

# GLOBAL DAIRY UPDATE



- Demand for dairy remains strong in China and Asia. Middle East and Africa and Latin America imports decline.



- Dairy exports from New Zealand and the USA continue to decline. Export growth from the EU increasing.



- Further increase in monthly European milk production. New Zealand production improved in November, however continues to be impacted by weather.



- In November, Fonterra New Zealand milk collection increased 3% to 199 million kgMS and Fonterra Australia milk collection increased 28% to 17 million kgMS.

- 2018 first quarter business update.
- Forecast Farmgate Milk Price for the 2017/18 season reduced to \$6.40 per kgMS.
- Milk collection forecast reduced to 1,525 million kgMS, in line with last season.
- Forecast earnings guidance of 35-45 cents per share announced following the Danone arbitration decision.



- Fonterra's first Sustainability Report released.
- Planting the Ashburton Hakatere River Trail.

## KEY DATES



28 February 2018  
Deadline for Application to  
Supply Fonterra

Late March 2018  
FY18 Interim Results  
Announcement

Late May 2018  
Q3 Business Update  
Announcement

1 June 2018  
Measurement Date for Share  
Standard 2018/19 Season



To view a chart that illustrates year-on-year changes in imports –

## DEMAND FOR DAIRY REMAINS STRONG IN CHINA AND ASIA.

### MIDDLE EAST AND AFRICA AND LATIN AMERICA IMPORTS DECLINE

#### LATIN AMERICA

**7%↑**

Import change for the 12 months to August 2017

**Latin America's dairy import volumes<sup>1</sup>** declined 5% in August compared to the same month last year. This decline was largely due to WMP imports, which were down 43% this month, offset by small increases in fluid and fresh dairy and whey powder.

For the 12 months to August, imports were up 7%, or 124,000 MT, compared to the same period the previous year.

Growth in imports was primarily driven by cheese, SMP and MPC/MPI which for the 12 months to date, were up a combined 13%, or 104,000 MT.

#### ASIA

**7%↑**

Import change for the 12 months to August 2017

**Asia (excluding China) dairy import volumes<sup>1</sup>** increased 5% in August compared to the same month the previous year. This growth continues to be driven by imports of SMP, largely from the Philippines.

For the 12 months to August, imports were up 7%, or 309,000 MT, compared to the same period last year.

Increases continue to be seen across all key import categories, in particular SMP, cheese and fluid and fresh dairy, which were up a combined 9%, or 193,000 MT.

#### MIDDLE EAST & AFRICA

**3%↓**

Import change for the 12 months to August 2017

**Middle East and Africa dairy imports<sup>1</sup>** in August decreased 9%, or 30,000 MT, compared to the same month the previous year.

Butter, WMP and fluid and fresh dairy led the decline, down a combined 28,000 MT.

Imports for the 12 months to August were down 3%, or 114,000 MT. Large declines were seen in WMP, butter, infant formula and cheese, down a combined 167,000 MT. These declines were partially offset by increases in fluid and fresh dairy and SMP, the region's largest import categories, up 68,000 MT and 22,000 MT respectively.

#### CHINA

**13%↑**

Import change for the 12 months to October 2017

**China dairy imports** increased 28%, or 43,000 MT, in October compared to the same month last year.

Imports across all major categories showed growth in October, in particular fluid and fresh dairy which grew 16,000 MT, or 31%.

Imports for the 12 months to October were up 287,000 MT compared to the same period last year. Strong import demand out of China continues with all key categories up for the period. WMP, infant formula and SMP imports all grew significantly, up 80,000 MT, 69,000 MT and 52,000 MT respectively.

<sup>1</sup> Estimates are included for those countries that have not reported import data.



## DAIRY EXPORTS FROM NEW ZEALAND AND US CONTINUE TO DECLINE. EXPORT GROWTH FROM THE EU INCREASING

To view a chart that  
illustrates year-on-year  
changes in exports –

### NEW ZEALAND

**4%** ↓

Export change for the 12  
months to October 2017

**Total New Zealand dairy exports** in October decreased 7%, or 23,000 MT, compared to the same month last year. The decline was driven by AMF, butter and WMP, down a combined 27,000 MT.

