

Fonterra Co-operative Group Limited

Results for Announcement to the Market

Reporting Period	Six months ended 31 January 2018
Previous Reporting Period	Six months ended 31 January 2017

	Amount (Million)	Percentage Change
Revenue from ordinary activities	NZ\$9,839	6%
Profit (loss) from ordinary activities after tax attributable to security holder ¹	NZ\$(354)	(186)%
Net profit (loss) attributable to security holders	NZ\$(348)	(183)%

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
Interim dividend	NZ\$0.10	\$0.00

Record Date	6 April 2018
Dividend Payment Date	20 April 2018

Comments	On 20 March 2018, the Board of Directors declared a dividend of 10.0 cents per share to be paid on 20 April 2018 to Shareholders on the share register at 6 April 2018.
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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.



INTERIM REPORT 2018

CONTENTS

HIGHLIGHTS	1
CHAIRMAN AND CHIEF EXECUTIVE OFFICER'S LETTER	2
OUR CO-OPERATIVE	8
OUR POTENTIAL	12
OUR PERFORMANCE	16
INTERIM FINANCIAL STATEMENTS	30

OUR CO-OPERATIVE

We have a unique strength coming from being a vertically integrated supply chain of scale – connecting high quality milk from pasture fed cows to customers around the world.

FARM SOURCE™ REWARDS
DOLLARS EARNED THIS YEAR

FS\$7M

NUMBER OF FARMERS WHO
HAVE EARNED FARM SOURCE™
REWARDS DOLLARS THIS YEAR

8,200

\$6.55 ↑

FORECAST
FARMGATE
MILK PRICE

10CPS

INTERIM
DIVIDEND
PER SHARE

1,480 ↓
M KGMS

2017/2018
NEW ZEALAND
MILK COLLECTION
FORECAST

Fonterra uses several non-GAAP measures when discussing financial performance. These measures include normalised segment earnings, normalised EBIT, EBIT, normalisation adjustments, normalised earnings per share, normalised NPAT 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 underlying 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. Please refer to page 48 for the reconciliation of the NZ IFRS measures to the non-GAAP measures and page 49 for definitions of the non-GAAP measures used by Fonterra.



OUR POTENTIAL

We focused on shifting more of our farmers' milk into higher value products. We remain on-track to deliver an additional 400 million LME to our Consumer and Foodservice business this year.

GOAL FOR LITRES OF MILK PROCESSED BY 2025

30_B

EXPECTED INCREASE IN DEMAND FOR FOOD BY 2050

50%

OUR PERFORMANCE

We delivered a strong Ingredients performance and continued to make progress in moving milk up the value chain, with volume growth across a number of Consumer and Foodservice markets.

INGREDIENTS NORMALISED EBIT

\$558_M

CONSUMER AND FOODSERVICE NORMALISED EBIT

\$193_M



We've introduced new financial tools to help our farmers become fully shared up.

\$458_M



GROUP NORMALISED EBIT (NZD)



Our Global Foodservice business topped \$2 billion in revenue last year, making it the sixth biggest exporter.

\$248_M



NORMALISED NPAT (NZD)



We've set up a new medical nutrition and 'healthy ageing' division and launched a fast-acting milk protein.

(\$348_M)



NET LOSS AFTER TAX (NZD)



CHAIRMAN AND CHIEF EXECUTIVE OFFICER'S LETTER

In what has been a challenging year to date for conditions on-farm, it's pleasing to be able to increase our forecast Farmgate Milk Price for the 2017/18 season to \$6.55 per kgMS and announce an interim dividend of 10 cents.

FARMERS WILL WELCOME WHAT IS THE THIRD HIGHEST FORECAST AVAILABLE FOR PAYOUT IN THE LAST DECADE, BUT THE CO-OPERATIVE IS ACUTELY AWARE OF THE CHALLENGES MANY OF OUR FARMERS HAVE FACED THIS SEASON WITH DIFFICULT WEATHER CONDITIONS IMPACTING MILK PRODUCTION AND THEREFORE FARM REVENUE.

The Board will decide how the Beingmate impairment and the Danone payment will be treated for final dividend purposes after the end of the financial year when it will have the full picture of its operating performance. Given the possible impact of these decisions, the Board is providing a forecast dividend range for the full-year of 25–35 cents per share.

Based on our dividend policy, this forecast dividend range would allow for the full impact of the Danone payment, at the low end, through to an adjustment for both the Beingmate impairment and the Danone payment as one-off events at the higher end.

In the circumstances, we have taken a prudent approach in determining the 10 cent interim dividend.

We continue to offer a dividend reinvestment plan at a discount of 2.5 per cent to the strike price. Eligible shareholders who wish to participate in the plan for the interim dividend need to submit a notice of participation by 6 April 2018.

As indicated in December, the decision in our arbitration with Danone resulted in a downward revision of our earnings guidance of 10 cents to 35–45 cents per share.



We remain disappointed that the arbitration tribunal did not fully recognise the terms of our supply agreement with Danone, including the agreed limitations of liability, which was the basis on which we had agreed to do business.

In this period, we have reported \$232 million related to the Danone arbitration, which represent the recall costs awarded to Danone and interest, and other costs associated with the arbitration. This brings the arbitration proceedings to a close.

The Co-operative has also re-assessed the value of our Beingmate investment so that it reflects a fair value at this point in time.

We have assessed the carrying value of Beingmate at \$244 million which is the fair value of the investment, less the costs to sell the asset.

Shareholders will be rightfully frustrated with this outcome.

While Fonterra appreciates the substantial opportunity to build a significant business in China, Beingmate's continued poor performance is unacceptable. The urgent recovery of the investment is a key priority for the senior management team and the Board.

The opportunity in the Chinese infant formula market remains – as does the potential for our Beingmate partnership – but an immediate business transformation is needed in order for Beingmate to benefit from the market opportunities.

THE GLOBAL SUPPLY AND DEMAND PICTURE REMAINS IN BALANCE

Our farmers have endured tough farming conditions across much of the country. A cold, wet spring followed by low rainfall in early summer and then unusually high summer temperatures resulted in milk collection across New Zealand declining. Our full-year forecast New Zealand milk collection has been revised to 1,480 million kgMS, down three per cent compared to last season's actual total collection of 1,526 million kgMS.

USEFUL FACT

Global demand for dairy nutrition remains strong, and we're seeing positive growth in China, Asia and Latin America.



Continuing strong global demand for dairy is being led by China – where imports are up 13 per cent over the last 12 months – and is strongly supported by growth in Asia and Latin America. However, we are mindful of the potential impact of strong spring production in Europe on market sentiment.

Fundamentally, the market is balanced and we would expect prices to stay at current levels.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER'S LETTER

ANCHOR™ IN SRI LANKA

Our farmer shareholders Ross and Shayney Wallis visited Sri Lanka where 1.3 billion glasses of Anchor™ milk are consumed each year.



FINANCIAL PERFORMANCE

While the overall improvement in the Farmgate Milk Price compared to last year is good news for farmers, it does increase the pressure on our margins across the business.

Our low starting inventory levels, which were then followed by reduced New Zealand milk collections due to the difficult weather conditions, impacted our overall sales volume in the first half.

In the context of these two key challenges, our half-year operating performance is in line with expectations.

Ongoing financial discipline has enabled the Co-operative to maintain a strong balance sheet and manage the impact of the Danone arbitration decision and Beingmate impairment.

Our debt and gearing levels are both traditionally higher at the end of the first six months of the year, reflecting the seasonal profile of our business. As at 31 January 2018, debt was \$7.1 billion – better than expected but \$945 million higher than the comparable period last year. This is due in part to lower earnings, the impact of the Danone arbitration, and the timing of capital expenditure – particularly the expansion of Clandeboy with a new mozzarella plant, and a new cream cheese plant build at our Darfield site.

As a result, our gearing ratio at the half-year has increased to 51.6 per cent. We remain committed to our end of year gearing range target of 40 - 45 per cent.

Normalised operating costs were up three per cent for the six months to 31 January 2018, after two years of declining costs. This is a result of increased research and development spending to support new product development, digital platforms and technology opportunities.

INGREDIENTS BUSINESS

Our Ingredients business delivered a strong result, with revenue up \$678 million, or nine per cent, and normalised EBIT also up nine per cent at \$558 million.

The increase in normalised EBIT is reflective of higher margins, improvements in optimisation of our overall product mix and increased demand in our business in Australia.

The result benefited from higher stream returns in the first half compared to the same period last year. This enabled the overall New Zealand Ingredients gross margin, including both reference and non-reference products, to increase by 14 per cent to \$734 million.

While revenue and gross margin per metric tonne for reference and non-reference products both increased, the relative increase in the milk price cost was greater for reference products, such as butter, due to the significant increase in fat prices. Stream returns on non-reference products were \$90 million, \$50 million ahead of the same period last year.

MOZZARELLA

Mozzarella is one of Fonterra's most profitable products.



CONSUMER AND FOODSERVICE

Our strategy emphasises making the most of our farmers' milk by shifting more volume into higher value products at velocity. Our high-value Consumer and Foodservice business delivered revenue of \$3.5 billion for the six months to 31 January 2018, an increase of seven per cent.

Overall, normalised EBIT decreased 38 per cent to \$193 million due to pressure on our margins in this business. It's important to note that this result is compared to an exceptional \$313 million last year when the first half-year input costs were considerably lower.

Higher input costs over the first half of this year meant margins were reduced by 15 per cent. Strong competition in the Co-operative's strategic markets, especially in Foodservice, limited our options to pass through the higher input costs.

Consumer and Foodservice volumes were two per cent lower. Our sales volumes in the key markets of Asia, Latin America, and Greater China improved but this was offset by lower volumes in Oceania.

Oceania volumes were primarily affected by operational start up challenges at our new distribution centre in New Zealand which have now been resolved.

CREATING VALUE IN CHINA

While our Beingmate investment has underperformed, which we are very concerned about, our integrated business in China is delivering positive results for our Co-operative. We expect this high growth in China to continue.

In our first half, China volumes accounted for 2.2 billion LME of our total 9.8 billion LME in Ingredients, with around 80 per cent of this milk sourced in New Zealand.

In our Consumer and Foodservice business, China volumes accounted for 600 million LME of the total 2.7 billion LME over the first half, with Consumer and Foodservice in Greater China achieving normalised EBIT of \$92 million on volume growth of three per cent.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER'S LETTER

INFANT MILK FORMULA

The China Infant Milk Formula market is growing at five per cent, with total value sales projected to grow from RMB84 billion to RMB100 billion (NZD18 billion to NZD22 billion) by 2020.



BEINGMATE

As a result of Beingmate's continued poor performance, its share price has deteriorated to a level where it is necessary for the Co-operative to reassess the value of its investment.

We have determined a fair value of \$244 million using an estimate of what someone would pay for a similar long-term equity stake in Beingmate today. In this instance, we have used Beingmate's base share price. We have therefore taken an impairment of \$405 million.

Clearly this outcome is unacceptable to our shareholders. The recovery of the value of this investment is the number one immediate priority for the Chief Executive and the senior management team.

As an 18.8 per cent shareholder, we do not have direct control over the company but we are working to influence its direction and continue to call for an urgent business transformation through our relationship with Beingmate's founder and majority shareholder.

The Board has a working group – that includes Independent Directors Simon Israel and Clinton Dines, who both have significant China experience and expertise – to provide guidance and oversight to management as they work to recover the investment.

CHINA FARMS

China Farms continued to lift efficiencies as our milk production increases. Operating costs per litre of milk are down six per cent over the reporting period. Our normalised EBIT has improved to a \$12 million loss, compared to a \$24 million loss in the same period last year.

Our China Farms result is buoyed by an internal raw milk price between China Farms and our Ingredients business which is currently higher than the unsustainably low domestic milk price.

The future of our investment in these farms is promising. Chinese demand for high-quality local fresh milk continues to grow and our recent partnerships with Alibaba and Starbucks in China have us well placed to maximise this opportunity.

In February this year, we launched a new 'Daily Fresh' milk range through Alibaba's Hema Fresh stores in Shanghai and Suzhou and volumes are growing rapidly. Sourced directly from the Co-operative's farm hub in Hebei province, the bottles of fresh milk capitalise on the continued shift in China's consumer market to premium products.

FONTERRA MILK FOR SCHOOLS

Fonterra Milk for Schools celebrated its fifth anniversary this year.



FONTERRA AUSTRALIA

In Australia, we continue to grow our market share, with milk supply increasing by 400 million litres to two billion litres since last season. We are now Australia's leading dairy processor in a competitive market and are taking advantage of good demand growth prospects especially in cheese, whey and nutritionals.

To meet growing consumer demand, we are focusing our annual capital expenditure on key sites in Victoria and Tasmania – most notably an expansion of Fonterra Australia's flagship Stanhope cheese facility in northern Victoria, almost doubling the size of the cheese plant.

Long term, we expect competition for milk volumes to increase. In preparation, our Australian business is working to improve our connection to local suppliers, beyond just the local milk price. This includes the recent launch of a tailored version of our Farm Source™ services and rewards programme, and continued discussions on the potential for developing an ownership model in Australia.

OUTLOOK

We expect our earnings to be weighted toward the second half of the year and that is reflected in our forecast earnings per share, which is in our target dividend range of 25 to 35 cents, giving a total forecast available for payout to our farmers of \$6.80 to \$6.90.

Despite more favourable weather conditions recently, we still expect our New Zealand milk volumes to be down for the year and will be managing our inventory and product mix carefully for the remainder of the season to ensure we maximise the overall value of our farmers' milk.

A strong commitment to our strategy of shifting more volume into higher value products at velocity is critical to the business achieving its forecast. We will continue to put as much milk as possible into higher value products, particularly into our Advanced Ingredients business, and Consumer and Foodservice business where we are still targeting an additional 400 million LME of volume this year.

Our management team is working hard to recover the impact of the Danone and Beingmate events, the latter being the primary focus for the senior management team and the Board.

Our Co-operative remains focused on providing high quality dairy nutrition to customers around the world and delivering sustainable value for our farmers – that's a sustainable Farmgate Milk Price, dividend, and return on their investment in the Co-op.

John Wilson
Chairman

Theo Spierings
Chief Executive Officer

A STRONG CO-OP DOING WHAT'S RIGHT

With weather extremes affecting production this season, it was as important as ever that we used the collective strength of our Co-operative to support our farmers, giving them services and advice.

\$17.8M

**FARM SOURCE™
REWARDS**

In the last financial year, our farmers earned \$17.8 million worth of Farm Source™ Rewards Dollars.



WE DEVELOPED NEW FLEXIBLE FINANCIAL TOOLS, INTRODUCED MY CONNECT WEBINARS TO UPDATE FARMERS ON IMPORTANT ISSUES, MAINTAINED OUR COMPETITIVE FARM SOURCE™ OFFERING FOR FARM SUPPLIES AND LOOKED AT NEW WAYS FOR OUR CO-OPERATIVE TO BUILD DEEPER CONNECTIONS WITH THE FARMERS WHO SUPPLY US IN AUSTRALIA AND LATIN AMERICA.

With the environment high on the national agenda, we demonstrated the significant progress our farmers and their Co-operative have already made, as well as making further sustainability commitments relating to water quality, emissions and on-farm best practice. We published our first stand-alone sustainability report, an independently audited report looking at our commitments and progress right across the global supply chain.

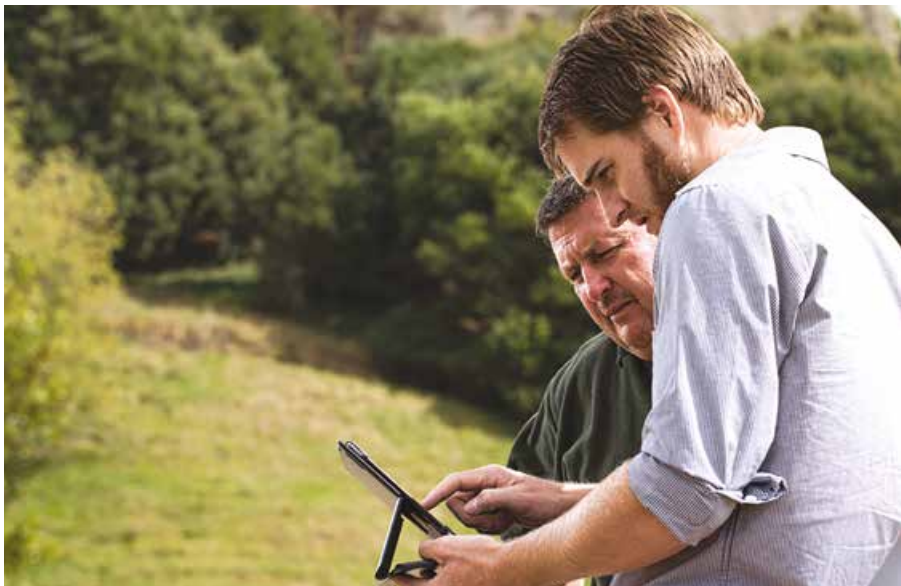
FARMING WITH FARM SOURCE™

Across a challenging half year for conditions on-farm, we have supported farmers by using our collective buying power for farm supplies through our Farm Source™ stores and by offering competitive terms.

We know that if farmers buy their supplies exclusively from us, we can make a real difference, with the average sized Fonterra farm saving approximately 10 cents per kgMS. As well as lowering the cost of farm supplies, we continue to reward farmers with Farm Source™ Rewards Dollars. In the year to date, 8,200 farmers have collectively earned almost seven million Farm Source™ Rewards Dollars, bringing the total number of Farm Source™ Rewards Dollars earned by farmers since inception to more than 40 million.

**TIAKI
SUSTAINABLE
DAIRYING**

This programme supports farmers in staying ahead of regulatory requirements and satisfying evolving consumer and market expectations.



**FLEXIBLE TOOLS TO HELP
FARMERS SHARE UP**

In the last financial year, our shareholders earned \$17.8 million worth of Farm Source™ Rewards Dollars. As well as redeeming these in store, farmers will have the option of using them to help meet their share requirements. The *Farm Source™ Rewards Dollars for Shares* scheme will allow farmers to use their Rewards Dollars to purchase shares during the offer window, before the share compliance date of December 1 each year.

Also new is the *Contract Fee for Units* programme where we can now redirect the contract fee from *Share-Up Over Time* contracts into a trust that will purchase units on the farmer's behalf. These units can then be used at a later date to acquire shares.

We have further simplified sharing up with the introduction of a *Strike Price Contract*. This is designed to help farmers who want to grow their businesses by providing greater flexibility for sharing up over time.

Under this programme, farmers buy a minimum shareholding in the first year - equal to 20 per cent of their production quantity. In subsequent years they will be required to buy additional shares only when the Farmgate Milk Price goes over the published Strike Price. This is set at \$5.25 for the 2018/19 season.

**MY CONNECT – BUILDING
KNOWLEDGE AND CONNECTION
TO OUR CO-OP**

The Shareholders' Council, supported by our Farm Source team, has led My Connect, a replacement for the Fonterra Networkers programme, designed to help farmers better connect with one another, share knowledge, and engage more with experts from within our business.

Our new My Connect Conference in May will be an opportunity for all Fonterra farmers to come together, share what's happening on-farm, hear updates and get insights from our strategic markets, and set the My Connect agenda for the coming season.

We've put farmers in charge of My Connect webinar content, asking them to vote for the topics which most interest them, such as understanding the Farmgate Milk Price or the strategy behind our global milk pools.

**FARM SOURCE™ EXPANDS
INTO AUSTRALIA**

In February, Farm Source™ was launched in Australia where Fonterra, as the country's leading processor, now collects two billion litres of milk from 1,300 farmers in Victoria and Tasmania.

The Australian offering has been tailored to local farmers who supply Fonterra through supply arrangements. It combines a range of farm services which have already been available to them with better, faster and easier-to-use tools and services that will support our suppliers' growth and profitability.

A STRONG CO-OP DOING WHAT'S RIGHT



NUTRIENT MANAGEMENT

95 per cent of supplying farms in New Zealand are participating in nutrient management reporting and benchmarking.

This initiative is part of a wider programme underway in Australia to secure our share of supply as our Co-operative works to expand our near-full production capacity across our key Australian sites. We are in the process of adding 500 million litres of processing capacity to meet growing demand for our Ingredients, Consumer and Foodservice products – particularly cheese from our Stanhope site.

We know our co-operative principles appeal to Australian farmers, along with the sense of certainty an ownership model provides. Therefore we are looking at how that might be achieved in Australia to provide a connection deeper than just the milk price.

We have provided similar opportunities in Latin America where farmer suppliers were offered the opportunity to acquire shares in Prolesur, our Chilean Ingredients business that supplies our Soprole™ operations with milk. These initiatives can provide closer connection with overseas farmers, without affecting our New Zealand shareholders' ownership and control of their Co-operative.

OPENING OUR GATES TO ALL OF NEW ZEALAND

The Co-operative's commitments and achievements in sustainability were acknowledged this year with the release of a sustainability report compiled using the internationally recognised Global Reporting Initiative (GRI) framework and independently assured.

The report gives an objective view of Fonterra's environmental footprint and our contribution to the United Nations' Sustainability Development Goals.

