOR THE 2017 SEASON**

This section sets out the Farmgate Milk Price for the 2017 Season. It also describes the way the Farmgate Milk Price relates to Fonterra's financial year ended 31 July 2017.

The Manual sets out the methodology for determining the base amount to be paid by Fonterra for milk supplied to Fonterra in New Zealand in a season. Fonterra's Milk Price Panel advises the Fonterra Board on matters concerning the Manual, including the calculation of the Farmgate Milk Price.

The Farmgate Milk Price is the total amount calculated under the Manual, and is **NZD$9.349 billion** for the 2017 Season. For convenience, the Manual also defines the 'Farmgate Milk Price per kgMS' as this total amount divided by Fonterra's total New Zealand milk supply (1.526 billion kilograms of milk solids (kgMS)), or NZD$6.13 per kgMS. This is referred to below as the Average Farmgate Milk Price calculated under the Manual.

The cost of New Zealand-sourced milk, as disclosed in Fonterra's most recent financial statements, is NZD$9.471 billion. The NZD$122 million difference between this amount and the Farmgate Milk Price of NZD$9.349 billion primarily reflects the following two factors:

- The financial statements report the cost of milk acquired during the financial year comprising the 12-month period ending 31 July 2017. In contrast, the Farmgate Milk Price for the season is the cost of milk supplied in respect of the 12-month period ending 31 May 2017.
- A commodity manufacturer of milk powders is unlikely to pay premiums for Specialty Milk (such as organic milk) or to pay as high a premium for Winter Milk that an integrated processor such as Fonterra would pay. Such payments are therefore a cost of New Zealand-sourced milk for Fonterra but are not a component of the Farmgate Milk Price.

TABLE 1: RECONCILIATION BETWEEN AVERAGE FARMGATE MILK PRICE CALCULATED UNDER THE MANUAL AND THE ANNOUNCED FARMGATE MILK PRICE

	$/kgMS
Average Farmgate Milk Price calculated under the Manual	6.13
Adjustment for portion of winter milk premiums paid, and other items	(0.01)
Announced Farmgate Milk Price (average price for milk supplied on standard terms of supply)	**6.12**

AVERAGE PRICE FOR MILK SUPPLIED ON STANDARD TERMS OF SUPPLY

The Average Farmgate Milk Price calculated under the Manual differs slightly from the average price paid by Fonterra for milk supplied on standard terms of supply by Fonterra's supplier-shareholders.

The largest driver of the difference is the portion of the premiums paid for Winter Milk, equal to the premium that a commodity manufacturer would be willing to pay for Winter Milk. That premium is funded from the aggregate amount calculated under the Manual, and slightly reduces the amount available to pay for milk supplied on standard terms.

The reduction due to Winter Milk premiums is partially offset by an increase due to instances where Fonterra has paid less for milk supplied on non-standard terms (for example, for non-share backed supply under deferred share purchase agreements) or where milk quality demerits have been applied.

Table 1 above shows the net impact of these adjustments is that the average price for milk supplied on standard terms of supply is NZD$6.12 per kgMS. Because this is the price that is of most relevance to most suppliers, it is the price that is referenced in Fonterra's general public communications relating to the 2017 Season, including in Fonterra's most recent financial statements and associated public announcements. For convenience, it is referred to in those communications as the Farmgate Milk Price.

FARMGATE MILK PRICE **REVENUE AND COSTS**

The most significant factor that affects the Farmgate Milk Price from season to season is revenue.

Table 2 below summarises the Farmgate Milk Price for the milk supplied in the 2015, 2016 and 2017 Seasons. Both Table 2 and Figure 1 below show that changes in the Farmgate Milk Price over the past three seasons have been driven mainly by changes in commodity prices converted into NZD.

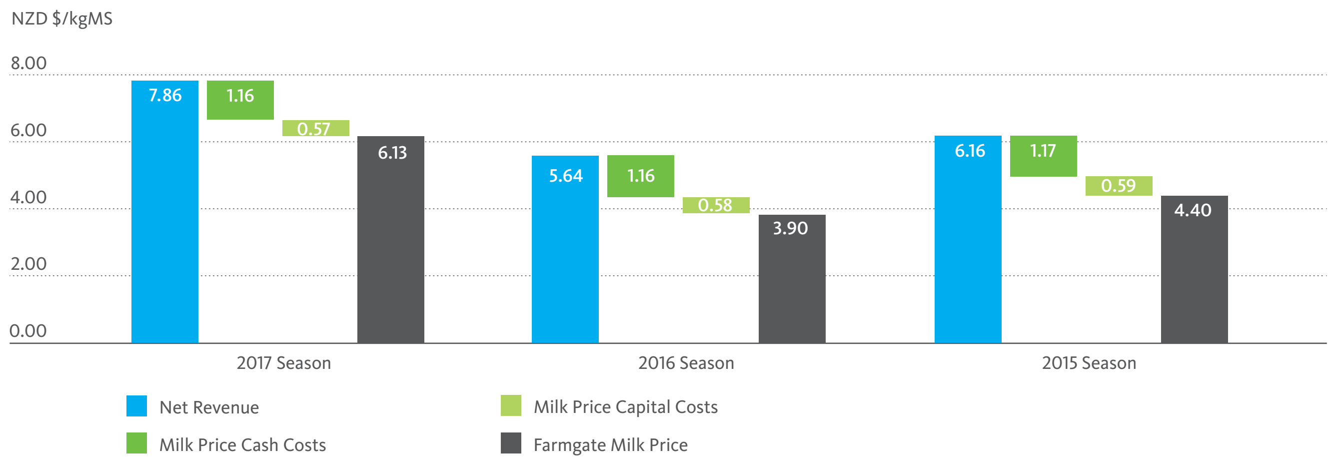
The first three subsections below describe the key factors that influence revenue.

Key determinants of the movements in average costs between the 2016 and the 2017 Seasons are explained in later subsections.

TABLE 2: FARMGATE MILK PRICE SUMMARY

SEASON	2017 NZD $ MILLION	2017 $/kgMS	2016 NZD $ MILLION	2016 $/kgMS	2015 NZD $ MILLION	2015 $/kgMS	2017/2016 % CHANGE ($/kgMS)	2016/2015 % CHANGE ($/kgMS)
Farmgate Milk Price Revenue	12,400	8.13	9,134	5.83	10,540	6.53	39.4%	−10.7%
Lactose	(415)	(0.27)	(302)	(0.19)	(603)	(0.37)	41.3%	−48.4%
Net Revenue	**11,985**	**7.86**	**8,832**	**5.64**	**9,937**	**6.16**	39.3%	−8.4%
Farmgate Milk Price Cash Costs	(1,763)	(1.16)	(1,815)	(1.16)	(1,889)	(1.17)	−0.3%	−1.0%
Farmgate Milk Price Capital Costs[3]	(873)	(0.57)	(915)	(0.58)	(952)	(0.59)	−2.1%	−0.9%
Total Costs	**(2,636)**	**(1.73)**	**(2,731)**	**(1.74)**	**(2,841)**	**(1.76)**	**−0.9%**	**−1.0%**
Farmgate Milk Price	**9,349**	**6.13**	**6,101**	**3.90**	**7,096**	**4.40**	**57.3%**	**−11.4%**
Million kgMS		**1,526**		**1,566**		**1,614**	−2.6%	−3.0%

FIGURE 1: CHANGES IN THE FARMGATE MILK PRICE SEASONS: 2015–2017



3 *Includes depreciation, tax and capital charge.*

FARMGATE MILK PRICE **REVENUE AND COSTS**

CONTINUED

MILK SUPPLY, PRODUCTION AND SALES VOLUMES

Farmgate Milk Price Revenue varies according to the milk supplied during the season, product mix, sales volumes and prices in NZD. Farmgate Milk Price Revenue is the most significant driver of the Farmgate Milk Price.