Exports for the 12 months to October were down 4%, or 120,000 MT, on the previous comparable period. Exports declined across most categories except fluid and fresh dairy and infant formula, which were up a combined 76,000 MT. The three largest export categories, WMP, SMP and cheese, declined a combined 4%, or 80,000 MT.

### AUSTRALIA

**1%** ↓

Export change for the 12  
months to October 2017

**Australian dairy exports** increased 12%, in October compared to the same month last year. Key drivers were fluid and fresh dairy, cheese and infant formula which were up a combined 28%, or 10,000 MT.

Exports for the 12 months to October were down 1% on the previous comparable period.

Fluid and fresh dairy and infant formula exports remain strong, up 24,000 MT, however declines in most other export categories led to an overall decline of 1%, or 10,000 MT.

### EUROPEAN UNION

**4%** ↑

Export change for the  
12 months to August 2017

**EU dairy exports** in August were up 6%, or 27,000 MT, relative to the same month the previous year.

Exports of SMP were up again this month, an increase of 79%, or 30,000 MT, compared to the same month last year. Europe's largest export category, fluid and fresh dairy, showed a decline of 2% for the month.

Exports for the 12 months to August were up 4%, or 204,000 MT, on the previous comparable period. SMP, infant formula, cheese and lactose exports increased a combined 297,000 MT, in part offset by declines in fluid and fresh dairy, butter and AMF.

### USA

**7%** ↑

Export change for the 12  
months to October 2017

**US dairy exports** decreased 10% in October, or 22,000 MT, compared to the same month the previous year. The decline in October is due to a reduction in SMP exports, down 25,000 MT, or 33%.

Exports for the 12 months to October were up 7%, or 152,000 MT, on the previous comparable period. The increase in exports continues to be driven by cheese and whey powder, up a combined 113,000 MT.



To view a chart that illustrates year-on-year changes in production –

## FURTHER INCREASE IN MONTHLY EUROPEAN MILK PRODUCTION.

NEW ZEALAND PRODUCTION IMPROVED IN NOVEMBER, HOWEVER CONTINUES TO BE IMPACTED BY WEATHER

### NEW ZEALAND

1% ↑

Production change  
for the 12 months to  
November 2017

**Total New Zealand milk production** in November was up 4% compared to the same month last year. This is largely due to improved weather conditions towards the end of spring and through early November. Dry weather across the country, has caused soil moisture and pasture quality to decrease, impacting collections in late November.

Dry conditions are expected to continue and intensify, which would significantly impact New Zealand production.

For the 12 months to November milk production was up 1% compared to the same period the previous year.

Fonterra collections have been reported for November, see page 5 for details.

### AUSTRALIA

2% ↓

Production change  
for the 12 months to  
October 2017

**Australia production** in October increased 7% compared to the same month last year due to favourable spring conditions across all major collection regions compared to wet September/October conditions last year.

Production for the 12 months to October was down 2% compared to the same period the previous year due to particularly poor spring conditions in 2016.

Fonterra collections in Australia have been reported for November, see page 5 for details.

### EUROPEAN UNION

0%

Production change  
for the 12 months to  
October 2017

**EU production** increased 7% in October compared to the same month last year, driven by strong global dairy prices.

France, Germany and the United Kingdom had the largest increases in production, up 7%, 9% and 5% respectively, in October.

Production for the 12 months to October was flat. While Ireland, Poland and Italy were up a combined 5%, however Germany and France, Europe's largest producers, were down a combined 2%.

### USA

2% ↑

Production change  
for the 12 months to  
October 2017

**US production** in October increased 1% compared to the same month last year largely due to increased productivity, as milk production per cow across all 23 major states continued to improve.

Milk production for the 12 months to September increased 2% compared to the same period the previous year.

