Fonterra Co-operative Group Limited

Investment Statement relating to an offer of Co-operative Shares, Peak Notes, Capital Notes and Redeemable Preference Shares

This is an Investment Statement for the purposes of the Securities Act 1978.
It is prepared as at 12 April 2012.

IMPORTANT INFORMATION
(The information in this section is required under the Securities Act 1978)

Investment decisions are very important. They often have long-term consequences. Read all documents carefully. Ask questions. Seek advice before committing yourself.

CHOOSING AN INVESTMENT
When deciding whether to invest, consider carefully the answers to the following questions that can be found on the pages noted below:

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In addition to the information in this document, important information can be found in the current registered prospectus for the investment. You are entitled to a copy of that prospectus on request.

THE FINANCIAL MARKETS AUTHORITY REGULATES CONDUCT IN FINANCIAL MARKETS
The Financial Markets Authority regulates conduct in New Zealand's financial markets. The Financial Markets Authority's main objective is to promote and facilitate the development of fair, efficient, and transparent financial markets.

For more information about investing, go to http://www.fma.govt.nz

FINANCIAL ADVISERS CAN HELP YOU MAKE INVESTMENT DECISIONS
Using a financial adviser cannot prevent you from losing money, but it should be able to help you make better investment decisions.

Financial advisers are regulated by the Financial Markets Authority to varying levels, depending on the type of adviser and the nature of the services they provide. Some financial advisers are only allowed to provide advice on a limited range of products.

When seeking or receiving financial advice, you should check—

- the type of adviser you are dealing with:
- the services the adviser can provide you with:
- the products the adviser can advise you on.

A financial adviser who provides you with personalised financial adviser services may be required to give you a disclosure statement covering these and other matters. You should ask your adviser about how he or she is paid and any conflicts of interest he or she may have.

Financial advisers must have a complaints process in place and they, or the financial services provider they work for, must belong to a dispute resolution scheme if they provide services to retail clients. So if there is a dispute over an investment, you can ask someone independent to resolve it.

Most financial advisers, or the financial services provider they work for, must also be registered on the financial service providers register. You can search for information about registered financial service providers at http://www.fspr.govt.nz

You can also complain to the Financial Markets Authority if you have concerns about the behaviour of a financial adviser.

Definitions

Capitalised terms used in this Investment Statement have defined meanings which appear in the Glossary section.

Legislation

All legislation referred to in this Investment Statement may be viewed at www.legislation.govt.nz.

New capital structure and further development of capital structure

At the special meeting of Shareholders on 30 June 2010 amendments to Fonterra's Constitution were approved. Details of certain of the changes and when they may come into effect are set out in this Investment Statement.

As at the date of this Investment Statement, Fonterra intends to implement various changes to its capital structure based on the proposals approved by shareholders on 30 June 2010. Please refer to page 3 for further information.

Cooling-off period

If you have not received an Investment Statement when you apply, Fonterra will send you a copy when it notifies you of the acceptance of your application. In such cases, you will have 10 working days (from the date your Investment Statement is sent to you) in which to decide to withdraw your application.

ANSWERS TO KEY QUESTIONS

WHAT SORT OF INVESTMENT IS THIS?

This Investment Statement covers the offer by Fonterra Co-operative Group Limited (**Fonterra**) of four different securities:

- Co-operative Shares (**Shares**)
- Peak Notes
- Capital Notes
- Redeemable Preference Shares

The answer to the question set out in the heading in this section is set out under the heading "*Capital Structure*" below.

CAPITAL STRUCTURE

Development of capital structure

This Investment Statement contains information about the current capital structure of Fonterra, including in relation to changes to Fonterra's Constitution approved by shareholders on 30 June 2010.

At a special meeting of shareholders on 30 June 2010 amendments to Fonterra's Constitution were approved. These amendments allow the Board to take the steps necessary to finalise and put in place a regime for Trading Among Farmers before 31 December 2013 or a later date determined by the Board. The amendments include pre-conditions that the Board must decide are satisfied before it resolves to implement Trading Among Farmers.

At the special meeting on 30 June 2010, shareholders also approved a new form of constitution that will apply if the Board, having determined that the pre-conditions have been satisfied, resolves that Fonterra move to adopt and implement Trading Among Farmers, and resolves that the new constitution shall, on a date determined by the Board, come into effect. The new form of constitution comprises Annexure 2 to Fonterra's current Constitution, and as such forms part of the amendments made to Fonterra's constitution on 30 June 2010.

In the event that Fonterra moves to adopt and implement Trading Among Farmers, the obligations on Fonterra to issue or redeem Shares under the current Constitution and the DIRA at a fair value determined in accordance with the current Constitution would cease. In place of those obligations, it is intended that Shareholders be permitted to trade Shares on a Fonterra Shareholders' Market, which is proposed to be a registered market operated by a registered exchange under the Securities Market Act 1988. As at the date of this Investment Statement, the Shares have not been approved for trading on a registered market, nor has any application been made to enable the Shares to be traded on a registered market. In addition, a Fonterra Shareholders' Fund would be established and a shareholder would be permitted to transfer a proportion of its Shares to a custodian to hold on behalf of that fund.

Further information regarding Trading Among Farmers is set out on pages 8 to 12.

As noted above, the amendments to Fonterra's Constitution enable the Board to put in place a regime for Trading Among Farmers before the end of December 2013 or a later date specified by the Board. However, the Board is not obliged to do so even if, during this period, the pre-conditions are met. There is no assurance or guarantee that Trading Among Farmers will be implemented or, if implemented, the final structure that will be implemented or the timing of such implementation.

The special meeting on 30 June 2010 was intended to be the only meeting for shareholders to vote on the amendments to Fonterra's Constitution before the implementation of Trading Among Farmers by the Board. It is not intended that there will be any further vote by shareholders on the implementation of Trading Among Farmers before it is introduced. Shareholders will be bound by that regime when it is implemented.

This Investment Statement may not be updated to reflect further progress on the development of Trading Among Farmers unless and until Trading Among Farmers is implemented. Any developments to the capital structure ultimately made may be different from any possible changes discussed prior to implementation.

Co-operative Shares

The terms of the Shares are set out in the Constitution, and are subject to the requirements of the Companies Act 1993, the Co-operative Companies Act 1996 and the DIRA.

If you supply milk to Fonterra you are deemed under the Constitution to have made an irrevocable application to become a Fonterra shareholder and to hold the number of Shares required to be held by the share standard. The

Board may permit you to use an unshared supply entitlement (refer below), and you may hold excess Shares (see pages 5 to 6). The share standard is one Share for each kilogram of milksolids obtainable from milk that you supply Fonterra in a Season (excluding milk supplied on Contract Supply).

The issue price and Surrender Value of the Shares is, or is based on, their "fair value". Each Season the fair value of the Shares is determined by the Board in accordance with the method set out in the Constitution (described in *How much do I pay?* below).

Each Share confers:

- the right to an equal share in dividends authorised by the Board, if any;
- the right to an equal share in the distribution of surplus assets of the Company; and
- on a poll or postal ballot of shareholders, one vote for every 1,000 kilograms of milksolids supplied to Fonterra as determined in accordance with the Constitution, excluding milk supplied under an unshared supply entitlement (refer below), and excluding milk supplied on Contract Supply.

Shares rank equally and without priority or preference amongst themselves. Should Fonterra be liquidated for whatever reason, Shares will rank behind and subordinate to all outstanding obligations of Fonterra (including the Capital Notes, Peak Notes and Redeemable Preference Shares).

Shares may not be issued to a new supplier whose supply or estimated supply is less than 1,000 kilograms of milksolids in a Season. For an existing supplier, Fonterra may be entitled to reject a surrender of Shares if it would cause that supplier to hold fewer Shares than a person is required to hold to commence supplying Fonterra.

Part A of the Constitution, which includes provisions relating to the matters in this section, cannot be altered or revoked unless the proposal is supported by both shareholders (by special resolution) and 50% or more of the Shareholders' Councillors (see *Can the investment be altered?* below).

New supplier and applications to increase supply

If you are a new supplier or apply to increase your supply, Fonterra will estimate your production levels. Fonterra will issue you Shares based on your estimated production (excluding Contract Supply). The amount you pay for your Shares will be either the fair value June Price or the Default Price for the Season that your supply commences or increases (see *How much do I pay?* below).

Changes in supply

The Board may, at any time during a Season, issue you with such number of Shares as is necessary to ensure you hold the number of Shares you are required to hold in accordance with the share standard for that Season, and if you elect, a number of excess Shares, subject to the limits described on pages 5 to 6. In exercising its discretion to issue Shares, the Company may rely on information provided by the shareholder. The amount you pay for these shares will be the June Price for that Season. If you elect to be issued excess Shares during a Season, the Board may require you to hold a minimum number of Shares continuously through a period determined by the Board and any such requirement would be a term of your milk supply to Fonterra. This will mean that you will be required to supply all milk to Fonterra during this period. You will not be able to give notice to Fonterra that you will cease to supply milk or apply to reduce supply, or surrender or transfer Shares, if you would be in breach of such a requirement.

If you increase supply in a Season, but do not hold sufficient Shares to cover that increase, the Board may permit you to elect to use an unshared supply entitlement. An unshared supply entitlement allows you to hold less shares than the number required by the share standard. The Board is not obliged to permit unshared supply entitlements in any Season, and, if it does, it can do so on such terms as it sees fit. The amount by which a shareholder is undershared cannot exceed 20% of the Shares required to be held by the shareholder by the share standard for that Season. The Board may, if it allows unshared supply, set a cap of less than 20%.

If it is determined at the end of a Season, based on your actual supply of milk to Fonterra during the Season, and taking into account any permitted unshared supply entitlement, that you hold less Shares than you are required to hold by the share standard for that Season, the Board will issue you with the number of additional Shares you are required to hold. The amount you pay for these Shares will be the fair value June Price for the following Season (see pages 13 to 16).

The Company may also, at any time during a Season, require a shareholder to surrender any Shares in excess of the number the shareholder is permitted to hold (refer below) and, if elected by a shareholder, some or all of any Shares held in excess of the number of Shares the shareholder is required to hold. The consideration received for any surrendered Shares will be the June Price in the Season in which the surrender takes place (less any amount not paid up on the Shares). In exercising its discretion to surrender Shares, the Company may rely on information provided by the shareholder.

If it is determined at the end of a Season, based on your actual supply of milk to Fonterra during the Season, that you hold more Shares than the aggregate of the number of Shares you are required to hold by the share standard for that Season and the number of excess Shares you are permitted to hold (refer to the limit described on pages 5 to 6), the Board will require you to surrender the number of Shares you hold in excess of the aggregate. You can also elect within 21 days of the end of the Season (or any longer period set by the Board) to surrender all or some of the Shares in excess of the number required by the share standard, in which case the Board will require the surrender of such number of Shares. The Board may determine that excess Shares will not be surrendered if the surrender would cause you to:

- be in breach of any terms and conditions on which you supply milk to Fonterra, including any milk you supply on Contract Supply (see page 8); or
- hold less Shares than the minimum number of shares you are required to hold by the Board as a condition of the issue of additional Shares (see page 4); or
- hold less Shares than the minimum a person must hold at that time to commence supplying milk to Fonterra.

The amount you will be paid for the surrender of the Shares will be the fair value June Price for the following Season (less any amount not paid up on the Shares) (see *How much do I pay?* below).

Ceasing supply and applications to reduce supply

If you apply to cease supply to Fonterra for a Season, your Shares will be surrendered unless your application to cease supply is in breach of any terms and conditions on which you supply milk to Fonterra, including any milk you supply on Contract Supply (see page 8). If you apply to reduce supply to Fonterra for a Season, Fonterra shall require you to surrender a commensurate number of Shares (such that you will only hold the Shares you are required to hold by the share standard for the Season, and if you elect, a number of excess Shares not exceeding 20% of the Shares required by the share standard, in each case based on your estimated supply of milk (excluding milk to be supplied on Contract Supply) during that Season). If you supply milk to Fonterra on Contract Supply then the reduction in supply will first be taken (reduced) from your growth contract quantity. The amount you will receive for any Shares surrendered will be either the fair value June Price or the Default Price for the Season your supply ceases or reduces (see *How much do I pay?* below).

Unshared supply entitlement

Unshared supply entitlements for any Season will be limited to 20% (or any lesser limit set by the Board, which could be zero) of the number of Shares required to be held by a shareholder by the share standard for that Season. The level of unshared supply entitlements may be further limited by additional rules set by the Board from time to time.

The Board will notify shareholders prior to the end of the Season as to whether unshared supply entitlements will be permitted and, if so, on what terms. This notification will include the price that will be paid for milk supplied under an unshared supply entitlement, which is expected to be lower than the amount paid for similar milk supplied in similar circumstances in compliance with the share standard.

The milk you supply under any unshared supply entitlement will not be taken into account in determining the number of votes you are entitled to as a shareholder.

Existing suppliers need to complete an Annual Supply Notification Form by the end of the application period each year which will advise Fonterra of any anticipated increase in supply for the upcoming Season. This is a requirement of the Terms and Conditions of Supply.

Maximum number of Shares

The maximum number of Shares you can hold in excess of the number required by the share standard is 20% of the Shares you are required to hold by the share standard for the Season. The retention of any excess Shares will be automatic up to this limit. Any Shares in excess of this limit will be surrendered. You can also elect within 21 days of the end of the Season (or any longer period set by the Board) to surrender all or some of the Shares in excess of the number required by the share standard. The Board may determine that excess Shares will not be surrendered if the surrender would cause you to:

- be in breach of any terms and conditions on which you supply milk to Fonterra, including any milk you supply on Contract Supply (see page 8); or

- hold less shares than the minimum number of shares you are required to hold by the Board as a condition of the issue of additional Shares (see page 4); or
- hold less Shares than the minimum a person must hold at that time to commence supplying milk to Fonterra.

If your decrease in supply is a result of diverting part of your supply to a processor other than Fonterra for a Season, Fonterra may require you to surrender a commensurate number of Shares (such that you will only hold the Shares you are required to hold by the share standard for the Season, and if you elect, a number of excess Shares not exceeding 20% of the Shares required by the share standard, in each case based on your estimated supply of milk (excluding milk to be supplied on Contract Supply) during that Season). The consideration you will receive for surrendered Shares will be the fair value June Price for the Season in which supply is diverted (less any amount not paid up on the Shares).

You will not receive any payment for milk in relation to any excess Shares because you will not have supplied any milk in relation to those Shares. However, you will be entitled to receive a dividend in respect of your excess Shares if the Board determines to pay a dividend. You can continue to hold excess Shares indefinitely subject to the limit noted above. If you surrender excess Shares you will receive the fair value of the Shares for the Season for which the Shares are surrendered, or in some cases the fair value of the Shares for the following Season. You will not receive the fair value of the Shares for the Season in which the excess Shares were issued (which could be higher or lower than the surrender value).

As shareholders' voting entitlements are based on milksolids supplied, holding excess Shares will not impact on voting entitlements.

If you cease supplying Fonterra, your Shares will be surrendered, as described under the heading *How do I cash in my investment?* below. If you apply to supply less milk to Fonterra, some of your Shares will be surrendered unless you elect to hold excess Shares subject to the limit described above or you supply milk to Fonterra on Contract Supply, in which case the reduction in supply will first be taken (reduced) from your contract quantity.