Figure 2 shows the relationship between when milk is collected during a season (the blue line), the volume of products manufactured from that milk (the grey line) and when that product is shipped (the green line). The key points to note are as follows:

- Milk supplied during the 2017 Season comprised 1.526 billion kgMS. Attachment 1 provides information on milk supplied every quarter for each of the past three seasons.
- This amount of milk is assumed to be converted into Reference Commodity Products. The mix between the various products that goes into the Farmgate Milk Price is aligned to Fonterra's actual mix between Whole Milk Powder (WMP) and Skim Milk Powder (SMP), and between butter and Anhydrous Milk Fat (AMF) (production of Buttermilk Powder (BMP) is a residual amount). Attachment 1 provides Farmgate Milk Price production by quarter for each Reference Commodity Product for the past three seasons.
- Sales volumes reflect the pattern of Fonterra's actual shipments of Reference Commodity Products manufactured from milk supplied during the season. Figure 2 shows the lag between production and shipment as well as the fact that minimal milk is supplied in June and July. These factors mean that shipments of products manufactured from milk collected in a season (beginning 1 June) do not normally commence until August at the earliest. Shipments are normally complete by the end of October in the following year, again as illustrated in Figure 3.

FIGURE 2: TIMING OF SUPPLY, PRODUCTION AND SALES VOLUMES

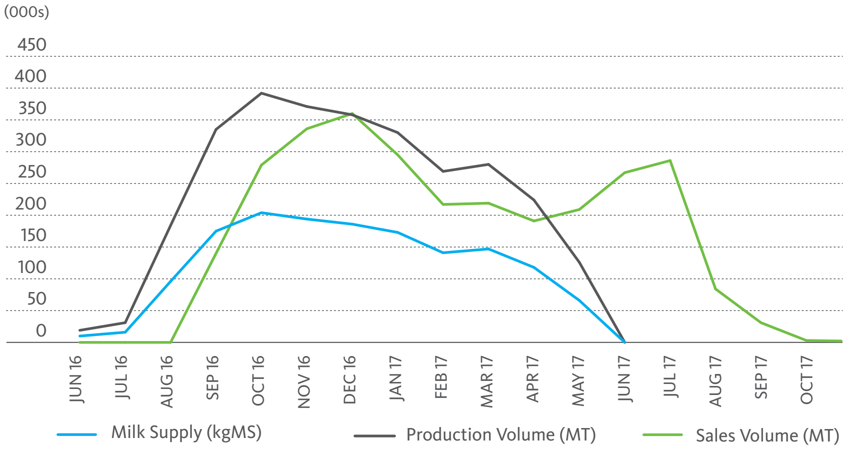
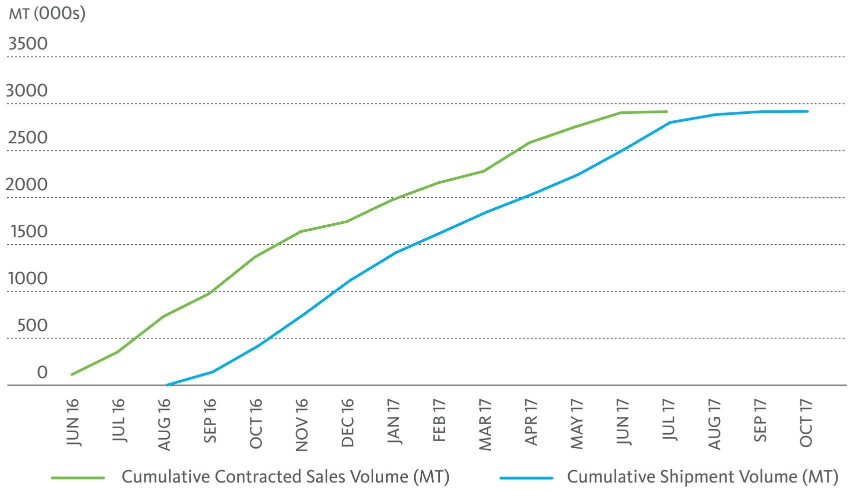


FIGURE 3: AVERAGE LAG BETWEEN WHEN PRICES WERE STRUCK AND SHIPMENT



Attachment 2 sets out sales volumes by quarter for each of the past three seasons.

Revenues are recognised when sales are invoiced, at the time of shipment. Sales prices included in the Farmgate Milk Price are always set prior to the month of shipment, primarily via GDT events. Figure 3 shows the average lag between when prices are struck and when product is shipped.

This matches Fonterra's actual average lag for product that is sold on terms that are typical for the sale of commodity products from New Zealand. To ensure that this is the case, contracts with more than five months between when a price is set and shipment occurs are not taken into account in determining shipment prices[4].

Attachment 3 sets out the average number of months prior to shipment that prices were struck for each quarter over the past three seasons. Attachment 3 also sets out the average percentage of sales contracted in each month prior to shipment in the past three seasons.

4 *For each of the 2015, 2016 and 2017 Seasons, approximately 7 per cent of Fonterra's sales of Reference Commodity Products were sold under contracts with more than 5 months between the price being set and shipment occurring.*

TABLE 3: WEIGHTED AVERAGE USD CONTRACT PRICE 2015 – 2017 SEASONS

WEIGHTED AVERAGE PRICE (USD) PER MT	2017	2016	2015	2017/2016 % CHANGE	2016/2015 % CHANGE
WMP	**2,854**	2,111	2,639	**35.2%**	−20.0%
SMP	**2,216**	1,803	2,552	**22.9%**	−29.4%
Butter	**4,221**	2,830	3,027	**49.2%**	−6.5%
AMF	**5,076**	3,227	3,577	**57.3%**	−9.8%
BMP	**2,211**	1,723	2,657	**28.3%**	−35.2%
				36.1%	−20.1%

2017 SEASON AVERAGE PRICES WERE HIGHER THAN 2016 SEASON BY

↑36.1%

PRICES

Between the 2012 and 2016 Seasons, GDT was the sole source of prices for WMP, SMP and AMF, and was a primary reference point for BMP and butter. Non-GDT contracts Fonterra entered into were also used to establish prices for butter and BMP.

For the 2017 Season, non-GDT contracts were also used to establish prices for WMP, SMP and AMF. The relevant contracts were for product of a similar specification and sold on similar terms to product sold on GDT.

Detailed rules in the Manual dictate which contracts can be taken into account. Contracts that are excluded, for example, include sales to Fonterra subsidiaries.

Attachment 1 highlights that WMP, SMP and AMF (2,599,000 MT) accounted for 89 per cent of the Farmgate Milk Price production of Reference Commodity Products (2,918,000 MT) in the 2017 Season.

The average shipment prices incorporate provisions for the lower prices received for 'downgrade product'. These are products that do not meet manufacturing specifications, some of which may only be suitable for use as stock feed.

Table 3 above shows the weighted average USD contract prices of Reference Commodity Products for the past three seasons. It shows that prices for the Reference Commodity Products increased on average by 36.1 per cent between the 2016 Season and the 2017 Season, compared to a decrease of 20.1 per cent between the 2015 Season and the 2016 Season. Average USD prices per MT for each Reference Commodity Product by quarter for the past three seasons are set out in Attachment 4.