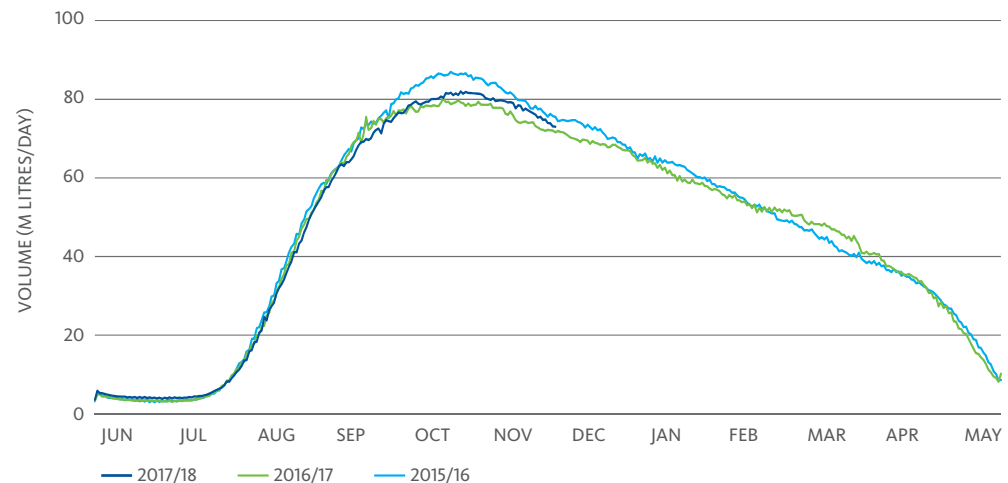
## OUR MARKETS

# FONTERRA MILK COLLECTION 2017/18 SEASON



To view a table that shows our detailed milk collection in New Zealand and Australia compared to the previous season –

### NEW ZEALAND MILK COLLECTION



#### NEW ZEALAND

**1%↑**

Increase for the season from 1 June to 30 November

Fonterra's milk collection across New Zealand for the six months to 30 November reached 702 million kgMS, 1% above the same period last season.

November collections reached 199 million kgMS. This is 3% ahead of last year, although collections in November last year were well down on more usual levels. Recent dry weather across the country, particularly in the lower North Island has caused soil moisture and pasture quality to decrease, impacting collections in late November and early December. This has supported our decision to bring the forecast milk collection for the 2017/18 season down to 1,525 million kgMS.

#### NORTH ISLAND

**1%↑**

Increase for the season from 1 June to 30 November

**North Island milk collection** in November reached 118 million kgMS, 1% up on November last season.

#### SOUTH ISLAND

**2%↑**

Increase for the season from 1 June to 30 November

**South Island milk collection** in November reached 81 million kgMS, 5% up on November last season.

#### AUSTRALIA

**26%↑**

Increase for the season from 1 July to 30 November

Fonterra's milk collection across Australia for the five months to 30 November reached 70 million kgMS, 15 million kgMS or 26% higher than last season.

Collections in November were up 28% on the same month last year. Growth has been driven by new suppliers who have moved to Fonterra in the past year and strong seasonal conditions across all regions.

## OUR MARKETS

# FONTERRA GLOBALDAIRYTRADE RESULTS



Fonterra GDT results at  
last trading event  
**19 December 2017:**

**3.3%** ↓

Change in Fonterra's  
weighted average product  
price from previous event

USD **3,008**

Fonterra's weighted  
average product price  
(USD/MT)

**28.6** <sup>000</sup> MT

Fonterra product quantity  
sold on GDT

### CHEDDAR

**8.3%** ↓

USD 3,389/MT

### RENNET CASEIN

**7.6%** ↓

USD 4,506/MT

### AMF

**6.5%** ↓

USD 6,392/MT

### SMP

**5.1%** ↓

USD 1,689/MT

### WMP

**2.7%** ↓

USD 2,755/MT

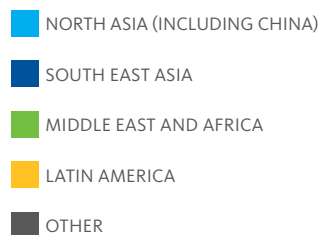
### BUTTER

**2.2%** ↓

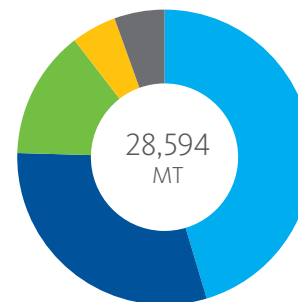
USD 4,474/MT

Fonterra GDT sales  
by destination:

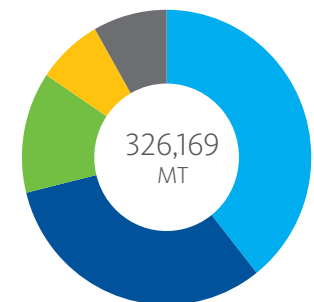
To view more information,  
including a snapshot of the  
rolling year-to-date results –



### LATEST AUCTION



### FINANCIAL YEAR-TO-DATE



► The next trading event will be held on 2 January 2018. Visit [www.globaldairytrade.info](http://www.globaldairytrade.info) for more information.

