

Market Announcement

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Fonterra Advises Changes to Farmgate Milk Price Manual

Filing of Reasons Paper on Farmgate Milk Price Manual for the 2016/17 Season

Fonterra Co-operative Group Limited ("Fonterra") has filed with the Commerce Commission its annual "Reasons" Paper in support of changes to its Fonterra's Milk Price Manual for the 2016/17 season. A copy of the Reasons Paper is attached.

This follows the annual review by Fonterra of the Milk Price Manual. The Dairy Industry Restructuring Act 2001 requires Fonterra to provide the Commerce Commission with its Milk Price Manual for the current season by 1 August, notify the Commission of any changes made in the Milk Price Manual, and provide reasons for them.

Changes to Fonterra's Farmgate Milk Price Manual

Fonterra's Constitution requires the Co-operative to pay the maximum sustainable Farmgate Milk Price each season based on the sale of commodity products in freely contested global markets. Fonterra uses a basket of Reference Commodity Products for this calculation and mainly uses sales made through Global Dairy Trade ("GDT"), the global auction platform for dairy ingredients. While spot sales of butter and buttermilk powder are already included in the Milk Price calculation, up until now, only GDT sales of commodity whole and skim milk powders and anhydrous milk fat have been included.

Fonterra will now include the revenue from spot sales of commodity whole and skim milk powders and anhydrous milk fat in its Farmgate Milk Price calculation. This change will be incorporated into the 2016/2017 season Milk Price. Spot sales are referenced to GDT and are direct-to-customer sales in the global commodities market of products with the same specifications as those sold on GDT.

The estimated impact of the change on the Farmgate Milk Price for the 2016/17 season amounts to an increase of four to five cents per kgMS based on analysis of the change over the past four years.

The change meets Fonterra's Constitutional requirement to pay the maximum sustainable Milk Price and regulatory requirements to pay an efficient, competitive Milk Price. It follows careful analysis and evaluation which determined that these spot sales clearly meet the definition of being sales of Reference Commodity Products into freely contested markets.

Since 2009, revisions to the Milk Price Manual each year as a result of required reviews have captured efficiencies on the cost side of the calculation and changes to the cost of capital. These changes have been on average up to five cents per kgMS each year. This change is the first relating to the revenue side of the calculation, but does not alter GDT Events sales remaining the predominant source of pricing information for Milk Price calculations.

The change has been approved by the Board (including Independent Directors) as required under the Fonterra Shareholders' Market rules. The change also complies with the Dairy Industry Restructuring Act and will be subject to the annual review of the Milk Price Manual by the Commerce Commission under its Milk Price oversight role under DIRA.

Other changes to the Milk Price Manual for the 2016/17 season include responses to matters raised by the Commerce Commission following its review of the Milk Price Manual for the 2015/16 season, the provision of additional detail on calculations of certain inputs into the Milk Price model, and minor technical or drafting changes.

This change does not alter the forecast earnings per share range for F17 announced today in a separate market announcement.

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