Issue of additional Shares:

Fonterra may issue additional Shares upon receiving an application by a shareholder or new supplier at the discretion of, and on terms set by, the Board. The Board may set a period during which shareholders or new suppliers can apply for additional Shares, and a date on which Shares applied for during that period will be issued. If no date is set, the additional Shares will be issued on or before 15 July next following the date the application is made or as soon as practicable thereafter. The amount you will pay for your additional Shares will be the fair value June Price for the Season in which the additional Shares are issued.

Fonterra will not issue additional Shares to you to the extent that following any issue you would hold more Shares than the maximum number of Shares you are permitted to hold (refer to the limit described above). If you are a new supplier, or have applied to increase or decrease supply for a Season, the number of Shares you are permitted to hold will be based on Fonterra's estimate of your supply for that Season (excluding for this determination any milk you will supply on Contract Supply). In all other cases, your maximum permitted holding will be based on your actual supply (excluding for this determination any milk you supply on Contract Supply) during the Season preceding the Season in which the additional Shares will be issued.

Peak Notes

In addition to holding Shares, shareholders are required to hold the number of Peak Notes required to be held by the Peak Note standard, determined in accordance with the Constitution. The Peak Note standard for the 2011-2012 Season was zero, and the Board has determined that the Peak Note standard for the 2012-2013 Season is also zero. There are no Peak Notes currently on issue and no Peak Notes will be issued in a Season for which the Peak Note standard is set as zero.

The Peak Note is a means by which suppliers contribute to peak processing capacity costs. Suppliers with high peak production profiles are asked to contribute more to the business by being required to hold more Peak Notes.

The issue price of each Peak Note is fixed at $30.

What are Peak Notes?

Peak Notes are unsecured, subordinated, non-interest bearing obligations of Fonterra which rank equally and without priority or preference amongst themselves.

New supplier

If you are a new supplier whose application to become a shareholder in that Season has been accepted by the Board, Fonterra must issue you with the number of Peak Notes you are required to hold under the Peak Note standard (based on Fonterra's estimate of your milk supply profile during that Season).

Changes in supply

If you hold fewer Peak Notes than required by the Peak Note standard in that Season (based on your milk supply profile during the preceding Season), Fonterra must issue you the additional number of Peak Notes you are required to hold. As Peak Notes are issued to you based on your peak milk supply profile (not your total production levels), your requirement to hold Peak Notes in any Season may change and, in particular, you may be required to hold additional Peak Notes even though your total milk supply has decreased.

If you hold more Peak Notes than required by the Peak Note standard in that Season (based on your milk supply profile during the preceding Season), Fonterra may redeem those excess Peak Notes (see *What are my returns?* below).

Shareholders who cease supply and are required to surrender their Shares must also redeem their Peak Notes (see *How do I cash in my investment?* below).

Shareholders may redeem excess Peak Notes by giving notice to Fonterra prior to 30 June in each year.

Terms of the Peak Notes

Peak Notes will continue in existence until redeemed by Fonterra (see *What returns will I get?* below).

The Peak Notes are constituted by, and issued under, the Peak Notes Trust Deed, which is summarised in the Prospectus.

In accordance with their subordinated nature, the Peak Notes are subject to certain restrictions on payments which may be made on the Peak Notes. The rights and powers of the Trustee and/or the holders of Peak Notes to enforce or compel payment by Fonterra are also restricted.

Should Fonterra be liquidated for whatever reason, Peak Notes will rank behind and subordinate to all outstanding obligations of Fonterra (including the Capital Notes). In all other respects, the Peak Notes will rank ahead of Redeemable Preference Shares and obligations to shareholders in their capacity as shareholders. Each Peak Note will become repayable by Fonterra on the commencement of liquidation of Fonterra.

Capital Notes

The Capital Notes are interest bearing, unsecured, subordinated, debt investments with no fixed maturity issued by Fonterra.

Fonterra may issue Capital Notes to shareholders who are redeeming Shares, Peak Notes, or Redeemable Preference Shares, in lieu of paying cash (see *How do I cash in my investment?* below). Fonterra may also redeem Capital Notes from shareholders in satisfaction of the issue price of Shares and Peak Notes.

The Capital Notes bear interest payable on a quarterly basis as described under the heading *What returns will I get?.*

The Capital Notes have no fixed maturity date and continue in existence until redeemed by Fonterra on an Election Date (see *How do I cash in my investment?* below) or are otherwise purchased by Fonterra with agreement from the holder, or are redeemed or repurchased by Fonterra from its shareholders in accordance with the Constitution and the DIRA (see *What returns will I get?* below).

The Capital Notes rank in point of priority and right of payment, and in all other respects, equally amongst themselves. On any liquidation of Fonterra, no payment will be made to holders in respect of the Capital Notes until Senior Debt has been paid in full. "Senior Debt" means all outstanding obligations of Fonterra except its obligations with respect to the Capital Notes and the Peak Notes, and to other creditors that have agreed to priority equal with or subsequent to the Capital Notes, and to shareholders in their capacity as shareholders. Capital Notes rank ahead of Peak Notes, Redeemable Preference Shares, Shares and obligations to shareholders in their capacity as shareholders.

The Capital Notes are constituted by, and issued under, the Capital Notes Trust Deed, which is summarised in the Prospectus.

Prior to any liquidation of Fonterra, the Trustee is restricted from taking any action against Fonterra in relation to the payment of the principal amount and accrued interest owing under the Capital Notes. This does not restrict the Trustee from appointing a liquidator for Fonterra in the limited circumstances described in the Capital Notes Trust Deed, including failure to pay interest on interest payment dates (where additional Capital Notes have not been issued in lieu thereof) and breaches of certain other covenants.

The Capital Notes have been accepted for listing by NZX Limited and will be quoted on the NZDX upon the completion of allotment procedures. However, NZX accepts no responsibility for any statement in this Investment Statement. The NZDX is a registered market under the Securities Markets Act 1988. The NZDX is operated by NZX, which is a registered exchange, regulated under the Securities Markets Act 1988.

Redeemable Preference Shares

Fonterra may issue Redeemable Preference Shares to shareholders as consideration for a proportion of the Surrender Value of Shares (whether the surrender is because of fluctuations in supply or cessation of supply) and the redemption of Peak Notes (as discussed on pages 36 to 39) only if permitted by the DIRA and the Constitution. The requirements include that the Board considers that paying cash and issuing Capital Notes would materially and adversely affect Fonterra's ability to implement its business plan.

A cumulative dividend will be paid on Redeemable Preference Shares as described under the heading *What returns will I get?.*

Redeemable Preference Shares rank in preference to all other Shares issued by Fonterra, rank equally and without priority or preference amongst themselves, but rank behind all other indebtedness of Fonterra (including, without limitation, Peak Notes and Capital Notes).

Redeemable Preference Shares do not have voting rights except the right to vote on actions that affect the rights attached to them.

The terms of the Redeemable Preference Shares are set out in the DIRA and the Constitution.

At the date of this Investment Statement, Fonterra has not issued any Redeemable Preference Shares.

Contract Supply

The Board may permit you to supply milk to Fonterra on Contract Supply. Any milk supplied on Contract Supply is not taken into account for the purpose of determining the number of Shares required to be held under the share standard. The Board is not obliged to offer Contract Supply to shareholders. If offered, there is no assurance that you will be able to participate in the Contract Supply offered. You should therefore not make any investment decisions on the assumption that Contract Supply will be offered in any Season, or that (if offered) you will be able to participate in Contract Supply.

The aggregate amount of milksolids obtained from milk supplied to Fonterra on Contract Supply in a Season must not exceed 15% of the total milksolids obtained from all milk supplied to Fonterra by shareholders in a 12 month period prior to the commencement of that Season selected by the Board.

The 15% limit does not apply to milk supplied to Fonterra under its right, separately from Contract Supply, to purchase milk from non-shareholders and to permit a shareholder to split supply, and treat one supply as being from a non-shareholding supplier.

If Contract Supply is offered, the Board will determine the terms of the Contract Supply, including how the shareholders who will supply milk on Contract Supply will be selected, and the amount to be paid for milk supplied on Contract Supply. The net amount you receive for milk supplied to Fonterra on Contract Supply is expected to be less than the amount you receive for similar milk you supply to Fonterra in similar circumstances in accordance with the share standard (see pages 17 to 18).

At the end of the term of any contract for the supply of milk on Contract Supply you may need to acquire more Shares to ensure you hold the minimum number you are required to hold pursuant to the Constitution. As the value of Shares changes each Season (see pages 19 and 20), the price you may have to pay for these additional Shares may be greater than the amount you received if you surrendered Shares on securing the right to make Contract Supply. The Board can also require you to hold a minimum number of Shares during any period you supply milk on Contract Supply, and you cannot give notice to Fonterra that you will cease supplying milk or apply to reduce supply, or transfer any Shares, if you would be in breach of the terms on which you supply milk on Contract Supply. The milk you supply on Contract Supply will not be taken into account when determining the number of votes you are entitled to as a shareholder (see page 4).

Trading Among Farmers

Transition to Trading Among Farmers

Fonterra's Constitution was altered on 30 June 2010, to enable the Board to take steps to prepare Fonterra for arrangements (collectively referred to as "**Trading Among Farmers**") that are expected to apply on and from the date the Board has resolved that a new constitution, set out as Annexure 2 to Fonterra's current Constitution ("**New Constitution**"), will take effect.

The Constitution sets out the framework for the Board to take transitional steps to implement a regime for Trading Among Farmers, including pre-conditions that the Board must decide are satisfied before any regime for Trading Among Farmers can commence.

The Constitution gives the Board the discretion to determine the final detailed design of any regime for Trading Among Farmers. However, the Board must design the regime within the scope of the pre-conditions and thresholds, limits and protections that are set out in the Constitution and the New Constitution.

Under the Constitution the Board can implement Trading Among Farmers before 31 December 2013 or a later date determined by the Board. However, the Board is not entitled to do so if, during this period, the pre-conditions have not been satisfied. If the pre-conditions are not satisfied for any reason and the Board does not move to adopt and implement Trading Among Farmers within the time period allowed, the New Constitution would not come into force and the pre-conditions and transition arrangements in the Constitution would come to an end. This would mean that all of the obligations of Fonterra to issue or redeem Shares under the current Constitution and the DIRA would remain in place.

The following sections outline (in summary terms only) the key features of the amendments made to Fonterra's Constitution on 30 June 2010. This is a summary only. For full details see Fonterra's Constitution which may be accessed on the Companies Office website at www.business.govt.nz/companies, or may be inspected at 9 Princes Street, Auckland for free during normal business hours.

Pre-conditions

The Constitution provides that the Board may, at such time as it determines that the following pre-conditions have been satisfied, resolve that Fonterra move to adopt and implement Trading Among Farmers, and resolve that the New Constitution shall, on a date determined by the Board, come into effect:

- An authorised fund ("**Fonterra Shareholders' Fund**") has been established (or will, at or about the commencement of Trading Among Farmers, be established), and the Board is satisfied that the Fonterra Shareholders' Fund has, or is reasonably likely to have, appropriate mechanisms, rules and governance structures, and the Board considers that such fund is reasonably likely to have sufficient number and dispersion of securities on issue so as to facilitate trading in those securities.
- A market ("**Fonterra Shareholders' Market**") has been established or will (at or about the commencement of Trading Among Farmers) be established, for the trading of Shares in the manner contemplated by the New Constitution and the Board is satisfied that the Fonterra Shareholders' Market is reasonably likely to have appropriate mechanisms, rules and governance structures (including as to liquidity, market conduct and disclosure), and the Board considers that sufficient number and dispersion of Shares are or will be on issue, such that, in the Board's opinion, the Fonterra Shareholders' Market is reasonably likely to provide a reliable and effective platform for the trading of Shares.
- All necessary amendments to legislation which the Board considers necessary to facilitate Trading Among Farmers have been enacted. The Dairy Industry Restructuring Amendment Bill was introduced to Parliament on 27 March 2012 ("**Bill**") sets out potential amendments to the DIRA in relation to the Farmgate Milk Price, Fonterra's Share price, and the regulatory regime to accompany Trading Among Farmers. The final form of any legislation that will result from the Bill is not yet known.
- All waivers, approvals, consents or other confirmations from regulatory and other bodies the Board considers are required to facilitate Trading Among Farmers have been obtained, on terms acceptable to the Board.
- The Board has provided the Shareholders’ Council a report setting out the basis on which the Board considers that the above pre-conditions have been satisfied and the Shareholders' Council has resolved (by a majority of 50% or more of Councillors) to support a resolution of the Board that the New Constitution come into effect.

Fonterra Shareholders' Fund

Under the Constitution, the Fonterra Shareholders' Fund could be introduced before Fonterra moves to adopt and implement Trading Among Farmers, but it is not yet decided whether such a fund will be established before Trading Among Farmers commences.

Key features of Trading Among Farmers under the New Constitution

Key features of Trading Among Farmers under the New Constitution are as follows:

Setting the share standard

- Fonterra will not be required to issue and redeem Shares. Instead shareholders will be able to buy and sell Shares on the Fonterra Shareholders' Market.
- The share standard will require shareholders to hold a minimum of one Share for each kilogram of milksolids produced.
- The share standard will be measured on a three-year rolling average of actual production over the previous three seasons. The Board may allow shareholders to provide an estimate of production and have the share standard measured against this.
- The ability for shareholders to split supply will be retained and the provisions relating to unshared supply and Contract Supply which are in the current Constitution will continue.

Entry and Exit

- The Board may permit new shareholders, purchasers of farms and new conversions, a longer period to acquire the number of Shares that they will need to hold to meet the share standard. Shareholders will generally be allowed to acquire their full Shareholding over a three year period (and the Board may set a number of Shares that must be bought in each Season).
- Shareholders who are exiting the Company may also be able to sell down their Shareholding over three Seasons.
- The Board will be able to set a period that is longer or shorter than the three-Season periods noted above for new and exiting shareholders (and can adjust the number of Shares that must be bought or sold in each Season depending on the length of that period).

Shares held by shareholders, in excess of the number required by the share standard, permitted to be held by an individual farmer

- The Board may, at its discretion, allow shareholders to hold a number of Shares based upon a range of between 100% and 200% of the share standard.
- The maximum number of Shares in excess of the number required by the share standard in which each shareholder (and its related parties) may hold interests is 5% of the total number of Co-operative Shares on issue at any time, regardless of a shareholder's production level.

The total number of Shares held by shareholders in excess of the number required by the share standard

- The total number of Shares held by all shareholders in excess of the number required by the share standard must be no more than 25% of the total number of Co-operative Shares on issue at any time. This percentage may be reduced by the Board.
- If the overall threshold is exceeded, the Board must take steps to bring the number of Shares held by shareholders in excess of the number required by the share standard down under the threshold over a time period decided by the Board.

Measurement and compliance

- Compliance with the share standard will be measured on the first day in each Season. Fonterra will issue a statement informing shareholders of their shareholdings at that time and the number of Shares required based on the three-year rolling average or expected production.