The Manual provides for the conversion of notional USD Farmgate Milk Price receipts to NZD for each month at the average rate at which Fonterra actually converts its USD-equivalent foreign currency receipts for the month, taking into account the costs and benefits of Fonterra's hedging activities. Fonterra's policy is to hedge 100 per cent of net recognised foreign currency trade receivables and payables. It also requires hedging of forecast cash receipts from sales for a period of up to 18 months within limits approved by Fonterra's Board. Fonterra uses both forward foreign exchange contracts and currency options to hedge its foreign exchange risk.

Fonterra's hedging policy is designed to provide certainty and to reduce the impact on the Farmgate Milk Price of volatility in the NZD, and results in the spot exchange rate at a particular point in time being reflected in the hedged conversion rate over the subsequent 18 months.

Table 4 shows that Fonterra's hedging policy resulted in an average foreign exchange conversion rate for the 2017 Season of USD:NZD 0.6924 against an average spot rate of USD:NZD 0.7171. This resulted in an increase in the Farmgate Milk Price of 28 cents relative to translation at the spot exchange rate. In comparison:

- In the 2015 and 2016 Seasons, hedging activities resulted in an average decrease in the Farmgate Milk Price of 37 cents relative to translation at the spot exchange rate.
- In the Seasons from 2011 to 2014, hedging activities resulted in an average increase in the Farmgate Milk Price of 46 cents per kgMS relative to translation at the spot exchange rate.

Attachment 5 on page 20 shows the average foreign exchange conversion rate (USD:NZD) for the Farmgate Milk Price Revenue for each quarter in the 2015 to 2017 Seasons, based on Fonterra's actual hedging contracts in place, compared to the weighted average spot exchange rate for the quarter.

FARMGATE MILK PRICE **REVENUE AND COSTS**

CONTINUED

As at 31 July 2017, Fonterra had foreign exchange contracts in place for approximately 71 per cent of the USD equivalent operating cash flow exposure expected to impact on the Farmgate Milk Price for the 2018 Season. If the balance was hedged based on a spot exchange rate of 0.7504,[5] the average USD:NZD conversion rate would be 73 cents.[6]

LACTOSE

Lactose is used as an ingredient in the manufacture of WMP, SMP and BMP to achieve a standard protein composition aligned to internationally recognised specifications. Most of the lactose content of milk powders is obtained from the milk supplied to Fonterra. However, a portion is purchased at international prices. Because the cost of purchased lactose depends on global prices and the exchange rate, it is presented in Table 2 and Figure 1 as a deduction from Farmgate Milk Price Revenue.

Table 5 provides the basis for the cost of purchased lactose in the 2017, 2016 and 2015 Seasons.

FARMGATE MILK PRICE CASH COSTS

Farmgate Milk Price Cash Costs reflect:

- Fonterra's actual collection costs, and supply chain costs benchmarked to Fonterra's actual costs.
- Costs associated with modern plants with sufficient capacity to process all milk collected by Fonterra, located on more than 20 reference manufacturing sites (most of which contain multiple plants) with associated overhead costs. The costs of operating these plants are based on daily processing capacities that match Fonterra's averages, and on operating parameters that reflect manufacturers' specifications and Fonterra's per-unit costs.

TABLE 4: EFFECT OF HEDGING POLICY ON THE FARMGATE MILK PRICE FOR THE 2015 – 2017 SEASONS

	2017		2016		2015	
SEASON	MILK PRICE	SPOT	MILK PRICE	SPOT	MILK PRICE	SPOT
Average Conversion Rate (USD:NZD)	**0.6924**	**0.7171**	0.7082	0.6820	0.7882	0.7312
Farmgate Milk Price (NZD/kgMS)	**6.13**	**5.85**	3.90	4.11	4.40	4.92
Effect of Hedging (NZD/kgMS)	**0.28**		−0.21		−0.52	

TABLE 5: PURCHASED LACTOSE AND PRICE

SEASON	2017	2016	2015	2017/2016 % CHANGE	2016/2015 % CHANGE
Purchased Lactose (000 Metric Tonnes)	**351**	350	346	**0.5%**	1.2%
Average Price (USD) per MT	**809**	640	1,406	**26.3%**	−54.5%
Total Lactose Purchases (USD $m)	**284**	224	486	**26.9%**	−53.9%

- Overhead and selling costs that are typical of a commodity-only business that sells product from New Zealand. Overhead costs are calculated by reference to Fonterra's actual costs, but exclude costs that are attributable to the much broader scope of Fonterra's business. Selling costs reflect the cost of selling product on GDT and through the relevant off-GDT channels, having regard to the volume of product assumed to be sold through each sales channel.

Table 6 and Figure 4 summarise the major categories of cash costs and the sources of movements in each category between the 2016 and 2017 Seasons.

The movements in costs are inclusive of the following:

- Milk supply decreased by 3 per cent in the 2017 Season compared to the 2016 Season. By itself, this resulted in fixed costs being spread across lower supply, increasing cash costs per kgMS by 0.8 cents. This was offset by the savings from the mothballing of 5 plants in response to reduced milk supply. The lower milk supply also resulted in a decrease in variable manufacturing and supply chain costs of NZD$20 million or 1.3 cents.
- Costs increased by an average of 1.1 per cent, or 1.3 cents per kgMS, due to price movements, net of the impact of various cost saving initiatives.
- The NZD$12 million decrease in costs relating to structural movements mainly reflects a reduction of NZD$14 million or 0.9 cents per kgMS, relating to savings arising out of the Velocity transformation programme that could reasonably be expected to also be realised by the Farmgate Milk Price business.

5 *The spot exchange rate at 9am on 31 July 2017, the last working day of Fonterra's 2017 financial year.*

6 *Fonterra uses currency options as well as forward exchange contracts to hedge its foreign currency receipts. Use of options means the average hedged conversion rate may vary with the spot exchange rate.*

TABLE 6: SUMMARY OF MOVEMENTS IN CASH COSTS

NZD $ MILLION	F16	VOLUME IMPACT[7]	COST / PRICE MOVEMENTS	STRUCTURAL CHANGES	ONE OFF	F17	% CHANGE DUE TO COST	TOTAL % CHANGE
Sales costs	108	(1)	3	(5)	–	**106**	**2.9%**	**–1.9%**
Variable manufacturing and supply chain costs	687	(20)	6	–	–	**673**	**0.9%**	**–2.0%**
Fixed manufacturing (including repairs and maintenance)/site overheads and supply chain costs	420	(15)	4	(3)	–	**406**	**1.1%**	**–3.3%**
Collection costs	349	(15)	1	4	–	**339**	**0.3%**	**–2.8%**
Other costs	252	–	5	(8)	(9)	**239**	**1.9%**	**–5.1%**
Total Cash Costs	**1,815**	**(51)**	**20**	**(12)**	**(9)**	**1,763**	**1.1%**	**–2.9%**
% movements		–2.8%	1.1%	–0.7%	–0.5%			

FARMGATE MILK PRICE CAPITAL COSTS

The Milk Price Model uses 'standard' plants to calculate both operating and plant-related capital costs. These plants have capacities that approximate Fonterra's average daily capacities for each type of plant and reflect current technology of the type typically employed across the industry.[8]

The standard plants are smaller than Fonterra's newest large manufacturing plants, such as the drier installed at Fonterra's Darfield Site in Canterbury in 2013 and the drier installed at Lichfield in 2016, but are larger and more efficient than Fonterra's older smaller plants.