Highlights in the report include:

- New Zealand has among the lowest greenhouse gas emissions per litre of milk collected in the world (0.85 per kgCO₂/kgFPCM).
- More than 140,000 Kiwi kids get a free 200ml serving of milk each school day from our Fonterra Milk for Schools programme, which celebrates its fifth anniversary this year.
- New specialised milk product was launched in Malaysia this year to help combat high rates of cholesterol and diabetes in this market.
- 95 per cent of supplying farms in NZ are participating in nutrient management reporting and benchmarking.
- 98.4 per cent of waterways on supplying farms in NZ are fenced to keep cows out of waterways and collection of milk was suspended at 78 farms in the past season due to non-completion of fencing.

In addition to reporting on our progress, 40 of our farmers invited Kiwis to see it for themselves in December. The Open Gates initiative received positive feedback from people who appreciated the chance to see on-farm initiatives like fencing of waterways and riparian planting.



OPEN GATES

We opened our gates to the New Zealand public to see for themselves the good work our farmers are doing.

COMMITTING TO WATER QUALITY

In November we announced six commitments to help improve water quality in farming regions. Each is underpinned by a set of clear actions.

These include supporting regional councils to set environmental limits for water use, investing \$250 million to drive a 20 per cent reduction in water use across our 26 manufacturing sites and almost doubling the Co-operative's network of Sustainable Dairying Advisors.

These commitments complement existing programmes including our Living Water partnership with the Department of Conservation, work with local communities and our promise to help restore 50 key freshwater catchments.

The commitments announced in November are:

1. Farm within regional environmental limits.
2. Encourage strong environmental farming practices.
3. Reduce water use and improve wastewater quality at manufacturing plants.
4. Build partnerships to improve waterway health.
5. Invest in science and innovation to find new solutions.
6. Make the products people value most.

CREATING SUSTAINABLE VALUE FOR ALL OF OUR FARMERS

Environmental sustainability is critical to our future. It's important to customers and they look to us to demonstrate it on-farm.

We have a good story to tell, firstly because our Co-operative's farmers recognised the need for change back in 2003 with initiatives such as the Clean Streams Accord, and secondly, because farmers have all invested time, money and passion into making far-reaching changes to their farm management systems.

Farmers have made these improvements because it's the right thing to do for the communities in which we live and operate. There's an added benefit in that customers globally are increasingly seeking out nutrition that can be verified as produced using ethical and sustainable practices.

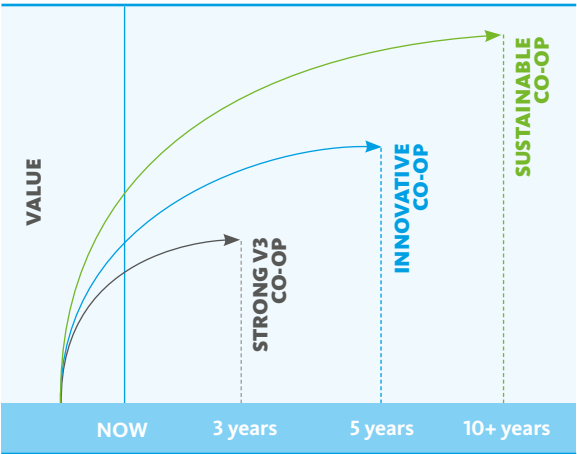
Fonterra's global Trusted Goodness™ programme earns our farmers greater value due to the grass-fed, Non-GMO and animal welfare standards behind their milk. The programme, which is represented by a global quality seal, is being progressively rolled out across parts of our NZMP brand and in the first half of the financial year has already delivered incremental price achievement of \$6.9 million over and above the equivalent standard products.

OUR POTENTIAL

We have a goal to be processing 30 billion litres of milk a year by 2025 across five to six countries. The growth required to achieve this goal is ambitious but our team is united in how we’re making it happen.



BUILDING THE FOUNDATIONS FOR OUR FUTURE SUCCESS.



STRONG V3 CO-OP

Demand-led optimisation of New Zealand milk, supported by milk pools.

INNOVATIVE CO-OP

Investment in technology and people for the future.

SUSTAINABLE CO-OP

Creation of sustainable value for all stakeholders.

It requires us to keep one eye on today and the other on the future, and sees us focusing on three horizons – creating a Strong V3 Co-op which will set the foundations for the future, an Innovative Co-op which will enable us to lead the future and a Sustainable Co-op which will ensure the future.

We’re working on all three, creating sustainable value for our shareholders – that’s a sustainable Farmgate Milk Price, dividend and investment in the Co-op. At the same time, we will be making a difference in the lives of two billion people and helping feed the world’s growing population, which by 2050 is expected to drive a 50 per cent increase in the demand for food.

A STRONG V3 CO-OP

A Strong V3 (Volume, Value, Velocity) Co-op is about converting more milk into higher returning products at speed.

At the heart of this strategy we continue to put more milk into the products that create the most value – that’s Consumer and Foodservice products and Advanced Ingredients like NZMP’s pharmaceutical lactose used in asthma inhalers .

We have been adding about 400 million additional LME to our Consumer and Foodservice business each year and we expect this to continue.

\$21.75_M

DOUBLE
11 SALES

Anchor™, Anlene™ and Annum™ sales during the Double 11 sales period increased by about 65 per cent compared to last year.



The Ingredients engine

Our Ingredients business represents two-thirds of Fonterra's earnings. Customers want to buy high volume, quality ingredients from a trusted source. We create value in these ingredients through our scale, having a lean supply chain that's focused on our customers' needs and prioritising demand for higher value ingredients.

Our manufacturing sites can process multiple products, giving us flexibility to respond to market changes and ensuring we are getting the most out of every drop of milk. That's why we have invested in sites like Clandeboye, where we can produce mozzarella, whey protein concentrate and edible lactose.

We have also taken our dairy manufacturing, food quality and sales expertise and applied it around the world. This means we can supplement our New Zealand milk source and create more opportunities to produce higher value products to meet growing global demand.

A good example of this from the first half of this year is our work with US whey protein concentrate and lactose manufacturer Columbia River Technologies – a joint venture between dairy co-op Tillamook and Threemile Canyon Farms. Each party brings something different to the table. Threemile Canyon Farms supply the milk, Tillamook makes the cheese, and using our intellectual property, we commercialise the whey and lactose by-products of the cheese making process. Whey protein is a key ingredient in infant formula and sports nutrition products, and demand is growing for these products, especially in the US, European and Asian markets.

The launch of our dedicated medical nutrition division this year further strengthens our focus on selling advanced ingredient solutions to help people suffering from malnutrition and other diseases, as well as help people age in good health. The global medical nutrition industry is valued at \$17.5 billion today and is expected to grow to almost \$24 billion by 2020.

Growing our Consumer and Foodservice business

Growth in demand from Consumer and Foodservice markets is also set to be significant. Key trends driving this are population growth, urbanisation and a growing middle class with an increasing enthusiasm for Western-style foods and greater awareness around healthy diets and lifestyles.

Our global brands – Anchor™, Anlene™ and Annum™ – and regional brands – like Western Star™ and Soprole™ – are trusted and well positioned to meet the needs of customers. Our strong sales over the Chinese Double 11 sales period, especially for our Anchor™ UHT milk which was the most popular product in the imported UHT milk category, are evidence of this.

We have expanded the Anlene™ proposition to make it relevant to the lives of more adults in Asia and are aiming for 18 per cent growth this year. We are building on Anlene's scientific roots in helping bone health and preventing osteoporosis and tapping into a global trend for healthy ageing – a market segment with an estimated value of \$8.5 billion per annum by 2026.

OUR
POTENTIAL



Anchor Food Professionals™ is in high demand from chefs across the globe. Our targeted product range and innovative chef-led strategy gives us a competitive edge in the Asian Bakery, Italian Kitchen and Quick Serve Restaurants channels. In December Anchor Food Professionals™ became New Zealand's sixth biggest export business, having generated \$2 billion in annual revenue.

The growth in tea and coffee consumption creates a new opportunity to further grow our Foodservice business. People are moving away from the traditional straight brew to more indulgent drinks, which increasingly means more dairy. That's why we are now carving out a new channel called Beverage House and selling cream, cream cheese and milk to the likes of Starbucks.

INNOVATIVE CO-OP

As we move further through the Innovative Co-op horizon, we prepare ourselves to lead in the face of fast-moving trends, sudden changes in customer behaviour and unprecedented changes in technology.

It requires us to innovate throughout our value chain and use technology to create more value. We've already started, stimulating teams to think differently, be fast and agile, and identify and deliver technology gains.

Disrupt

Our Disrupt programme encourages and fosters diverse ideas for new business models from our people around the world. In just two years, the initiative has involved some 1,300 individuals, spanning at least eight languages,

27 nationalities, and included thinking from people aged between 21 and 60.

We have already implemented four Disrupt ideas. Some are highly digital – such as using technology to extend the reach of our Foodservice business to cities where we don't have a sales team on the ground – and some require us to just think differently about old challenges. For example, our 'Reach the Unreached' venture in Sri Lanka is an innovative new business model that gets affordable dairy nutrition to rural people who wouldn't normally have access to it.

Velocity and Velocity^{NXT}

Velocity is our way of working. It's both a mindset of accountability and action, and a set of tools for uncovering and delivering significant value in our business. Over the last two-and-a-half years more than 4,260 initiatives have been completed by employees and delivered improvements in working capital, earnings and Farmgate Milk Price. Of these, 675 have been completed this year.

Many of these initiatives are incremental improvements but we are also challenging ourselves to be bold and harness emerging technologies that will streamline our business, improve process and capture value in new ways.

Velocity^{NXT} supports our people to implement both sustainable and disruptive initiatives that are more complex to develop as they typically require new technology, tools, capabilities and greater cross-functional collaboration – such as advanced analytics, machine learning, the Internet of Things, and robotics and software automation.



SUSTAINABLE CO-OP

Strong healthy local environments and communities are the foundation for sustainable and profitable dairy farming. That's why the Sustainable Co-op horizon is important. It requires us to look at how we create value for our farmers, customers and local communities. We are looking at the future challenges facing global food producers and making sure we are considering the long-term implications of the actions and plans today.

We have organised our Sustainable Co-op priorities into three main areas that will make the biggest difference to people's lives:

- **Nutrition:** improving health and wellbeing through products and services we deliver.
- **Environment:** achieving a healthy environment for farming and society.
- **Community:** delivering prosperity for our farmers and wider communities.

In December 2017 we published our first Sustainability Report. It highlights our commitment to an open discussion on how we're taking our responsibilities seriously and where we are making real progress.

Making changes today that will ensure the future

We have created new global Food and Nutrition Guidelines, endorsed by the New Zealand Nutrition Foundation. The guidelines help ensure we're continuously moving our product portfolio towards reduced use of added sugars, salt and other additives.

Our farmers continue to make a significant contribution to improving water quality in New Zealand's waterways. We're investing to improve our waste water treatment at sites like Brightwater and we've improved our storm water management systems at our sites in Takaka and Tirau in the first half of the year.

Our energy efficiency gains from last season meant we saved enough energy to power all the households in Hamilton city for nearly four years, and we're continuing to focus on reducing energy use across our sites.

We have made good progress on our roadmap with the Ministry for the Environment for a low emission future. In particular, we have completed a feasibility study to assess how we could transition to renewable energy sources and we continue to look for ways to demonstrate what's possible. This year we approved investment to convert the boiler at our Brightwater site to co-fire with wood biomass. This will reduce carbon emissions at the site by 25 per cent.

Details of how we are delivering our third priority are covered in depth in this report's 'Our Co-op' and 'Our Performance' sections.

GROUP OVERVIEW

We delivered strong Ingredients performance and continued to make progress in moving milk up the value chain, with volume growth across a number of Consumer and Foodservice markets.

\$9.8B

SALES REVENUE

Up six per cent compared with the same period last year.



HIGHLIGHTS

- Operating performance in line with expectations, normalised EBIT of \$458 million.
- Results impacted by Danone arbitration decision and Beingmate impairment.
- Volume in LME down 11 per cent, due to record low opening inventory and reduced milk collection.
- A strong Ingredients performance, generating normalised EBIT of \$558 million, up nine per cent.
- In our Consumer and Foodservice businesses we increased prices but not enough to recover the higher input costs, resulting in a 38% decline in normalised EBIT.
- Higher gearing mainly due to lower earnings, including abnormal items.

Sales revenue for the six months to 31 January 2018 rose six per cent to \$9.8 billion, reflecting improved global prices for dairy.

USEFUL FACT

Starbucks in Mainland China uses Fonterra milk from New Zealand and China. By 2020, we have plans to be a major supplier to all Starbucks stores in China. Milk products will be supplied from our China Farms and New Zealand.



Revenue increased despite a decline in total sales volume of 1.3 billion LME, as we started the year with record low opening inventory followed by a second year of lower milk collections. Milk collections this season were heavily impacted by the difficult weather conditions experienced across New Zealand. As a result, sales volumes in our Ingredients business were down 11 per cent compared to the same time last year. In Consumer and Foodservice, we moved 2.7 billion LME into higher value products over the six months ended 31 January 2018. This included volume growth in Greater China, Latin America and Asia, but was offset by declines in Oceania as our New Zealand business exited some private label contracts and experienced operational challenges at our new distribution centre.

CONSUMER AND FOODSERVICE

Our new Foodservice channel, Beverage House, will sell cream, cream cheese and milk to the likes of Starbucks.



NZD MILLION	SIX MONTHS ENDED 31 JANUARY 2018	SIX MONTHS ENDED 31 JANUARY 2017	CHANGE
Volume (LME, billion)	10.5	11.7	(11%)
Volume ('000 MT)	2,003	2,131 ¹	(6%)
Sales revenue	9,839	9,241	6%
Gross margin	1,662	1,761	(6%)
Gross margin percentage	17%	19%	
Reported operating expenses	(1,864)	(1,232)	51%
Normalised operating expenses	(1,263)	(1,232)	3%
Reported EBIT	(176)	644	(127%)
Normalised EBIT	458	607	(25%)
Net finance costs	(201)	(157)	28%
Tax credit/(expense)	29	(69)	(142%)
Net (loss)/profit after tax	(348)	418	(183%)
Earnings per share (cents)	(22)	26	(185%)
Dividend per share (cents)	10	20	(50%)
Gearing ratio ²	51.6%	46.6%	
Free cash flow	(690)	(417)	(65%)
Capital expenditure	346	244	42%

1. China Farms volumes for the 2017 half 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.
2. Gearing ratio is economic net interest bearing debt divided by economic net interest bearing debt, plus equity, excluding hedge reserves.

GROUP OVERVIEW

\$458M

NORMALISED EBIT

Operating performance in line with expectations.



GROWING DEMAND

In the USA, more than 50 per cent of all food and beverage spend is now out of home, and the China foodservice dairy market has grown by 30 per cent between 2013 and 2017.

Group normalised EBIT of \$458 million was down 25 per cent compared to the same period last year. Our Ingredients business delivered a strong result, with normalised EBIT of \$558 million, up nine per cent on last year, driven by a solid performance from New Zealand and an improved performance in Australia. We made good progress on our five "must win battles" in Consumer and Foodservice. However, these could not fully recover the impact of higher commodity prices which compressed margins. As a result, normalised EBIT for Consumer and Foodservice declined 38 per cent to \$193 million.

Growth in Greater China was driven by a strong performance from our Consumer business, which delivered double-digit volume growth for the first six months of the year. We continued to make progress in our Foodservice business. However, margins have declined compared to the same period last year when margins were higher due to the lower dairy commodity price environment. The benefits of our turnaround in the Australia Consumer and Foodservice business have continued to improve the Oceania result. However, higher dairy commodity prices and operational challenges in New Zealand have impacted overall earnings. Our Soprole™ business in Latin America continues to perform well. The decline in the Brazilian economy has been challenging. However, we have made further market share gains in the chilled dairy category this year.

Our China Farms' result has improved compared to last year due to the efficiencies generated from the farms being fully stocked with livestock and further on-farm cost control. We are well positioned to benefit from the shift in demand from ambient products towards fresh milk in the Greater China market.

USEFUL FACT

This year we celebrated the tenth birthday of our Hangu Farm, east of Beijing, which was our first farm in Greater China.



Normalised operating costs were up three per cent for the six months to 31 January 2018, after two years of declines. The increased spend this half has been targeted at new product innovation, digital platforms and technology opportunities. We will continue to focus our spend in these key areas where we see long-term benefits to our business.

Our reported EBIT has decreased 127 per cent to a loss of \$176 million for the six months to 31 January 2018 reflecting the \$196 million relating to the Danone arbitration decision, and the impairment and share of operating losses from our investment in Beingmate of \$433 million.



STRONG CO-OPERATIVE

Ongoing financial discipline has enabled the Co-operative to maintain a strong balance sheet and absorb the impact of abnormal items incurred over this period. This included the recall costs awarded to Danone and the impact of the impairment of our investment in Beingmate.

Economic net interest-bearing debt and gearing are both typically higher for the Co-operative at the end of the first six months of the year, reflecting the seasonal profile of our business. As at 31 January 2018, economic net interest-bearing debt was \$7.1 billion and better than expected due to higher cash collections following strong Ingredients sales in the second quarter. Relative to the previous comparable period, economic net interest-bearing debt was \$945 million higher as additional funding was required over the period. This is due to lower earnings, including the Danone arbitration decision, the timing of capital expenditure, the impact of the translation of overseas debt due to a lower New Zealand Dollar, and the final dividend being part-paid early in the prior year. Consistent with the higher seasonal debt level and the impact of the Beingmate impairment on retained earnings, the gearing ratio at half year has increased to 51.6 per cent. We continue to be committed to our target end of year gearing of 40-45 per cent.

Efficient working capital management continues to be a key focus of our financial discipline. The investment required in working capital has increased due to the higher milk price, and increased inventory volumes, including an increased portion of higher value products. Increased inventory volumes this period reflect the record low closing volumes in the prior period in our Ingredients business returning to more normal levels, and growth in milk collection in our Australian business.

During the period, expenditure on capital investments was in line with expectations but higher than the previous comparable period due to timing differences. Spend is also typically proportionally lower in the first six months of the year as scheduled maintenance occurs at our sites during winter when volumes are lower.

The interim dividend of 10 cents per share reflects the lower earnings this year as well as our commitment to financial discipline and maintaining a strong balance sheet. This is in line with Fonterra's dividend policy to pay out 65-75 per cent of adjusted net profit after tax over time.

INGREDIENTS

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

\$558M

NORMALISED EBIT

Ingredients
Normalised EBIT was up nine percent.



EXPORT

During peak season, one container of product is loaded every three minutes for export.

HIGHLIGHTS

- Normalised EBIT of \$558 million, up nine per cent.
- Lower sales volumes due to record low opening inventories and a two percent decrease in New Zealand milk collections for the season to date.
- Sales revenue increased nine per cent due to higher dairy commodity prices.
- Australian Ingredients gross margin up \$23 million, or 86 per cent.

VOLUME

Fonterra's milk collection across New Zealand was down two per cent to 1,036 million kgMS for the 2017/18 season to 31 January 2018. Lower collections were primarily due to the difficult weather conditions experienced this season, with a very wet spring followed by a hot, dry summer, which affected soil and pasture quality across the country. Although the rain in early January helped in some regions, collections for the season to date have declined, with the North Island down three per cent, and the South Island flat compared to last season.

In Australia, milk collection for the 2017/18 season to 31 January 2018 was 100 million kgMS, 27 per cent up on the same period last season. This volume includes milk collected directly and through third parties. The Australian business has benefited from an improvement in product mix and has attracted new suppliers to Fonterra over the course of the year. The increase in volumes collected represents a significant gain in market share of around four per cent for Fonterra.

Total sales volumes in Ingredients were 9.8 billion LME, a decrease of 11 per cent compared to the same period last year. This decline reflects our record low opening inventory volumes and the unusual profile of New Zealand milk collection this season. Opening inventory at the start of the period was approximately 63,000 metric tonnes lower than the previous period, a decline of 15 per cent, as we continued our efforts to drive lower inventory levels. Our total Ingredients' sales include 132 million LME from our China Farms as we continue to progress our strategy of a vertically integrated milk pool in China.

11% ↓

LOWER VOLUMES

Sales volumes for Ingredients were 9.8B LME, down from 11B LME for the same period last year.



INHALABLE LACTOSE

The pharmaceutical lactose made at Kapuni is used in asthma inhalers all around the world.

NZD MILLION	SIX MONTHS ENDED 31 JANUARY 2018	SIX MONTHS ENDED 31 JANUARY 2017	CHANGE
Volume (LME, billion)	9.8	11.0	(11%)
Volume ('000 MT)	1,441	1,543 ¹	(7%)
Sales revenue	7,906	7,228	9%
Total gross margin	874	801	9%
– New Zealand product mix	734	644	14%
New Zealand Reference products	372	246	51%
New Zealand Non-reference products	362	398	(9%)
– Australia Ingredients	50	27	86%
– China raw milk ²	(9)	(9)	-
– Other gross margin ³	99	139	(29%)
Normalised EBIT ⁴	558	510	9%
Gross margin (\$ per MT)			
– Reference products (\$ per MT)	413	253	63%
– Non-reference products (\$ per MT)	1,309	1,178	11%

¹ China Farms volumes for the 2017 half 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.

² China raw milk gross margin represents the net benefit/(loss) from the external sale of milk produced by China Farms and sold to the Ingredients business in China at an internal raw milk price.

³ Other gross margin for the six months ended 31 January 2017 has been restated to reflect the China raw milk gross margin that was presented for the first time in the 2017 annual review.