- Each shareholder will have a period set by the Board, not being less than six months from the beginning of the season, to buy or sell Shares to ensure compliance with the minimum Shareholdings required under the share standard, but subject to the maximum holdings which any shareholder is allowed to hold.
- The Board may arrange for shareholders who do not want to buy and sell Shares on the Fonterra Shareholders' Market themselves to have an independent agent buy or sell Shares on their behalf during the compliance period.
- Shareholders who fail to comply within the required period will have Shares bought or sold for them on the Fonterra Shareholders' Market by an independent agent once the compliance period has expired, to meet minimum and maximum requirements. Such shareholders may have to meet the costs associated with these transactions.
- Fonterra will have the ability to ensure that shareholders are complying with the share standard.
- The Board may set a base level of Shares that a shareholder has to hold at all times during a Season, which could be less than the share standard described above.
- Shareholders who breach the rules and fail to rectify the position when requested to do so may be subject to adverse consequences and incur costs that Fonterra would be able to recover.

Fonterra Shareholders' Market

- It is intended that Fonterra will enter into contractual arrangements with a market operator to establish a Fonterra Shareholders' Market and to provide the rules and procedures for trading the Shares on the Market on terms approved by the Board. As at the date of this Investment Statement, the Shares have not been approved for trading on a registered market, nor has any application been made to enable the Shares to be traded on a registered market.
- Fonterra may offer a facility for shareholders to request an independent agent to buy and sell Shares on their behalf.

Registered Volume Providers (or RVPs)

- The Board may appoint one or more Registered Volume Providers to enhance the operation and liquidity of the Fonterra Shareholders' Market and/or any market for securities issued by the Fonterra Shareholders' Fund.
- The terms on which any RVP is appointed will be set out in a contract between the RVP and Fonterra. Such contract must include provisions stating that only a custodian may hold Shares for an RVP and that neither the custodian nor an RVP will be permitted to exercise any voting rights in relation to these Shares.
- No more than 5% of Shares may be held at any one time by a custodian for RVPs.

Fonterra Shareholders' Fund

- The pre-conditions require that a Fonterra Shareholders' Fund must have been, or will at the commencement of Trading Among Farmers be, established, and that the Board must be satisfied that the Fonterra Shareholders' Fund has, or is reasonably likely to have, appropriate mechanisms, rules, and governance structures, and must consider that such fund is reasonably likely to have sufficient number and dispersion of securities on issue so as to facilitate trading in those securities.
- The New Constitution sets an overall threshold which is intended to ensure that no more than 25% of all Shares may be subject to contracts with the Fonterra Shareholders' Fund.
- However, the Board intends, as a matter of policy, that a target will be set such that no more than 20% of Shares could be subject to contracts with the Fund. This policy can be changed by the Board.
- The Board will be able to set a threshold on the number of Shares that any individual shareholder could contract to the Fonterra Shareholders' Fund.
- Like the overall threshold on Shares held by shareholders in excess of the number required by the share standard, it is possible that the overall threshold on Shares subject to contracts with the Fund could be exceeded. If this happens, the New Constitution requires the Board to take steps to manage the overall number of Shares subject to contracts with the Fund, having regard to the overall threshold.

Voting

- Shareholders will be restricted from transferring votes to third parties under commercial arrangements. In particular, a shareholder may not transfer any of their voting rights to a Registered Volume Provider or the Fonterra Shareholders' Fund or any other similar fund that might be established. If votes are transferred in this way, the Board may disallow the votes and take other steps to prevent the shareholder and the recipient of the votes from continuing the arrangement.

Tax

- It is your responsibility to seek appropriate professional guidance in respect of income tax.
- In general terms, you should only be taxed on any gain on the disposal of your Shares if you acquired those Shares for the purpose of resale or you are in the business of dealing in Shares. Both situations are unlikely where you buy and sell Shares to comply with the share standard. Fonterra has received a non-binding confirmation from the Inland Revenue Department ("IRD") that, under the envisaged Trading Among Farmers regime, any gains will not be taxable provided you are buying and selling Shares to comply with the share standard.
- If, however, you buy and sell Shares held in excess of the number required by the share standard with the aim of making a profit from those trades, any gain may be subject to income tax. The tax consequences of any Share transaction would depend on your personal circumstances and we recommend you obtain your own professional advice on potential tax outcomes.
- Farmer Shareholders would continue to receive a taxable gross return in respect of dividends on Shares required to be held by the share standard provided the legislative requirements are complied with. Dividends on Shares held in excess of the number required by the share standard would also be taxable (as a dividend) but would be subject to RWT at the rate of 33% in the absence of imputation credits. This would be refunded by the IRD if the Shareholder was not in a taxpaying position (or the RWT exceeds the Shareholder's tax liability).
- Once Trading Among Farmers is implemented, Fonterra would not obtain a deduction for dividends paid on Shares held in excess of the number required by the share standard. Fonterra could continue to deduct dividends paid on Shares required to be held by the share standard (being the large majority of its Shares) provided the legislative requirements are complied with. The exception to this is where the dividend relates to Shares that have been placed with the Fonterra Shareholders' Fund. In this case Fonterra would not obtain a deduction for dividends paid to the Fund.
- If Fonterra has insufficient tax losses, the non-deductibility of part of its dividends may put Fonterra into a taxpaying position which would give rise to imputation credits. These imputation credits can be attached to dividends paid on Shares held in excess of the number required by the share standard. Imputation credits can be used to offset the tax on dividends relating to Shares held in excess of the number required by the share standard and are non-refundable but they can generally be carried forward if unutilised.

While the current Constitution enables the Board to put in place a regime for Trading Among Farmers before the end of December 2013 or a later date specified by the Board, the Board is not obliged to do so even if, during this period, the preconditions are met. There is no assurance or guarantee that Trading Among Farmers will be implemented or, if implemented, the final structure that will be implemented or the timing of such implementation.

WHO IS INVOLVED IN PROVIDING IT FOR ME?

Fonterra is the issuer of the Shares, Peak Notes, Capital Notes and Redeemable Preference Shares. As at the date of this Investment Statement, Fonterra's registered office is at 9 Princes Street, Auckland, 1010.

The Trustee for the Peak Notes and Capital Notes is The New Zealand Guardian Trust Company Limited, whose registered office as at the date of this Investment Statement is at Level 7, Vero Centre, 48 Shortland Street, Auckland, 1010.

The directors of Fonterra as at the date of this Investment Statement are Colin Charles Armer, Malcolm Guy Bailey, John Charles Ballard, Ian James Farrelly, David Alexander Jackson, David Nigel Macleod, John Anthony Monaghan, Nicola Mary Shadbolt, Henry William van der Heyden, Jim William van der Poel, John Anthony Waller, Ralph Graham Waters and John Speer Wilson**.**

The names of the directors of Fonterra and the registered office of Fonterra and the Trustee set out above may change after the date of this Investment Statement. The names of the current directors and registered office of Fonterra and the Trustee can be found at any time by searching the public register maintained by the Companies

Office of the Ministry of Economic Development on its website at www.business.govt.nz/companies (no fee is payable to obtain this information).

Fonterra has been operating in its current form since 16 October 2001. Fonterra's principal activities (as distinct from those of its subsidiaries) are to collect milk from supplier shareholders and sell it to subsidiaries, and oversee and support the operations of the Fonterra Group. Fonterra also pays the supplier shareholders for the milk supplied, and, if the Board so elects, may pay a dividend to shareholders. The subsidiaries treat and distribute milk and cream and manufacture, market and sell milk products. The Fonterra Group processes around 90% of New Zealand's milk supply.

Fonterra's core business is the collection of milk and the manufacture and sale of commodity and specialty dairy ingredients which are mostly sold in the globally-traded dairy market, which it largely carries out through its subsidiaries. The Fonterra Group carries out its business through strategic business units that are defined by its core ingredients business and businesses operating in geographical areas: Standard and Premium Ingredients; Australia/New Zealand ("**ANZ**"); Asia/Africa and Middle East ("**AME**"); and Latin America.

The Fonterra Standard and Premium Ingredients business represents the collection, processing and distribution of New Zealand milk, global sales and marketing of Standard and Premium Ingredients, international farming, sustainability, external relations, RD1 and group functions. The Fonterra ANZ business represents fast moving consumer goods (FMCG) operations in New Zealand (including export to the Pacific Islands) and all FMCG and Ingredients operations in Australia. It includes foodservice sales in Australia and New Zealand, except for foodservice sales to Quick Service Restaurants. The Fonterra AME business represents FMCG operations in Asia, Africa and the Middle East, and foodservice sales in Asia/AME and China. The Latin America business represents FMCG operations in Chile and equity accounted investments in South America.

The Fonterra Group's brands include ANCHOR, ANLENE, ANMUM, MAINLAND, SOPROLE, CHESDALE, TIP TOP, BEGA and FRESH 'N FRUITY.

HOW MUCH DO I PAY?

Co-operative Shares

What do I have to pay?

If you wish to begin supplying Fonterra or intend to increase your existing supply to Fonterra in the next Season, you may apply to Fonterra during the application period, which is required to run from at least 15 December to 28 February.

The benefits of applying during the application period are that:

- Fonterra must accept your application (subject to certain minimum supply, transport cost exceptions and capacity constraint notices); and
- you may choose to:
    - elect to pay the fair value Share price to be set on 1 June (**"June Price"**), which you will not know at the time you apply. The process for setting the June Price is described below under *What returns will I get?*; or
    - lock in a Share price based on the price published at the time you made your application (**"Published Price"**). This is not the price you will pay. What you will pay is either the June Price (if it is within 7.5% of the Published Price) or a price determined by reference to the difference between the June Price and that Published Price (called the **"Default Price"**).

Note: Existing suppliers are not required to apply during the application period to increase supply but may wish to do so, for example, to fix the Default Price (see below).

The Default Price is determined by reference to the difference between the June Price and the price published when you applied, as follows:

- if the June Price is within + or -7.5% of the Published Price, then you pay the June Price;
- if the June Price exceeds the Published Price by more than 7.5%, then you pay the Published Price plus 7.5%; or
- if the June Price is lower than the Published Price by more than 7.5%, then you pay the Published Price less 7.5%.

If you apply during the application period and you want to pay the June Price, you must stipulate this in your application. If you do not stipulate a price, you must pay the Default Price. Some examples of how this works are set out in the box on page 16.

If you apply during the application period and you are in a geographical area to which a capacity constraint notice applies then the references above to the June Price mean the June Price in the first Season for the supply of milk (which may be the Season immediately following the application period during which you apply or the following Season, depending on when supply commences under the capacity constraint).

If you apply outside the application period, you do not have the opportunity to choose the method of determining the price; you must pay the June Price.

There are other circumstances in which you may be offered or issued Shares by Fonterra. These are described under the heading "Co-operative Shares" on pages 3 to 6. Also as described in that section, the price for a Share in those circumstances will be the June Price in the Season in which the issue is made.

What is the Published Price?

Fonterra must disclose a Published Price throughout the application period (and the June Price as soon as it is set) on its website (www.fonterra.com), and also publish it once in the daily newspapers of Whangarei, Auckland, Hamilton, Rotorua, Hawke's Bay, New Plymouth, Palmerston North, Wellington, Nelson, Christchurch, Dunedin and Invercargill.

Fonterra may amend the Published Price during the application period but must publish any such amendment. Published prices could change, for example, because of changes in circumstances which impact on Fonterra's business prospects.

All references in this Investment Statement to the Published Price are references to the most recent Published Price at the time you make your application.

When do I have to pay for my Shares?

New suppliers: All Shares must be fully paid for by the later of 1 June and the day of the Season on which you commence supply, unless the Board offers a deferred payment arrangement. The Board will notify shareholders prior to the start of a season as to whether a deferred payment arrangement will be offered and, if so, on what terms. The Board is not obliged to offer a deferred payment arrangement in any season.

Fonterra may at its discretion require payment of a non-refundable deposit. If this applies, you will be advised upon application, and details as to the amount and timing of any deposit will be provided at that time. Any deposit will not be more than 20% of the total amount payable, and will not be payable before the earlier of 15 working days after Fonterra accepts your application, or the last day of the application period.

Existing suppliers increasing supply: You are not required to apply during the application period to increase your supply. If you do apply to increase your supply, all Shares applied for must be fully paid for by the due date that will be specified in Fonterra's acceptance of your application. This will not be earlier than 1 June. If you apply to increase supply, you have the option to elect to pay the June Price or the Default Price (see "What do I have to pay?" above). The Board may offer a deferred payment arrangement (see "New suppliers" above).

If you apply to increase supply, Fonterra may at its discretion require payment of a non-refundable deposit. If this applies, you will be advised upon application, and details as to the amount and timing of any deposit will be provided at that time. Any deposit will not be more than 20% of the total amount payable, and will not be payable before the earlier of 15 working days after Fonterra accepts your application, or the last day of the application period.

If you increase your supply, but do not apply to do so, you do not have to pay for the additional Shares until Fonterra issues them on or before 15 July in the Season following the Season you increase your supply (unless Fonterra exercises its discretion to require you to subscribe and pay for Shares relating to the increased supply during the Season you increase your supply). While this means you do not have to pay for the Shares until the end of the Season, you do not have the opportunity to choose the method of determining the share price - you must pay the June Price for the Season following the Season in which you increased supply.

Capacity constraint: All Shares in circumstances where a capacity constraint notice applies must be fully paid for by the later of 1 June and the day of the Season on which you commence supply.

Fonterra may at its discretion require payment of a non-refundable deposit. If this applies, you will be advised upon application, and details as to the amount and timing of any deposit will be provided at that time. Any deposit will not be more than 20% of the total amount payable, and will not be payable before the earlier of 15 working days after Fonterra accepts your application, or the last day of the application period.

Other circumstances: There are other circumstances in which you may be offered or issued Shares by Fonterra. These are described under the heading "Co-operative Shares" on pages 3 to 6. Payment terms in respect of certain of these circumstances are described below, otherwise payment terms will be set by Fonterra.

Other issues during a Season: The payment terms that will apply to any other issues of Shares during a Season will be set by the Board on the issue of such Shares.

Issue of additional Shares: The Board may determine whether to issue additional Shares in any season. If the Board makes such a determination, the period during which Shareholders and new suppliers can apply for additional Shares, and the terms of issues of those additional Shares, may be set by the Board (see page 6).

What consideration can I use to pay for the Shares?
New suppliers: You must pay for your Shares in cash, unless you have Capital Notes, in which case Fonterra can require you to pay in part or in whole by redeeming Capital Notes having an aggregate principal amount equal to the issue price of the Shares.

Other circumstances: The Board may require you to pay for any additional Shares by:

- paying cash;
- redeeming any Capital Notes you hold;
- redeeming any excess Peak Notes you hold; or
- any combination of the above.

Share price examples:

These examples are intended to provide you with an illustration of how the price of your Shares will be determined. These examples are extreme and are for illustrative purposes only. They are not intended to reflect what may, in fact, occur.

In the following example, Suppliers A, B, C and D apply to start or increase supply for the next Season. The same methodology used in these examples would apply to determining the Surrender Value for Shares under "*How do I cash in my investment?*" on page 36.

On 15 December Fonterra publishes a price for Shares of $6.70.
On 15 January Fonterra changes this price to $7.30.
On 15 February Fonterra again changes the price to $6.10.
On 31 May Fonterra sets the June Price at $6.65.