The basis for deriving the benchmark depreciation, tax costs and capital charge is set out in detail in the Manual. In broad terms:

- The capital charge on fixed assets is designed to recover the full cost (through a depreciation charge) of the manufacturing and other assets required to manufacture Reference Commodity Products over the assets' economic lives, and to generate a return at the benchmark Weighted Average Cost of Capital (WACC, see below) on the undepreciated balance each year.
- The capital charge is calculated in a manner that results in it growing each year approximately in line with capital goods inflation, as long as the WACC does not change. This means that changes in the average age of the asset base do not result in material year-on-year movements in the capital charge, and therefore in the Farmgate Milk Price.
- The Farmgate Milk Price cost base also includes a provision for a capital charge on the monthly net working capital balances implied by the sale and manufacture of the Reference Commodity Products, and by the phasing of Fonterra's payments for milk to its suppliers. Each of these items varies somewhat between years, resulting in some annual variation in this element of the capital charge.
- The WACC used to determine the capital charge is specified on an after tax basis, so the Farmgate Milk Price cost base includes a separate provision for corporate tax. This amount is a relatively constant proportion of the WACC charges on fixed assets and net working capital each year.

FIGURE 4: SOURCES OF MOVEMENTS IN AVERAGE CASH COSTS

7 *Volume Impact considers only the change to milk solids collected in the 2017 Season on the 2016 Season cost base.*

8 *The average daily processing capacity of the standard WMP and SMP plants installed prior to the 2013 Season is approximately 1.9 million litres. Incremental and replacement WMP and SMP plants incorporated in the asset base since the 2013 Season have an average daily processing capacity of approximately 2.5 million litres, equivalent to the plants installed by Fonterra at Darfield in 2011 and Pahiatua in 2015.*

FARMGATE MILK PRICE **REVENUE AND COSTS**

CONTINUED

Table 7 shows the capital costs and the total book value of the Farmgate Milk Price fixed asset base and monthly average net working capital for the 2017, 2016 and 2015 Seasons.

Two matters are relevant to a comparison of capital costs between the 2017 and 2016 Seasons:

- In the 2017 Season, the WACC was 5.6 per cent, down from 5.9 per cent in 2016. By itself, this change resulted in a reduction of NZD$21 million in the capital charge on fixed assets, a reduction of NZD$4 million in the charge on net working capital, and a reduction of NZD$10 million in the tax charge, partially offset by an increase in depreciation expense of NZD$7 million. The fixed asset-related reductions were partially offset by an increase in capital costs due to the effects of the underlying methodology, which is designed to result in an aggregate capital charge that increases approximately in line with inflation and milk supply, holding other things equal.
- NZD$14 million of the reduction in the WACC charge on net working capital between 2016 and 2017 is due to the reduction in average net working capital, which is primarily attributable to the later timing, on average, of payments for milk in 2017 relative to 2016, with a smaller contribution from the earlier receipt of cash due to sales on average occurring earlier in 2017 than 2016.

TABLE 7: CAPITAL COSTS, BOOK VALUE OF FIXED ASSET BASE AND AVERAGE NET WORKING CAPITAL

NZD $ MILLION	2017	2016	2015
WACC rate % (post-tax)	**5.6%**	5.9%	6.1%
Depreciation	**265**	266	263
WACC Charge – fixed assets	**398**	407	393
WACC Charge – net working capital	**55**	73	120
Tax	**155**	169	176
Total capital costs	**873**	915	952
Total fixed assets (book value)	**7,195**	6,961	6,505
Average Net Working Capital	**913**	1,308	2,335

CALCULATION OF BENCHMARK WEIGHTED AVERAGE COST OF CAPITAL (WACC)

The WACC used to determine the Fixed Asset Capital Charges and the Net Working Capital Charge is calculated using the 'simplified Brennan Lally' methodology employed by the Commerce Commission[9]. The methodology applied through to the 2011 Season provided for input parameters into the WACC to be updated every four years. Consequently, the WACC was held constant at 8.5 per cent between the 2009 and 2011 Seasons, and reflected market interest rates as of mid-2008. From the 2012 Season, the methodology was revised to be based on rolling five-year averages of market interest rates, including the five-year New Zealand government stock rate, resulting in a reduction in the WACC from 7.7 per cent for the 2012 Season to 6.8 per cent for the 2014 Season.

In the 2015 Season, the WACC methodology was changed to incorporate a 'specific risk premium' of 0.15 per cent and a reduction in the asset beta from 0.45 to 0.38, on the basis of a review by an independent expert, Associate Professor Alastair Marsden of the University of Auckland. At the request of the Commerce Commission Dr Marsden undertook further analysis in the 2016 and 2017 Seasons, the result of which was to confirm his previous recommendation. The 2017 Season WACC was 5.6 per cent and the 2018 Season WACC will be 5.4 per cent, both reflecting further reductions in five-year average government stock rates.

9 See, for example, http://www.comcom.govt.nz/regulated-industries/input-methodologies-2/input-methodologies-review/cost-of-capital-im-review/

FARMGATE MILK PRICE **MANUAL CHANGES**

Since the Manual was introduced in the 2009 Season, various minor refinements have been made as practical issues were identified and addressed. Such refinements are to be expected given the importance to Fonterra of ensuring the Farmgate Milk Price approach is robust. Any modification to the Manual is required to be consistent with the Milk Price Principles which are set out in both the Manual and Fonterra's Constitution.

The Manual itself also allows for adjustments to various parameters. An example of this is the Detailed Rule that allows for the addition of new Reference Commodity Products if certain conditions established in the Manual are met.[10] The Manual also provides for reviews of various aspects of the Manual to be carried out at least once every four years. These reviews can result in changes to the application of rules in the Manual or inputs into the Farmgate Milk Price. A review of overhead costs was undertaken in the 2015 and 2016 Seasons and the results were incorporated into the 2016 Farmgate Milk Price.

As noted in Appendix 1, the Commerce Commission's final report on the 2016/17 Manual was released on 14 December 2016.

The Board approved a number of amendments to the Manual in July 2017, which will take effect from the 2018 Season. The updated version of the Manual is available on www.fonterra.com. There are no amendments that could be considered substantive.

10 Rule 3 in Part B of the Manual.

CHANGES IN APPROACH **TO THE CALCULATION**

Fonterra included in the 2015 Manual an undertaking to disclose any changes to the application of the Manual that result in materially different values of any input into the Farmgate Milk Price calculation.

One Manual amendment resulted in materially different values of inputs into the Farmgate Milk Price calculation for the 2017 Season. This amendment was disclosed in the 2016 Fonterra Farmgate Milk Price Statement:

- An amendment to the definition of Qualifying Reference Sales in Part C of the Manual. The practical implication of this change aligns the approach used to determine prices for WMP, SMP and AMF to the approach currently used for butter and BMP, by including sales undertaken off the GDT platform of similar specification product and sold on similar terms to GDT sales. The primary reason for making this change was that it has become increasingly clear in recent years that GDT sets the 'base' price for sales of Reference Commodity Products, with sales undertaken off GDT mostly being transacted at higher prices.
  This change has resulted in an increase in the Farmgate Milk Price for the 2017 Season that is 6 cents per kgMS.

APPENDIX 1
FARMGATE MILK PRICE OVERVIEW

RATIONALE FOR FARMGATE MILK PRICE

Fonterra currently collects around 82 per cent of New Zealand's milk production. Because Fonterra purchases such a large proportion of New Zealand's total milk, there is no 'market price' for milk that is independent of the price paid by Fonterra. As a result, since its formation in 2001, Fonterra has calculated a Farmgate Milk Price that enables total returns to be allocated between payments for milk and returns on the capital invested by Fonterra farmer shareholders and by unit holders in the Fonterra Shareholders' Fund.