⁴ Normalised EBIT for Ingredients excludes unallocated costs.

INGREDIENTS

NEW ZEALAND INGREDIENTS – REVENUE AND VOLUME ¹	SIX MONTHS ENDED 31 JANUARY 2018	SIX MONTHS ENDED 31 JANUARY 2017	CHANGE
Production Volume ('000 MT)			
Reference products	1,266	1,292	(2%)
Non-reference products	483	457	6%
Sales Volume ('000 MT)			
Reference products	900	973	(8%)
Non-reference products	277	338	(18%)
Revenue Per MT (NZD)			
Reference products	4,783	3,873	23%
Non-reference products	5,726	5,201	10%

¹ Figures exclude bulk liquid milk. The bulk liquid milk volume for the six months ended 31 January 2018 was 34,000 MT (six months ended 31 January 2017 was 37,000 MT).

VALUE

The Ingredients business delivered a strong result, particularly given the significant reduction in opening inventories and the variability in milk collections this season. Revenue was up \$678 million, or nine per cent, and normalised EBIT was \$558 million, also an increase of nine per cent. The increase in normalised EBIT is reflective of higher margins, improvements in our overall product mix and stronger operational performance from our business in Australia.

USEFUL FACT

NZMP SureStart™ Lipid 100, our breakthrough milk lipid ingredient, was selected as a finalist in the 'Ingredient of the Year – Infant Nutrition' at the NutraIngredients Awards 2017.



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

Revenue for both reference and non-reference products has increased, up 23 per cent and 10 per cent respectively even with the lower volumes due to higher prices for the period to 31 January 2018.

The overall New Zealand Ingredients' gross margin, including both reference and non-reference products, increased by 14 per cent to \$734 million. Gross margins for reference products increased 51 per cent or \$126 million for the six-month period. Last year, with rapidly increasing dairy commodity prices, we made lower margins on these products due to the natural pricing lag inherent in our sales contracts. This year as prices stabilised, albeit at a higher level, margins for our reference product portfolio improved. For non-reference products, gross margin was \$362 million, a decline of nine per cent compared to the same period last year, largely driven by lower volumes.

Product stream returns result from the relative difference between reference product and non-reference product prices and costs. For the six months to 31 January 2018, non-reference product stream returns were \$90 million, \$50 million ahead of the comparable period last year. These additional stream returns were predominantly due to the improved margins for non-reference products this period.

\$734_M

NEW ZEALAND INGREDIENTS GROSS MARGIN

The overall New Zealand Ingredients gross margin increased by 14 per cent to \$734 million.

Our Australian Ingredients business delivered another stronger performance for the six months to 31 January 2018, compared to the same period last year with a gross margin of \$50 million, up \$23 million or 86 per cent. This was driven by strong demand for butter and cream and greater efficiencies at our factories.

Our Ingredients' gross margin included a \$9 million loss for the six-month period, representing the difference between the domestic milk price and the internal raw milk price paid to China Farms.

USEFUL FACT

In Australia we produced 27 per cent more milk in the first six months compared to the same period last year.



Our New Zealand operations faced some challenges over the course of the first half, as difficult weather conditions impacted the country. Previous investments in capacity and lower milk collections this season have ensured there were no peak costs for the six months to 31 January 2018.

NEW STANHOPE PLANT

The expansion of Stanhope in Australia will almost double the size of our new cheese plant.



Our Global Operations team tightly managed capital expenditure through the year by focusing on value added products, efficiency gains and sustainability improvements. This year we invested in our mozzarella plant at Clandeboye and in a new cream cheese plant at our site in Darfield. In addition to this, our Ingredients business in Australia will benefit from further investments at key sites in Victoria and Tasmania to increase capacity and meet growing demand for our products, particularly mozzarella. The majority of this spend will be at our Stanhope site, where we are almost doubling the size of our plant. This will increase cheese production by a further 35,000 metric tonnes for a range of cheeses, including cheddar, mozzarella and parmesan.

CONSUMER AND FOODSERVICE

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

\$3,473_M

SALES REVENUE

Consumer and Foodservice sales revenue increased seven per cent.

HIGHLIGHTS

- › Sales revenue up seven per cent.
- › Increased volumes in Greater China, Latin America and Asia.
- › We increased prices but these were not sufficient to recover the impact of higher commodity prices, resulting in a decrease of 38 per cent in normalised EBIT.
- › Strong Consumer growth in Greater China.
- › Consistent earnings in Greater China and Latin America in a higher dairy commodity price environment.

VOLUME

We achieved volume growth in Greater China, Asia and Latin America, but this was offset by the decline in volumes in Oceania. As a result, overall volumes in our Consumer and Foodservice business declined two per cent. Given the significant increase in prices for butter, which has a high LME factor, our product mix shifted away from butter, towards UHT cream, which has a relatively lower LME factor. As a result, total LMEs in Foodservice were flat compared to the same period last year.

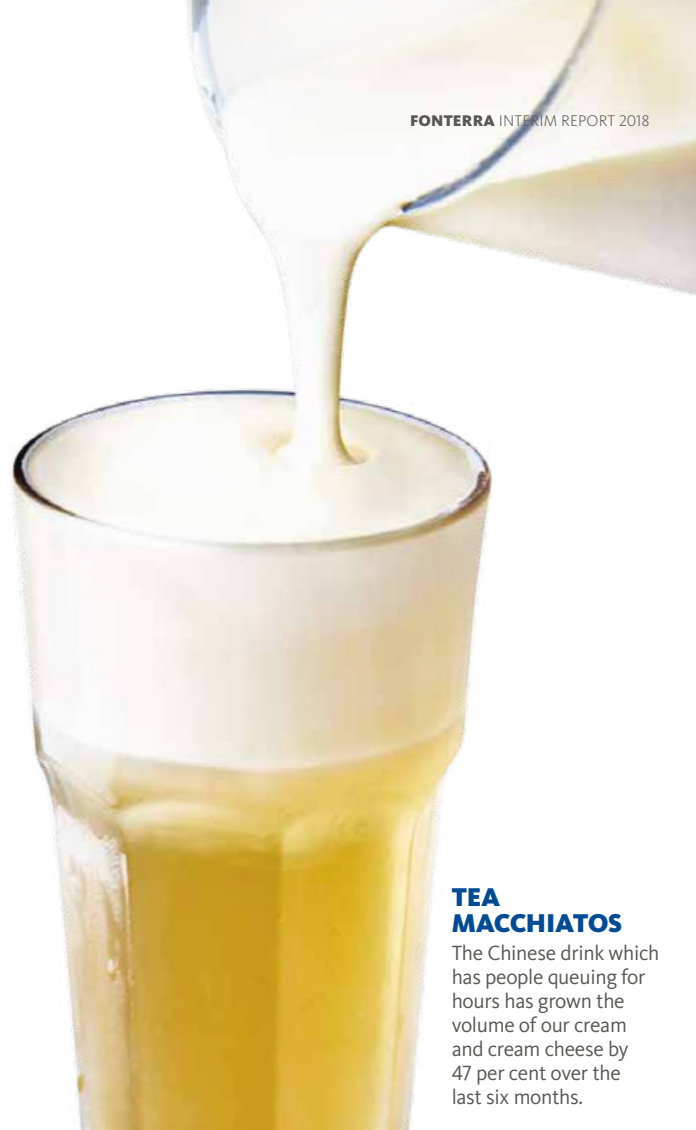
- **Greater China:** additional 16 million LME, largely due to strong growth in our Consumer business, as well as further expansion in our Foodservice business in Mainland China.
- **Oceania:** good demand in Australia, however overall volumes down due to higher fat prices in our butter portfolio, operational challenges in New Zealand and our exit from parts of our private label portfolio.
- **Asia:** growth of two per cent due to strong demand in Malaysia, Thailand and Vietnam.
- **Latin America:** three per cent volume growth, reflecting growth in Soprole™ but partially offset by challenging economic environments in Brazil and Venezuela.

VALUE

Our Consumer and Foodservice business delivered revenue of \$3.5 billion for the six months to 31 January 2018, an increase of seven per cent. Our normalised EBIT of \$193 million decreased 38 per cent, as the increased prices were not sufficient to recover the impact of higher commodity prices, which compressed margins.

WESTERN STAR CREAM

Our Cobden site in Australia has a state of the art bottling facility where we produce Western Star™ cream.



TEA MACCHIATOS

The Chinese drink which has people queuing for hours has grown the volume of our cream and cream cheese by 47 per cent over the last six months.

NZD MILLION	SIX MONTHS ENDED 31 JANUARY 2018	SIX MONTHS ENDED 31 JANUARY 2017	CHANGE
Volume (LME, billion)	2.7	2.7	(2%)
Consumer	1.6	1.6	(3%)
Foodservice	1.1	1.1	0%
Volume ('000 MT)	893	908	(2%)
Sales revenue	3,473	3,239	7%
Gross margin	821	963	(15%)
Gross margin (%)	24%	30%	
Consumer	27%	31%	
Foodservice	17%	27%	
Normalised EBIT	193	313	(38%)

NORMALISED EBIT: KEY PERFORMANCE DRIVERS NZD MILLION	SIX MONTHS ENDED 31 JANUARY 2018	SIX MONTHS ENDED 31 JANUARY 2017
Normalised EBIT prior year	313	241
Volume	(20)	102
Price	301	(38)
Cost of goods sold	(420)	21
Operating expenses	4	32
Other	15	(45)
Normalised EBIT	193	313

CONSUMER AND FOODSERVICE

CONSUMER AND FOODSERVICE PERFORMANCE

SIX MONTHS ENDED	LME (BILLION)			NORMALISED EBIT (\$M)		
	31 JANUARY 2018	31 JANUARY 2017	CHANGE	31 JANUARY 2018	31 JANUARY 2017	CHANGE
Consumer and Foodservice	2.7	2.7	(2%)	193	313	(38%)
Greater China	0.6	0.6	3%	92	96	(4%)
Latin America	0.4	0.4	3%	30	35	(14%)
Asia	0.9	0.9	2%	56	124	(55%)
Oceania	0.8	0.9	(10%)	15	58	(74%)

The key performance drivers table shows increased prices contributed an additional \$301 million to earnings for the six months to 31 January 2018. Although we had improvements in performance at our key sites, higher input prices resulted in an increase in cost of goods sold of \$420 million. This year the average commodity prices for our key Foodservice products, such as butter and cream, increased by 80 per cent and 18 per cent respectively.

Our strategy for Consumer and Foodservice is focussed on five 'must win battles' which will help us drive a greater value proposition for the business. These are innovation, strategic pricing, route to market, cost leadership and digital. We track these initiatives through our Velocity programme which enables us to measure performance and act in an agile manner. For the six months to 31 January 2018 we delivered around \$90 million from our key 'must win battle' initiatives, which partially offset the increase in cost of goods sold this year.

For the six months to 31 January 2018 our Greater China and Latin American businesses produced solid earnings in a higher dairy commodity price environment:

- **Greater China:** largest contributor to earnings with normalised EBIT of \$92 million, but slightly down on last year due to increased input costs.
- **Latin America:** consistent performance by Soprole™ earnings impacted by challenging markets in Brazil and Venezuela.
- **Asia:** normalised EBIT of \$56 million, a 55 per cent decline, driven by the lag in pricing on our periodic contracts in a rising commodity price environment.
- **Oceania:** strong performance in Australia, more than offset by margin compression and operational challenges in New Zealand.

REGIONAL UPDATE

Greater China

Our Greater China business continues to grow volume with an additional 16 million LME, as we progress our strategy of moving more volume into higher value products. On a metric tonne basis volume in Greater China has increased 15 per cent. However, the shift in our product mix away from butter, with its relatively higher LME factor, towards UHT cream has impacted growth on an LME basis. We have made progress in driving growth in our online presence, with sales via TMall and JD.com growing 81 per cent and 73 per cent respectively.

Normalised EBIT has declined four per cent to \$92 million in an environment where average input costs have increased by more than 55 per cent. Our Consumer business delivered double-digit volume growth along with a positive EBIT contribution, E-Commerce channel growth, price structure optimisation and portfolio expansion. The Foodservice business continued to perform well, reflecting the success of our Anchor Food Professional™ model, particularly in mainland China, where sales of our UHT whipping cream have performed strongly, up 62 per cent. Foodservice margins have declined compared to the same period last year when margins were higher due to the lower dairy commodity price environment, particularly for butter.

The Greater China result has been normalised to exclude the \$433 million impact of losses relating to and the impairment on our 18.8 per cent investment in Beimgate.



Latin America

Sales volumes in Latin America were up three per cent. The ongoing solid performance of Soprole™ in Chile was partially offset by challenging conditions in Venezuela and Brazil. This resulted in normalised EBIT being down \$5 million to \$30 million for the period.

Our Soprole™ business continues to perform well with strong demand in the mature cheese and butter categories. This resulted in increased volumes and improved margins despite the higher input costs this year. We achieved strong growth in our higher value yoghurt and dairy desserts categories.

The economy in Brazil continues to provide challenges, with further retraction seen in the chilled dairy category this year. However, focus on product innovation and sales execution has enabled us to gain market share and improve margins in a competitive environment.

Asia

Our business in Asia continued to deliver volume growth with 874 million LME, up two per cent on the same time last year. However, normalised EBIT declined by 55 per cent to \$56 million, as the sharp increase in input costs could not be fully recovered through pricing. This was further impacted by price controls in some of our markets.

Indonesia had good volume growth in Foodservice. In Consumer, Anlene™ has performed well on the back of the launch of our Anlene™ Actifit range and our new “Total Anlene” campaign as we continue to expand our offering to customers. Our Malaysian business achieved strong volume growth due to the launch of Fernleaf™ UHT and our Anlene™ Gold formulation, which better supports joint mobility.

Oceania

The solid performance in our Australian business was impacted by a disappointing result from our Consumer business in New Zealand. This is reflected by the 74 per cent decline in normalised EBIT for Oceania, down to \$15 million this year from \$58 million in the previous comparable period.

Our Australian business is performing well, with normalised EBIT stable despite significantly higher input costs and lower overall sales volumes. The business has continued to focus on key product categories such as cheese and butter, where demand is growing and where we have strong brands and market share.

The New Zealand business has faced some challenges this year, with increased dairy commodity prices and lower category growth. Although we had strong ice cream demand this summer, record high fat prices impacted overall performance. In addition, our exit from some of our private label portfolio and operational start up challenges at our new distribution centre have impacted the overall Oceania result.

CHINA FARMS

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

6%

OPERATING COSTS

We delivered a six per cent reduction in operating costs on our China Farms.



HEMA FRESH

The milk bottles have unique labels for each day of the week, emphasising freshness.

HIGHLIGHTS

- › Continued focus on efficiencies and cost control to offset low milk prices.
- › Fresh milk sales introduced into retail formats.
- › Sales volumes down 15 per cent as the comparable period included milk powder sales.

VOLUME

Our farming operations in China comprise seven farms across two hubs, with around 34,000 milking cows. We finished this farm development programme in 2016 and all of our farms are fully operational and stocked with productive livestock.

Sales volumes decreased by 15 per cent to 132 million LME for the six months to 31 January 2018, as the comparable period last year included sales of milk powder.

USEFUL FACT

This year we launched our Daily Fresh milk range into Alibaba's new premium food stores, Hema Fresh, using milk sourced directly from our farms in the Hebei province.



We are progressing with our third hub, a joint venture between Fonterra and Abbott, which leverages our expertise in dairy nutrition and farming, and Abbott's continued commitment to business development in China. Construction of the first two farms is complete and further development will follow over the coming years.

CHINA

China is our largest and most strategically important market.



NZD MILLION	SIX MONTHS ENDED 31 JANUARY 2018	SIX MONTHS ENDED 31 JANUARY 2017	CHANGE
Volume (LME, billion)	0.1	0.2	(15%)
Volume ('000 MT)	10	13 ¹	(19%)
Sales revenue	123	122	1%
Normalised EBIT	(12)	(24)	49%

¹ China Farms volumes for the 2017 half 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.

VALUE

Operating performance for China Farms has improved from a normalised EBIT \$24 million loss in the previous comparable period to a \$12 million loss, largely due to ongoing cost control and scale efficiencies on-farm as our production volumes increase. For the six months to 31 January, we delivered a 0.20 RMB per litre or six per cent reduction in operating costs, due to more efficient operations as well as improved fixed cost and overhead recoveries. The China Farms' result also benefited from the internal raw milk price between China Farms and Ingredients. This reflects the long-term milk price forecast for high quality milk in China, and the fact that the responsibility for driving the greatest value from the raw milk produced in China now resides with the Ingredients team.

USEFUL FACT

Last year China Farms was the only dairy business in China to obtain Safety Quality Food (SQF) certification. This year we were recertified with an "excellent" grade for all seven farms.



INTERIM FINANCIAL RESULTS

For the six months ended
31 January 2018

CONTENTS

DIRECTORS' STATEMENT	31
INCOME STATEMENT	32
STATEMENT OF COMPREHENSIVE INCOME	33
STATEMENT OF FINANCIAL POSITION	34
STATEMENT OF CHANGES IN EQUITY	35
CASH FLOW STATEMENT	36
BASIS OF PREPARATION	37
NOTES TO THE FINANCIAL STATEMENTS	38

DIRECTORS' STATEMENT

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

The Directors of Fonterra Co-operative Group Limited (Fonterra) present to Shareholders the financial statements for Fonterra and its subsidiaries (together the Group) and the Group's interest in its equity accounted investments for the six months ended 31 January 2018.

The Directors present financial statements for the six months, 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 NZX Listing Rules.

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 financial statements for the six months ended 31 January 2018.

For and on behalf of the Board:



JOHN WILSON
CHAIRMAN

20 March 2018



BRUCE HASSALL
DIRECTOR

20 March 2018

INCOME STATEMENT

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

		GROUP \$ MILLION		
		SIX MONTHS ENDED		YEAR ENDED
	NOTES	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Revenue from sale of goods		9,839	9,241	19,232
Cost of goods sold	2	(8,177)	(7,480)	(15,968)
Gross profit		1,662	1,761	3,264
Other operating income		52	90	190
Selling and marketing expenses		(346)	(329)	(641)
Distribution expenses		(278)	(283)	(550)
Administrative expenses		(461)	(440)	(810)
Other operating expenses		(178)	(180)	(334)
WPC80 recall costs		(196)	–	–
Impairment of equity accounted investees		(405)	–	(35)
Net foreign exchange (losses)/gains		(29)	30	29
Share of profit/(loss) of equity accounted investees		3	(5)	7
(Loss)/profit before net finance costs and tax		(176)	644	1,120
Finance income		11	17	34
Finance costs		(212)	(174)	(389)
Net finance costs		(201)	(157)	(355)
(Loss)/profit before tax		(377)	487	765
Tax credit/(expense)		29	(69)	(20)
(Loss)/profit after tax		(348)	418	745
(Loss)/profit after tax is attributable to:				
Equity holders of the Co-operative		(354)	413	734
Non-controlling interests		6	5	11
(Loss)/profit after tax		(348)	418	745
		GROUP \$		
		SIX MONTHS ENDED		YEAR ENDED
		31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Earnings per share:				
Basic and diluted earnings per share		(0.22)	0.26	0.46

STATEMENT OF COMPREHENSIVE INCOME

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

	GROUP \$ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
(Loss)/profit after tax	(348)	418	745
Items that may be reclassified subsequently to profit or loss:			
Cash flow hedges and other costs of hedging, net of tax	(128)	56	128
Net investment hedges and translation of foreign operations, net of tax	209	(127)	(124)
Hyperinflation (loss)/gain attributable to equity holders	(1)	4	(1)
Share of equity accounted investees' movements in reserves	(1)	1	–
Other reserve movements	1	(2)	(2)
Total items that may be reclassified subsequently to profit or loss	80	(68)	1
Items that will not be reclassified subsequently to profit or loss:			
Net fair value gains on investments in shares	4	2	2
Foreign currency translation gain/(loss) attributable to non-controlling interests	12	1	(3)
Hyperinflation movements attributable to non-controlling interests	–	3	–
Non-controlling interests other movements	–	(2)	(2)
Total items that will not be reclassified subsequently to profit or loss	16	4	(3)
Total other comprehensive income/(expense) recognised directly in equity	96	(64)	(2)
Total comprehensive (expense)/income	(252)	354	743
Total comprehensive (expense)/income is attributable to:			
Equity holders of the Co-operative	(270)	347	737
Non-controlling interests	18	7	6
Total comprehensive (expense)/income	(252)	354	743