Supplier A applies on 15 December and does not elect the June Price. Supplier A therefore pays the Default Price. In this case, the Default Price will be the June Price of $6.65 (because the June Price is within + or - 7.5% of the Published Price at 15 December).

Supplier B applies on 15 January and does not elect the June Price. Supplier B therefore pays the Default Price. In this case, the Default Price will be the Published Price at 15 January minus 7.5%, which equals $6.75 (because the June Price falls below the published price at 15 January by more than 7.5%).

Supplier C applies on 15 February and does not elect the June Price. Supplier C therefore pays the Default Price. In this case, the Default Price will be the Published Price at 15 February plus 7.5%, which equals $6.56 (because the June Price exceeds the Published Price at 15 February by more than 7.5%).

Supplier D applies on 15 December and elects the June Price (which has not been published at the time of the application). Supplier D therefore pays $6.65.

Cooling-off period

If you have not received an Investment Statement when you apply, Fonterra will send you a copy when it notifies you of the acceptance of your application. In such cases, you will have 10 working days (from the date your Investment Statement is sent to you) in which to decide to withdraw your application.

Trading Among Farmers

In the event that Fonterra moves to adopt and implement Trading Among Farmers, the obligations on Fonterra to issue or redeem Shares under the current Constitution and the DIRA at a fair value determined in accordance with the current Constitution would cease. In place of those obligations, it is intended that Shareholders be permitted to trade shares on a Fonterra Shareholders' Market, which is proposed to be a registered market operated by a registered exchange under the Securities Market Act 1988. As at the date of this Investment Statement, the Shares have not been approved for trading on a registered market, nor has any application been made to enable the Shares to be traded on a registered market. In addition, a Fonterra Shareholders' Fund would be established and a shareholder would be permitted to transfer a proportion of its Shares to a custodian to hold on behalf of that fund.

The price at which Shares would be acquired or disposed of on the Fonterra Shareholders' Market would be determined by the buyers and sellers trading on that market. The price of Shares may rise or fall due to numerous factors including those which affect the performance of Fonterra or the actual or perceived value of Fonterra, restrictions on persons who may participate in the Fonterra Shareholders' Market, and the operation of the Fonterra Shareholders' Market including its inter-relationship with the Fonterra Shareholders' Fund.

While the current Constitution enables the Board to put in place a regime for Trading Among Farmers before the end of December 2013 or a later date specified by the Board, the Board is not obliged to do so even if, during this period, the preconditions are met. There is no assurance or guarantee that Trading Among Farmers will be implemented, or, if implemented, the final structure that will be implemented or the timing of such implementation.

Further information regarding Trading Among Farmers is set out on pages 8 to 12.

Peak Notes

What do I have to pay?

The issue price of each Peak Note is fixed at $30.

When do I have to pay for my Peak Notes?

The payment times for Peak Notes are the same as those described for Shares above.

What consideration can I use to pay for the Peak Notes?

The Board may require you to pay for Peak Notes by:

- paying cash;
- redeeming any Capital Notes you hold; or
- a combination of both.

Capital Notes

No money is payable by you if Fonterra issues you Capital Notes as consideration for the surrender or redemption of your Shares, Peak Notes or Redeemable Preference Shares as described under the heading "*How do I cash in my investment?*" below.

Redeemable Preference Shares

No money is payable by you for Redeemable Preference Shares.

Fonterra may issue Redeemable Preference Shares to you as consideration for some or all of the Surrender Value of your Shares and the redemption of your Peak Notes in the limited circumstances outlined under the heading "*What sort of investment is this?".*

Payments

Any payments required in respect of the securities above should be sent to the following address:

Fonterra Co-operative Group Limited
9 Princes Street
Private Bag 92 032
Auckland Mail Centre.

WHAT ARE THE CHARGES?

There are no application fees payable for new or existing suppliers. However, Fonterra may introduce or amend application fees from time to time.

Other than any applicable application fee and the applicable issue price for the securities, there are no charges associated with the issue of Fonterra's securities. As a supplying shareholder, however, you may be required to pay Fonterra for other services relating to the supply and collection of milk to Fonterra under the Terms and Conditions of Supply. Fonterra may, at its discretion, pay directors' fees to its directors.

WHAT RETURNS WILL I GET?

The information in this section should be read in conjunction with the information contained under the heading *What are my risks?.*

There are three primary sources of return from the Fonterra business for supplying shareholders, namely:

- an amount paid for the milk you supply Fonterra;
- dividends (if any) paid on Shares held during a Season; and
- the change in value (if any) in the fair value of your Shares.

These returns are affected in different ways by the Fonterra business and the risks the Fonterra business faces.

Any liability for taxation on returns that is described in this section is based on current enactments as at the date of this Investment Statement.

Payment for milk

The Board will determine the amount that it will pay for milk having primary regard to the recommendation of the Milk Price Panel as to the Farmgate Milk Price, which is calculated in accordance with Fonterra's "Farmgate Milk

Price Manual". All relevant factors (including dividends, and any amounts to be retained for investment or other purposes) are taken into account in the Board's determination of the amount it will pay for milk.

The Farmgate Milk Price Manual is overseen by the Board and is required to reflect the "Milk Price Principles" which are set out in the Constitution. The Milk Price Panel is appointed by the Board to oversee the governance of the Farmgate Milk Price and the Farmgate Milk Price Manual, in accordance with its terms of reference. The Farmgate Milk Price Manual is administered by a separate Milk Price Group resourced by an external service provider. The head of the Milk Price Group reports directly to the Chair of the Milk Price Panel and is required to be an independent party.

The Bill proposes amendments to the DIRA, which include the introduction of a Farmgate Milk Price monitoring and oversight regime and requirements in relation to maintaining a Milk Price Panel. Further information regarding the proposed changes to DIRA regarding the Farmgate Milk Price are set out on page 30.

The amount paid for milk is a payment made for milk supplied by a shareholder and is not a return on any of the securities. During a Season the Board may estimate from time to time the amount to be paid for milk for that Season, expressed in dollars per kilogram of milksolids.

The final payout amount for milk supplied during a Season is only determined by the Board following the end of that Season. There is no assurance or guarantee as to the level of any amount paid for milk.

The Board will authorise the times of interim and final payments for each Season. Payments for special terms and conditions for the supply of milk will be made as agreed with those individual shareholders.

Special terms and conditions may be agreed for Contract Supply and for supply under unshared supply entitlements, if they are permitted in any Season.

A "capacity charge" has applied since the Season ended 31 May 2007. In effect, this is a replacement for Peak Notes. It is an adjustment that will be made to all milk payments reflecting each shareholder's peak production profile. Each shareholder will be permitted to supply a certain amount of milk during peak. Supply over that, and a charge will be deducted from your milk payments. Supply below that, and your milk payments will be increased.

Calculation of the adjustment will be set out in the terms and conditions of supply. The amount of the adjustment will be calculated at the end of each Season based on the amount of milksolids obtainable from milk supplied to Fonterra during the Season.

The capacity charge will apply to all milk you supply to Fonterra, whether you supply under your Shares or an unshared supply entitlement, or on Contract Supply.

Dividends

General

Fonterra can pay dividends on Shares. However, it is under no obligation to do so. The Board may at its discretion authorise the times of payment of interim and final dividends for each Season.

As at the date of this Investment Statement, Fonterra's policy is to pay the Distributable Profit for a season (after retentions) as a dividend on shares held on specified record dates during that Season. This is permitted by section CD34B of the Income Tax Act 2007 which provides that the 20 working day rule for fixing a date in section 125(2) of the Companies Act does not apply to shareholders' entitlements to receive distributions where a co-operative company has given a notice of election to the Registrar of Companies before the distributions are paid, the date is fixed before the entitlements arise and that date is within the year or period to which the distribution relates. The proposed record date for an interim dividend for each financial year is 31 March with the interim dividend to be paid by 20 April. The proposed record date for the final dividend for each financial year is 31 May with the final dividend payment to be made by 20 October. This policy may be changed by the Board. There is no assurance or guarantee as to the level of any dividend that may be paid.

Dividend/retention policy

The Board may at any time in the future advise you on its approach to the payment of dividends (including its approach to retentions). As noted above, the Board may change its policy and approach in relation to dividends and retentions at its discretion and at any time. As a result, any approach or policy on the payment of dividends (including any approach to retentions) advised by the Board may change before the proposed payment dates for any interim dividend and the proposed payment date for any final dividend. Accordingly, the existence and amount of any dividend return on any Shares you hold (including any excess Shares issued to you) will not be apparent until a formal decision on an interim dividend and a final dividend is made by the Board and implemented. Fonterra may provide earnings guidance from time to time to the Exchange, which may include information on dividends.

The Distributable Profit achieved by Fonterra in the past has been very volatile, and has in certain financial years been very low, and no assurance is given as to the level of dividend that may be paid in the future. The level of return on Shares is a risk for you as an investor in Shares.

The principal factors that could impact on dividends (as well as other returns) are set out under "Impacts on returns" on pages 20 and 22, and the principal risks that could impact on dividends are set out under "What are my risks?" on pages 26 to 36. The policy and approach of the Board in relation to dividends in any season is not necessarily indicative of its policy and approach to dividends in any subsequent season.

Co-operative Share fair value

Fair value return on surrender

Your return on Shares will be the price you receive, less any amount not paid up on that Share, if you surrender your Shares, as described under the heading *How do I cash in my investment?.* If, as an existing supplier, you give a "notice of withdrawal" during the application period to decrease or cease supply for the upcoming Season, you may choose either the June Price or the Default Price for the upcoming Season for payment for the Shares you wish to surrender. If you do not give a "notice of withdrawal" to decrease or cease supply, or you give a notice of withdrawal outside the application period which Fonterra accepts, the June Price for the upcoming Season will apply. The June Price and the Default Price are described more fully above under *How much do I pay?*

You can give a notice of withdrawal and election of either the June Price or the Default Price during the application period. If you do not make an election by the end of the application period the Default Price applies.

The form of consideration you may receive for surrendered Shares is described on page 37. If you give a notice of withdrawal during the application period, or a notice of withdrawal outside the application period (which Fonterra accepts), Fonterra must pay you the Surrender Value of your Shares within 30 working days after the end of the Season in which you give that notice.

If you give a notice of withdrawal, but do not actually decrease your supply during the next Season, Fonterra may determine the amount of milksolids you will supply during that Season and require you to subscribe and pay for Shares immediately based on that determination.

How are the June Price and the Default Price determined?

The June Price and Published Price (which then determines the Default Price) of Shares are determined by the Board in accordance with the Constitution. The relevant provisions of the Constitution require an additional factor to be taken into account in determining those prices. However, transitional provisions provide that this new factor is not fully taken into account for a period of time, and set out a separate regime to apply in this transition period.

The regimes to apply following the transition period, and during the transition period, are described below.

Throughout, and after, the transition period there will be both a June Price and a Default Price for each Season (although, as discussed below, the methodology for determining these prices in each period will differ). The benefit of the Default Price is that you have the ability in the December to February application period to limit your exposure to movements in the fair value Share price between December and June to no more than 7.5%. If you have made an application or given a notice of withdrawal and do not choose the June Price you will not have to pay any more (if you are applying for Shares) or receive any less (if you are intending to surrender Shares) than + or - 7.5% of the Published Price for any Share you are subscribing for or surrendering. However, in choosing the benefits of certainty that go with the Default Price, there is also the risk that the Default Price may result in you paying more than you need to pay (if you are applying for Shares) or receiving less than you could have received (if you are surrendering Shares) if you had elected the June Price.

After the transition period

Following the transition period, the June Price of the Shares will be determined by the Board within a fair value range set by the independent valuer (appointed by the Shareholders' Council) in accordance with Fonterra's Constitution. The June Price might not be the mid point of that range. The current independent valuer is Grant Samuel & Associates Pty Limited (the **"Valuer"**). As at the date of this Investment Statement, the Valuer has no relationship (other than that of independent valuer) with, or interest in, Fonterra or any associated persons of Fonterra, nor does it have any interest in the Shares or any relationship with any other person who has a material interest in the Shares.

The Constitution sets out the matters that the Valuer will take into account when determining the fair value range. These include the return on the commodity business, the return on the consumer business, expected changes in milk volumes supplied to Fonterra, forecasted exchange rate movements and any limitations or restrictions on the circumstances under which Shares may be issued, surrendered or otherwise transacted ("**Restrictions**"). The Restrictions recognise the intended transition to Trading Among Farmers (refer page 8 to 12). A December interim fair value range will be determined by the Valuer, and an interim valuation price will be determined by the Board in the same manner as the June Price and this will be the Published Price. That price could be amended if updated fair value ranges were received. The independent valuer's December 2011 valuation derived standalone valuation determinations from a discounted cash flow analysis and a market approach which included an analysis of selected public companies and an analysis of selected transactions. This involved a consideration of the market approach valuation along with the discounted cash flow analysis to derive an overall enterprise value for Fonterra.

The June Price will be based on an updated valuation by the Valuer. In May of each year, the Valuer will provide the Board with its final fair value range and the Board will choose the June Price within that range. Accordingly, the relevant Published Price (and hence the Default Price) may differ from the June Price.

Transition period

To allow for the transition to a fair value range taking into account the Restrictions, transitional provisions relating to the setting of the fair value range and the determination of the Published Price and the June Price have been included in the Constitution ("**Transitional Provisions**"). The Transitional Provisions will apply in respect of the 2010/2011 Season, and for each subsequent Season until transition is complete as described below. Each Season which is subject to the Transitional Provisions is called a "Transition Season".

Under the Transitional Provisions, the Valuer must set an interim and final fair value range in respect of each Transition Season which takes into account the Restrictions ("**Restricted Market Value Range**"), and also an interim and final fair value range which does not ("**Fair Value Range**").

The December interim valuation price for each Transition Season will be:

- set within the interim Restricted Market Value Range, if the Base Price is equal to or less than the mid point of the interim Restricted Market Value Range;
- set within the interim Fair Value Range, if the Base Price is equal to or greater than the mid point of the interim Fair Value Range; or
- the Base Price, in all other circumstances.

The June Price for each Transition Season will be:

- set within the Restricted Market Value Range, if the Base Price is equal to or less than the mid point of the final Restricted Market Value Range;
- set within the Fair Value Range, if the Base Price is equal to or greater than the mid point of the final Fair Value Range; or
- the Base Price, in all other circumstances.

If the Board sets the June Price for a Transition Season within the Fair Value Range, then that June Price will be the Base Price for each subsequent Transition Season, subject to any subsequent change in accordance with this paragraph.

If the Board sets the June Price within the final Restricted Market Value Range, transition will be complete and the Transitional Provisions will cease to apply. From then on, the June Price and Published Price will be set as described above.

Again, the Published Price (and Default Price) for a Transition Season may differ from the June Price.

In the event that Fonterra moves to adopt and implement Trading Among Farmers, the regimes for the determination of the price of a Share (including that applying in the Transition Period) will cease to apply.