FARMGATE MILK PRICE METHODOLOGY

The Farmgate Milk Price has been calculated in accordance with the Manual by:

- Determining the revenue that Fonterra would earn if the equivalent of all the milk Fonterra collects were converted into commodity specifications of WMP and SMP, and their by-products, which are butter, AMF and BMP. These products are referred to in the Manual as 'Reference Commodity Products'. Prices reflect USD prices achieved on the twice-monthly GlobalDairyTrade (GDT) trading events, or prices achieved by Fonterra in off-GDT sales, all of which use the most recent relevant GDT price as a key reference point. Selling prices are converted to NZD using Fonterra's actual average monthly foreign exchange conversion rate[11].
- Deducting costs, including the cost of transporting raw milk to factories, and the cost of efficiently manufacturing Reference Commodity Products and then transporting them to the point of export from New Zealand, along with selling and administration expenses. These costs also include amounts for depreciation of fixed assets and an appropriate return on investment, including investment in working capital.

The balance comprises the Farmgate Milk Price. While this is an aggregate amount, it is usually referred to on the basis of a Farmgate Milk Price per kgMS.

RATIONALE FOR REFERENCE COMMODITY PRODUCTS

Manufacture of the Reference Commodity Products comprised approximately 74 per cent of Fonterra's total New Zealand ingredients production in the 2017 Season.

Almost all additional milk collected over the past decade in New Zealand by Fonterra and its competitors has been used to make milk powders. Because returns from the sale of milk powders and their by-products represent the 'marginal' returns that would drive the price of milk in a competitive market in New Zealand, the Farmgate Milk Price is based on these products. Returns from non-powder commodities, such as cheese and casein, have largely been irrelevant in driving investment in the dairy industry over the past 10 years and are therefore not taken into account in determining the Farmgate Milk Price.

The Farmgate Milk Price approach does not include any returns earned by Fonterra from specialised ingredients and consumer branded products. These types of products earn premiums over the returns to standard commodity ingredients. It is therefore appropriate that these premiums are recognised in Fonterra's earnings rather than in the Farmgate Milk Price.

FARMGATE MILK PRICE GOVERNANCE

The Fonterra Board sets the total amount to be paid by Fonterra for all milk supplied to it in New Zealand in each season. For the 2017 Season, this amount is made up of the Farmgate Milk Price and Approved Adjustments (e.g. premium payments for some Winter Milk and Specialty Milk such as organic milk).

Both Fonterra's Constitution and the Dairy Industry Restructuring Act (2001) (DIRA) require Fonterra to maintain the Manual, which sets out Fonterra's policies and methodology for determining the Farmgate Milk Price. The Manual must reflect the Milk Price Principles set out in Fonterra's Constitution. The Farmgate Milk Price has been calculated in accordance with the Manual since the start of the 2009 Season.

The Fonterra Board has established a robust governance structure to oversee the setting of the Farmgate Milk Price, which comprises the elements illustrated in the diagram on page 12.

1 Milk Price Panel

The Milk Price Panel plays a key role in overseeing the integrity of the Farmgate Milk Price. It has five members. Two are Fonterra-appointed directors (one of whom is the Chair), one is a Fonterra farmer-elected director and two are appropriately qualified nominees of the Fonterra Shareholders' Council.

The current members of the Panel are: Scott St John (Chair) and David Jackson, who are appointed Fonterra directors; Ashley Waugh, who is a farmer-elected Fonterra director; and Andrew Wallace and Bill Donaldson, who are nominees of the Fonterra Shareholders' Council.

The Panel oversees the governance of the Farmgate Milk Price and the Manual, including changes to the Manual and verification by independent external experts of key parameters (such as resource usage rates, product yields and fixed manufacturing costs).

11 From the 2017 Season, a mixture of GDT and non-GDT prices were used for all Reference Commodity Product prices.

APPENDIX 1
FARMGATE MILK PRICE OVERVIEW CONTINUED

The Panel is responsible for:

- overseeing the calculation of the Farmgate Milk Price and making a recommendation on it to the Fonterra Board
- providing recommendations to the Fonterra Board on changes to the Manual
- providing assurance to the Fonterra Board that the Farmgate Milk Price has been calculated each year in accordance with the Manual.

The Fonterra Board is responsible for the forecast of the annual Farmgate Milk Price.

2 Milk Price Group

The Milk Price Group is a working group established by Fonterra. The Head of the Milk Price Group is independent of Fonterra's management and reports directly to the Chair of the Milk Price Panel. The role of the Milk Price Group includes:

- ensuring that the Farmgate Milk Price is calculated in accordance with the Manual and making recommendations in respect of the Farmgate Milk Price to the Panel
- considering any proposed amendments to the Manual, including those the Milk Price Group itself considers are appropriate, and ensuring they are in accordance with the Milk Price Principles in Fonterra's Constitution
- providing assurance to the Fonterra Board over the calculation of the forecast of the Farmgate Milk Price
- managing engagement with External Reviewers
- engaging with the Commerce Commission, including to ensure full disclosure of all material aspects of the Farmgate Milk Price derivation each year.

The functions of the Milk Price Group are contracted out to Ernst & Young and other technical experts who are not employees of Fonterra.

3 External Reviewers

External reviewers provide expert advice on various inputs, as well as assurance over the accuracy of financial models. In addition they participate in reviews of key parameters of the Farmgate Milk Price at regular intervals (which can be up to four years).

4 External Auditor

The external auditor audits the Farmgate Milk Price each year and provides assurance that the Farmgate Milk Price has been determined in accordance with the Milk Price Principles, Methodologies and Detailed Rules of the Farmgate Milk Price Manual. Fonterra's external auditor is PricewaterhouseCoopers.

5 Commerce Commission Farmgate Milk Price Oversight

Subpart 5A of DIRA, which was passed into law in July 2012, gives the Commerce Commission an oversight role with respect to Fonterra's Farmgate Milk Price.

The purpose of Subpart 5A is to promote the setting of a Farmgate Milk Price that provides an incentive to Fonterra to operate efficiently, while providing for contestability in the market for the purchase of milk from farmers (section 150A). Each year, the Commission is required to review and report on the extent to which the Manual and Fonterra's actual Farmgate Milk Price are consistent with this purpose:

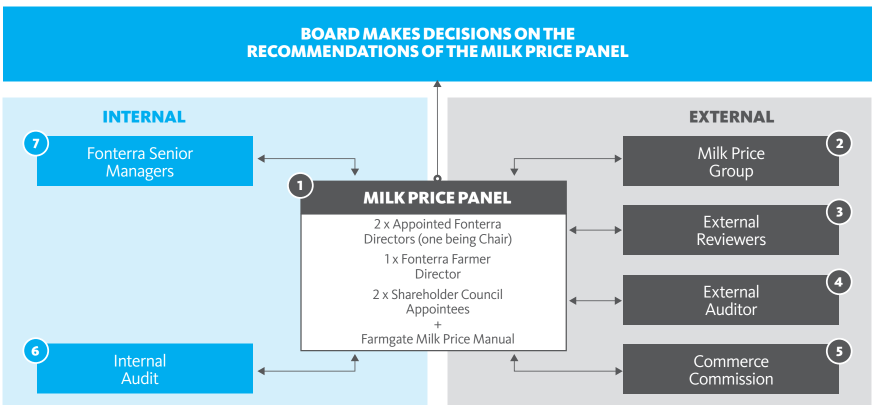
- The Commerce Commission's final report on the Manual for the 2016/17 Season was released on 14 December 2016 and can be found at http://www.comcom.govt.nz/regulated-industries/dairy-industry/review-of-fonterra-s-farm-gate-milk-price-and-manual/statutory-review-of-milk-price-manual/201617-season/
- The final report on the F17 Farmgate Milk Price calculation was released on 15 September 2017 and can be found at http://comcom.govt.nz/regulated-industries/dairy-industry/review-of-fonterra-s-farm-gate-milk-price-and-manual/statutory-review-of-milk-price-calculation-2/review-of-milk-price-calculation-201617-season/

6 Internal Audit

Fonterra's internal audit team provides assurance over the processes and controls relating to Fonterra data used in the calculation of the Farmgate Milk Price.