STATEMENT OF FINANCIAL POSITION

AS AT 31 JANUARY 2018

		GROUP \$ MILLION		
		SIX MONTHS ENDED		YEAR ENDED
	NOTES	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
ASSETS				
Current assets				
Cash and cash equivalents		359	348	393
Trade and other receivables		2,328	2,210	2,303
Inventories		5,017	4,566	2,593
Tax receivable		41	23	32
Derivative financial instruments		395	454	580
Other current assets		332	140	181
Total current assets		8,472	7,741	6,082
Non-current assets				
Property, plant and equipment		6,555	6,112	6,391
Equity accounted investments		609	916	887
Livestock		298	317	319
Intangible assets		3,200	3,071	3,115
Deferred tax assets		507	328	363
Derivative financial instruments		196	242	239
Other non-current assets		324	617	446
Total non-current assets		11,689	11,603	11,760
Total assets		20,161	19,344	17,842
LIABILITIES				
Current liabilities				
Bank overdraft		7	9	11
Borrowings	5	1,383	983	1,112
Trade and other payables		2,242	2,176	2,117
Owing to suppliers		2,737	2,359	1,330
Tax payable		39	31	34
Derivative financial instruments		91	49	43
Provisions		79	47	40
Other current liabilities		41	38	44
Total current liabilities		6,619	5,692	4,731
Non-current liabilities				
Borrowings	5	6,229	5,768	5,151
Derivative financial instruments		466	567	547
Provisions		142	158	148
Deferred tax liabilities		9	26	9
Other non-current liabilities		8	8	8
Total non-current liabilities		6,854	6,527	5,863
Total liabilities		13,473	12,219	10,594
Net assets		6,688	7,125	7,248
EQUITY				
Subscribed equity		5,877	5,841	5,858
Retained earnings		961	1,638	1,637
Foreign currency translation reserve		(343)	(555)	(552)
Hedge reserves		64	120	192
Other reserves		9	10	5
Total equity attributable to equity holders of the Co-operative		6,568	7,054	7,140
Non-controlling interests		120	71	108
Total equity		6,688	7,125	7,248

STATEMENT OF CHANGES IN EQUITY

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

GROUP \$ MILLION	ATTRIBUTABLE TO EQUITY HOLDERS OF THE CO-OPERATIVE						NON-CONTROLLING INTERESTS	TOTAL EQUITY
	SUBSCRIBED EQUITY	RETAINED EARNINGS	FOREIGN CURRENCY TRANSLATION RESERVE	HEDGE RESERVES	OTHER RESERVES	TOTAL		
As at 1 August 2017	5,858	1,637	(552)	192	5	7,140	108	7,248
(Loss)/profit after tax	–	(354)	–	–	–	(354)	6	(348)
Other comprehensive (expense)/income	–	(1)	209	(128)	4	84	12	96
Total comprehensive (expense)/income	–	(355)	209	(128)	4	(270)	18	(252)
Transactions with equity holders in their capacity as equity holders:								
Dividend paid to equity holders of the Co-operative	–	(321)	–	–	–	(321)	–	(321)
Equity instruments issued	19	–	–	–	–	19	15	34
Dividend paid to non-controlling interests	–	–	–	–	–	–	(21)	(21)
As at 31 January 2018 (unaudited)	5,877	961	(343)	64	9	6,568	120	6,688
As at 1 August 2016	5,833	1,384	(428)	64	6	6,859	88	6,947
Profit after tax	–	413	–	–	–	413	5	418
Other comprehensive income/(expense)	–	1	(127)	56	4	(66)	2	(64)
Total comprehensive income/(expense)	–	414	(127)	56	4	347	7	354
Transactions with equity holders in their capacity as equity holders:								
Dividend paid to equity holders of the Co-operative	–	(160)	–	–	–	(160)	–	(160)
Equity instruments issued	8	–	–	–	–	8	–	8
Dividend paid to non-controlling interests	–	–	–	–	–	–	(24)	(24)
As at 31 January 2017 (unaudited)	5,841	1,638	(555)	120	10	7,054	71	7,125
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 (audited)	5,858	1,637	(552)	192	5	7,140	108	7,248

CASH FLOW STATEMENT

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

	GROUP \$ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Cash flows from operating activities			
(Loss)/profit before net finance costs and tax	(176)	644	1,120
Adjustments for:			
Foreign exchange losses/(gains)	127	(38)	(1)
Depreciation and amortisation	275	289	526
Other	431	(12)	15
	833	239	540
(Increase)/decrease in working capital:			
Inventories	(2,419)	(2,161)	(177)
Trade and other receivables	3	(561)	(634)
Amounts owing to suppliers	1,273	1,641	745
Payables and accruals	227	78	(100)
Other movements	8	(6)	(48)
Total	(908)	(1,009)	(214)
Cash flows from operations	(251)	(126)	1,446
Net taxes paid	(41)	(41)	(70)
Net cash flows from operating activities	(292)	(167)	1,376
Cash flows from investing activities			
Cash was provided from:			
– Proceeds from disposal of property, plant and equipment	4	97	105
– Proceeds from sale of livestock	58	41	62
– Proceeds from sale of investments	6	–	–
– Co-operative support loans	138	4	41
– Other cash inflows	1	3	10
Cash was applied to:			
– Acquisition of property, plant and equipment	(400)	(277)	(690)
– Acquisition of livestock	(24)	(53)	(89)
– Acquisition of intangible assets	(74)	(29)	(103)
– Advances to and investments in equity accounted investees	(92)	(36)	(42)
– Other cash outflows	(15)	–	–
Net cash flows from investing activities	(398)	(250)	(706)
Cash flows from financing activities			
Cash was provided from:			
– Proceeds from borrowings	2,811	2,788	4,174
– Interest received	9	6	13
– Other cash inflows	–	36	38
Cash was applied to:			
– Interest paid	(199)	(186)	(393)
– Repayment of borrowings	(1,589)	(2,058)	(3,968)
– Dividends paid to non-controlling interests	(21)	(24)	(28)
– Dividends paid to equity holders of the Co-operative	(302)	(152)	(456)
– Other cash outflows	(58)	–	(2)
Net cash flows from financing activities	651	410	(622)
Net (decrease)/increase in cash and cash equivalents	(39)	(7)	48
Cash and cash equivalents at the beginning of the year	382	357	357
Effect of exchange rate changes on cash balances	9	(11)	(23)
Cash and cash equivalents at the end of the period	352	339	382
Reconciliation of closing cash balances to the statement of financial position:			
Cash and cash equivalents	359	348	393
Bank overdraft	(7)	(9)	(11)
Closing cash balances	352	339	382

BASIS OF PREPARATION

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

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 interim financial statements, as at and for the six months ended 31 January 2018, 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 interim financial statements have been prepared in accordance with International Accounting Standard 34: Interim Financial Reporting and New Zealand Equivalent to International Accounting Standard 34: Interim Financial Reporting. They have also been prepared in accordance with Generally Accepted Accounting Practice (GAAP) applicable to for-profit entities. They should be read in conjunction with the financial statements for the year ended 31 July 2017.

These interim 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.

The preparation of interim financial statements requires management to make judgements, estimates, and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates. In preparing these interim financial statements, the significant judgements made by management in applying the Group's accounting policies and key sources of estimation uncertainty were the same as those applied to the financial statements for the year ended 31 July 2017.

Investment in Beingmate Baby & Child Food Co., Ltd.

Throughout the period Beingmate's share price has traded significantly below the share price at the time Fonterra acquired its investment and the base share price used in the valuation assessment at 31 July 2017. As a result the carrying value of the investment has been assessed for impairment. To assess the recoverable amount of the investment a fair value less costs to sell methodology has been applied. This methodology continues to be appropriate as the uncertainty in forecasting future cash flows following changes in regulations in the market remains.

The fair value of the investment 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. The key assumptions used in determining the fair value are the base share price and the net premium above the base share price (acquisition premium) that would be paid for a long-term strategic investment of a similar size.

The value of the investment has reduced since 31 July 2017 as a result of the following:

- Reduction in the base share price, reflecting the decrease in the traded price of Beingmate shares from 31 July 2017, and

- Reduction in the net premium. The premium reflects that Beingmate is an established local participant in a growth market and has a number of brands registered under the new regulations effective 1 January 2018. The significant reduction in the net premium from 31 July 2017 reflects the poor financial performance, reduction in market share, and the operational and governance challenges experienced by Beingmate.

The value of the investment on a fair value basis supports a carrying value of \$244 million, therefore an impairment loss of \$405 million has been recognised in the period (after share of losses of \$28 million and favourable foreign currency translation movements of \$60 million).

The assumptions underlying the calculation of the Fair Value of the 18.8% strategic investment in Beingmate are:

RMB PER SHARE	AS AT	
	31 JAN 2018 (UNAUDITED)	31 JULY 2017 (AUDITED)
Weighted average share price period	15 trading days from 22 January 2018	30 trading days pre-trading halt date up to 10 July 2017
Weighted average base price	5.36	13.66
Net premium (including cost to sell)	0.52	2.45
Implied value per share	5.88	16.11

For the year ended 31 July 2017, Beingmate shares were on a trading halt from 12 July 2017 to 4 September 2017, therefore in the absence of an active market, the period immediately before the trading halt (26 May to 10 July 2017) was considered the most appropriate period to determine the base price given during this period the shares traded at a relatively stable range.

For the six months ended 31 January 2018, to remove the impact of market volatility, a 15 trading day period immediately after the forecast earnings downgrade announced by Beingmate on the 21 January 2018 was used (22 January 2018 to 9 February 2018). It was appropriate to use information from immediately after the reporting date as the Beingmate share price continued to decline despite no new information being provided to the market. We considered this the most appropriate period as the market had fully reflected the earnings downgrade impact.

C) ACCOUNTING POLICIES

The same accounting policies are followed in these interim financial statements as were applied in the Group's financial statements for the year ended 31 July 2017.

Accounting Standards issued but not yet effective

The two accounting standards issued but not yet effective that could be expected to have a material impact on the Group's financial statements are:

NZ IFRS 15 Revenue from Contracts with Customers

There has been no change to Fonterra's preliminary assessment that the application of NZ IFRS 15 will not have a material impact on its financial position and performance.

NZ IFRS 16 Leases

During the six months to 31 January 2018 Fonterra has continued to assess the impact of NZ IFRS 16 and evaluate the policy choices. The impact of adoption on Fonterra's financial position and performance has not yet been fully assessed. Fonterra has evaluated the transition options and plans to utilise the modified retrospective approach. This means that the cumulative effect of adopting NZ IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings on 1 August 2019 with no restatement of comparative information.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

PERFORMANCE

1 SEGMENT REPORTING

The financial information reviewed by the Fonterra Management Team has evolved over the past two years to reflect the changes in the management structure to support the operations of the Group. From 1 August 2017 the financial information reviewed by the Fonterra Management Team is solely based on the previously identified 'strategic platforms'.

a) Operating segments

Operating segments reflect the way financial information is regularly reviewed by the Fonterra Management Team (FMT). The measure of profit or loss used by the FMT to evaluate the underlying performance of operating segments is normalised segment earnings before net finance costs and tax. To enable underlying segment performance to be compared between reporting periods a normalised segment income statement has been presented. Comparative segment income statements have been re-presented on a normalised basis.

Transactions between segments are based on estimated market prices, with the exception of the sale of milk from China Farms to Ingredients. The transfer price used for these transactions is an amount reflective of long-term milk price trends in China.

Unallocated costs represent corporate costs including Co-operative Affairs and group services.

REPORTABLE SEGMENT	DESCRIPTION
Ingredients	Represents the collection, processing and distribution of the ingredients business in New Zealand, global sales and marketing of New Zealand and non-New Zealand ingredients products, Fonterra Farm Source™ stores, the ingredients business in Australia (including Milk Supply and Manufacturing) and the ingredients business South America.
Consumer and foodservice	
– Oceania	Represents the fast-moving consumer goods (FMCG) and foodservice businesses in New Zealand and Australia (including export to the Pacific Islands).
– Asia	Represents FMCG and foodservice businesses in Asia (excluding Greater China), Africa and the Middle East.
– Greater China	Represents FMCG and foodservice businesses in Greater China.
– Latin America	Represents FMCG and foodservice businesses in South America and the Caribbean.
China Farms	Represents farming operations in China.

a) Operating segments continued

	GROUP \$ MILLION								
	31 JANUARY 2018 (UNAUDITED)								
	INGREDIENTS	CONSUMER AND FOODSERVICE					CHINA FARMS	UNALLOCATED COSTS AND ELIMINATIONS	TOTAL
		OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	TOTAL			
Normalised segment income statement									
External revenue ¹	6,448	1,002	905	731	750	3,388	–	–	9,836
Inter-segment revenue	1,455	85	–	–	–	85	123	(1,663)	–
Revenue from sale of goods	7,903	1,087	905	731	750	3,473	123	(1,663)	9,836
Cost of goods sold	(7,032)	(879)	(694)	(549)	(530)	(2,652)	(131)	1,638	(8,177)
Segment gross profit	871	208	211	182	220	821	(8)	(25)	1,659
Operating expenses	(391)	(192)	(154)	(98)	(196)	(640)	(14)	(218)	(1,263)
Net other operating income	32	1	2	7	3	13	8	(1)	52
Net foreign exchange gains/(losses)	15	(2)	(3)	1	1	(3)	4	(37)	(21)
Share of profit/(loss) of equity accounted investees	31	–	–	–	2	2	(2)	–	31
Normalised segment earnings before net finance costs and tax	558	15	56	92	30	193	(12)	(281)	458
Normalisation adjustments:									
Reduction in the carrying value of investment in Beingmate ²	–	–	–	(433)	–	(433)	–	–	(433)
WPC80 recall costs ³	(196)	–	–	–	–	–	–	–	(196)
Time value of options ⁴	(5)	–	–	–	–	–	–	–	(5)
Segment earnings before net finance costs and tax	357	15	56	(341)	30	(240)	(12)	(281)	(176)
Finance income									11
Finance costs									(212)
Loss before tax									(377)
Other segment information:									
Volume ⁵ (liquid milk equivalents, billion)	9.78	0.82	0.87	0.60	0.37	2.66	0.13	(2.12)	10.45
Volume ⁵ (metric tonnes, thousand)	1,441	309	161	129	294	893	10	(341)	2,003
Depreciation and amortisation (\$ million)	(198)	(15)	(7)	(1)	(14)	(37)	(14)	(26)	(275)

1 Total Group revenue from the sale of goods is \$9,839 million, the difference of \$3 million relates to the normalisation of time value of options.

2 Of the \$433 million normalisation adjustment, \$405 million relates to the impairment of equity accounted investees and \$28 million to the share of losses of Beingmate.

3 The \$196 million normalisation adjustment relates to operating expenses.

4 Of the \$5 million normalisation adjustment, \$3 million relates to revenue offset by \$8 million of net foreign exchange losses.

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

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

a) Operating segments continued

	GROUP \$ MILLION								
	31 JANUARY 2017 (UNAUDITED)								
	INGREDIENTS	CONSUMER AND FOODSERVICE					CHINA FARMS	UNALLOCATED COSTS AND ELIMINATIONS	TOTAL
		OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	TOTAL			
Normalised segment income statement									
External revenue ¹	6,159	920	835	567	751	3,073	–	–	9,232
Inter-segment revenue	1,060	68	98	–	–	166	122	(1,348)	–
Revenue from sale of goods	7,219	988	933	567	751	3,239	122	(1,348)	9,232
Cost of goods sold	(6,427)	(745)	(645)	(369)	(517)	(2,276)	(128)	1,351	(7,480)
Segment gross profit	792	243	288	198	234	963	(6)	3	1,752
Operating expenses	(367)	(186)	(165)	(83)	(204)	(638)	(20)	(207)	(1,232)
Net other operating income	23	2	3	5	3	13	12	–	48
Net foreign exchange gains/(losses)	37	(1)	(2)	–	–	(3)	(2)	12	44
Share of profit/(loss) of equity accounted investees	25	–	–	(24)	2	(22)	(8)	–	(5)
Normalised segment earnings before net finance costs and tax	510	58	124	96	35	313	(24)	(192)	607
Normalisation adjustments:									
Gain on sale of Darnum manufacturing plant ²	42	–	–	–	–	–	–	–	42
Time value of options ³	(5)	–	–	–	–	–	–	–	(5)
Segment earnings before net finance costs and tax	547	58	124	96	35	313	(24)	(192)	644
Finance income									17
Finance costs									(174)
Profit before tax									487
Other segment information:									
Volume ⁴ (liquid milk equivalents, billion)	10.98	0.91	0.86	0.58	0.36	2.71	0.16	(2.14)	11.71
Volume ^{4,5} (metric tonnes, thousand)	1,543	335	156	112	305	908	13	(333)	2,131
Depreciation and amortisation (\$ million)	(208)	(15)	(8)	(1)	(17)	(41)	(13)	(27)	(289)

1 Total Group revenue from the sale of goods is \$9,241 million, the difference of \$9 million relates to the normalisation of time value of options.

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

3 Of the \$5 million normalisation adjustment, \$9 million relates to revenue offset by \$14 million of net foreign exchange losses.

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

5 China Farms volumes for the six months ended 31 January 2017 (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.

a) Operating segments continued

	GROUP \$ MILLION								
	31 JULY 2017 (AUDITED)								
	INGREDIENTS	CONSUMER AND FOODSERVICE					CHINA FARMS	UNALLOCATED COSTS AND ELIMINATIONS	TOTAL
		OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	TOTAL			
Normalised segment income statement									
External revenue ¹	12,986	1,810	1,668	1,272	1,478	6,228	–	–	19,214
Inter-segment revenue	2,280	142	142	5	–	289	269	(2,838)	–
Revenue from sale of goods	15,266	1,952	1,810	1,277	1,478	6,517	269	(2,838)	19,214
Cost of goods sold	(13,793)	(1,514)	(1,309)	(918)	(1,032)	(4,773)	(246)	2,844	(15,968)
Segment gross profit	1,473	438	501	359	446	1,744	23	6	3,246
Operating expenses	(725)	(339)	(298)	(156)	(357)	(1,150)	(31)	(429)	(2,335)
Net other operating income	106	2	3	6	7	18	14	10	148
Net foreign exchange gains/(losses)	42	–	(5)	–	3	(2)	(1)	9	48
Share of profit/(loss) of equity accounted investees	47	–	–	–	4	4	(4)	1	48
Normalised segment earnings before net finance costs and tax	943	101	201	209	103	614	1	(403)	1,155
Normalisation adjustments:									
Gain on sale of Darnum manufacturing plant ²	42	–	–	–	–	–	–	–	42
Reduction in the carrying value of investment in Beingmate ³	–	–	–	(76)	–	(76)	–	–	(76)
Time value of options ⁴	(1)	–	–	–	–	–	–	–	(1)
Segment earnings before net finance costs and tax	984	101	201	133	103	538	1	(403)	1,120
Finance income									34
Finance costs									(389)
Profit before tax									765
Other segment information:									
Volume ⁵ (liquid milk equivalents, billion)	21.30	1.74	1.70	1.28	0.74	5.46	0.34	(4.16)	22.94
Volume ⁵ (metric tonnes, thousand)	3,019	636	310	237	600	1,783	26	(648)	4,180
Depreciation and amortisation (\$ million)	(367)	(31)	(15)	(2)	(33)	(81)	(26)	(52)	(526)
Capital employed ⁶ (\$ million)	7,950	463	117	22	270	872	789	(518)	9,093
Return on capital ⁷	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.

1 Total Group revenue from the sale of goods is \$19,232 million, the difference of \$18 million relates to the normalisation of time value of options.

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

3 Of the \$76 million normalisation adjustment, \$35 million relates to impairment of equity accounted investees and \$41 million relates to the share of losses of Beingmate.

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

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

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

7 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.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

b) Geographical revenue

	GROUP \$ MILLION								
	CHINA	REST OF ASIA	AUSTRALIA	NEW ZEALAND	UNITED STATES	EUROPE	LATIN AMERICA	REST OF WORLD	TOTAL
<i>Geographical segment external revenue:</i>									
Six months ended 31 January 2018 (unaudited)	2,094	2,650	860	1,021	321	337	1,095	1,461	9,839
Six months ended 31 January 2017 (unaudited)	1,565	2,404	785	977	650	430	1,065	1,365	9,241
Year ended 31 July 2017 (audited)	3,383	5,165	1,592	2,056	1,254	838	2,162	2,782	19,232

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

c) 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				
<i>Geographical segment non-current assets:</i>								
As at 31 January 2018 (unaudited)	5,409	424	1,300	868	774	1,167	1,044	10,986
As at 31 January 2017 (unaudited)	5,376	301	1,294	797	723	1,540	1,002	11,033
As at 31 July 2017 (audited)	5,479	347	1,285	840	738	1,481	988	11,158

	GROUP \$ MILLION		
	AS AT		
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
<i>Reconciliation of geographical segment's non-current assets to total non-current assets:</i>			
Geographical segment non-current assets	10,986	11,033	11,158
Deferred tax assets	507	328	363
Derivative financial instruments	196	242	239
Total non-current assets	11,689	11,603	11,760

2 COST OF GOODS SOLD

	GROUP \$ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Opening inventory	2,593	2,401	2,401
Cost of milk:			
– New Zealand sourced	6,580	6,078	9,471
– Non-New Zealand sourced	737	521	932
Other costs	3,284	3,046	5,757
Closing inventory	(5,017)	(4,566)	(2,593)
Total cost of goods sold	8,177	7,480	15,968

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 2017	1,606,933
Shares issued under the dividend reinvestment plan ²	3,309
Balance at 31 January 2018 (unaudited)	1,610,242
Balance at 1 August 2016	1,602,703
Shares issued under the dividend reinvestment plan ²	1,369
Balance at 31 January 2017 (unaudited)	1,604,072
Balance at 1 August 2016	1,602,703
Shares issued under the dividend reinvestment plan ²	4,230
Balance at 31 July 2017 (audited)	1,606,933

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

2 Total value of \$19 million (31 January 2017: \$8 million; 31 July 2017: \$25 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 January 2018, 137,366,342 Co-operative shares (31 January 2017: 123,422,471; 31 July 2017: 126,047,304) were legally owned by the Custodian, on trust for the benefit of the Fund.