## Dairy commodity prices and New Zealand dollar trend

The New Zealand dollar  
remained volatile in  
November but ultimately  
finished the month close  
to unchanged.





## 2018 THREE-MONTH BUSINESS UPDATE

### VOLUME

**3.9**<sup>B LME</sup>

↓ DOWN 20%

### REVENUE

**\$4.0**<sup>B</sup>

↑ UP 4%

### GROSS MARGIN

**16.7**%

↓ DOWN FROM 21.9%

### OPEX

**\$636**<sup>M</sup>

↑ UP 2%

### CAPEX

**\$142**<sup>M</sup>

↑ UP 22%

Fonterra's performance for the three months to 31 October was broadly in line with expectations. Overall volume was down 20% to 3.9 billion LME, reflecting low opening inventories and milk collection phased towards the end of the quarter. Despite these lower volumes, revenue increased 4% to \$4.0 billion due to strong global pricing and demand, and the business' continued efforts to drive more volume into higher-value products.

New Zealand Ingredients experienced a challenging first quarter. The historically low opening inventory levels and phasing of milk collections outlined above, limited our ability to achieve additional sales volumes. Total gross margin percentage in the Ingredients business was lower than the first quarter

of FY17 but in line with the second half of FY17.

The Consumer and Foodservice business delivered a solid first quarter. Our businesses in Greater China and Asia delivered increased sales despite significantly higher input costs however volumes are slightly down overall on last year. We continue to target 400 million incremental LMEs into Consumer and Foodservice for the full year. Overall gross margin percentage was 24% for the three months to October. While this is down on the first quarter last year which benefited from lower input costs, it is ahead of the final quarter of FY17.

Our China Farms operations achieved volume growth of 6% for the year-to-date, as both hubs operate to near

full capacity. Performance improved due to efforts to reduce operating costs and the change in strategic focus implemented last year.

Capital expenditure of \$142 million is in line with our expectations for this stage in the financial year, with an expected full year spend of around \$800 million.

## THE OUTLOOK

In early December 2017, Fonterra reduced the forecast Farmgate Milk Price for the 2017/18 season by 35 cents to \$6.40 per kgMS.

This decision reflects a prudent approach to ongoing volatility in the global dairy market.

The forecast milk collection for the season has also been reduced to 1,525 million kgMS in line with the previous season, as a result of the continued challenging weather conditions across the country.

In response to the outcome of the Danone arbitration proceedings, our forecast earnings per share range has been revised to 35 to 45 cents. This means that the total available for payout to farmers in the 2017/18 season is forecast to be \$6.75-\$6.85 before retentions.





## NEW ZEALAND INGREDIENTS

### Fonterra manufactures five commodity products that inform the Farmgate Milk Price.

These are referred to as reference products. All other products are referred to as non-reference products. The pricing relativities between reference product prices and non-reference product prices are known as stream returns and can impact Fonterra's gross margins.

Reference products are whole milk powder (WMP), skim milk powder (SMP), butter, anhydrous milk fat (AMF), and butter milk powder (BMP).

New Zealand milk collections for the season to October were flat compared to the same period last year. While there was some recovery in collections towards the back half of October, heavy rainfall throughout spring put significant pressure on production over the peak. Dry weather across the country in November and early December particularly in the lower North Island has caused soil moisture and pasture quality to decrease, impacting recent collections. This has contributed to our decision to bring the forecast collection for the 2017/18 season down to 1,525 million kgMS, broadly in line with last year.

Sales for the first quarter were over 20% lower than the same period last

year due to both lower opening inventory and milk collections being weighted towards the end of the quarter.

If dry conditions continue through the summer collections are likely to be impacted, further affecting sales in our ingredients business.