7 Fonterra Senior Managers

Fonterra senior managers provide internal oversight of the calculation of the actual and forecast Farmgate Milk Price in accordance with the Manual and detailed models and procedures.



Source: Fonterra

APPENDIX 2

INDEPENDENT ASSURANCE REPORT

TO THE DIRECTORS OF FONTERRA CO-OPERATIVE GROUP LIMITED

Scope

We have audited the application of the Principles, Methodologies and Detailed Rules as defined in the Farmgate Milk Price Manual of 1 August 2016 (the Manual) by the Milk Price Group (MPG) in deriving the aggregate amount payable for New Zealand supplied milk for the season ended 31 May 2017 of NZD$9.349 billion, which is NZD$6.13 on a per kilogram of milk solids (kgMS) basis (the Farmgate Milk Price). We have confirmed the balances contained in the Farmgate Milk Price Statement for the season ended 31 May 2017 (the Farmgate Milk Price Statement) are correctly extracted from the calculation of the Farmgate Milk Price.

Information other than our scope and the assurance report

The Directors are responsible for the Farmgate Milk Price Statement. Our opinion on the Farmgate Milk Price Statement does not cover information other than the balances we confirm have been correctly extracted from the calculation of the Farmgate Milk Price and we do not express any form of assurance conclusions on the other information.

In connection with our scope, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Farmgate Milk Price Statement or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this assurance report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Milk Price Group's Responsibilities

The MPG are responsible for the calculation of the Farmgate Milk Price based upon the Manual, ensuring the Farmgate Milk Price has been derived in accordance with the Principles, Methodologies and Detailed Rules set out in the Manual. The MPG is also responsible for the preparation of the Farmgate Milk Price Statement.

Our Independence and Quality Control

We have complied with the independence and other ethical requirements of Professional and Ethical Standard 1 (Revised) issued by the New Zealand Auditing and Assurance Standards Board, which is founded on the fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

The firm applies Professional and Ethical Standard 3 (Amended) and accordingly maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards, and applicable legal and regulatory requirements.

Independent Auditors' Responsibilities

We are responsible for expressing an independent opinion on whether the MPG has complied, in all material respects, with the Principles, Methodologies and Detailed Rules set out in the Manual in deriving the Farmgate Milk Price, and that the balances, in all material respects, in the Farmgate Milk Price Statement have been correctly extracted from those calculations, and reporting our opinion to you.

We conducted our independent assurance engagement in accordance with ISAE (NZ) 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information* and SAE 3100 *Compliance Engagements* issued in New Zealand. Those standards require that we comply with ethical requirements and plan and perform our procedures to obtain reasonable assurance about whether, the MPG has complied, in all material respects, with Principles, Methodologies and Detailed Rules of the Manual in deriving the Farmgate Milk Price, and that the balances, in all material respects, in the Farmgate Milk Price Statement have been correctly extracted from those calculations.

Inherent Limitations

Our engagement includes examining, on a test basis, evidence relevant to the amounts used to derive the Farmgate Milk Price and the balances in the Farmgate Milk Price Statement. It also includes assessing the significant assumptions, estimates and judgements made by the MPG in the calculation of the Farmgate Milk Price and ensuring the Principles, Methodologies and Detailed Rules applied are consistent with those set out in the Manual. Because of the inherent limitations, it is possible that fraud, error or non-compliance may occur and not be detected. As the procedures performed are undertaken on a test basis, our assurance engagement cannot be relied on to detect all instances where the Principles, Methodologies and Detailed Rules set out in the Manual have not been complied with. Our opinion expressed in this report has been formed on that basis.

APPENDIX 2
INDEPENDENT ASSURANCE REPORT
TO THE DIRECTORS OF FONTERRA CO-OPERATIVE GROUP LIMITED CONTINUED

Our firm carries out other services for the Fonterra Co-operative Group Limited in relation to advisory services, other assurance and attestation services. Partners and employees of our firm may deal with the Fonterra Co-operative Group Limited on normal terms within the ordinary course of the trading activities of the Fonterra Co-operative Group Limited. These matters have not impaired our independence as auditor of the Farmgate Milk Price.

Independent Assurance Opinion

In our opinion the MPG has complied, in all material respects, with the Principles, Methodologies and Detailed Rules in the Manual in deriving the aggregate amount payable for New Zealand-supplied milk for the season ended 31 May 2017 of NZD$9.349 billion, which is NZD$6.13 on a per kgMS basis. We have confirmed the balances contained in this Farmgate Milk Price Statement for the season ended 31 May 2017 are correctly extracted, in all material respects, from the Farmgate Milk Price calculation.

Restriction on Distribution or Use

This report is made solely to the Directors. Our report has been prepared at the request of the Directors and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than Fonterra Co-operative Group Limited for this report, or for the opinions we have formed.

PricewaterhouseCoopers

PricewaterhouseCoopers
Auckland, New Zealand
23 September 2017

ATTACHMENT 1
MILK SUPPLIED AND PRODUCTION VOLUMES

2017 SEASON	MILK SUPPLIED (MILLION kgMS)	PRODUCTION (000 MT) OF FINISHED PRODUCT					
		WMP	SMP	BUTTER	AMF	BMP	TOTAL
JUN 16 TO AUG 16	122	134	59	16	19	5	**234**
SEP 16 TO NOV 16	573	668	250	98	59	23	**1,098**
DEC 16 TO FEB 17	500	604	200	88	46	20	**957**
MAR 17 TO MAY 17	331	421	110	54	30	14	**630**
TOTAL	**1,526**	**1,826**	**619**	**256**	**154**	**63**	**2,918**

2016 SEASON	MILK SUPPLIED (MILLION kgMS)	PRODUCTION (000 MT) OF FINISHED PRODUCT					
		WMP	SMP	BUTTER	AMF	BMP	TOTAL
JUN 15 TO AUG 15	127	165	44	11	18	5	**243**
SEP 15 TO NOV 15	609	727	255	99	64	24	**1,169**
DEC 15 TO FEB 16	515	587	225	100	49	22	**984**
MAR 16 TO MAY 16	315	382	115	51	35	15	**597**
TOTAL	**1,566**	**1,862**	**639**	**261**	**166**	**65**	**2,993**

2015 SEASON	MILK SUPPLIED (MILLION kgMS)	PRODUCTION (000 MT) OF FINISHED PRODUCT					
		WMP	SMP	BUTTER	AMF	BMP	TOTAL
JUN 14 TO AUG 14	127	168	43	10	17	5	**244**
SEP 14 TO NOV 14	643	728	287	113	70	27	**1,225**
DEC 14 TO FEB 15	521	665	175	88	45	19	**992**
MAR 15 TO MAY 15	323	440	83	42	32	13	**611**
TOTAL	**1,614**	**2,000**	**589**	**254**	**164**	**63**	**3,071**

ATTACHMENT 2
SALES VOLUMES

2017 SEASON	SHIPMENTS (000 MT) OF FINISHED PRODUCT					
	WMP	SMP	BUTTER	AMF	BMP	TOTAL SALES
AUG 16 TO OCT 16	257	104	27	30	2	**419**
NOV 16 TO JAN 17	616	222	86	50	17	**991**
FEB 17 TO APR 17	405	115	62	29	16	**628**
MAY 17 TO JUL 17	485	155	59	39	24	**761**
AUG 17 TO OCT 17	62	24	23	6	3	**118**
TOTAL	**1,826**	**619**	**256**	**154**	**63**	**2,918**