	UNITS (THOUSANDS)
Balance at 1 August 2017	126,047
Units issued	19,504
Units surrendered	(8,185)
Balance at 31 January 2018 (unaudited)	137,366
Balance at 1 August 2016	111,992
Units issued	22,222
Units surrendered	(10,792)
Balance at 31 January 2017 (unaudited)	123,422
Balance at 1 August 2016	111,992
Units issued	29,933
Units surrendered	(15,878)
Balance at 31 July 2017 (audited)	126,047

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

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

4 DIVIDENDS PAID

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

DIVIDENDS	\$ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
2017 Final dividend – 20 cents per share ¹	321	–	–
2017 Interim dividend – 20 cents per share ²	–	–	321
2016 Final dividend – 10 cents per share ³	–	160	160

1 Declared on 23 September 2017 and paid on 20 October 2017 to all Co-operative shares on issue at 9 October 2017.

2 Declared on 21 March 2017 and paid on 20 April 2017 to all Co-operative shares on issue at 5 April 2017.

3 Declared on 18 August 2016 and paid on 9 September 2016 to all Co-operative shares on issue at 1 September 2016.

Dividend declared after balance date

On 20 March 2018, the Board declared an interim dividend of 10 cents per share, to be paid 20 April 2018 to all Co-operative shares on issue as at 6 April 2018.

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 6 April 2018. Full details of the Dividend Reinvestment Plan are available in the 'Investors/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 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Net interest-bearing debt position			
Total borrowings	7,612	6,751	6,263
Cash and cash equivalents	(359)	(348)	(393)
Interest-bearing advances	(323)	(481)	(435)
Bank overdraft	7	9	11
Net interest-bearing debt	6,937	5,931	5,446
Value of derivatives used to manage changes in hedged risks on debt instruments	123	184	155
Economic net interest-bearing debt	7,060	6,115	5,601

Total borrowings in the table above are represented by:

	GROUP \$ MILLION		
	AS AT		
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Commercial paper	239	313	164
Bank loans	1,763	1,226	854
Finance leases	134	139	137
Capital notes	35	35	35
NZX-listed bonds	500	499	500
Medium-term notes	4,941	4,539	4,573
Total borrowings	7,612	6,751	6,263
Included within the statement of financial position as follows:			
Total current borrowings	1,383	983	1,112
Total non-current borrowings	6,229	5,768	5,151
Total borrowings	7,612	6,751	6,263

LONG-TERM ASSETS

6 PROPERTY, PLANT AND EQUIPMENT

	GROUP \$ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Additions	310	205	754
Disposals	(7)	(20)	(48)
Capital commitments	236	159	235

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.

EQUITY ACCOUNTED INVESTEE NAME	COUNTRY OF INCORPORATION AND PRINCIPAL PLACE OF BUSINESS	OWNERSHIP INTERESTS (%)		
		AS AT		
		31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
DMV Fonterra Excipients GmbH & Co KG	Germany	50	50	50
Beingmate Baby & Child Food Co., Ltd ¹	China	18.8	18.8	18.8
Falcon Dairy Holdings Limited	Hong Kong	51	51	51

All investees have balance dates of 31 December.

¹ For further information on the carrying value of the investment in Beingmate please refer to the 'Basis of Preparation' section of these financial statements.

OTHER

8 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.

On 1 December 2017, the Singapore arbitration panel issued its award (judgement), finding in favour of Danone and ordered Fonterra to pay EUR105 million (\$183 million) in recall costs to Danone. Following a comprehensive review of the award, Fonterra has accepted the outcome. Fonterra paid the award in December 2017.

In addition to the recall costs, Fonterra has agreed to pay Danone EUR29 million (\$49 million) representing interest on the award amount and Danone's costs in connection with the arbitration proceedings.

It is unclear whether Danone will continue to pursue the New Zealand High Court proceedings that were stayed pending the decision in the Singapore arbitration. Due to the uncertainty regarding whether Danone will seek to re-initiate these proceedings, and the nature and scope of these potential proceedings in light of the arbitration findings and award, no amount has been recognised in relation to these proceedings.

The Directors believe that these proceedings have been adequately 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 January 2018 (31 January 2017: nil; 31 July 2017: nil).

NOTES TO THE FINANCIAL STATEMENTS

CONTINUED

FOR THE SIX MONTHS ENDED 31 JANUARY 2018

9 FAIR VALUE

Fair value hierarchy

The fair value hierarchy described below is used to provide an indication of the level of estimation or judgement required in determining fair value:

- 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 and liabilities measured at fair value on the statement of financial position:

	GROUP \$ MILLION								
	LEVEL 1			LEVEL 2			LEVEL 3		
	AS AT			AS AT			AS AT		
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Derivative assets									
– Commodity derivatives	21	22	30	5	1	1	–	–	–
– Foreign exchange derivatives	–	–	–	390	453	595	–	–	–
– Interest rate derivatives ¹	–	–	–	175	220	193	–	–	–
Derivative liabilities									
– Commodity derivatives	(4)	(26)	(7)	–	(1)	(2)	–	–	–
– Foreign exchange derivatives	–	–	–	(77)	(23)	(24)	–	–	–
– Interest rate derivatives ¹	–	–	–	(476)	(566)	(557)	–	–	–
Investments in shares	12	8	10	15	–	–	7	–	9
Investment in Beingmate ²	–	–	–	–	–	–	244	–	617
Livestock	–	–	–	–	–	–	298	317	319
Fair value	29	4	33	32	84	206	549	317	945

1 Includes cross-currency interest rate swaps.

2 The key assumptions used in determining the fair value of the investment in Beingmate are the base share price and the premium above base 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			AS AT			AS AT		
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Financial assets									
Long-term advances	138	481	300	–	–	–	133	489	289
Financial liabilities									
Borrowings									
– NZX-listed bonds	(500)	(499)	(500)	(512)	(490)	(510)	–	–	–
– Capital notes	(35)	(35)	(35)	(34)	(33)	(33)	–	–	–
– Medium-term notes	(4,941)	(4,539)	(4,573)	–	–	–	(5,223)	(4,780)	(4,829)
– Finance leases	(134)	(139)	(137)	–	–	–	(149)	(158)	(155)

10 NET TANGIBLE ASSETS PER SECURITY

	GROUP		
	AS AT		
	31 JAN 2018 UNAUDITED	31 JAN 2017 UNAUDITED	31 JUL 2017 AUDITED
Net tangible assets per security¹			
\$ per listed debt security on issue	5.79	6.73	6.86
\$ per equity instrument on issue	2.17	2.53	2.57
Listed debt securities on issue (million)	603	603	603
Equity instruments on issue (million)	1,610	1,604	1,607

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

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 49. These are non-GAAP measures and are not prepared in accordance with 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 IFRS.

Reconciliations for the IFRS measures to certain non-GAAP measures referred to by Fonterra are detailed below.

Reconciliation from the IFRS measure of profit for the period to Fonterra's normalised EBITDA

	GROUP \$ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2018	31 JAN 2017	31 JUL 2017
(Loss)/profit for the period	(348)	418	745
Add: Depreciation	229	240	435
Add: Amortisation	46	49	91
Add: Net finance costs	201	157	355
(Less)/Add: Taxation (credit)/expense	(29)	69	20
Total EBITDA	99	933	1,646
Add: WPC80 recall costs	196	–	–
Add: Reduction in the carrying value of investment in Beingmate	433	–	76
Add: Time value of options	5	5	1
Less: Gain on sale of Darnum manufacturing plant	–	(42)	(42)
Total normalisation adjustments	634	(37)	35
Normalised EBITDA	733	896	1,681

Reconciliation from the NZ IFRS measure of profit for the period to Fonterra's normalised EBIT

	GROUP \$ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2018	31 JAN 2017	31 JUL 2017
(Loss)/profit for the period	(348)	418	745
Add: Net finance costs	201	157	355
(Less)/Add: Taxation (credit)/expense	(29)	69	20
Total EBIT	(176)	644	1,120
Add/(Less): Normalisation adjustments (as detailed above)	634	(37)	35
Total normalised EBIT	458	607	1,155

Reconciliation from the NZ IFRS measure of profit for the period to Fonterra's normalised earnings per share

	GROUP \$ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2018	31 JAN 2017	31 JUL 2017
(Loss)/profit for the period	(348)	418	745
Add/(Less): Normalisation adjustments (as detailed above)	634	(37)	35
Add: Normalisation adjustment to net finance costs	26	–	–
(Less)/Add: Tax on normalisation adjustments	(64)	8	12
Total normalised earnings	248	389	792
Less: Share attributable to non-controlling interests	(6)	(5)	(11)
Net normalised earnings attributable to equity holders of the Parent	242	384	781
Weighted average number of shares (thousands of shares)	1,608,821	1,603,698	1,604,744
Normalised earnings per share (\$)	0.15	0.24	0.49

GLOSSARY

NON-GAAP MEASURES

Fonterra refers to non-GAAP financial measures throughout the Interim Report, 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 Interim Report.

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 earnings per share (EPS)	means normalised profit after tax attributable to equity holders divided by the weighted average number of shares for the period.
Normalised profit after tax	means net profit after tax after normalisation adjustments, and the interest and tax impact of those 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.

SHAREHOLDER INFORMATION

FONTERRA BOARD OF DIRECTORS

John Wilson
Clinton Dines
Brent Goldsack
Bruce Hassall
Simon Israel
Andrew Macfarlane
John Monaghan
Nicola Shadbolt
Donna Smit
Scott St John
Ashley Waugh

FONTERRA MANAGEMENT TEAM

Theo Spierings
Marc Rivers
Lukas Paravicini
Miles Hurrell
Robert Spurway
Judith Swales
Kelvin Wickham

REGISTERED OFFICE

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New Zealand

FARMER SHAREHOLDER AND SUPPLIER SERVICES

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FONTERRA SHARES AND FSF UNITS REGISTRY

Computershare Investor
Services Limited
Private Bag 92119
Auckland 1142
New Zealand

Level 2, 159 Hurstmere Road
Takapuna
Auckland 0622
New Zealand

CAPITAL NOTES REGISTRY

Link Market Services Limited
PO Box 91976
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New Zealand

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Auckland Central 1010
New Zealand

INVESTOR RELATIONS ENQUIRIES

investor.relations@fonterra.com

www.fonterra.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 **Marc Rivers** Authority for event, e.g. Directors' resolution **Directors' resolution**

Contact phone number **(09) 374 9000** Contact fax number **(09) 374 9001** Date **20 / 03 / 2018**

Nature of event
Tick as appropriate

Bonus Issue ☐	If ticked, state whether: Taxable ☐ / Non Taxable ☐	Conversion ☐	Interest ☐	Rights Issue Renounceable ☐
Rights Issue non-renounceable ☐	Capital change ☐ Call ☐ Dividend ☒	If ticked, state whether: Interim ☒ Full Year ☐	Special ☐	DRP Applies ☒

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**

Strike price per security for any issue in lieu or date Strike Price available. Tick if OR provide an explanation of the ranking

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) \$0.100	Source of Payment Retained earnings
Currency NZD	Supplementary dividend details - FSM Rule 6.8.5
Total monies \$161,024,235	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 \$0.033000	Imputation Credit (Give details)
Foreign Withholding Tax \$	FDP Credits (Give details)

Timing

(Refer Appendix 4 in the FSM Rules)

Record Date 5pm

For calculation of entitlements -

6 April, 2018

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.

20 April, 2018

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:



Market Announcement

21 March 2018

FONTERRA ANNOUNCES 2018 INTERIM RESULTS

Results Highlights

- Forecast Farmgate Milk Price \$6.55 per kgMS
- Interim dividend of 10 cents per share – to be paid in April
- Full year forecast dividend range 25 – 35 cents per share
- Total forecast cash payout \$6.80 - \$6.90
- Revenue \$9.8 billion, up 6% from the 2017 interim results
- Normalised EBIT \$458 million*, down 25% from the 2017 interim results
- Beingmate investment impairment \$405 million
- Normalised Net profit after tax (NPAT) \$248 million*, down 36% from the 2017 interim results
- NPAT \$348 million loss, down 183% from the 2017 interim results
- Normalised interim earnings per share 15 cents*
- Ingredients normalised EBIT \$558 million*, up 9% from the 2017 interim results
- Consumer and Foodservice normalised EBIT \$193 million*, down 38% from the 2017 interim results

** Non-GAAP measures. Information on the non-GAAP financial information used by Fonterra are found at the end of this document.*

Forecast cash payout

Fonterra Co-operative Group Limited today increased its forecast Farmgate Milk Price for the 2017/18 season to \$6.55 per kgMS and announced a full year forecast dividend range of 25 - 35 cents per share with an interim dividend of 10 cents per share.

Chairman John Wilson says the ongoing strong global demand for dairy and stable global supply are continuing to support global prices, particularly for the important Whole Milk Powder category.

“Farmers will welcome a forecast cash payout of \$6.80 - \$6.90, which would be the third highest in the last decade. This is also good news for New Zealand as it represents around \$10 billion flowing into the country’s economy. However, we are very aware of the challenges many of our farmers are facing this season with difficult weather conditions impacting production.

“While the global supply and demand picture remains positive and we expect prices to stay around current levels, we will be watching for any impact on market sentiment as spring production volumes build in Europe,” he added.

Fonterra’s Greater China business continues to perform well overall but the Co-operative has re-assessed the value of its Beingmate investment so that it reflects a fair value at this point in time.

Commenting on this decision, Mr Wilson says the Board has assessed the carrying value of Beingmate at \$244 million and therefore taken an impairment of \$405 million.

“While we appreciate the substantial opportunity and privilege of our business in China, our shareholders and unitholders will be rightfully disappointed with this outcome. Beingmate’s continued under-performance is unacceptable. The turnaround of the investment is a key priority for our senior management team.”

“The opportunity in the Chinese infant formula market remains, as does the potential for our Beingmate partnership – but an immediate business transformation is needed for Beingmate to benefit from the ongoing changes in the market.”

In December, Fonterra paid \$183 million to Danone following the conclusion of an arbitration that arose from the WPC80 precautionary recall in 2013.

Mr Wilson says the Board will decide how the Beingmate impairment and the Danone payment will be treated for final dividend purposes after the end of the financial year when it will have the full picture of Fonterra’s operating performance. Given the possible impact of these decisions, the Board is providing a forecast dividend range for the full-year of 25 – 35 cents per share, rather than just the earnings per share guidance normally given.

“Based on our dividend policy, this forecast dividend range would allow for the Board to add back the Beingmate impairment at the lower end through to an adjustment for both Beingmate and Danone as one-off events at the higher end.

“In the circumstances, we have taken a prudent approach in determining the 10 cent interim dividend.”

Our Business Performance

Chief Executive Theo Spierings says the operating performance for the first half year was generally as expected.

“We knew going into this year we would have to carefully manage low starting inventory levels. This was followed by reduced New Zealand milk collections due to difficult weather conditions, further impacting our volumes available for sale.

“On top of this, we also had to navigate higher input costs which squeezed our margins.

“So, at the end of the first half, our total sales volumes are down 11 per cent to 10.5 billion LME, and normalised earnings before interest and tax (EBIT) 25 per cent lower at \$458 million* compared to \$607 million in the same period last year,” says Mr Spierings.

“Despite this, overall sales revenue in the business was up six per cent to \$9.8 billion compared to the same period last year, mainly due to the improved global prices for dairy.

“While our reported net profit after tax (NPAT) shows a loss of \$348 million, it includes the payment to Danone and the Beingmate impairment. As these are one-off events, our normalised Net Profit After Tax of \$248 million* is a better reflection of our underlying operating performance for the half year.”

Commenting on the Ingredients business Mr Spierings says the team achieved a strong result with normalised EBIT growth of nine per cent to \$558 million* compared to \$510 million* in the same period last year, despite lower sales volumes of 9.8 billion LME.

“The result benefited from higher stream returns in the first half – \$90 million compared to \$40 million for the same period last year. These additional stream returns were predominantly due to improved margins for non-reference products during this period.

In relation to Fonterra’s Consumer and Foodservice business, Mr Spierings says the higher input costs meant margins were reduced by 15 per cent over the period, with strong competition in the

Co-operative's strategic markets, especially in Foodservice, limiting the short-term options to pass through the higher costs.

"Consumer and Foodservice's volumes were two per cent lower compared to the same period last year. Our sales volumes in Asia, Latin America, and Greater China improved but they were offset by lower volumes in Oceania, caused primarily by operational start-up challenges at our new distribution centre in Auckland, which is now operating as we'd expect.

"Overall, Consumer and Foodservice normalised EBIT was \$193 million* compared to an exceptional \$313 million* in the prior comparable period when input costs were considerably lower."

Mr Spierings says the Co-operative's China Farms strategy is beginning to bear fruit and the farms' improved performance is reflected a normalised EBIT loss of \$12 million* – half the \$24 million* loss for the same period last year.

"This result is helped by the price the Ingredients business pays China Farms for its milk, which is currently higher than the unsustainably low domestic milk price. This approach is producing better results by allowing the China Farms managers to focus on ongoing on-farm efficiencies and the Ingredients managers to focus on getting the best price for our high-quality milk.

"The potential is strong as Chinese demand for high-quality local fresh milk continues to grow. In February this year, we launched a new premium 'Daily Fresh' milk range alongside Alibaba's Hema Fresh stores in Shanghai and Suzhou. This milk is sourced directly from our farm hub in Hebei province. While early days, the opportunity for scale and reach alongside Alibaba is huge."

Our Greater China Business

In talking about Fonterra's Greater China business, Mr Spierings says that while the Beingmate investment has underperformed, the Co-operative's integrated Greater China business is delivering positive results for shareholders and unitholders and continues to have high growth prospects.

"In our first half, China volumes accounted for 2.2 billion LME of our total 9.8 billion LME in ingredients, with around 80 per cent of this milk sourced in New Zealand. In our Consumer and Foodservice business, China volumes accounted for 600 million LMEs of the total 2.7 billion LMEs sold over the first half, with Consumer and Foodservice in Greater China achieving normalised EBIT of \$92 million* on volume growth of three per cent compared to the same period last year.

"Clearly the outcome of re-assessing the value of our investment in Beingmate downwards is unacceptable to our shareholders and unitholders. The recovery of the value of this investment is the number one immediate priority for me and the senior management team.

"To be blunt, the investment in Beingmate has not gone the way we expected and there are things we would do differently knowing what we know now. We are very focused on doing all we can to get things where they need to be.

"As an 18.8 per cent shareholder, we do not have direct control over the company but we are influencing its direction and continue to call for an urgent business transformation by working co-operatively with Beingmate's founder and majority shareholder. We see there are a number of opportunities to reverse the current performance, unlock the distribution network and meet customers' preferences for e-commerce.

"While this seems like a slow process and we're not allowed to share all of the information about Beingmate's business, we are working hard in the background to get ourselves in a position where there is a tangible action plan for transforming Beingmate that we can share more widely and monitor progress," says Mr Spierings.

A working group of the Board – that includes Independent Directors Simon Israel and Clinton Dines, who both have significant China experience and expertise – is providing guidance and oversight as the senior management team work to recover the investment.

Outlook

Fonterra expects its earnings to be weighted to the second half of the year.

Despite more favourable weather conditions recently, the Co-operative still expects its New Zealand milk volumes to be down for the year and will be managing its inventory and product mix carefully for the remainder of the season to ensure it maximises the overall value of its farmers' milk.

Mr Spierings says a strong commitment to the V3 strategy of shifting more volume into higher value products at velocity is critical to the business achieving its forecast.

"We will continue to put as much milk as possible into higher value products, particularly into our Advanced Ingredients business, and Consumer and Foodservice business where we are still targeting an additional 400 million litres of volume this year.

"Our Co-operative remains focused on delivering sustainable value for our farmers – that's a sustainable Farmgate Milk Price, dividend, and return on their investment in the Co-op as we provide high quality dairy nutrition to consumers around the world."

The record date for the payment of the dividend is 6 April 2018, and the payment date is 20 April 2018. The Co-operative will continue to offer a dividend reinvestment plan, the strike price at which shares are issued incorporating a discount of 2.5%. Eligible shareholders who wish to participate in the dividend reinvestment plan for this dividend need to submit a notice of participation by 6 April 2018.

Click [here](#) to view Fonterra's Interim Results presentation and Interim Review.

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, normalised earnings per share, normalised NPAT 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 underlying 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.

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 48 to 49 of Fonterra's Interim Report that is available on Fonterra's website [here](#).

ENDS

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PERFORMANCE REVIEW

Interim Result 2018

21 MARCH 2018
FONTERRA CO-OPERATIVE GROUP LIMITED

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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This presentation does not constitute investment advice, or an inducement, recommendation or offer to buy or sell any securities in Fonterra or the Fonterra Shareholders' Fund.