Revenue was up significantly on the back of higher prices for both reference and non-reference products. These higher prices account for some of the decline in gross margin percentage. The remainder of the impact was due to a lower regulated return, lower price achievement per metric tonne, and higher fixed costs given the lower volumes.

As sales increase over the remainder of the year, we expect total gross margins to improve, however this is likely to be weighted towards the second half of the year.

Despite reference prices increasing versus last quarter and non-reference prices declining, overall stream returns are balanced for the period. This reflects strong demand for our protein and cheese products, both from external customers and in our foodservice business, and supports a production mix shift towards non-reference products, up 9% versus a 1% decrease in reference products.

	Q1 FY17	Q2 FY17	Q3 FY17	Q4 FY17	Q1 FY18	CHANGE Q1 FY17 TO Q1 FY18
<b>PRODUCTION VOLUME<sup>1</sup> (000 MT)</b>						
Reference products	588	704	461	84	583	(1%)
Non-reference products	218	239	221	71	237	9%
<b>SALES VOLUME<sup>1,2</sup> (000 MT)</b>						
Reference products	369	604	386	481	287	(22%)
Non-reference products	164	211	185	212	130	(21%)
<b>REVENUE<sup>1,2</sup> (\$ PER MT)</b>						
Reference products	3,452	4,130	4,798	4,618	4,928	43%
Non-reference products	4,955	5,370	5,781	6,094	5,777	17%

1 Excludes bulk liquid milk.

2 Excludes China and Latin America foodservice sales and revenue which is included in the production volume.



# OUR PERFORMANCE

## CONSUMER AND FOODSERVICE



Our strategy is to convert as much milk as possible into higher-value products.

Consumer and Foodservice delivered a solid performance for the three months to 31 October 2017 on the back of a very strong first quarter last year.

Our key regions of Greater China and Asia grew as demand in the foodservice channel continues to grow, however overall volumes

decreased by 3% to 1.3 billion LME.

Gross margin of 24% is behind the same period last year, reflecting significantly higher input costs compared to the first quarter of FY17.

Product mix has also changed this quarter as customers respond to rising

prices. The business has maintained a strong focus this quarter on moving sales into higher-returning products rather than growing absolute sales volume.

### CONSUMER AND FOODSERVICE THREE-MONTH PERFORMANCE

	ASIA	GREATER CHINA	LATIN AMERICA	OCEANIA	TOTAL
<b>VOLUME (M LME)</b>					
First quarter FY18	427	273	181	412	1,293
First quarter FY17	414	271	184	469	1,338
% Change	3%	1%	(1%)	(12%)	(3%)
<b>GROSS MARGIN (%)</b>					
First quarter FY18	23%	29%	29%	18%	24%
First quarter FY17	33%	39%	33%	24%	31%

#### GREATER CHINA

Greater China delivered volumes of 273 million LME for the three months to 31 October, an increase of 1%, on the back of a very strong first quarter last year. The decline in gross margin percentage was largely due to the significant increase

in input costs and the resulting shift in product mix, as demand moved in response to price changes. The business has remained focused on converting as much volume as possible into higher-value products.

#### OCEANIA

In the previous comparable period volumes included sales from divested businesses in Australia. Adjusting for this, Oceania volumes declined 8%. This overall decline was in part due to heavy competition in the New Zealand market.

Gross margins in Oceania also declined on the back of higher input costs and a changing product mix in response to higher prices this year.

#### ASIA

The Asia region delivered volume growth of 3% compared to the first quarter last year, with a total of 427 million LME sold. Our foodservice business continues to perform well, delivering further volume

growth on a very strong quarter one last year. Gross margin percentage was behind last year, due to higher input costs and a change in mix.

#### LATIN AMERICA

Our Soprole business continues to perform well in Chile, with volume growth and strong market positioning. The overall Latin America result continues to be impacted by challenging conditions in Venezuela and Brazil.

While the economy in Brazil is showing some early signs of improvement, the dairy market continues to retract albeit at a slower rate. Our operations are focused on cost leadership and continuing to gain market share.



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## Fonterra's first Sustainability Report released

Earlier this month, the Co-op released its first standalone Sustainability Report.