2016 SEASON	SHIPMENTS (000 MT) OF FINISHED PRODUCT					
	WMP	SMP	BUTTER	AMF	BMP	TOTAL SALES
AUG 15 TO OCT 15	195	31	14	16	0	**255**
NOV 15 TO JAN 16	712	281	94	71	25	**1,184**
FEB 16 TO APR 16	413	147	58	27	13	**658**
MAY 16 TO JUL 16	447	147	65	41	19	**720**
AUG 16 TO OCT 16	94	33	29	11	9	**176**
TOTAL	**1,862**	**639**	**261**	**166**	**65**	**2,993**

2015 SEASON	SHIPMENTS (000 MT) OF FINISHED PRODUCT					
	WMP	SMP	BUTTER	AMF	BMP	TOTAL SALES
AUG 14 TO OCT 14	253	35	24	20	5	**337**
NOV 14 TO JAN 15	671	208	83	48	15	**1,025**
FEB 15 TO APR 15	519	150	60	33	14	**775**
MAY 15 TO JUL 15	431	117	46	38	16	**648**
AUG 15 TO OCT 15	127	80	41	25	13	**286**
TOTAL	**2,000**	**589**	**254**	**164**	**63**	**3,071**

ATTACHMENT 3
AVERAGE NUMBER OF MONTHS PRIOR TO SHIPMENT THAT PRICES WERE STRUCK

2017 SEASON	AVERAGE NUMBER OF MONTHS PRIOR TO SHIPMENT				
	WMP	SMP	BUTTER	AMF	BMP
AUG 16 TO OCT 16	2.9	3.2	3.0	2.8	2.7
NOV 16 TO JAN 17	3.1	3.1	3.2	3.1	2.6
FEB 17 TO APR 17	2.6	2.9	2.9	2.8	2.4
MAY 17 TO JUL 17	2.6	2.5	2.5	2.6	2.7
AUG 17 TO OCT 17	3.7	3.8	3.1	3.7	3.6
	2.9	**3.0**	**2.9**	**2.9**	**2.7**

2016 SEASON	AVERAGE NUMBER OF MONTHS PRIOR TO SHIPMENT				
	WMP	SMP	BUTTER	AMF	BMP
AUG 15 TO OCT 15	3.1	2.7	2.8	2.8	N/A[12]
NOV 15 TO JAN 16	3.1	3.4	2.8	3.3	3.3
FEB 16 TO APR 16	2.8	3.0	2.9	2.7	2.6
MAY 16 TO JUL 16	2.9	2.8	2.6	2.6	3.2
AUG 16 TO OCT 16	2.9	2.9	2.9	3.3	2.9
	3.0	**3.1**	**2.8**	**3.0**	**3.0**

2015 SEASON	AVERAGE NUMBER OF MONTHS PRIOR TO SHIPMENT				
	WMP	SMP	BUTTER	AMF	BMP
AUG 14 TO OCT 14	2.6	2.9	3.0	3.0	3.1
NOV 14 TO JAN 15	3.0	3.0	2.8	3.2	2.6
FEB 15 TO APR 15	3.0	3.1	2.7	3.0	2.5
MAY 15 TO JUL 15	2.8	2.6	2.5	2.6	2.4
AUG 15 TO OCT 15	3.1	3.2	3.0	3.1	3.2
	2.9	**3.0**	**2.8**	**3.0**	**2.7**

The tables on the next page supplement those above by providing information on the average percentages of sales contracted in each of months 1 to 5 prior to shipment in the 2015 to 2017 Seasons.

12 Not applicable: No BMP sales informed the Farmgate Milk Price revenue in this quarter.

ATTACHMENT 3
CONTINUED

AVERAGE % OF SALES CONTRACTED IN EACH MONTH PRIOR TO SHIPMENT

2017 SEASON	AVERAGE PERCENTAGE OF SALES CONTRACTED IN EACH OF MONTHS 1-5 PRIOR TO SHIPMENT				
	WMP	SMP	BUTTER	AMF	BMP
1	11%	9%	9%	10%	11%
2	31%	31%	29%	29%	33%
3	29%	27%	29%	32%	37%
4	18%	19%	18%	20%	18%
5	11%	13%	14%	9%	1%

2016 SEASON	AVERAGE PERCENTAGE OF SALES CONTRACTED IN EACH OF MONTHS 1-5 PRIOR TO SHIPMENT				
	WMP	SMP	BUTTER	AMF	BMP
1	8%	6%	7%	10%	7%
2	33%	29%	37%	33%	32%
3	28%	28%	32%	28%	24%
4	19%	24%	17%	19%	29%
5	13%	13%	6%	11%	8%

2015 SEASON	AVERAGE PERCENTAGE OF SALES CONTRACTED IN EACH OF MONTHS 1-5 PRIOR TO SHIPMENT				
	WMP	SMP	BUTTER	AMF	BMP
1	8%	6%	9%	7%	10%
2	33%	34%	33%	32%	41%
3	27%	31%	36%	31%	26%
4	20%	19%	18%	19%	20%
5	12%	10%	4%	11%	3%

ATTACHMENT 4
AVERAGE USD PRICES

2017 SEASON	**USD PER MT OF FINISHED PRODUCT**				
SHIPMENT PERIOD	**WMP**	**SMP**	**BUTTER**	**AMF**	**BMP**
AUG 16 TO OCT 16	2,271	1,919	2,936	3,840	1,767
NOV 16 TO JAN 17	2,709	2,236	3,589	4,655	2,338
FEB 17 TO APR 17	3,250	2,576	4,388	5,497	2,656
MAY 17 TO JUL 17	3,005	2,135	5,016	6,073	1,900
AUG 17 TO OCT 17	2,951	2,102	5,601	6,270	1,909
	2,854	**2,216**	**4,221**	**5,076**	**2,211**
FULL SEASON GDT-ONLY PRICES	**2,837**	**2,188**	**4,184**	**4,977**	**2,172**

Full season GDT-only prices are disclosed for the first time for the 2017 Season, following the inclusion of the non-GDT sales of WMP, SMP and AMF in the Farmgate Milk Price. Quarterly prices are the total weighted average prices informing the Farmgate Milk Price, consistent with prior season disclosures.

2016 SEASON	**USD PER MT OF FINISHED PRODUCT**				
SHIPMENT PERIOD	**WMP**	**SMP**	**BUTTER**	**AMF**	**BMP**
AUG 15 TO OCT 15	1,957	1,480	2,467	2,732	N/A[13]
NOV 15 TO JAN 16	2,093	1,789	2,769	3,093	1,868
FEB 16 TO APR 16	2,239	1,950	3,000	3,654	1,732
MAY 16 TO JUL 16	2,065	1,765	2,832	3,331	1,567
AUG 16 TO OCT 16	2,221	1,732	2,853	3,374	1,632
	2,111	**1,803**	**2,830**	**3,227**	**1,723**

2015 SEASON	**USD PER MT OF FINISHED PRODUCT**				
SHIPMENT PERIOD	**WMP**	**SMP**	**BUTTER**	**AMF**	**BMP**
AUG 14 TO OCT 14	3,130	3,217	3,213	3,642	4,122
NOV 14 TO JAN 15	2,694	2,761	2,808	3,417	3,056
FEB 15 TO APR 15	2,423	2,487	3,217	3,922	2,713
MAY 15 TO JUL 15	2,593	2,482	3,338	3,781	2,351
AUG 15 TO OCT 15	2,419	1,938	2,733	3,072	1,919
	2,639	**2,552**	**3,027**	**3,577**	**2,657**

13 Not applicable: No BMP sales informed the Farmgate Milk Price revenue in this quarter.

ATTACHMENT 5
AVERAGE USD:NZD CONVERSION AND SPOT RATES

Note that the spot data is based on the weighted average conversion rate that would have been achieved if the revenue collected during the shipping period was converted at the average spot rate in the month of collection. Certain average spot exchange rate figures for the 2016 Season differs from those disclosed in the 2016 Farmgate Milk Price Statement, as forecast exchange rates have been replaced with actual exchange rates.