Global Context

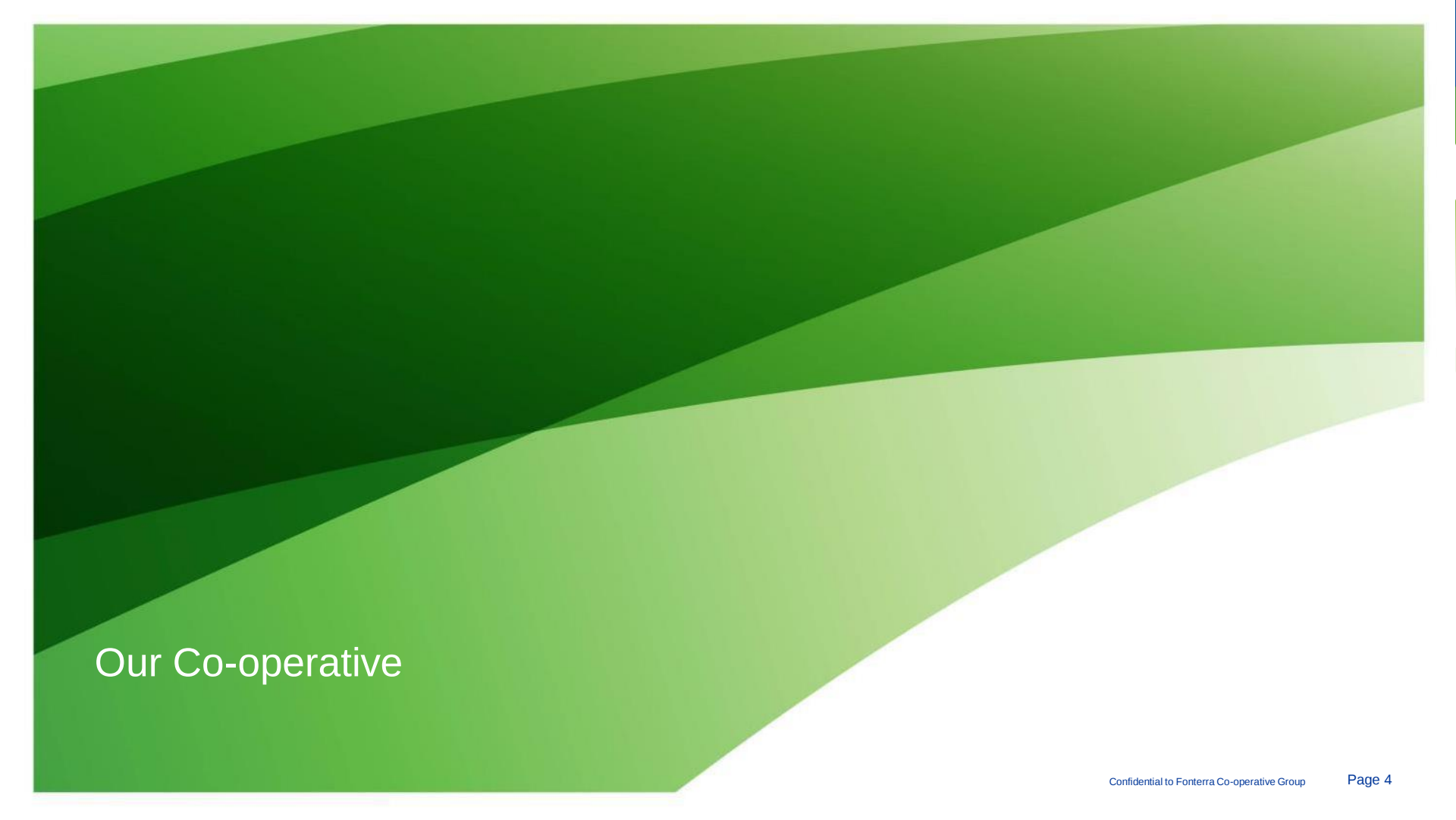
- Industry outlook continues to be positive
- Global dairy prices reflect ongoing strong demand
- An increase in EU production may cause price volatility

Value Creation

- Operating performance in line with expectations
- Danone costs and Beingmate impairment impacted our result
- Greater China operations making a significant contribution

Trust

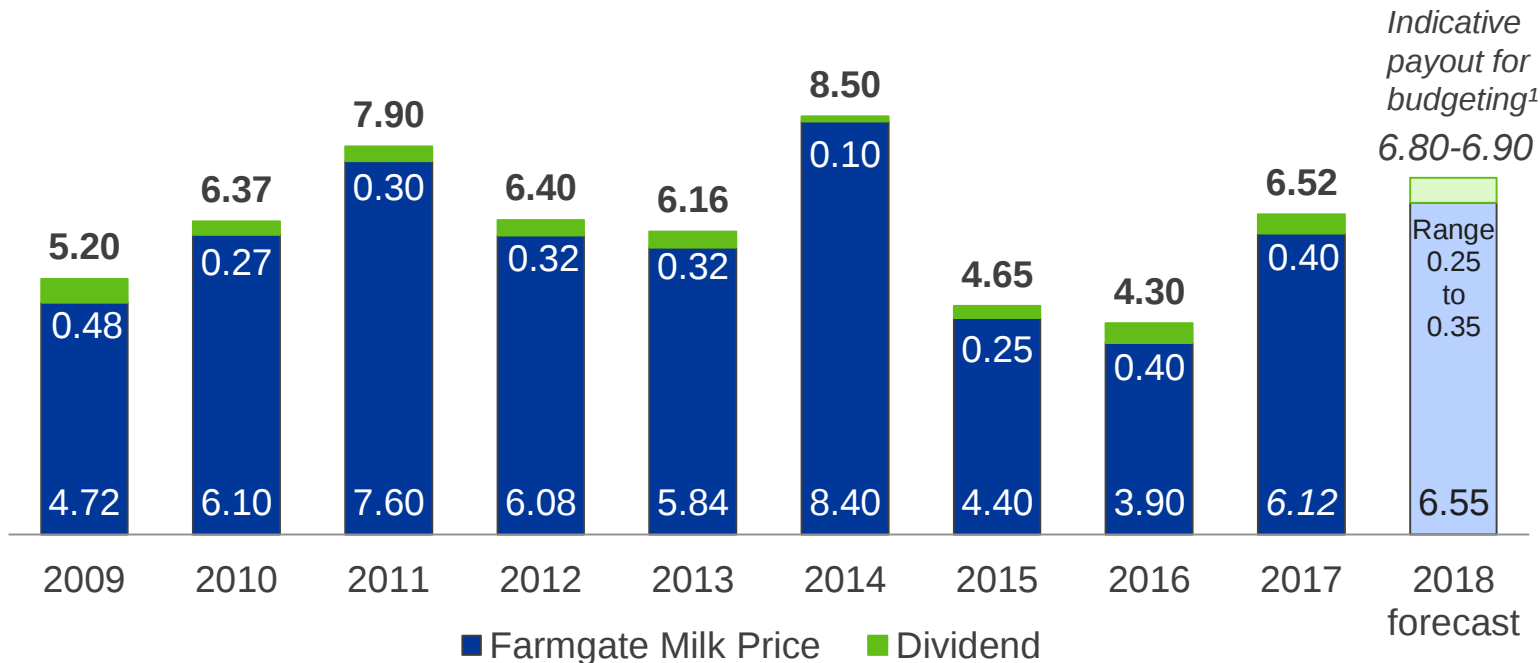
- Comprehensive sustainability report issued
- Creating strong, healthy local environments and communities
- Advancing innovation and investing in the future



Our Co-operative

Higher forecast pay-out for farmers

Improved Farmgate Milk Price, plus forecast dividend range

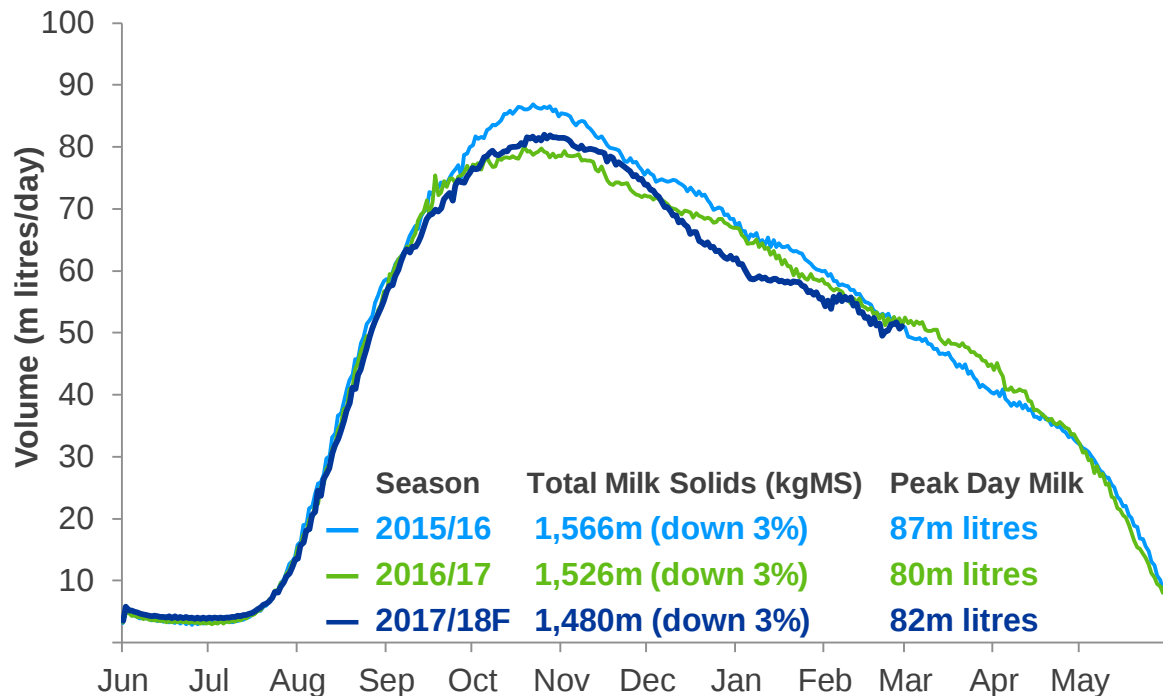


1. For farm budgeting purposes a target full year dividend range of 25-35 cents per share is assumed. The dividend will be calculated in accordance with Fonterra policy of paying out 65-75 per cent of adjusted net profit after tax over time.

Note: Farmgate Milk Price: \$ per kgMS; Dividend: \$ per share

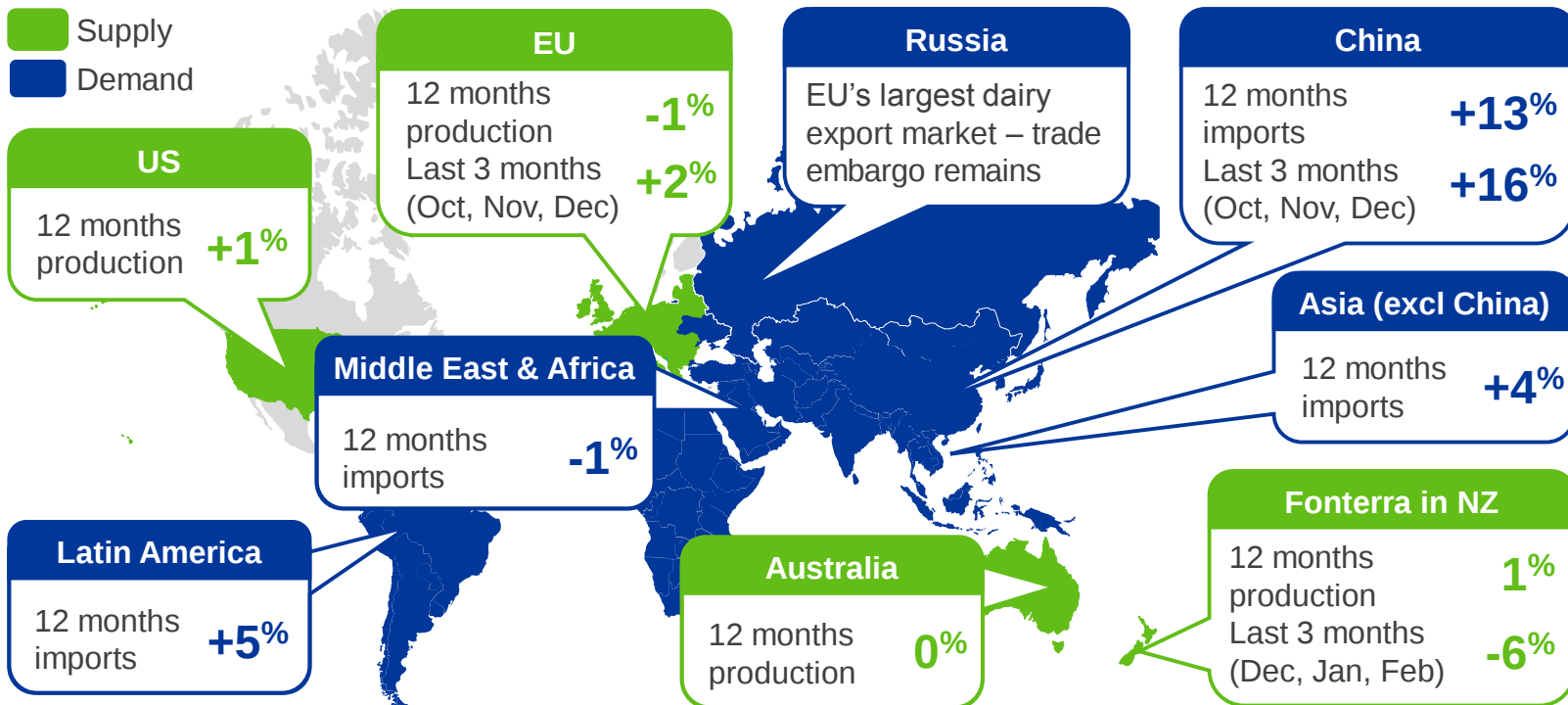
Difficult weather conditions impacted New Zealand supply

Outlook for lower volumes overall this season



- Season forecast is 1,480 million kgMS, 3% down on last year
- Driven by difficult weather conditions impacting pasture growth
- Last season benefited from strong late season collections

Global demand for dairy remains strong



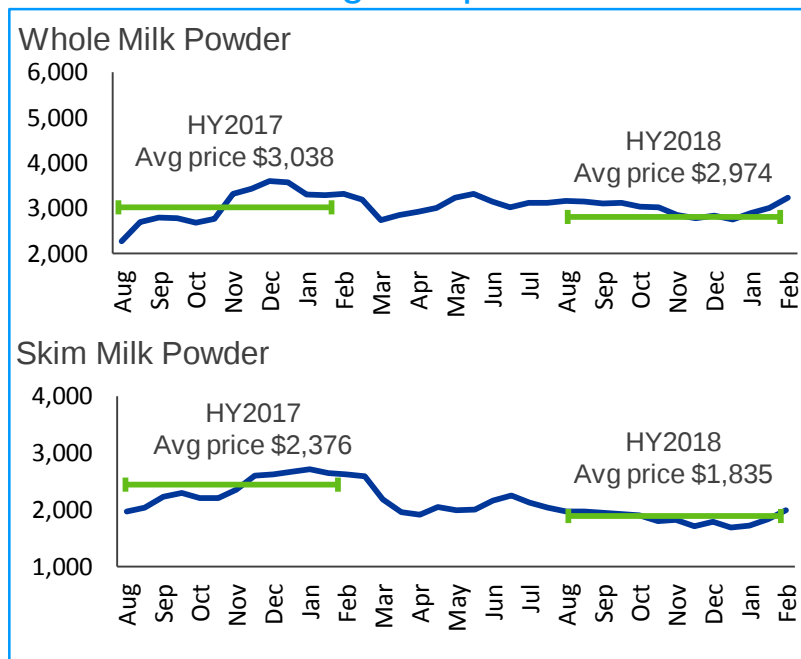
Note: All 12 month figures are rolling 12-months compared to previous comparable period: Australia (Jan), EU (Dec), United States (Dec), China (Dec), Asia (Oct), Middle East & Africa (Oct), Latin America (Oct)

Source: Government milk production statistics; GTIS trade data; Fonterra analysis

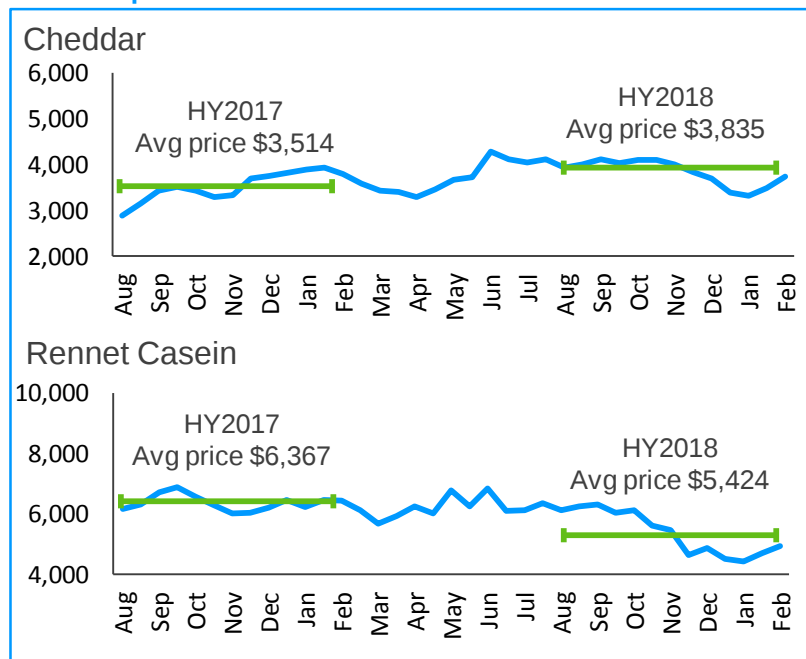
Stable WMP prices – key driver of milk price

Positive stream returns contribute to earnings this half

Products informing milk price



Other products

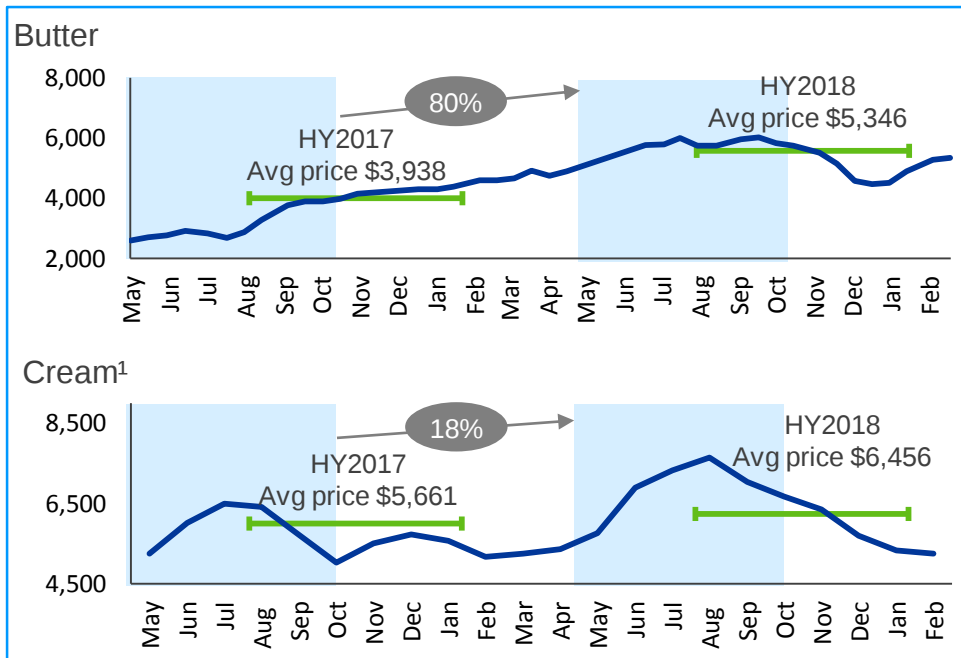


Note: All prices in US dollars per MT, growth rate percentages represent growth for the six months to 31 January 2018. Source: GDT data

HY refers to the six month period ended 31 January

Higher input costs impacting returns

Significant increase in fat prices, particularly butter



- Transfer price for Consumer and Foodservice set quarterly
 - Based on market prices
 - 3-month lag
- Significant increase in commodity prices HY18 vs. HY17
 - Butter prices up 80%
 - Cream¹ prices up 18%

- Pricing period determining the transfer price from Ingredients to Consumer and Foodservice for the six months ended 31 Jan
- Year-on-year growth between pricing periods of May to October
- Average price for the reporting period August to January

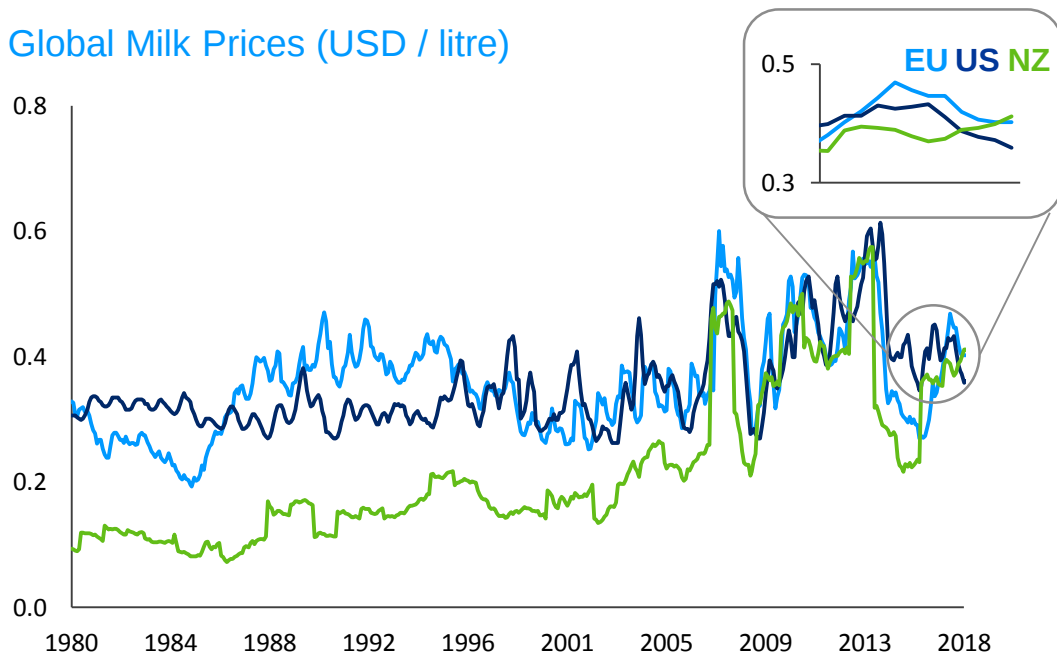
1. Prices for fresh cream have been used as a proxy for UHT cream.