It has been produced to international reporting standards to ensure its integrity and provides an objective view of our social and environmental performance.

The report shows the Co-op has made significant

progress in some areas, and has plans in place where there is more work to be done.

We are proud of the progress the Co-operative has made in most areas thanks to the commitment and hard work of our farmers, people, and partners that work alongside our Co-operative.



[Read the full 2018 Sustainability Report –](#)

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## Planting the Ashburton Hakatere River Trail

Over 100 volunteers from Environment Canterbury, Ashburton District Council, Fonterra and others descended on the Ashburton Hakatere River Trail to help plant around 500 trees along the riverbank.

The 19-kilometre trail winds from the Ashburton Township to the river mouth at Hakatere, passing riverside willows and farmland on the way, and is a well-used walking and cycling track. The river itself is an important wildlife habitat for both birds and fish, and supports breeding colonies of the endangered black-billed gull.

The Ashburton Water Zone Committee organised the event and member, Angela Cushnie, says it is part of an ongoing project to make the district a more beautiful place for everyone to enjoy.

"We're a small community and it's great to see so many people out there working together to make a positive difference and to show our children we all have a role to play in keeping our district beautiful.



"The planting was very successful and everyone had a blast, but it was also a great opportunity to talk to people and get their ideas about what other things we can do to improve the area and others across the district," says Angela.

Fonterra Area Manager for Mid-Canterbury South, Antoinette Archer, says everyone had fun and it was a wonderful opportunity to help a great cause.

"As well as helping out with the planting, we ran the BBQ for the post-match event, and we also brought along some Calci-Yum to make sure the volunteers were well-fed. It was great seeing so many different people from different organisations spend a bit of their time

to improve the river for everyone."

The volunteers spent two hours planting along the trail, followed by the BBQ.

Riparian planting helps improve water quality as the plants act like filters, helping to slow down any surface water running off the land into the river. They also filter out nutrients and sediment, removing at least 60% of nitrogen and 65% of phosphorous. The plants also create shade which reduces weed growth and helps bring the water temperature down providing a healthier environment for water life.

# SUPPLEMENTARY INFORMATION

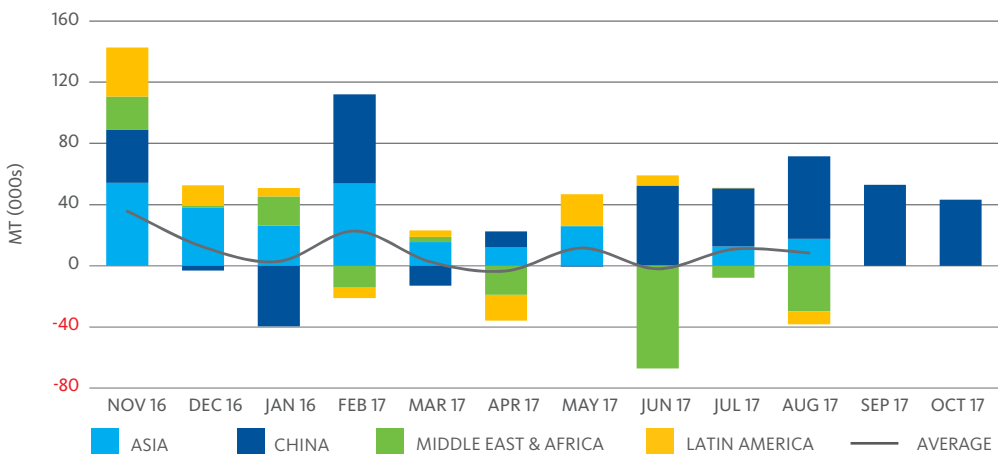
## Global Dairy Market

The charts on the right illustrate the year-on-year changes in imports, exports and production for a range of countries that are important players in global dairy trade.

The absolute size of the bars represents the change in imports, exports or production, relative to the same period the previous year.