2017 SEASON	FONTERRA'S AVERAGE CONVERSION RATE	SPOT EXCHANGE RATE
AUG 16 TO OCT 16	0.6766	0.7156
NOV 16 TO JAN 17	0.6830	0.7117
FEB 17 TO APR 17	0.6922	0.6978
MAY 17 TO JUL 17	0.7071	0.7364
AUG 17 TO OCT 17	0.7136	0.7504[14]
REVENUE-WEIGHTED ANNUAL AVERAGE	**0.6924**	**0.7171**

2016 SEASON	FONTERRA'S AVERAGE CONVERSION RATE	SPOT EXCHANGE RATE
AUG 15 TO OCT 15	0.7359	0.6581
NOV 15 TO JAN 16	0.7231	0.6637
FEB 16 TO APR 16	0.7076	0.6803
MAY 16 TO JUL 16	0.6849	0.7130
AUG 16 TO OCT 16	0.6790	0.7275
REVENUE-WEIGHTED ANNUAL AVERAGE	**0.7082**	**0.6820**

2015 SEASON	FONTERRA'S AVERAGE CONVERSION RATE	SPOT EXCHANGE RATE
AUG 14 TO OCT 14	0.8035	0.7848
NOV 14 TO JAN 15	0.7957	0.7628
FEB 15 TO APR 15	0.7943	0.7488
MAY 15 TO JUL 15	0.7706	0.6727
AUG 15 TO OCT 15	0.7625	0.6492
REVENUE-WEIGHTED ANNUAL AVERAGE	**0.7882**	**0.7312**

14 The spot exchange rate for the period from August to October 2017 equals the spot rate at 9am on 31 July 2017, the last working day of Fonterra's 2017 financial year.

GLOSSARY

In this Statement, unless the context otherwise requires, the following terms have the meanings set out next to them:

AMF means anhydrous milk fat.

Approved Adjustments means an amount approved by the Fonterra Board to be paid for milk in addition to, or to be subtracted from, the amount calculated under the Farmgate Milk Price Manual.

BMP means buttermilk powder.

Detailed Rules means the detailed rules for calculating the Farmgate Milk Price as set out in the Manual.

DIRA means the Dairy Industry Restructuring Act 2001, which authorised Fonterra's formation and regulates its activities.

Farmgate Milk Price means Fonterra's Farmgate Milk Price as determined under the Manual.

Farmgate Milk Price Capital Costs are defined in the Manual.

Farmgate Milk Price Cash Costs are defined in the Manual.

Farmgate Milk Price Manual or **Manual** means Fonterra's Farmgate Milk Price Manual.

Financial year means Fonterra's financial year, which runs from 1 August to the following 31 July.

Fonterra means Fonterra Co-operative Group Limited.

GlobalDairyTrade or **GDT** means the electronic auction platform that is used to sell commodity dairy products.

Independent Processors means entities which are independent of Fonterra and process raw milk.

kgMS means kilograms of milk solids.

Methodologies means the methodologies for calculating the Farmgate Milk Price as set out in the Manual.

Milk Price Model means the model used to calculate the Farmgate Milk Price set out in the Manual.

Milk Price Principles or **Principles** means the Milk Price Principles set out in Fonterra's Constitution.

MT means metric tonnes.

NZD means New Zealand dollars.

Raw Milk Regulations means the Dairy Industry Restructuring (Raw Milk) Regulations 2001 or, where applicable, the Dairy Industry Restructuring (Raw Milk) Regulations 2012.

Reference Commodity Products means the commodity products used to calculate the Farmgate Milk Price, comprising WMP, SMP, BMP, AMF and butter.

Season means the 12-month period from 1 June to the following 31 May.

SMP means skim milk powder.

Specialty Milk means milk that has special properties such as organic milk.

USD means United States dollars.

Winter Milk means milk supplied by farmers in the months of May, June and July.

WMP means whole milk powder.

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Shareholder And Supplier Services
Freephone 0800 65 65 68
For global locations visit www.fonterra.com

APPENDIX 3 – FSM Rules

EMAIL: announce@nzx.com

Notice of event affecting securities

FSM Rule 6.8.2. For rights, Rules 6.6.8 and 6.6.10.
For change to allotment, FSM Rule 6.8.1, a separate notice is required.

Number of pages including this one (Please provide any other relevant details on additional pages)

Full name of Issuer	**Fonterra Co-operative Group Limited**
Name of officer authorised to make this notice	**Paul Washer**
Authority for event, e.g. Directors' resolution	**Directors' resolution**
Contact phone number	**(09) 374 9000**
Contact fax number	**(09) 374 9001**
Date	**23 / 09 / 2017**

Nature of event
Tick as appropriate

Bonus Issue	☐
If ticked, state whether: Taxable	☐
/ Non Taxable	☐
Conversion	☐
Interest	☐
Rights Issue Renouncable	☐
Rights Issue non-renouncable	☐
Capital change	☐
Call	☐
Dividend	X
If ticked, state whether: Interim	☐
Full Year	X
Special	☐
DRP Applies	X

EXISTING securities affected by this

If more than one security is affected by the event, use a separate form.

Description of the class of securities	**Shares (FCG)**
ISIN	**NZFCGE0001S7**

If unknown, contact NZX

Details of securities issued pursuant to this event

If more than one class of security is to be issued, use a separate form for each class.

Description of the class of securities	**N/A**
ISIN	

If unknown, contact NZX

Number of Securities to be issued following event	**N/A**
Minimum Entitlement	
Ratio, e.g 1 for 2	for
Conversion, Maturity, Call Payable or Exercise Date	**N/A**
Treatment of Fractions	**N/A**
Tick if pari passu	☐
OR provide an explanation of the ranking	
Strike price per security for any issue in lieu or date Strike Price available.	

Enter N/A if not applicable

Monies Associated with Event

Dividend payable, Call payable, Exercise price, Conversion price, Redemption price, Application money.

In dollars and cents

Amount per security (does not include any excluded income)	**$0.200**
Source of Payment	**Profit**
Currency	**NZD**
Total monies	**$321,386,502**

Supplementary dividend details - FSM Rule 6.8.5

Amount per security in dollars and cents	
Date Payable	

Taxation

Amount per Security in Dollars and cents to six decimal places

In the case of a taxable bonus issue state strike price	$
Resident Withholding Tax	**$0.066000**
Imputation Credits (Give details)	
Foreign Withholding Tax	$
FDP Credits (Give details)	

Timing (Refer Appendix 4 in the FSM Rules)

Record Date 5pm *For calculation of entitlements -*	**9 October, 2017**
Application Date *Also, Call Payable, Dividend / Interest Payable, Exercise Date, Conversion Date. In the case of applications this must be the last business day of the week.*	**9 October, 2017**
Notice Date *Entitlement letters, call notices, conversion notices mailed*	**N/A**
Allotment Date *For the issue of new securities. Must be within 5 business days of application closing date.*	**N/A**

OFFICE USE ONLY
Ex Date:
Commence Quoting Rights:
Cease Quoting Rights 5pm:
Commence Quoting New Securities:
Cease Quoting Old Security 5pm:

Security Code:

Security Code:

NZX