Impacts on returns

The principal factors that could impact on the returns to you are:

- a significant change in the volume of milksolids supplied to Fonterra, for example due to a material change in Fonterra's nation-wide share of milk supply or factors affecting farm production levels, or increased competition for acquisition of milk solids;

- movements in the international price for commodity products derived from milk, including without limitation, whole milk powder, skim milk powder, anhydrous milk fat, butter, dry salt cheese, casein, milk protein concentrate and lactose;
- movements in foreign exchange rates, including translational risk principally converting foreign denominated earnings into New Zealand dollars, and transactional risk which, among other things, may affect our customers' or end users' local exchange rates and propensity to acquire Fonterra products;
- material losses arising from the use of derivatives, including but not limited to instruments used to manage foreign exchange risk;
- maintenance of net earnings in Fonterra's consumer and ingredients businesses or Joint Ventures, including in the event of higher commodity prices, price controls, quality or contamination (accidental or malicious) resulting in brand or corporate reputational damage and/or increased competition in end markets;
- maintenance of projected net earnings derived from the sale of commodity dairy products;
- the achievement of the projected benefits arising from new capital investment;
- investments in, mergers with, acquisitions and/or divestments of interests in other entities and businesses;
- a change in the cost of capital for Fonterra;
- a material change in Fonterra's ability to access overseas markets either through foreign government actions resulting in increased tariffs, reduction in quotas or the imposition of new quotas, increased subsidies, regulatory changes, food assurance issues or changes to the way trade restrictions are administered, other government action in foreign jurisdictions where Fonterra has business interests such as nationalisation of assets, price controls or other matters affecting foreign assets or business returns;
- changes to the current regulatory framework for Fonterra or the dairy industry in New Zealand, including the Farmgate Milk Price monitoring and oversight regime proposed in the Bill. Further information regarding the proposed changes is set out on pages 30 to 32;
- changes in the Valuer's fair value range from valuation to valuation. These changes can result from a number of matters including, but not limited to, changes in the Valuer's assessment of Fonterra's sustainable earnings taking into account the matters set out in the Constitution and the effect of shareholder subscription for, and surrender of, capital in Fonterra. A change in the Valuer's fair value range may also result from the transition to a fair value range taking into account the Restrictions (see pages 19 and 20);
- the determination by the Board of a Fair Value for a Co-operative Share, such value not necessarily being the midpoint of the Valuer's fair value range. Further information on the Fair Value for a Co-operative Share is set out on pages 19 and 20;
- changes to the capital structure of Fonterra;
- a change in the dividend policy;
- the level of retentions by Fonterra. Retentions may reduce the dividends paid on Shares. The Board has regard to a wide range of factors in deciding whether and how much to retain at the end of each financial year;
- the Farmgate Milk Price for milk supplied by shareholders during a Season. The determination of the final Farmgate Milk PricePrice will directly impact on the Distributable Profit, and on the amount of any dividend paid on Shares. Changes to the Farmgate Milk Price Manual, which may be amended in accordance with its provisions, may impact on the allocation of revenues or costs to the Farmgate Milk Price and, as a result, on the Distributable Profit. Further information regarding the determination of the Farmgate Milk Price is set out on pages 17 and 18;
- the amount paid for milk determined by the Board, which may be less than or greater than the Farmgate Milk Price;
- material changes in Fonterra's costs (for example, without limitation, compliance costs including emissions trading schemes or the price of utilities such as energy supplies, or higher costs associated with meeting more stringent conditions on any discharges from a plant);
- material loss of essential supplies (including but not limited to raw milk, water, electricity, gas and labour);

- material changes to Fonterra’s ability to manufacture (including but not limited to failure of plant, or restrictions imposed on the operation of plant by any authority);
- changes in the volume and value of products derived from milk supplied and changes in the quality of products produced;
- the achievement or not of the projected benefits from major business improvement initiatives;
- material changes arising from ways that we contract with customers (including but not limited to length or term of contract) that are different to the assumptions in the Farmgate Milk Price calculation;
- a change in Fonterra’s or one of its brand’s reputation; and
- material changes in tax regimes in New Zealand or overseas or tax rates applicable to Fonterra or to you in respect of your investment.

One or more of these factors may occur as a result of a particular event or series of events including but not limited to climatic events, such as droughts, other natural events such as earthquakes or volcanic activity, or biosecurity outbreaks.

Broadly, the Shares will be treated for income tax purposes in much the same way as ordinary shares issued by a New Zealand company. Where Fonterra uses the applicable “treasury stock” provisions or satisfies the “brightline” and other applicable tests under the capital reduction provisions in the Income Tax Act 2007, the proceeds received on the surrender of a Share should not be taxable as a dividend for income tax purposes. If the surrender proceeds constitute a dividend, the amounts paid to the shareholder may be reduced to the extent that Resident Withholding Tax (**“RWT”**) and Non-Resident Withholding Tax (**"NRWT"**) is required to be deducted by Fonterra from the redemption proceeds. RWT will be deducted from the dividend to the extent that the dividend is not covered by imputation credits (unless the shareholder has provided Fonterra with a valid certificate of exemption for RWT purposes). NRWT may also be deducted from dividends paid to non-residents.

These comments are of a general nature only and you should consult your own tax adviser for advice in light of your own particular circumstances.

The person legally liable to pay any returns on the Shares is Fonterra.

In addition, some of the other Fonterra securities may produce returns and these are each discussed in turn below.

Peak Notes

Your return on a Peak Note will be the fixed value of each Peak Note (i.e. $30) which you will receive if you (or Fonterra) elect to redeem any excess Peak Notes you hold (as described below).

No interest

Peak Notes do not bear any interest.

Redemption

At Fonterra’s option: If you hold more Peak Notes than required by the Peak Note standard in a Season, Fonterra may redeem those excess Peak Notes on or before 15 July in that Season or as soon as practicable thereafter. Fonterra may also, at any time, at its option, on 30 business days’ notice, redeem on a pro rata basis, all or any excess Peak Notes.

At your option: If you hold excess Peak Notes in a Season, you may (on giving the Board written notice before 30 June of that Season) require Fonterra to redeem all or any of those excess Peak Notes on or before 15 July in that Season, or as soon as practicable thereafter.

In both cases, the value of the consideration for the redemption of each Peak Note is its fixed value (i.e. $30).

Fonterra may, at its option, pay the fixed value of the Peak Notes being redeemed:

- in cash; or
- by issuing you Capital Notes having an aggregate market value equal to the Peak Notes fixed value (described below); or
- by issuing you Shares with an aggregate fair value equal to the Peak Notes fixed value, but only to the extent that you require more Shares to meet the share standard; or

- any combination of the above.

Payment for the surrender of the Peak Notes will be made in the same time limits described above in respect of the Shares.

In limited circumstances (described above under the heading *What sort of investment is this?*) on page 8, Fonterra may also pay the fixed value of the Peak Notes being redeemed by issuing Redeemable Preference Shares with an issue price equal to that fixed value.

Broadly, Peak Notes are financial arrangements for income tax purposes. However, as they are not interest bearing, while they are held they should not result in gross income or deductible expenditure for income tax purposes. Where you acquire or dispose of Peak Notes for their fixed value, there should be no tax consequences for you. Where Peak Notes are acquired or disposed of for a price other than their fixed value, broadly any gain may give rise to gross income for income tax purposes and, depending on your individual circumstances, any loss may be deductible. Again, these comments are of a general nature only and you should consult your own tax adviser for advice in light of your own particular circumstances.

The person legally liable to pay any returns on the Peak Notes is Fonterra.

There are no Peak Notes currently on issue, and the Peak Note standard is currently set at zero (meaning shareholders are not currently required to hold any Peak Notes).

Capital Notes

Your return on the Capital Notes will be a combination of:

- the interest rate attaching to the Capital Notes, which is at the date of this Investment Statement 5.3% per annum. There is no minimum number of Capital Notes that must be held for interest to be payable;
- the cash you receive should Fonterra elect to redeem all or part of your Capital Notes on any Election Date;
- the cash you receive should you require Fonterra to repurchase the Capital Notes issued to you in the circumstances described below; and
- the price you receive if you choose to sell your Capital Notes.

The market price of the Capital Notes will, amongst other factors, be subject to general interest rate movements and supply and demand and may therefore fluctuate up and down on a daily basis.

Interest

Capital Notes bear interest payable on a quarterly basis. On 10 July 2011, the interest rate was reset to 4.66% per annum, comprising the One Year Government Stock Rate (as defined in the Capital Note Trust Deed) as determined by the calculation agent (which was 2.86% ("**Base Rate**")) plus the applicable margin (1.80%).

The interest rate is reviewed on 10 July in each year (**"Interest Rate Reset Date"**) and changed in line with the then current Base Rate and the applicable margin. Following each review, Fonterra will notify Capital Note holders of the change in the interest rate, which became effective on the relevant Interest Rate Reset Date.

The Base Rate will be redetermined on each Interest Rate Reset Date. The Base Rate determined on any date will apply from (and include) that date to (but exclude) the date on which it is redetermined.

The margin applicable to the Capital Notes as at 10 July 2011 was 1.80%, due to the Rating Agency's A credit rating of the Capital Notes on that date. The applicable margin will be determined on each interest payment date (set out below) on the basis of the credit rating of the Capital Notes on that date. The margin determined on any date will apply from (and include) that date to (but exclude) the date on which it is redetermined. If there is a change in the credit rating of the Capital Notes then the margin will be redetermined on (and with effect from) the interest payment date at the end of the current interest period. Ratings are statements of opinion, not statements of fact or a recommendation to buy, hold or sell any securities. A rating may be changed, suspended, or withdrawn at anytime.

The margin applicable for the determination of the interest rate will depend on the credit rating of the Capital Notes and will be determined in accordance with the following table:

Credit Rating of Rating Agency	*Margin*
AA	1.50%
AA-	1.60%
A+	1.70%

A	1.80%
A-	1.95%
BBB+	2.20%
BBB	2.60%
BBB-	3.00%
No Credit Rating	3.00%

If there is a change in the rating agency (who is, as at the date of this Investment Statement, Standard & Poor's Ratings Services) the ratings identified in the above table will be deemed to be the equivalent ratings of the new rating agency.

The person legally liable to pay interest on the Capital Notes is Fonterra.

Interest payments

Interest will accrue and be calculated daily from (and including) the date of allotment of the Capital Note or, if the Company so elects, the interest payment date immediately preceding the date of allotment of the Capital Note, in each case on the basis of a 365 day year.

Interest will cease to accrue on the Capital Notes on redemption or purchase by Fonterra or if a liquidator is appointed for Fonterra. Interest at the interest rate will accrue on the aggregate of the principal amount of a Capital Note and accrued interest thereon at the date of liquidation until the Capital Note is redeemed by payment of both the principal amount and accrued interest to the date of liquidation and interest accrued after the date of liquidation.

The interest payment dates for each Capital Note are 10 January, 10 April, 10 July and 10 October or if any such date is not a business day, the next business day. Interest payments will be made to the Capital Note holder recorded on the register on the Friday between ten and three days prior to the relevant interest payment date. Interest payments will be made by cheque or direct bank credit.

Issue of Notes in lieu of interest

If the Board resolves that payment of interest on an interest payment date would have, or be likely to have, a material adverse effect on Fonterra, Fonterra may issue further Capital Notes to holders in lieu of the payment of all or part of a cash payment of interest due on the interest payment date. Such further Capital Notes will, however, constitute interest for income tax purposes (see *Deductions and withholdings* below) and the total number of further Capital Notes issued to you will be reduced to reflect any RWT, NRWT (or Approved Issuer levy) payable as a consequence. Such Capital Notes will be issued on the same terms as the Capital Notes issued under this Investment Statement. Fonterra may not, during the interest period following an interest payment date on which Fonterra has elected to issue further Capital Notes in lieu of interest (or at any time during which interest remains unpaid where Fonterra has not issued Capital Notes in lieu thereof):

- make any distribution to shareholders (including financial assistance in respect of any shares in Fonterra) or make any payments for the supply of milk in excess of permitted supplier payments (as defined in the Prospectus); or
- make any payment of any indebtedness ranking equally or subsequent in priority to the Capital Notes.

Election Date

The Capital Notes have an election date of 10 July in each year commencing on 10 July 2002 (**"Election Date"**). Fonterra has the option to redeem all or part of the Capital Notes for cash on an Election Date. This option prevails over any right of a holder in respect of any Capital Note. Fonterra will give notice in writing to holders of its election to exercise its option (**"Election Notice"**) at least 30 days before the Election Date. The redemption price will be the greater of:

(a) the principal amount of the Capital Note; and

(b) the amount determined by Fonterra as representing:

 (i) the volume weighted average sale price at which Capital Notes have been traded on the NZDX during the 10 business days preceding (but not including) the date on which Fonterra issues an Election Notice, discounted if necessary to reflect the interest that has accrued on a Capital Note during the period from (and including) the last interest payment date to (but excluding) the date on which Fonterra issues the Election Notice; or

(ii) where Capital Notes have not traded on the NZDX on more than 5 of those 10 business days, or where the Capital Notes have ceased to be quoted on the NZDX, the amount determined by an independent, reputable financial institution selected by Fonterra, in consultation with the Trustee to be a fair market price for such Capital Notes.

Fonterra's option to redeem Capital Notes may be exercised in respect of some or all of the Capital Notes on a non pro rata basis.

Fonterra will only redeem Capital Notes if, in the reasonable opinion of the Board, Fonterra will be solvent (as defined in the Prospectus) immediately following the payment of the aggregate amount owing under the Capital Notes to be redeemed to the holders on the Election Date.

Further details regarding Fonterra's option to redeem Capital Notes on Election Dates is set out in the Capital Notes Trust Deed and in the Prospectus.

Repurchase of Capital Notes by Fonterra

The following applies only if Fonterra (or an associated person of Fonterra) acquired Capital Notes during the month immediately before Capital Notes were issued to you as payment for the surrender of your Shares or Peak Notes.

Under the DIRA, you may elect to require Fonterra to purchase some or all of the Capital Notes issued to you at any time within 6 weeks after the date they were issued by giving written notice to Fonterra.

Fonterra must repurchase your Capital Notes by paying cash for a price not less than 97.5% of the market price at which they were issued to you. Payment must be made within 10 working days after receiving your written notice.

Deductions and withholdings

All amounts payable by Fonterra in respect of the Capital Notes shall, except as otherwise required by law, be paid free of deductions or set off. RWT will be deducted from payments of interest to resident holders (and non-resident holders carrying on business through a fixed establishment in New Zealand) unless Fonterra is satisfied, at least 10 business days prior to the relevant interest payment date, that such deductions are not legally required. For income tax purposes, interest includes the amount by which the redemption proceeds exceed the issue price for the Capital Note.

RWT will be deducted from the gross amount of interest paid or credited to holders in accordance with the provisions of the Income Tax Act 2007.

Non-corporate holders that supply their IRD number to Fonterra may elect for RWT to be deducted at a rate of 10.5%, 17.5%, 30% or 33%. Non-corporate holders who do not supply their IRD number to Fonterra or who do not make an election will have RWT deducted at a rate of 33%.

Corporate holders that supply their IRD number to Fonterra may elect for RWT to be deducted at a rate of 28% or 33%. Corporate holders that supply their IRD number to Fonterra but who do not make an election will have RWT deducted at a rate of 28%. Corporate holders who do not supply their IRD number to Fonterra and who do not make an election will have RWT deducted at a rate of 33%.