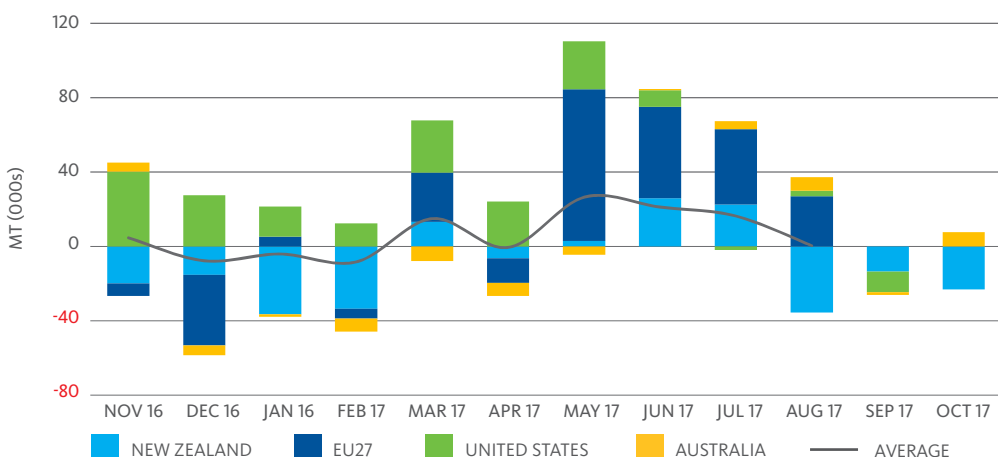
Averages are shown where data is complete for the regions presented.

### IMPORTS



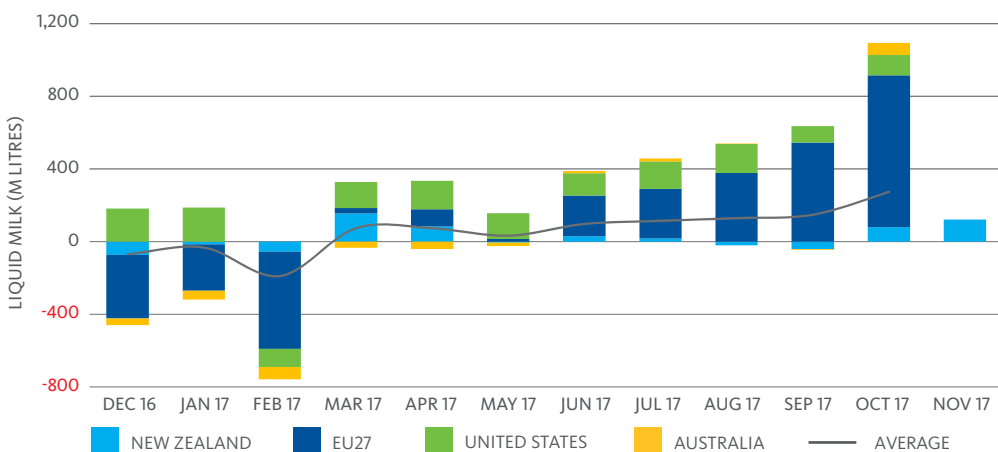
NOTE: Data for Asia, Middle East and Africa and Latin America to August, China to October.

### EXPORTS



NOTE: Data for EU to August; New Zealand, US and Australia to October.

### PRODUCTION



NOTE: Data for EU, Australia, and US to October, New Zealand to November.

SOURCE: Government milk production statistics/GTIS trade data/Fonterra analysis.

# SUPPLEMENTARY INFORMATION

## Fonterra milk production

The table on the right shows Fonterra milk solids collected in New Zealand and Australia compared to the previous season.

MILK COLLECTION (MILLION KGMS)	NOVEMBER 2017	NOVEMBER 2016	MONTHLY CHANGE	SEASON- TO-DATE 2017/18	SEASON- TO-DATE 2016/17	SEASON- TO-DATE CHANGE
Total Fonterra New Zealand	199.1	193.7	2.7%	70.1.5	694.8	1.0%
North Island	117.8	116.3	1.3%	444.7	442.1	0.6%
South Island	81.3	77.5	4.8%	256.8	252.7	1.6%
Fonterra Australia	17.4	13.6	27.8%	70.0	55.4	26.3%