Note: All prices in US dollars per MT, Source: GDT data, Dairy Australia and UDSNZ. HY refers to the six month period ended 31 January

Globally competitive cash pay-out

Driven by our demand-led strategy

Global Milk Prices (USD / litre)



- Higher NZ pay-out this season
- Farmgate Milk Price Manual reinforces competitive milk price
- The 2016 manual change has added six cents per kgMS to milk price for the 2017/18 season-to-date

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 Dec 2017); Fonterra announced pay-out (milk price and dividend) (NZ from Jan 2018); USDA;

European Milk Market Observatory (Netherlands milk price)



Our Potential

Operating performance in line with expectations

Result impacted by lower volumes and abnormal items

VOLUME	REVENUE	GROSS MARGIN	NORMALISED OPEX ¹
10.5B LME	\$9.8B	\$1,662M	\$1,263M
↓ 11%	↑ 6%	↓ 6%	↑ 3%

NORMALISED EBIT	NORMALISED NPAT ²	NET PROFIT AFTER TAX	INTERIM DIVIDEND
\$458M	\$248M	\$(348M)	10CPS
↓ 25%	↓ 36%, EPS ² 15c	↓ 183%	

Ingredients

Volume (LME) ³	↓ 9.8B
Gross Margin	— 11.1%
Normalised EBIT	↑ \$558M

Consumer and Foodservice

Volume (LME) ³	↓ 2.7B
Gross Margin	↓ 23.6%
Normalised EBIT	↓ \$193M

China Farms

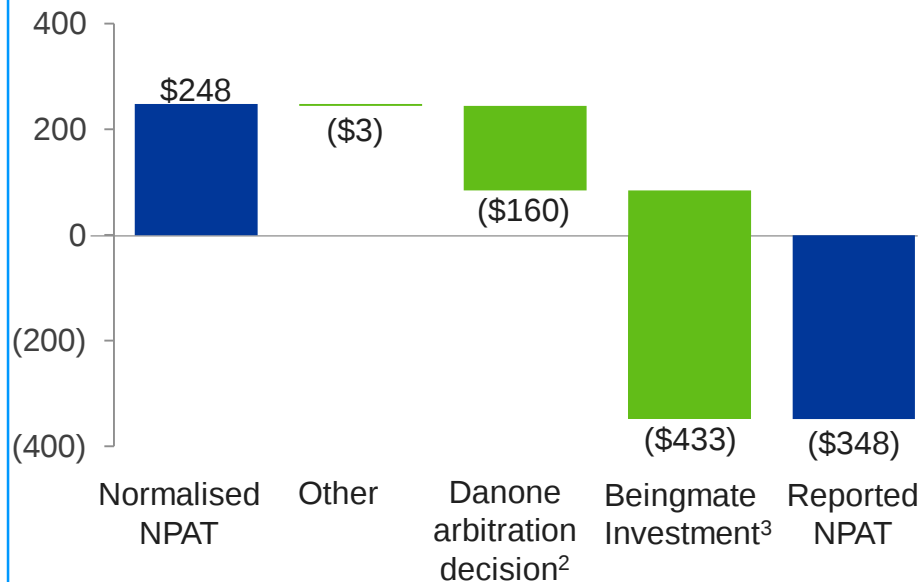
Volume (LME) ³	↓ 0.1B
Gross Margin	↓ (6.1)%
Normalised EBIT	↑ \$(12)M

1. Reported OPEX has been adjusted to normalise the impact of the Danone arbitration. 3. Includes inter-company sales. Prior year volumes include 30m LME of milk powders not included this year.

Result impacted by Danone costs and Beingmate

Normalised earnings better reflect operating performance

Half Year NPAT¹ reconciliation (\$m)



- Normalised NPAT of \$248m
 - Equates to normalised Earning Per Share of 15 cents
 - Total normalisations of \$596m
- Beingmate investment normalisation includes unrealised impairment and share of operating losses
- Danone arbitration decision amount includes the finance costs of the payment and a tax credit

1. NPAT is net profit after tax.

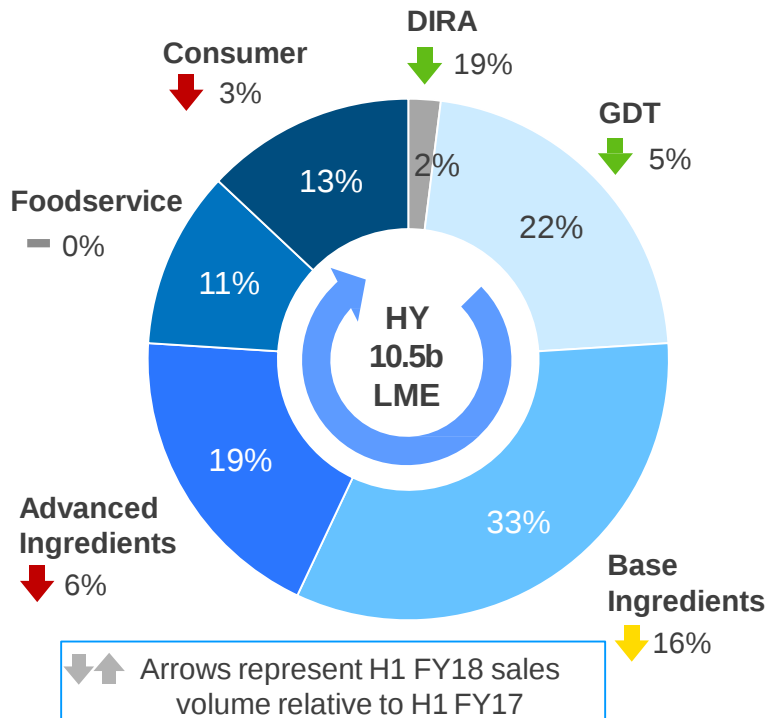
2. Includes \$26m of net finance costs, and \$62m of tax credits.

3. Beingmate investment includes \$405m of impairment and \$28m share of operating losses.

Strategy focussed on moving volume to value

Lower volumes but increased proportion in higher value categories

- 1 **Optimise**
NZ milk
- 2 **Build and grow**
beyond our current
consumer positions
- 3 **Deliver**
on Foodservice potential
- 4 **Grow**
our Anlene™ business
- 5 **Develop**
leading positions in
paed & maternal nutrition
- 6 **Selectively invest**
in milk pools
- 7 **Align**
our business and organisation

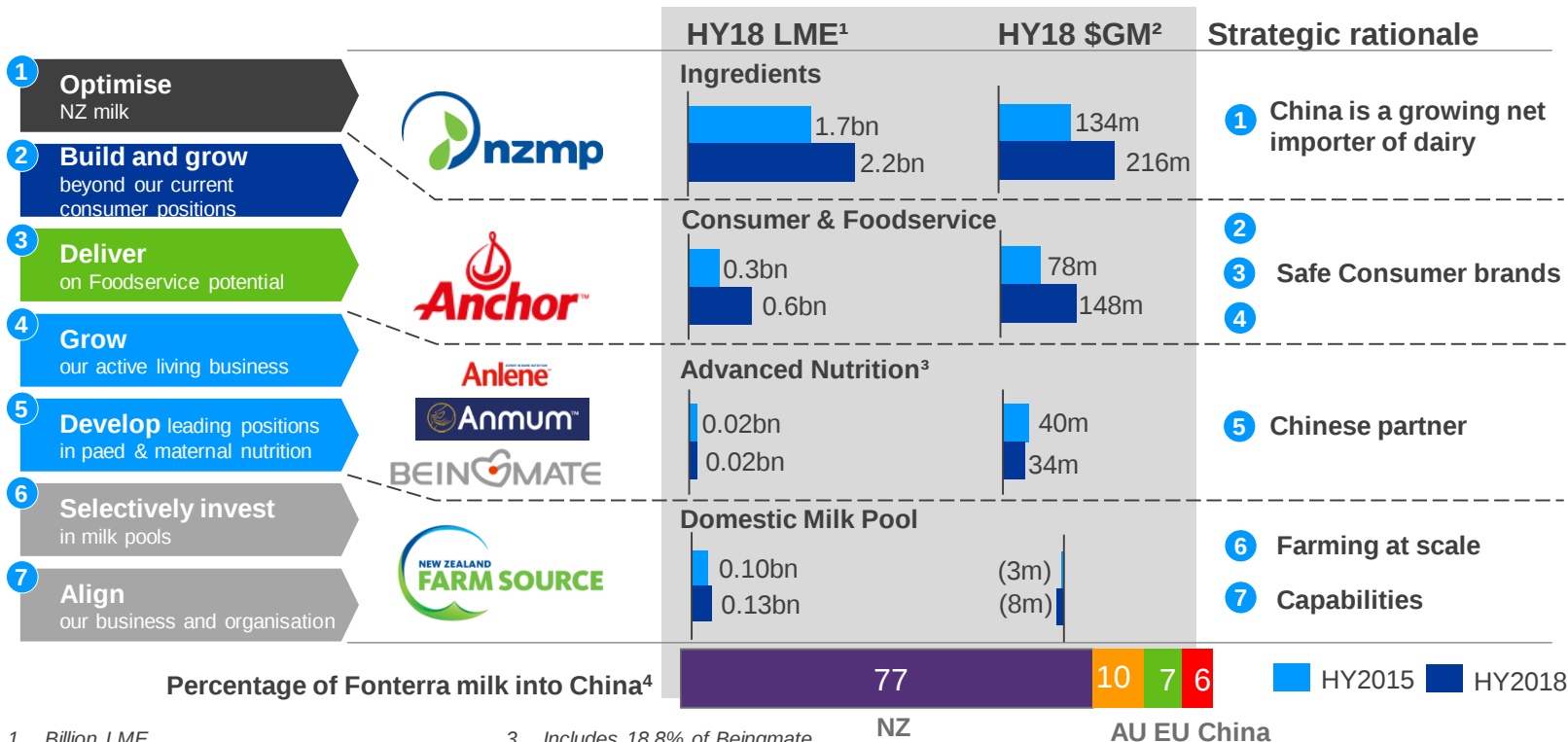


- Volumes down 11% to 10.5b LME
- GDT
 - Volumes aligned with lower production
- Ingredients
 - Lower milk collections, low opening inventory
- Consumer & Foodservice
 - Moved from butter to higher margin cream
 - Challenges in NZ impacting Consumer

Note: Wheel shows percentage of total first six months external sales (LME); Consumer, Foodservice and Ingredients growth rates include intercompany sales

Greater China integrated strategy

Growing volume and value in our most important market



1. Billion LME.

2. Gross margin in \$ million.

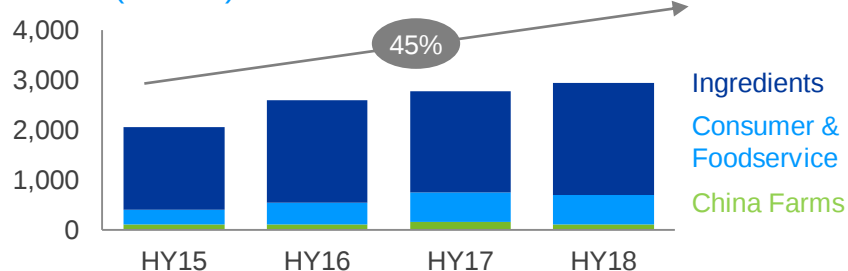
3. Includes 18.8% of Beingmate.

4. Indicative share of sourcing.

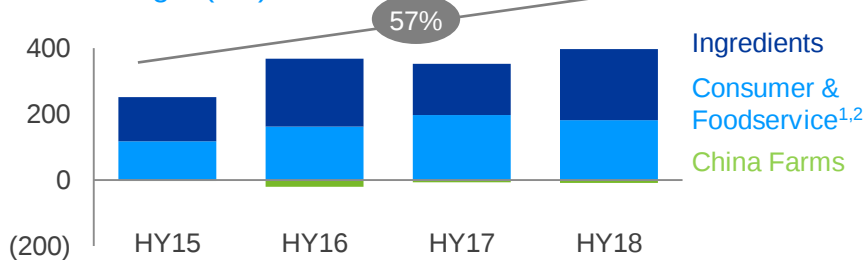
Greater China growing volumes and earnings

Currently 23% of Fonterra total gross margin and 28% of volume

Volume (m LME)



Gross Margin (\$m)



- Our integrated business in Greater China, including Taiwan and Hong Kong, is delivering value
- Gross margin of \$390 million, 23% of total Fonterra gross margin
- From HY15 to HY18:
 - Volume growth of 45% and gross margin growth of 57%
 - Consumer and Foodservice volumes have doubled and gross margin is up 54%
 - Ingredients volumes and gross margin up 36% and 61%

1. Consumer and foodservice includes Quick Service restaurants and corporate overheads allocation.

2. H1 2018 includes normalisation adjustment for Beingmate impairment and share of losses.

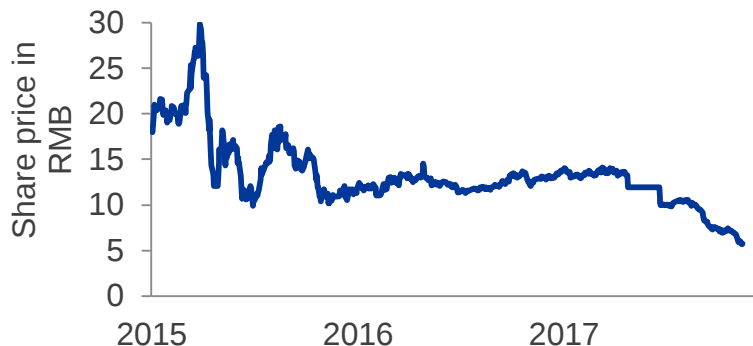
Impairment of Beingmate investment

Asset value now aligned to current share price

Fair value approach

- Estimate of what a market participant would pay for a similar long-term strategic stake
- Based on current share price
- Equivalent to a RMB 5.88 share price
- Reduction in asset value to \$244m after impairment of \$405m and \$28m share of losses
- Can be revalued as share price changes

Declining share price



1 Strategic rationale continues

- Infant formula market growth
- Regulatory opportunity
- Brand equity

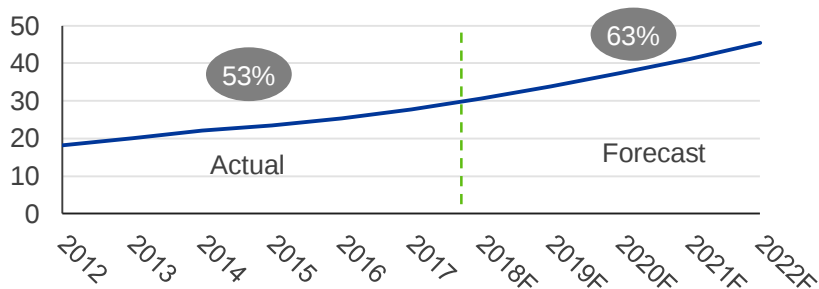
2 Way forward

- Appointment of new CEO
- Implement business transformation
- Continue utilising existing governance structure

China Farms – fresh milk in China

Well positioned for increasing demand for fresh milk

Fresh milk consumption in China – retail sales (RMB bn)¹



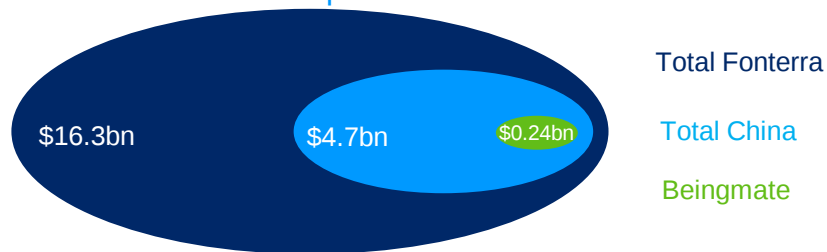
1. Milk consumption in China – packaged food retail sales.

Source: Euromonitor data

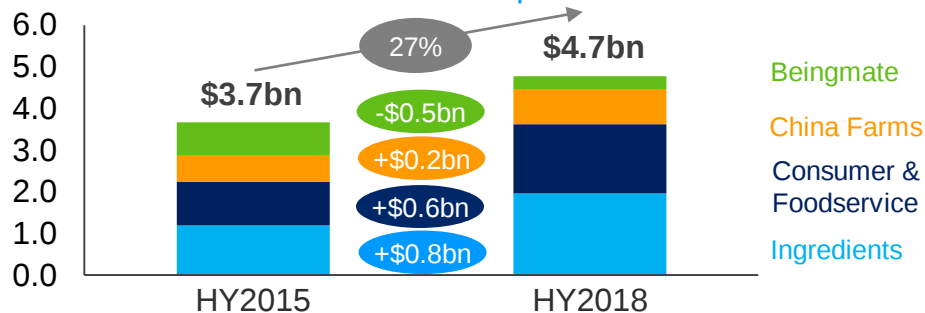
- Market in China is shifting from ambient to fresh milk
 - 6-year growth of 53%, forecast to grow a further 63% in the next five years
- Fonterra is well positioned for this, with current capacity exceeding 400 million LME
- Already moving milk to higher value products
 - Daily fresh milk now in Alibaba's Hema stores
 - Anchor™ barista milk in Starbucks
- Fresh milk sales at a premium

Greater China operations are a substantial business

Breakdown of Fonterra's Enterprise Value for HY2018



Breakdown of Greater China's Enterprise Value



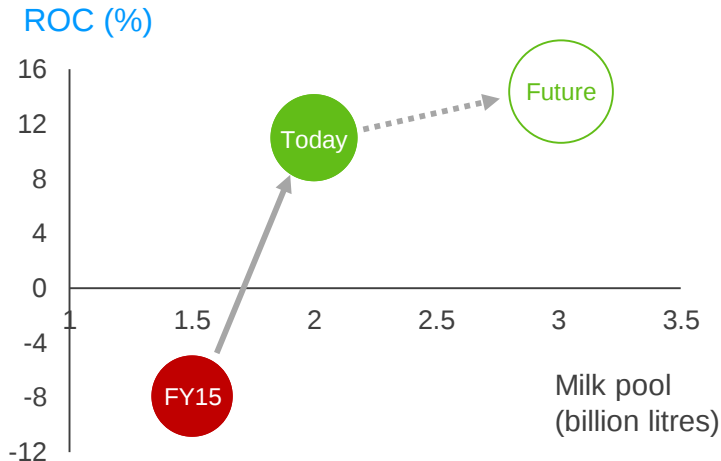
- Based on our current share price, Fonterra's Enterprise Value (EV)¹ exceeds \$16bn
- Greater China's share of EV estimated to be \$4.7bn Beingmate and China Farms included at current book value and balance based on pro-rata share of gross margin
- Conservative estimate relative to valuation of similar China businesses, plus upside potential of China Farms
- Since 2015 the EV of Fonterra's business in Greater China has grown by \$1.0bn or 27%

1. Enterprise value ("EV", being market value of equity plus net economic debt) is based on Fonterra's share price and shares outstanding as at 31 January, plus average net debt for the respective half year period. 2. Greater China's share of EV is calculated as a sum of book value of Farms, plus Fonterra's carrying value of its investment in Beingmate as at 31st January 2018, plus a pro-rata share of EV (excluding Beingmate and Farms) on the basis of gross margin (16% HY15, 23% HY18)

Australia – strategic update

Growing volume and value in Australia

- Continued strong performance from Australia this half year
 - Total Australia normalised EBIT of around \$38m
 - Ingredients gross margin up \$23m or 86%
 - C&FS normalised EBIT stable despite the significant increase in input costs
- We are now Australia's largest milk processor
 - Milk pool has grown by 400m litres of milk this season
 - Our market share has increased 4% – now around 22%
- Playing to our strengths in cheese, whey and nutritionals
 - Stanhope expansion will almost double the size of our new cheese plant over the next two years
 - Further investment in debottlenecking our plants across sites over the next two years