It is important that a holder elect the correct RWT rate. Electing an RWT rate lower than the holder's personal tax rate may result in a requirement to file a tax return (or the provision of an income statement by Inland Revenue), and to account for the tax shortfall. Conversely, if a holder elects an RWT rate higher than the holder's personal tax rate, a tax return may need to be filed in order to obtain the relevant tax refund.

RWT will not be deducted where the New Zealand tax resident holder provides a copy of their current RWT exemption certificate to Fonterra.

In addition, gains or losses arising as a result of the disposal of Capital Notes may be subject to income tax. Investors are urged to seek tax advice in relation to tax matters with reference to their particular circumstances.

NRWT will be deducted from payments of interest to non-resident holders (except to non-resident holders carrying on business through a fixed establishment in New Zealand), unless Fonterra is satisfied that such deductions are not legally required. Fonterra has obtained and intends to maintain Approved Issuer status. In most cases, this will allow Fonterra, at the request and expense of a non-resident holder (other than a non-resident holder carrying on business through a fixed establishment in New Zealand), to make payments to that Holder without deducting NRWT. Instead it will deduct the Approved Issuer levy from the Holder's interest payments.

Again, these comments are of a general nature only and you should consult your own tax adviser for advice in light of your own particular circumstances.

Redeemable Preference Shares

Your return on Redeemable Preference Shares will be a combination of:

- the dividend attaching to the Redeemable Preference Shares, which will be 50% or more of the interest rate on Capital Notes issued at the same time as, or most recently before, the Redeemable Preference Shares were issued; and
- the redemption value of Redeemable Preference Shares, which will be at least the fair value of the Shares for which the Redeemable Preference Shares were issued or the price you receive if you choose to sell your Redeemable Preference Shares.

The price of the Redeemable Preference Shares will, amongst other factors, be subject to general interest rate movements and supply and demand and may therefore fluctuate up and down on a daily basis. Fonterra must ensure that the Redeemable Preference Shares are tradable.

Dividend

A cumulative dividend will be paid on the Redeemable Preference Shares. The dividend rate will be determined by the Board by reference to a percentage of the interest rate of the Capital Notes, but must be 50% or more of the interest rate on Capital Notes issued at the same time as, or most recently before, the Redeemable Preference Shares were issued.

Redemption

Election option: At a time specified by Fonterra, but no later than 3 years after the Redeemable Preference Shares are issued to you, you may elect to convert your Redeemable Preference Shares into:

- Shares at least equal to the fair value of the Shares that you are entitled to hold under the Constitution for which the Redeemable Preference Shares were issued; or
- cash or Capital Notes as determined by Fonterra.

At Fonterra's option: Fonterra must redeem each Redeemable Preference Share on the date determined by the Board at the time of its issue. That redemption date will be no later than 3 years after their issue.

The Redeemable Preference Shares are redeemable at Fonterra's option for cash for an amount, or the issue of Capital Notes, at least equal to the fair value of the Shares for which the Redeemable Preference Shares were issued.

It is possible that, in certain circumstances, a redemption of Redeemable Preference Shares may be a dividend for income tax purposes. To the extent that the redemption proceeds constitute a dividend, the amounts paid or otherwise credited to or applied on behalf of the shareholder may be reduced to the extent that RWT or NRWT is required to be deducted by Fonterra from the redemption proceeds. RWT will be deducted from the dividend to the extent that the dividend is not covered by imputation credits (unless the shareholder has provided Fonterra with a valid certificate of exemption for RWT purposes). NRWT may also be deducted from dividends paid to non-residents. Again, these comments are of a general nature only and you should consult your own tax adviser for advice in light of your own particular circumstances.

The person legally liable to pay any returns on the Redeemable Preference Shares is Fonterra.

WHAT ARE MY RISKS?

The principal risks for you are that you do not recover the sum which you paid for the securities when you come to exit Fonterra, or when you surrender securities (for example after a reduction in supply or change to your milk supply profile) or you do not receive the returns on your investment as described under the heading *What returns will I get?*. You may not recover the sum you paid and/or receive the returns described for a number of reasons including:

- reduction in the fair value of Shares;
- fluctuations in the amount paid for milk;
- fluctuations in dividends;
- a change in the dividend policy;

- Fonterra may become insolvent or be placed in receivership, voluntary administration, statutory management or liquidation or cease to have sufficient assets to pay returns to shareholders and noteholders;
- the operational and financial performance of Fonterra may be worse than expected;
- the Board exercising its right to issue Redeemable Preference Shares that are not immediately redeemable as consideration for the surrender of Shares; and
- in the event of a change in company tax rates, individual income tax rates, or the way such rates affect a shareholder's taxable income, such changes may impact on the returns to shareholders.

The likelihood that you will not recover the sum you paid and/or receive the returns described is affected by numerous risk factors. The principal risk factors affecting Fonterra are outlined under the headings below. The Shares will, in many instances, be more sensitive to the risks outlined below (as these securities reflect the underlying value of the Fonterra business) than the Capital Notes, Peak Notes and Redeemable Preference Shares (as the value and return on these securities is more related to Fonterra's ability to meet its obligations to pay the amounts owing on them).

You could receive none of, or less than, the returns described under the heading *What returns will I get?* if Fonterra becomes insolvent for any reason. However, providing you have paid fully for the securities you hold you will not be liable to pay any money to any person as a direct consequence of your holding Fonterra securities if Fonterra becomes insolvent. You should be aware that, on the liquidation or receivership of Fonterra, any outstanding liabilities of Fonterra will likely rank ahead of the securities offered under this Investment Statement (for a description of how the securities rank in priority, as between one another, see *What sort of investment is this?)*.

The return you will receive for your Shares when you exit Fonterra or reduce supply will be an amount established in accordance with the valuation procedures in the Constitution. As a consequence, your return will be dependent on the valuation methodology adopted by the Valuer, and the Board's determination of the fair value under the Constitution at that time. These share valuation uncertainties are in addition to the risks associated with Fonterra's operational and financial performance described elsewhere which those values are intended to reflect.

A reduction in the fair value of Shares could occur because the Board determines a lower fair value than the fair value that applied at the time you subscribed for your Shares.

Fonterra may issue you with Capital Notes in payment for your Shares, Peak Notes or Redeemable Preference Shares (see *How do I cash in my investment?* below). You can elect to continue to hold those Capital Notes (they earn interest, at a rate that is reviewed annually) or trade them. The amount you will receive for those Capital Notes if you elect to sell them will vary depending on whether they are redeemed or repurchased by Fonterra under the Capital Notes Trust Deed (for a price determined in accordance with the Capital Notes Trust Deed) or sold. See *What returns will I get?* above.

If Fonterra's operational and financial performance is worse than expected, the future returns you receive in respect of the securities offered under this Investment Statement may be less than the price you paid for them and the returns may be less than you anticipated. Some of the principal factors which may affect Fonterra's performance are outlined under the headings below. The following risks can impact to differing degrees on the three principal sources of return (amounts paid for milk, dividends and changes in the Share fair value). Given that Fonterra carries out its business largely through its subsidiaries, risks that could affect the Fonterra Group could also affect Fonterra and so risks relating to both Fonterra and the Fonterra Group are outlined below.

Use of Fonterra capital to pay exiting or reducing shareholders

As at the date of this Investment Statement, Fonterra is required to pay exiting or reducing shareholders out of its own resources. If there were a significant number of exiting or reducing shareholders in any year, as a result of shareholders switching supply to competitors or for any other reason, Fonterra would be placed under financial pressure which would affect the fair value Share price and returns. This risk is managed, but not removed, by the availability of Capital Notes and Redeemable Preference Shares.

Trading Among Farmers

In the event that Fonterra moves to adopt and implement Trading Among Farmers, the obligations on Fonterra to issue or redeem Shares under the current Constitution and the DIRA at a fair value determined in accordance with the current Constitution, and the risks associated with those obligations, would cease.

In place of those obligations, it is intended that shareholders be permitted to trade shares on a Fonterra Shareholders' Market, which is proposed to be a registered market operated by a registered exchange under the

Securities Market Act 1988. As at the date of this Investment Statement, the Shares have not been approved for trading on a registered market, nor has any application been made to enable the Shares to be traded on a registered market. In addition, a Fonterra Shareholders' Fund would be established and a shareholder would be permitted to transfer a proportion of its Shares to a custodian to hold on behalf of that fund. It is proposed that the price at which Shares would be acquired or disposed of on the Fonterra Shareholders' Market would be a determined by the buyers and sellers trading on that market.

Accordingly, the implementation of Trading Among Farmers would give rise to pricing and other risks associated with any investment in a company with tradeable shares. The price of Shares may rise or fall due to numerous factors including those which affect the performance of Fonterra or the actual or perceived value of Fonterra, restrictions on persons who may participate in the Fonterra Shareholders' Market, and the operation of the Fonterra Shareholders' Market including its inter-relationship with the Fonterra Shareholders' Fund.

While various capital structure models have been considered in the development of Trading Among Farmers, the final structure is likely to be novel. Accordingly, until it is launched, it is uncertain how the Trading Among Farmers model will perform and no assurance can be given as to whether you will recover the sum you paid for your Shares and/or receive the returns described above in relation to your Shares. In the event that Trading Among Farmers ceases, the Bill proposes that the obligation on Fonterra to issue and redeem Shares will be reinstated. The exact nature and mechanics of any obligations which would be reinstated are not yet determined.

Further information regarding Trading Among Farmers is set out on pages 8 to 12.

Global business risks

Fonterra, through the Fonterra Group, sells over 90% of the milksolids it processes to markets outside New Zealand and must retain its global competitiveness.

Changes in commodity prices may impact adversely on Fonterra's future performance. Commodity prices can be volatile, with substantial increases and decreases occurring over a relatively short period. This volatility may have a material impact on the Fonterra Farmgate Milk Price. It may also have a material impact on the returns to Fonterra from its consumer and other value add and arbitrage businesses, which may result in changes to Fonterra's Distributable Profit and any dividend paid on Shares. Price volatility in Fonterra Group's principal products can result in substantial shifts in the levels of returns received and can impact Fonterra's balance sheet. (Please see section below entitled *Global financial environment*.) Changes in particular markets' demands for dairy commodities may over time create positive or negative arbitrage between those markets' domestic and international dairy commodity prices. This may have a material impact on the Distributable Profit and/or any dividend paid on Shares, as well as the fair value share price.

International trade in dairy products is heavily influenced by foreign government actions including tariffs, quotas, price controls, other non-tariff barriers, subsidies and food-related regulation. The interaction of these factors is complex and can result in substantial shifts in the competitiveness of Fonterra and the Fonterra Group and the levels of returns from overseas markets. Fonterra, through the Fonterra Group, sells significant volumes of product across borders which exposes Fonterra and the Fonterra Group to the risk of breaching foreign customs regulations, import duty regulations and other laws. This risk may potentially result in extended legal action, financial penalties, prosecution, temporary trade embargoes and even permanent loss of market access. In addition, the relativity between the domestic market and international market prices may result in dumping allegations being made against Fonterra and the Fonterra Group.

A significant amount of the Fonterra Group's revenue is earned from sales to non-OECD and developing markets that are economically and politically less stable than developed economies. A foreign country may become politically unstable resulting in the loss of an investment, or default in payment by a significant debtor. Global business risks include war, nationalisation of assets, economic instability or downturn, deflation or inflation/hyperinflation, currency volatility, price control, political interference and political uncertainty. Certain political, commercial or economic events in one country may also disrupt delivery of Fonterra product to other intended markets.

The international market for dairy products is also affected by general economic conditions in the major world economies such as Europe, the United States of America, China and Japan. For example, a recession or recovery in these economies would be expected to affect world commodity prices, including those for dairy products. As well, the international market for dairy products can be affected by consumption trends such as if consumers were to move their preferences to substitute dairy proteins and fats with vegetable solids / soy proteins.

The retail market structure in New Zealand and overseas is changing. In particular, there is a growing global concentration of retail customers in the supermarket sector including in Australia and New Zealand, together with an increased drive by these customers to grow their Private Label offers. This carries the risk of squeezing margins and also the risk of losing market share if a supply contract is lost. Throughout the international market there are also continual changes in product markets, distribution channels, consumer preferences and tastes (including as a result of emerging health trends) – all of which could impact adversely on Fonterra's future performance. In light of all these considerations, Fonterra regularly reviews its marketing strategies and investments portfolio in overseas jurisdictions.

Lobby activities by non-governmental organisations or other commercial or customer groups may result in increased regulatory controls on the trade, production or marketing of Fonterra products in New Zealand or overseas. Examples include climate change, health factors related to particular food groups, or marketing of particular products such as breast milk substitutes.

Exchange rate risk

Fluctuations in the value of the New Zealand dollar relative to other currencies impact on the value in New Zealand dollars of:

- sales of product to, and the relative value of costs incurred in, countries operating with those currencies;
- receivable amounts owed on those sales at any one time;
- investments in businesses, joint ventures or assets owned within those countries;
- returns from overseas businesses; and
- foreign currency liabilities.

Fluctuation in currency exchange will have a direct impact on the payments for milk and Distributable Profit and may also have an impact on any dividend paid on Shares, as well as the fair value Share price.

Fonterra uses a range of strategies in order to attempt to reduce the impact of foreign currency fluctuations and has a financial risk management ("**FRM**") policy applicable to the Fonterra Group that is regularly reviewed.

Although the Fonterra Group's main foreign currency exposure will generally be measured in US dollars, the effect of the FRM policy takes account of all significant foreign currency exposures. Similarly, balance sheet exposures will be hedged according to the guidelines of the FRM policy.

The Fonterra Group is vulnerable to foreign currency changes as well as other factors, including any variation in commodity prices, changes in product mix, operating efficiencies, and changes in exposure due to higher or lower sales volumes. Fonterra and the Fonterra Group adopt a number of mechanisms which seek to reduce the relevant exposures.

Market Price Risk

Fonterra's revenue is impacted by fluctuations in the value of global dairy commodity prices. When global dairy commodity prices are high Fonterra's revenue from the sale of commodity products increases and conversely when global dairy prices are low Fonterra's revenue from the sale of commodity products decreases.

Fluctuations in global dairy commodity prices impact both the milk price and non-milk price product portfolios. While the global prices of these two portfolios have some correlation fluctuations in global dairy commodity prices also create volatility of Fonterra's earnings.

Fonterra has well established policies and procedures which set out the approach for managing the impact of global dairy commodity price risk on profit. These include an annual Hedge Programme and dairy commodity price risk management policy. Whilst this approach includes the use of dairy commodity derivatives for price risk management it should be noted that the dairy commodity exchange traded futures and options contracts are at a very early stage of development and that there are limitations to the extent that earnings volatility can be hedged until sufficient liquidity in these futures and options contracts develops.

Fonterra dynamically manages its dairy commodity hedge book via commodity derivatives and also undertakes limited proprietary trading for the purpose of accelerating the development of liquidity in dairy commodity derivatives and for monetising proprietary market insights. This activity is controlled through a robust governance framework and control environment.