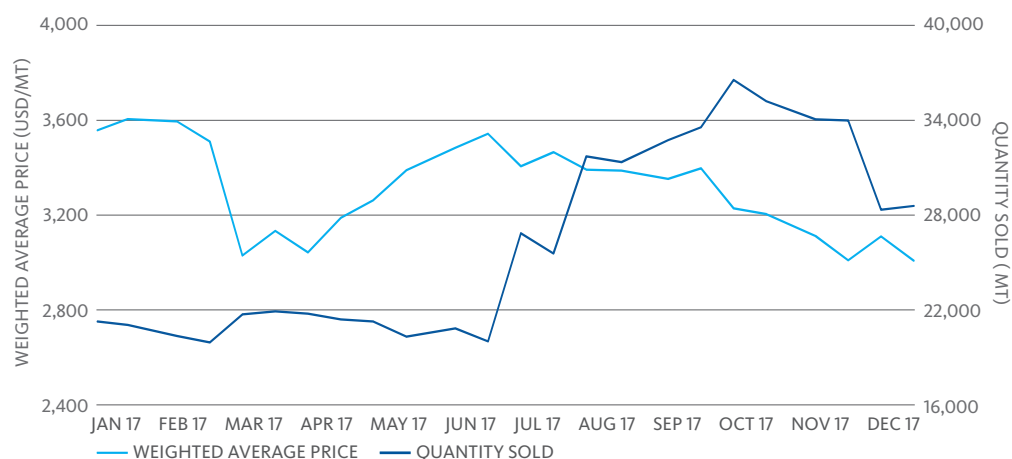
## Fonterra GDT results

This table provides more information on the latest results, including a snapshot of the year-to-date results.

	LAST TRADING EVENT (19 DECEMBER 2017)	YEAR-TO-DATE (FROM 1 AUGUST 2017)
Quantity Sold on GDT (Winning MT)	28,594	326,169
Change in Quantity Sold on GDT over same period last year	33.9%	10.6%
Weighted Average Product Price (USD/MT)	3,008	3,223
Change in Weighted Average Product Price over same period last year	(19.8%)	4.2%
Change in Weighted Average Product Price from previous event	(3.3%)	–

## Fonterra GDT Results

This chart shows Fonterra GDT prices and volumes over the past 12 months.



# GLOSSARY

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## AMF

Anhydrous Milk Fat.

## BMP

Butter Milk Powder.

## DIRA

Dairy Industry Restructuring Act 2001 (New Zealand).

## Farmgate Milk Price

The price for milk supplied in New Zealand to Fonterra by farmer shareholders.

## Fluid and Fresh Dairy

The Fonterra grouping of fluid milk products (skim milk, whole milk and cream – pasteurised or UHT processed), concentrated milk products (evaporated milk and sweetened condensed milk) and yoghurt.

## GDT

GlobalDairyTrade, the online provider of the twice monthly global auctions of dairy ingredients.

## kgMS

Kilogram of milk solids, the measure of the amount of fat and protein in the milk supplied to Fonterra.

## LME (Liquid Milk Equivalent)

A standard measure of the amount of milk (in litres) allocated to each product based on the amount of fat and protein (“milk solids”) in the product relative to the amount of fat and protein in a standardised raw milk.

## Non-Reference Products

All dairy products, except for Reference Products, produced by the NZ Ingredients business.

## Reference Products

The dairy products used in the calculation of the Farmgate Milk Price, which are currently WMP, SMP, BMP, butter and AMF.

## Season

New Zealand: A period of 12 months to 31 May in each year.

Australia: A period of 12 months to 30 June in each year.

## SMP

Skim Milk Powder.

## WMP

Whole Milk Powder.

## Fonterra Strategic Platforms

### Ingredients

The Ingredients platform comprises bulk and specialty dairy products such as milk powders, dairy fats, cheese and proteins manufactured in New Zealand, Australia, Europe and Latin America, or sourced through our global network, and sold to food producers and distributors in over 140 countries.

It also includes Fonterra Farm Source™ retail stores.

### Consumer

The Consumer platform comprises branded consumer products, such as powders, yoghurt, milk, butter, and cheese. Base products are sourced from the ingredients business and manufactured into higher-value consumer dairy products.

### Foodservice

The Foodservice platform comprises a range of branded products and solutions for commercial kitchens, including bakery butter, culinary creams, and cheeses.

### China Farms

The China Farms platform comprises the farming operations in China, which produce high quality fresh milk for the Chinese market.