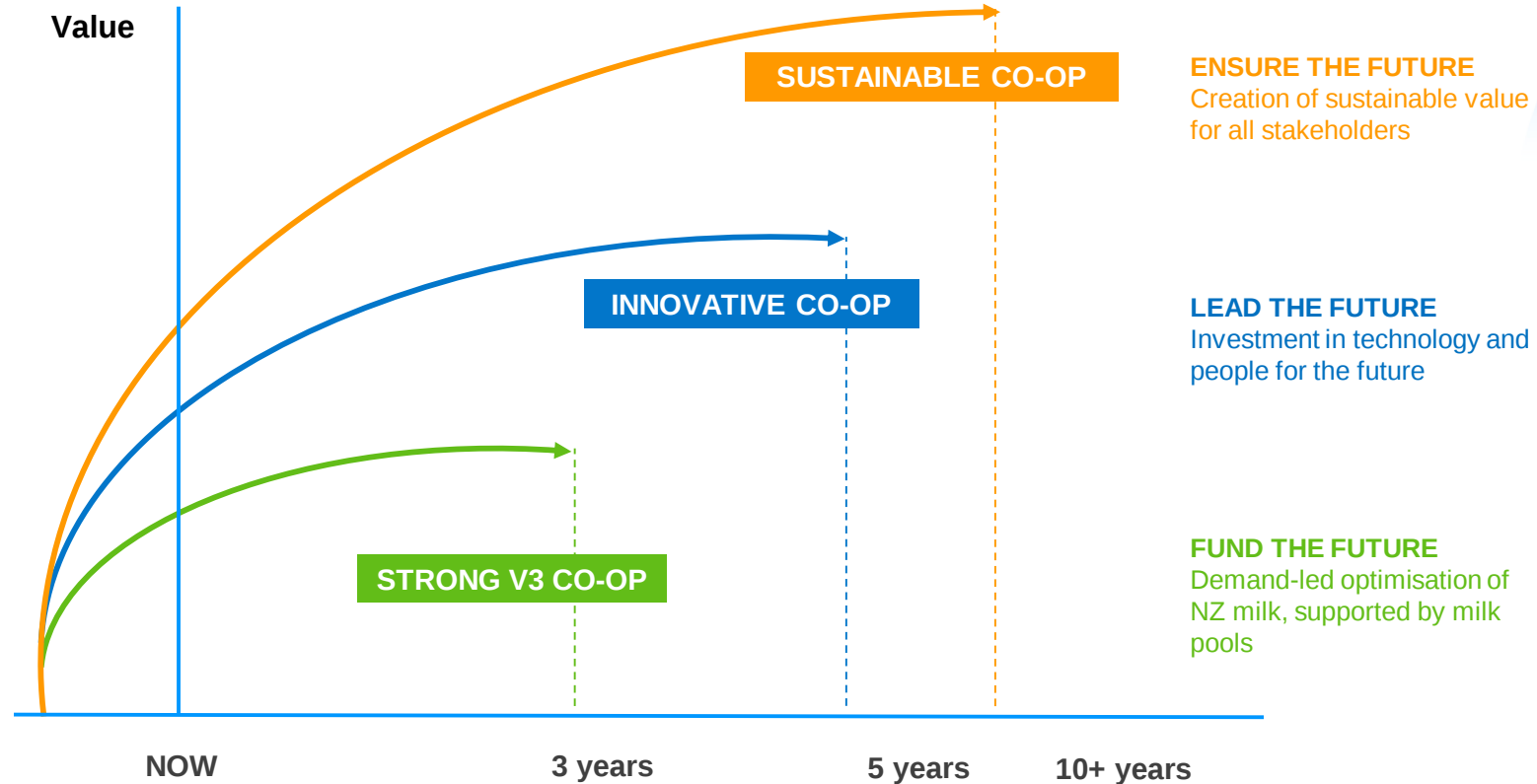
1. FY17 compared with FY15.

A win-win strategic relationship with a2 Milk Company

- Milk pools
 - Source A2 milk from Fonterra farmers in NZ and Australia
 - Expand those pools over time
- Nutritional products
 - Supply of nutritional milk powder products from Fonterra facilities in NZ and Australia
- Distribution and sales networks
 - Opportunity to utilise Fonterra's distribution and sales networks in South East Asia and the Middle East
- a2MC branded product opportunities
 - Exclusive period to develop a2MC butter, and cheese for Australia and NZ and China-sourced fresh milk
- NZ consumer opportunities
 - Exclusive rights to produce, distribute, sell and market a2 Milk™ fresh milk in New Zealand



Our journey to making a difference to the lives of 2 billion people

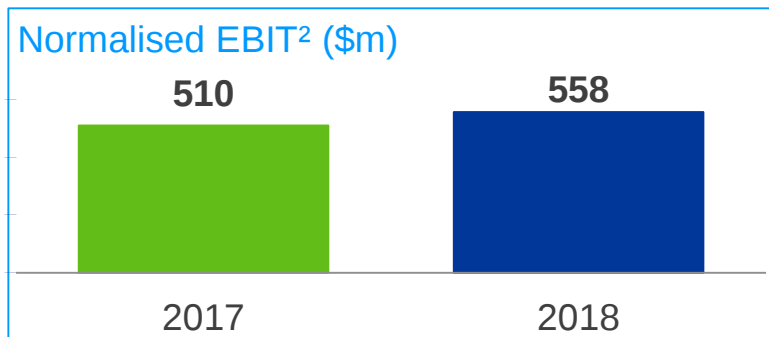
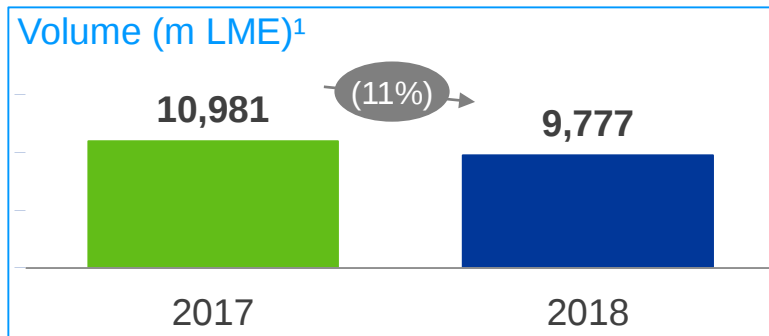




Our Performance

Ingredients

Solid result and with lower collection volumes



1. Includes sales to other strategic platforms.

Volume

- Record low opening inventory
- Unusual profile of milk collection in New Zealand due to difficult weather conditions

Value

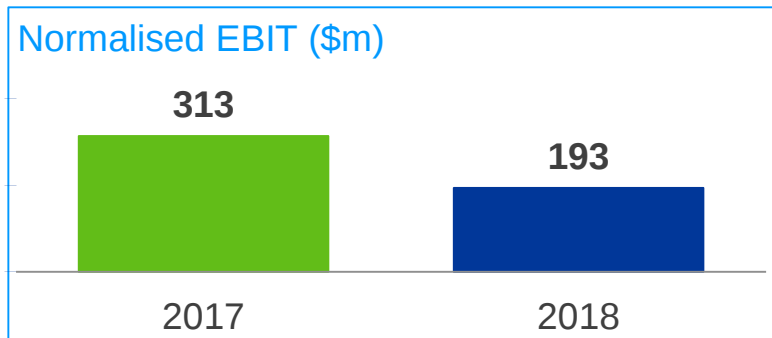
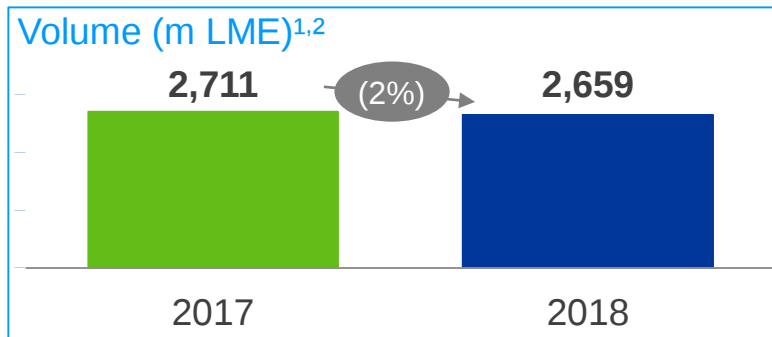
- Normalised EBIT growth of \$48m, an increase of 9%
- Positive stream returns of \$90m, \$50m ahead of prior period
- Lower price achievement due to increased competition in our protein portfolio
- Improvements in our Australian product mix

Velocity

- UHT expansion at Waitoa, cream cheese plant at Darfield and a new mozzarella plant at Clandebye
- Our innovation pipeline is continuing to drive new products in our Advanced Ingredients portfolio

Consumer and Foodservice

Areas of volume growth but tighter margins from higher input costs



1. Includes sales to other strategic platforms.

2. On a comparable business basis volumes were down 1% due to transferred/discontinued businesses this period

Volume

- Holding volumes despite shift in product mix away from butter, as consumer demand responds to higher prices
- Consumer volumes impacted by exit from parts of our private label portfolio and operational challenges in NZ
- Full year target of an additional 400m LME remains

Value

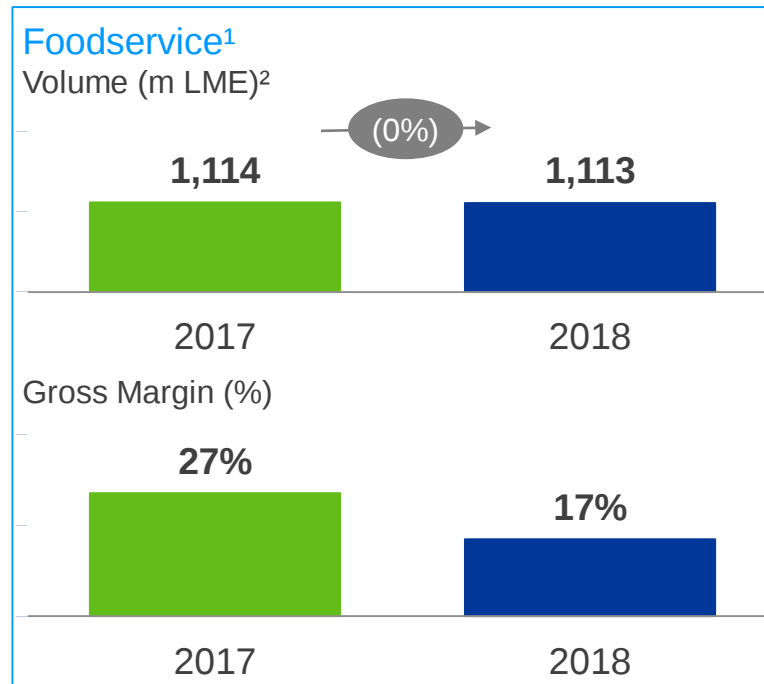
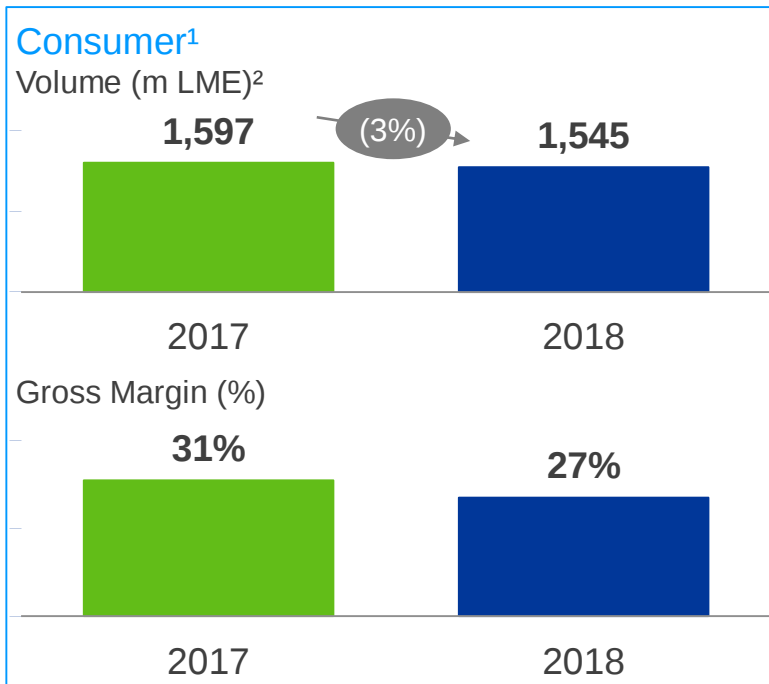
- Tighter margins compared to HY17
 - Increased pricing contributed \$301m to earnings
 - However not able to fully recover the \$420m impact of significantly higher input costs
- NZ operational challenges impacting Oceania

Velocity

- Successful relaunch of Anlene in South East Asia
- Accelerated product development in China
 - Fresh milk into Alibaba's Hema Fresh stores

Consumer and Foodservice

Robust consumer margins largely absorb higher input costs



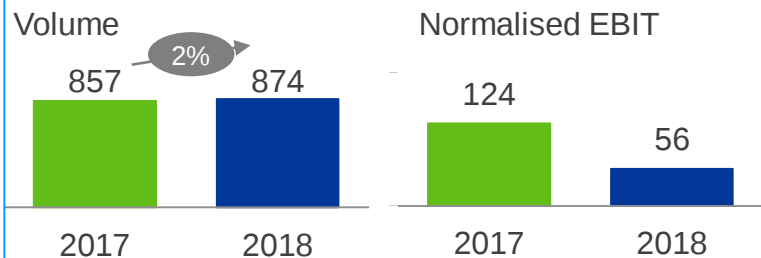
1. On a comparable business basis Consumer volumes were 2% down due to transferred/discontinued businesses this period.

2. Includes sales to other strategic platforms.

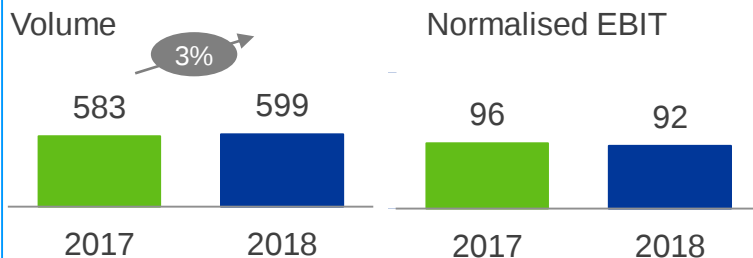
Consumer and Foodservice

Solid performance in Greater China and Latin America

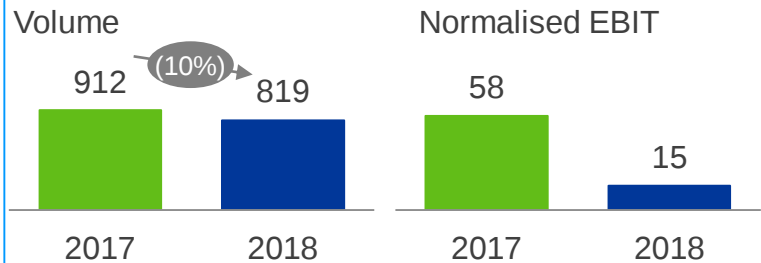
Asia



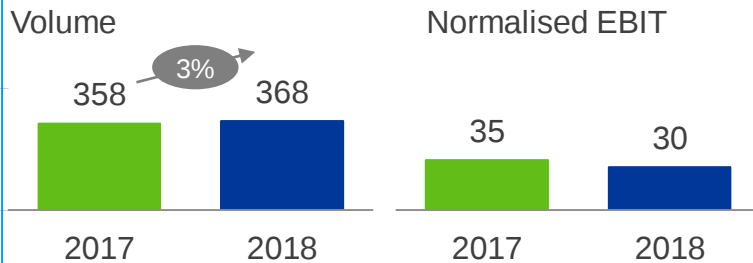
Greater China



Oceania¹



Latin America¹



1. On a comparable business basis volumes in Oceania were 8% down due to transferred/discontinued businesses this period.

Note: All volumes include intercompany sales

Strong Co-op and financial discipline continues

Higher half year debt and gearing but reducing at full year

GEARING¹

51.6%

↑ Up from 46.6%

NET DEBT²

\$7.1B

↑ 15%

WORKING CAPITAL

80 DAYS

↑ Up 12 days

CAPEX

\$346M

↑ 42%

CREDIT RATING

A

STABLE

Fitch

A-

STABLE

S&P

1. Gearing ratio is economic net interest-bearing debt divided by economic net interest-bearing debt plus equity excluding cash flow hedge reserve.

2. Economic net interest-bearing debt.

Summary and outlook for second half of FY18

Operating performance in line with expectations

- Solid Ingredients' results with low opening inventory and lower collection volumes
- Consumer and Foodservice achieved areas of volume growth but tighter margins from higher input costs
- Danone costs and Beingmate impairment impacted overall result
- Balance sheet and cash flows remain strong

Forecast Farmgate Milk Price of \$6.55 per kgMS

- Strong global demand reflected in prices
- Full-year New Zealand milk collection forecast is 3% lower than last year

Forecast payout range for budgeting \$6.80-\$6.90

- Forecast normalised earnings range maintained
- Earnings will be weighted towards the second half of FY18
- A full year dividend range of 25-35 cents per share

The background of the slide is an abstract composition of several overlapping, flowing shapes in various shades of blue and green. The shapes create a sense of movement and depth, with some areas being more saturated than others. The overall effect is modern and professional.

Supplementary Information

Normalised EBIT reconciliation

\$ million	Six months ended 31 January 2018	Six months ended 31 January 2017
Profit after tax	(348)	418
Add: Net finance costs	201	157
(Less):Add: Taxation (credit)/expense	(29)	69
Total reported EBIT	(176)	644
Add: Danone recall costs	196	—
Add: Reduction in carrying value of Beingmate	433	—
Less: Gain on Darnum sale (part share to JV)	—	(42)
Add: Time value of options	5	5
Total normalisation adjustments	634	(37)
Total normalised EBIT	458	607

New Zealand Ingredients product mix

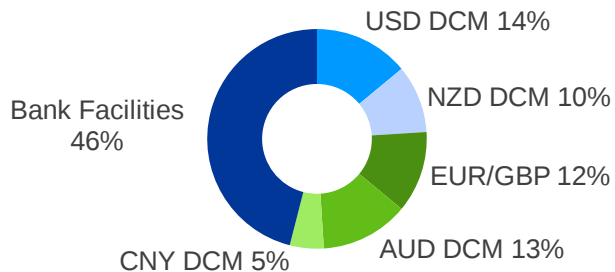
	Six months ended 31 January 2018		Six months ended 31 January 2017	
	\$ million	\$ per MT	\$ million	\$ per MT
Sales volume (000 MT)				
Reference products	900	–	973	–
Non-reference products	277	–	338	–
Revenue				
Reference products	4,305	4,783	3,768	3,873
Non-reference products	1,586	5,726	1,758	5,201
Cost of milk				
Reference products	3,316	3,684	2,901	2,982
Non-reference products	830	2,995	1,013	2,997
Gross margin				
Reference products	372	413	246	253
Non-reference products	362	1,309	398	1,178

Note: Reference products are products used in the calculation of the Farmgate Milk Price – WMP, SMP, BMP, Butter and AMF; Milk solids used in the products sold were 488 million kgMS reference and 146 million kgMS non-reference (previous comparable period 547 million kgMS reference and 190 million non-reference)

Diversified and prudent funding position

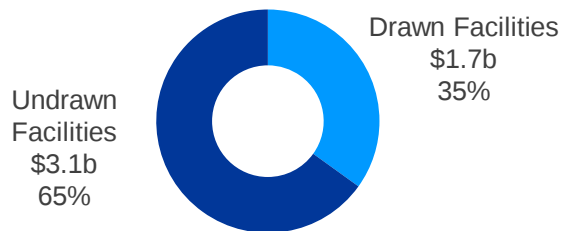
Diversified profile¹

At 31 January 2018



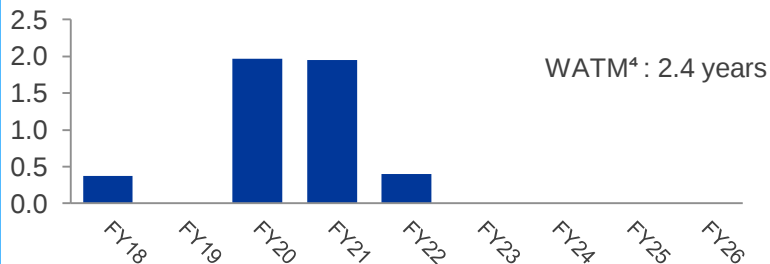
Prudent liquidity

At 31 January 2018 (\$ billion)



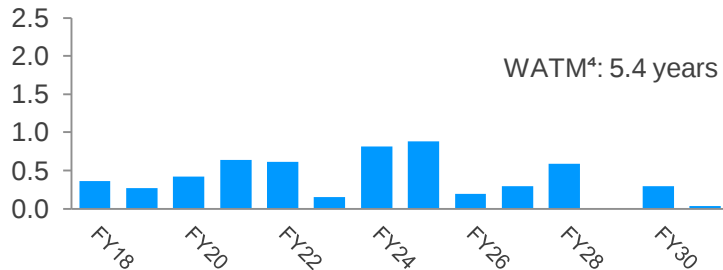
Bank facility maturity profile²

At 31 January 2018 (\$ billion)



DCM maturity profile³

At 31 January 2018 (\$ billion)



1. Includes undrawn facilities and commercial paper.

2. FY18 maturity represents short-term working capital borrowings subsidiaries.

3. Excluding commercial paper.

4. WATM is weighted average term to maturity.