Under its dairy commodity price risk policy, Fonterra also uses non-market based tools to manage the risk of fluctuating global dairy commodity prices on profit. These include aligning the contract pricing, duration and phasing of the milk price and non-milk price product portfolios.

Contract pricing risk

The Fonterra Group enters into short and long term forward contracts for the sale of its production of commodity dairy products each year. Selling products in this manner, and the terms of such contracts, change from year to year. Any advantage or disadvantage of sales of commodity products under longer term forward contracts, relative to sales of products made at shorter term market prices at any particular time, will change as a result of the variation in market prices for commodity dairy products.

Regulatory risk

The majority of milk supplied to Fonterra is sourced from New Zealand. The formation of Fonterra was authorised by the Dairy Industry Restructuring Act 2001 ("**DIRA**"), which established a regulatory framework for the New Zealand dairy industry (**"Regulatory Framework"**). The Regulatory Framework has two key possible effects on Fonterra:

- Fonterra faces competition in acquiring milk from farmers as the Regulatory Framework provides for new entry (both large and small scale) into the New Zealand dairy markets.
- Fonterra could face additional costs in collecting milk from farmers and processing that milk as it is required to maintain open entry.

The extent of, and reasons for, these possible effects are set out below.

In addition, the Regulatory Framework may be amended from time to time including in a way that could have an adverse impact on Fonterra. Some of the potential changes (including proposed changes under the Bill) are discussed below.

Farmgate Milk Price

The price that Fonterra pays for milk supplied by its Shareholders is set by the Board in accordance with Fonterra's Constitution, and is not currently subject to specific legislative or regulatory requirements. Further information regarding the determination of the Farmgate Milk Price is set out on pages 17 and 18.

During 2011 Fonterra's setting of the Farmgate Milk Price was considered in reviews undertaken by the Commerce Select Committee, the Regulations Review Committee, the Commerce Commission and officials. On 27 March 2012 the Dairy Industry Restructuring Amendment Bill was introduced to Parliament, which, amongst other things, proposes the following changes:

- Providing a set of milk price principles to provide a basis for assessing whether Fonterra's Farmgate Milk Price has been appropriately set.
- Embedding Fonterra's current Farmgate Milk Price governance arrangements into the DIRA, including requirements for Fonterra to maintain a Milk Price Panel, for a majority of the members of the Milk Price Panel (including the chairperson) to be independent, and for Fonterra to maintain a Farmgate Milk Price Manual (which is to be publicly available).
- Introducing of a Farmgate Milk Price monitoring and oversight regime under which it is proposed that the Commerce Commission will be required to review the Farmgate Milk Price Manual and audit the assumptions and inputs used in calculating the Farmgate Milk Price, and report publicly on its conclusions. Under the Bill, the Commerce Commission's monitoring and oversight role is proposed to be funded by a levy on Fonterra which is not yet fixed.

As at the date of this Investment Statement, the Bill is not yet enacted. It is uncertain whether any or all of the requirements currently proposed by the Bill will be enacted. Fonterra intends to make a submission on the Bill. Fonterra's submission will be publicly available when made.

Supply of raw milk to independent processors in New Zealand

Fonterra is required by regulations to supply raw milk to independent processors who seek it, including competitors, currently up to an aggregated maximum of 600 million litres per year (around 4% of Fonterra's total annual milk supply). This current aggregate may, by Order in Council under the DIRA, be increased up to a maximum of 5% of raw milk supplied to Fonterra. Unless Fonterra and the purchaser of the raw milk agree otherwise, the price of the milk must be calculated according to the formula set out in the Dairy Industry Restructuring (Raw Milk) Regulations 2001. Of the 600 million litres to be supplied in the current Season, Fonterra must supply Goodman Fielder New Zealand Limited (a domestic based consumer dairy company competing with Fonterra's New Zealand consumer businesses) with up to 250 million litres and any other independent processor up to 50 million litres. This requirement makes new entry into the New Zealand dairy markets easier as other processors can commence or continue business without establishing their own network of milk suppliers. The supply of raw milk to Goodman Fielder New Zealand Limited, and other processors and related pricing arrangements, have the effect of facilitating competition in New Zealand between that company and Fonterra's largest New Zealand operating consumer company, Fonterra Brands (New Zealand) Limited.

In January 2012 the Government announced proposed changes to the Dairy Industry Restructuring (Raw Milk) Regulations. The proposed changes include:

- Increasing the total amount of raw milk available to independent processors in a season to 5 percent of Fonterra's raw milk supply (the limit would increase from 600 million litres to 770 million litres for the next three seasons, and be reset periodically from the season beginning 1 June 2015).
- Removing the $0.10 per kilogram of milk solids seasonal margin in the default price.
- Removing the "October Rule" whereby in any month other than October, the maximum quantity of raw milk that an independent processor can require at the default price is 110% of the quantity it took in October, and introducing maximum monthly limits intended to reflect the seasonal dairy supply curve.
- Making an independent processor ineligible for regulated raw milk in a season beginning on or after 1 June 2015 if it has had 30 million or more litres of own supply in the three immediately preceding seasons.
- Allowing Goodman Fielder to take flat supply of its 250 million litre per season entitlement (ie Goodman Fielder will not be subject to the monthly limits).

As at the date of this Investment Statement, the changes have yet to be finalised and announced. It is uncertain whether any or all of the requirements currently proposed changes to these regulations will be enacted. Fonterra has provided a submission to the Ministry of Agriculture and Forestry which sets out its views on the proposed changes. Fonterra's submission is publically available at www.maf.govt.nz.

Suppliers able to supply competitors

Fonterra is required to allow its supplying shareholders to supply up to 20% of their milk to a third party if the shareholders meet certain conditions, without Fonterra being able to discriminate against them in any way, provided the milk does not have a unique patentable feature. Again, this makes it easier for other processors to gain access to milk supply as they will be able to take milk from Fonterra suppliers without having to ask those suppliers to cease supplying Fonterra entirely.

Open entry

Fonterra must accept all new suppliers who make an application during the application period, and whose transportation costs are no more than any existing Fonterra supplier in the region, subject to minimum delivery and quantity requirements and certain capacity constraints on Fonterra. Therefore, Fonterra does not have the discretion to refuse to accept suppliers, except in the limited circumstances referred to above, and may also be required to provide additional collection and processing capacity to accept additional supply.

Open exit

A supplying shareholder who wants to leave Fonterra may do so by giving notice by the end of February in any year for exit on 31 May of that year, except where the supplier has a longer-term contract (there are limits on the number of long-term supply contracts Fonterra can enter into, see *Limits on long-term supply contracts* below). When the supplier leaves, they will receive cash, Capital Notes or Redeemable Preference Shares that are equal to the value of the Shares and Peak Notes they surrender. Open exit makes it easier for a new or existing processor to encourage suppliers to leave Fonterra as that processor need only agree to pay the supplier a payment for milk that is competitive with Fonterra's price. Open exit also makes it easy for suppliers to leave dairying and use their land for other purposes. Suppliers will be paid out the current value of their capital investment in Fonterra if they leave Fonterra. Accordingly, Fonterra faces the dual risk of loss of revenue (milk supply diverted to a competitor or milk supply terminating due to cessation of dairying) and loss of capital (departing and reducing suppliers requesting a return of their capital). In addition, Fonterra's milk processing assets could become under-utilised, which may affect overall financial performance.

In the event that Fonterra moves to adopt and implement Trading Among Farmers, the exit requirements set out above will cease to apply. Further information on Trading Among Farmers is set out on pages 8 to 12.

Non-discrimination

Fonterra must offer to each new supplying shareholder the same terms and conditions of milk supply as it offers to a current supplying shareholder in the same circumstances (or terms which are different only to reflect different circumstances). Similarly, the terms of securities (such as Shares and Peak Notes) issued to new suppliers must be the same as for current suppliers. As a result, although Fonterra is permitted to respond to competition it cannot do so in a manner which breaches these requirements.

Limits on long-term supply contracts

Fonterra must offer suppliers, as a minimum, a one year supply contract. It may offer longer-term contracts but it must ensure that at least a third of all the milk produced in a 160 kilometre radius of any point in New Zealand is either supplied to someone other than Fonterra or under a contract to Fonterra that expires at the end of the Season, or which can be terminated at the supplier's option without penalty.

This means that, at any time, some milk supply will always be available for other processors to acquire, provided that they agree to pay the supplier a price that makes that supplier willing to leave Fonterra.

Share price

The method for determining the Share price is currently set out in Fonterra's Constitution. Further information on the determination of Fonterra's Share price is set out on pages 13 to 17.

The Draft Bill proposes changes to the DIRA which would require Fonterra to adopt a particular "fair value" methodology to determine its share price if Trading Among Farmers is not launched by 31 December 2013, or if Trading Among Farmers ends. The proposed changes aim to impose a Share price equal to Fonterra's fair market value. Fonterra considers there is a risk that the proposed changes would not have their desired effect and would impose a Share price greater than its fair market value.

As at the date of this Investment Statement, the Bill has not been enacted.

Removal of export monopoly

The DIRA specifies a small number of designated export markets in relation to which an export licence is required. These licences are allocated based on the proportion of milksolids collected by a New Zealand dairy processor. As at the date of this Investment Statement, under this system Fonterra can expect to obtain around 90 per cent of the export rights available, with that percentage varying in the future according to the proportion of total milksolids collected by Fonterra in New Zealand.

The value of the export rights to the designated markets can vary significantly as a result of changes to supply and demand in the relevant markets and also as a result of changes to global commodity prices for the relevant products.

Food safety and environmental risk

In many overseas markets in which the Fonterra Group operates, New Zealand is perceived as a source of safe, high quality dairy products. The Fonterra Group and joint ventures in which it is involved source around 30% of the product they sell from countries outside New Zealand. Some of the countries and areas where the Fonterra Group and joint ventures in which it is involved source dairy products include Australia, USA, Europe, South American countries, Sri Lanka, China and other Asian countries. There can be significant quality or food safety issues associated with dairy product being sourced from other countries and these issues could have a significant effect on the returns from the relevant Fonterra business or joint venture business, as well as the overall reputation of Fonterra and the Fonterra Group. Anything adversely impacting on the perception of New Zealand dairy products or on the reputation of Fonterra and the Fonterra Group internationally could impact on the ability to make future sales of product at favourable prices and therefore have a significant impact on Fonterra's performance and the overall value of Fonterra or of the relevant business unit affected.

As with any food business, there is an inherent risk that Fonterra products might be contaminated in the production process or from raw milk supply adulteration, or might otherwise be affected by food safety issues or adverse publicity. The storage, use, production and transport of hazardous substances by (and on behalf of) the Fonterra Group involves risks relating to accidents or spills, contamination and harm to the environment or people. Contamination and food safety issues, accidents with and/or spills of hazardous substances harming the environment or people, or adverse publicity (even if from false, malicious or reckless allegations), may potentially involve significant cost and reputational harm. Reputational harm could also affect the ability of Fonterra' and the Fonterra Group to maintain the value of its brands. The Fonterra Group operates under quality control procedures which it considers to be effective. These manage but do not remove the risk of contractor or supplier conduct having adverse consequences for the Fonterra Group due to food or environmental contamination.

Food businesses generally, including dairy, also face increased scrutiny as a result of global concerns about obesity and other health issues such as heart disease and diabetes, and increased regulator scrutiny of product label health claims.

In addition, there are risks associated with wider environmental concerns including water usage and agricultural emissions, discharges to land and water, genetic modification issues, animal welfare concerns and concerns over the potential environmental impacts of shipping products over long distances ("**food miles**") linked with dairying in New Zealand, which may impact on the marketing of, and returns for, dairy products in New Zealand or internationally.

Reputational risk

The occurrence of any of these risk factors has the potential to impact on the reputation of Fonterra and the Fonterra Group and as a result the value of the Fonterra Group's brands could be adversely affected.

Brands ownership

Numerous brands are owned and used by Fonterra and its subsidiaries, and in some cases third party licensees, across a number of countries. Brands carry a significant value on the Fonterra Group's balance sheet. An event adversely affecting the value of a brand in one jurisdiction could have a negative effect in another jurisdiction with a resultant adverse effect on Fonterra's financial performance both in terms of loss of profits and potentially a writedown of the balance sheet value of the brand.

Risks associated with being an agricultural business

The Fonterra Group is an agricultural based business and could therefore be adversely affected by factors such as changes in climate (for example, drought) or by biosecurity or other issues including serious outbreaks of disease in cows (such as foot and mouth disease). These factors could disrupt business and cause reputational harm, in terms of perceived safety and quality of product, and reliability of supply. Reputational harm would impact on the Fonterra Group's ability to make future sales of products at favourable prices and therefore on returns to shareholders. These risks are mitigated somewhat by the geographical diversification of the Fonterra Group's milk production and New Zealand's border controls and bio-hazard risk management strategies. However, given that the majority of the Fonterra Group's raw milk is produced in New Zealand, if factors such as these occurred in New Zealand they may have a material adverse effect on Fonterra's financial performance.

Fonterra also faces the risk of loss of supply arising from competition for land use in New Zealand and to competing milk processors. Supplying dairy farmers could choose to use their land for activities other than dairying, such as other agricultural uses or for urban development. This gives rise to the risks of loss of revenue, loss of capital and under-utilisation of milk processing assets as discussed under the heading *Open exit* above.

Expansion risk

The pursuit of expansion by the Fonterra Group involves exposure to financial and operational risks, whether they involve the acquisition of businesses or interests in businesses (including through joint ventures and the acquisition of minority or majority shareholdings), or the introduction of new product lines. The financial performance of acquisitions and joint ventures impacts on Fonterra's financial performance. Fonterra seeks to mitigate the risk from expansion by thoroughly analysing prospective opportunities and adopting risk reduction programmes when implementing them. Individual propositions are only progressed if they can reasonably be expected to result in enhanced performance and profitability for the Fonterra Group.

The Fonterra Group has a number of joint venture interests including significant investments in joint ventures in Europe (the DMV-Fonterra Excipients Joint Venture with FrieslandCampina), South America (the Dairy Partners Americas Joint Venture with Nestlé), and North America (the DairiConcepts Joint Venture with Dairy Farmers of America) as well as significant investments in a number of companies around the world.

Operating businesses through joint ventures means that the Fonterra Group does not have full control over these businesses, which exposes Fonterra to greater risk. These risks are mitigated by a variety of actions and controls which include the agreements which are entered into when the joint venture is formed, Fonterra taking up board directorships, audits through the Fonterra internal audit function as well as regular strategy and performance reviews.

Fonterra owns and/or operates offshore farming ventures. In addition to the business risks associated with business expansion outlined above, these ventures will be exposed to other risks, including risks common to agricultural businesses, such as disease, milk quality, and environmental sustainability, and risks associated with operations in other jurisdictions. The occurrence of adverse effects in these areas could impact on the reputation or profitability of the ventures.

International trade environment

While the World Trade Organisation ("**WTO**") provides a framework of rules for international agricultural trade, there remains significant risk of countries restricting imports of dairy products or affecting global dairy returns, whether through changes in tariffs and quotas, or through their domestic regulatory regimes. A particular example of the former is the recent implementation of quotas on milk protein concentrates (specialised protein products) into Canada. An example of the latter is the intervention price cuts introduced as part of the EU Common Agricultural Policy reforms since 2003, which have reduced the Fonterra Group's returns from that market, or the commercial impacts of regulations for the administration of imports into the EU of New Zealand quota butter and cheese.

Liberalisation of the international trade environment, for example through the Doha Development Round of WTO negotiations, or through bilateral or plurilateral Free Trade Agreements, present mostly positive opportunities for the Fonterra Group. But they also carry risks which could damage the Fonterra Group's business in some areas – for example, exclusion or disadvantaging of New Zealand product compared with rival companies or countries as a result of new agreements, changes to rules around geographical Indicators or changes to labelling or composition requirements.

It is possible that New Zealand's climate change obligations could add further costs to the Fonterra Group's activities depending on policies and programmes adopted by the New Zealand Government. In December 2011, the Kyoto Protocol's first commitment period was extended until December 2017, continuing New Zealand's obligations in that respect. At the same time, the New Zealand Emissions Trading Scheme is set to continue, and will likely merge with Australia in upcoming years. The Government plans to review the legislated 2015 entry of agricultural emissions into the New Zealand Emissions Trading Scheme in 2014, with a focus on whether effective emissions reduction technologies have been developed at that time. Until then, the amount and timing of costs impacting on Fonterra will not be clear.

Production and Supply Chain risks

A major catastrophe, accident or local disaster of significant magnitude (for example, an earthquake or fire that destroys a manufacturing facility or general business infrastructure) could materially adversely affect Fonterra's financial performance and position. To an extent, some of these risks are mitigated by insurance cover and business continuity planning.

Production delays (including as a consequence of industrial action, product tampering, technology failure or disruption in energy or water supplies) and other supply chain difficulties of getting product to market (including industrial or other action affecting roading, shipping or a significant failure in automated systems or computer technology) would also impact adversely on Fonterra's financial performance.

Production may also be disrupted in the event of material non-compliance with environmental or other approvals authorising the production and associated processes, or from those approvals not being renewed (or being renewed on more onerous terms).

Management risks

Fonterra is subject to numerous risks inherent in the management of the day to day business activities of the Fonterra Group. Such risks are inherent in the people, processes, systems and structures employed in the conduct of its business. For example, both domestically and overseas, the Fonterra Group may be unable to attract or retain the right staff in the right place at the right time.

Inherent risks also arise in connection with the changes associated with the implementation of the wide-reaching technological, process and cultural initiatives that the Fonterra Group is pursuing.

Bio-technology

The Fonterra Group is undertaking long-term biotechnology research, with the future option of commercialising developments in a responsible manner, according to the needs and wishes of its customers, consumers and key stakeholders. The Fonterra Group's current research activities have been approved by the relevant regulatory authorities. If the Fonterra Group were to consider undertaking any field trials of any genetically modified organisms, the Fonterra Group would need to comply with all relevant laws, regulations and standards, including obtaining all necessary approvals from the appropriate regulatory authorities. The Fonterra Group would only undertake such a course of action if it were regarded as being in the interests of Fonterra's stakeholders, including customers.

The Fonterra Group's current policy is not to accept milk in any of its operations from genetically modified cows, cloned animals or their identifiable offspring. Fonterra will comply with all regulatory requirements, including labelling.

Litigation risk

The Fonterra Group has a number of claims and legal actions arising from the normal course of its business activities, which it is currently defending. However, the Directors, having reviewed legal and accounting advice and having made their own inquiries of management, expect that either the outcome will not be adverse for Fonterra, or that any adverse outcome will not have a material adverse effect on Fonterra's financial position.

General risks

Other special factors and risks that could materially affect the trading prospects, financial performance or position of Fonterra and the Fonterra Group include:

- a downturn in general economic and business conditions (domestic and global);
- New Zealand's international image being significantly tarnished with Fonterra and the Fonterra Group being adversely affected by association, resulting in loss of international customers and/or markets;
- increased pressure on energy and water resources in New Zealand and overseas;
- increased competition (domestic and global), including the risk that competitors actively pursue and capture a material segment of the Fonterra Group's customer base or supplier base;
- decreases in customer demand;
- changes in timing and amount of forecast capital expenditure;
- changes to industry relevant regulation;
- changes to business alliances;
- changes to prices paid for milk to suppliers;
- changes in tax rates or tax regimes in New Zealand and overseas;
- adverse returns from derivatives, including but not limited to instruments used to manage foreign exchange risk;
- serious injury or death (in particular in manufacturing and logistics operations, and notwithstanding health and safety procedures) particularly as it has potential to impact on employer reputation, compliance costs, staff morale and productivity, and may attract media exposure and additional regulatory scrutiny;
- actions by employees in breaching policy and procedures, notwithstanding the requirements on employees as outlined in Fonterra policies and standards including Fonterra's Ethical Behaviour policy, particularly as such actions may impact on Fonterra's reputation;
- changes to New Zealand and international prices for dairy products; and
- climatic conditions.

Many of these factors are beyond the control of Fonterra and the Fonterra Group.

Global financial environment

Adverse effects in the global economy arising out of events in credit markets and financial services industry can impact the global trading environment and result in a global liquidity crisis.

As with other businesses, a credit and liquidity crisis could impact the purchasing patterns of some of the Fonterra Group's customers.

Fonterra uses debt to partially fund the operations of the Fonterra Group. The debt is provided by a combination of bank loans and debt issued in the global capital markets. On an on-going basis, Fonterra is required to refinance credit lines and debt coming to maturity. This refinancing of debt is effectively managed by spreading the maturities of existing debt to ensure that refinancing requirements are limited at any point in time, maintaining sufficient undrawn, committed funding facilities and supported by building strong relationships with banks and other lenders.

The scope and extent of a global liquidity crisis cannot be predicted and, as a result, it is not possible to assess with any certainty any additional impact that such a crisis may have on the funding, operations and activities of the Fonterra Group. While largely unpredictable, a sustained continuation and/or escalation of a global liquidity crisis could adversely impact the business and operations of Fonterra and the Fonterra Group.

CAN THE INVESTMENT BE ALTERED?

Co-operative Shares and Redeemable Preference Shares

The rights and obligations attaching to the Shares and the Redeemable Preference Shares may be altered by a special resolution of shareholders whose rights are affected in the same way (a special resolution is one passed by a majority of 75% or more of the votes of those shareholders entitled to vote and voting on the question). Under certain circumstances set out in the Companies Act 1993 a shareholder whose rights are affected by a special resolution may require Fonterra to purchase their Shares.

In addition, certain provisions of the Constitution cannot be altered or revoked unless supported by a majority of the Shareholders' Councillors.

If you do not hold enough Shares to comply with the share standard the Board may require you to increase the number of Shares you hold. If you hold more Shares than the share standard requires, plus an additional 20% as described on page 5, the Board may require you to surrender your excess Shares.

At the special meeting on 30 June 2010, shareholders approved a new form of constitution that will apply if the Board, having determined that the pre-conditions have been satisfied, resolves that Fonterra move to adopt and implement Trading Among Farmers, and resolves that the new constitution shall, on a date determined by the Board, come into effect. Further information regarding Trading Among Farmers is set out on pages 8 to 12.

Peak Notes

The rights and obligations attaching to Peak Notes that are set out in the Constitution may be altered by a special resolution as noted above in respect of the Shares. In addition, certain provisions of the Constitution cannot be altered or revoked unless supported by a majority of the Shareholders' Councillors.

The terms of the Peak Notes set out in the Peak Notes Trust Deed (and any amending or supplemental deed) cannot be altered without the agreement of holders. Fonterra and the Trustee may agree to change the Peak Notes Trust Deed (and any amending or supplemental deed). Holders will not be notified of changes to the Peak Notes Trust Deed which are necessary to correct manifest error, or which are of a formal or technical nature, or which are necessary or desirable to comply with any law, or which the Trustee considers are not likely to be materially prejudicial to holders and certain other types of changes which are described in the Peak Notes Trust Deed and in the Prospectus. Certain other types of change require the approval of an extraordinary resolution of holders (i.e. a resolution passed by 75% of the holders who are entitled to vote, and do vote, in favour of the resolution). More specific details about the types of changes that can be made are provided in the Peak Notes Trust Deed and in the Prospectus.

Capital Notes

The interest rate payable in respect of the Capital Notes will change as explained under the heading *What returns will I get?.*

The main terms of the Capital Notes cannot be altered without the agreement of holders. Fonterra and the Trustee may agree to change the Capital Notes Trust Deed (and any amending or supplemental deed). Holders will not be notified of changes which are necessary to correct manifest error, or which are of a formal or technical nature, or which are necessary or desirable to comply with any law, or which the Trustee considers are not likely to be materially prejudicial to holders and certain other types of changes which are described in the Capital Notes Trust Deed and in the Prospectus. Certain other types of change require the approval of an extraordinary resolution of holders (i.e. a resolution passed by 75% of the holders who are entitled to vote, and do vote, in favour of the resolution). More specific details about the types of changes that can be made are provided in the Capital Notes Trust Deed and in the Prospectus.

You should also be aware that as at the date of this Investment Statement, Fonterra is continuing to further develop its capital structure. Please refer to page 3 for further information.

HOW DO I CASH IN MY INVESTMENT?

Co-operative Shares

Surrender

If you decrease supply and therefore hold more shares than you are required to hold by the share standard you may either:

- surrender your excess Shares and receive the Surrender Value for those Shares; or
- hold excess shares as permitted by the Constitution (see pages 5 to 6).

If you cease supplying Fonterra, your Shares will be surrendered. If you apply to supply less milk to Fonterra, some of your Shares will be surrendered. The number to be surrendered will be impacted if you supply any milk under Contract Supply.

Fonterra may pay the Surrender Value of Shares by:

- issuing Capital Notes with a total market value at least equal to the value of the Shares being surrendered. The total market value of the Capital Notes is calculated in accordance with the DIRA;
- issuing Redeemable Preference Shares, but only in the circumstances described under the heading *What sort of investment is this?*; or
- paying cash.

You should refer to the Constitution if you require more information about the surrender of Shares.

Fonterra may be entitled to reject a surrender of Shares if it would cause that supplier to:

- hold fewer Shares than a person is required to hold to commence supplying Fonterra; or
- if the surrender would be in breach of any terms and conditions under which you supply Fonterra (including the terms and conditions of Contract Supply); or
- hold less Shares than the minimum number of Shares you are required to hold by the Board as a condition of the issue of additional Shares (see pages 4 and 5).

Transfer of Shares

Your right to transfer Shares is limited and subject to the restrictions contained in the Constitution and in any Contract Supply arrangement you have with Fonterra. Under the Constitution, Shares may not be transferred by a shareholder to:

- any person unless that person is either a shareholder or a person whose application to become a shareholder has been accepted in writing by Fonterra or is approved by the Board as a shareholder; or
- a shareholder, who following the transfer would hold more Shares than permitted by the Constitution (see pages 5 to 6); or
- any person if that Share is subject to a resolution of the Board requiring its surrender.

In addition, the Co-operative Companies Act 1996 provides that a supplying shareholder may transfer Shares and applicable voting rights held by that shareholder to a sharemilker.

These limitations are subject to the regulatory requirements (as outlined under the heading *What are my risks?*) requiring acceptance of new shareholders within a limited time after their application.

In addition, the Board may refuse to register transfers in specified circumstances, including where:

- the Board, in its absolute discretion, believes that the proposed transferee is either not a desirable person to become a shareholder in Fonterra or that registration of the transfer would not be in the best interests of Fonterra;
- the Shares are not fully paid up;
- Fonterra has a lien on the Shares;
- the transferor has an undischarged liability to Fonterra; or
- the transfer would cause the transferor to be in breach of any terms and conditions of the supply of milk to Fonterra, including the terms of any supply of milk on Contract Supply or the terms of any additional Shares issued at the discretion of the Board from time to time (see page 4).

You should refer to the Constitution and Terms and Conditions of Supply if you require more information about the transfer of Shares.

There is no established market for the sale of the Shares.

At a special meeting of shareholders on 30 June 2010, amendments to Fonterra's Constitution were approved. These amendments allow the Board to take the steps necessary to finalise and put in place a regime for Trading Among Farmers, which will involve the trading of Shares on the Fonterra Shareholders' Market. Further information regarding Trading Among Farmers is set out on pages 8 to 12.

Peak Notes

Shareholder right of redemption

Shareholders may redeem excess Peak Notes by giving written notice to Fonterra prior to 30 June in each year. Fonterra may, at its option, pay the fixed value of the Peak Notes being redeemed:

- in cash; or
- by issuing you Capital Notes having an aggregate market value equal to the Peak Notes' fixed value; or
- by issuing you Shares with an aggregate fair value equal to the Peak Notes' fixed value, but only to the extent that you require more Shares to meet the share standard; or
- any combination of the above.

In limited circumstances (described above under the heading *What sort of investment is this?*), Fonterra may also pay the fixed value of the Peak Notes being redeemed by issuing Redeemable Preference Shares with an issue price equal to that fixed value.

Fonterra's option to redeem

Fonterra may at any time, at its option, on 30 business days notice, redeem on a pro rata basis, all or any excess Peak Notes for cash or by issuing Shares, Capital Notes or (in the limited circumstances described above under *What sort of investment is this?)* Redeemable Preference Shares or any combination of the above.

Limited rights of transfer

Peak Notes have only limited rights of transfer. Peak Notes may not be transferred by a shareholder to:

- any person who is not:
  - Fonterra or a subsidiary of Fonterra; or
  - a shareholder; or
  - a person whose application to become a shareholder has been accepted in writing by Fonterra or approved by Fonterra as a shareholder; or
  - a sharemilker who is approved by the Board in accordance with either rules established by the Board from time to time in accordance with the Constitution, or any applicable enactment; or
- a shareholder (including any sharemilker who is qualified to hold Peak Notes as described above) who, following the transfer, would hold more Peak Notes than required or permitted to be held by that shareholder in accordance with the Constitution.

There is no established market for the transfer of Peak Notes.

Capital Notes

No right of redemption

Prior to any liquidation of Fonterra and subject to the provisions of the DIRA as referred to below, Capital Note holders have no right to require Fonterra to redeem or repurchase their Capital Notes.

Right to transfer

You can sell or transfer your Capital Notes to another person or organisation at any time, using the form commonly used for security transfers, in multiples of $1,000 and subject to the requirement that any Capital Note holder must have a minimum holding of $5,000.

The market for selling Capital Notes

The Capital Notes have been accepted for listing by NZX Limited and will be quoted on the NZDX upon completion of allotment procedures. However, NZX accepts no responsibility for any statement in this Investment Statement. The NZDX is a registered market under the Securities Markets Act 1988. The NZDX is operated by NZX, which is a registered exchange, regulated under the Securities Markets Act 1988. Fonterra considers that there will be an established market for transferring Capital Notes. If this is relevant to you, you should contact your investment adviser.

As the Capital Notes are quoted on the NZDX, they are transferable using NZX's electronic trading settlement and transfer system. For as long as the Capital Notes are traded on the NZDX, Fonterra is not required to issue certificates under the Capital Notes Trust Deed.

Dairy Industry Restructuring Act 2001

Section 103 of the DIRA requires Fonterra to repurchase Capital Notes issued to exiting shareholders or shareholders who are reducing supply in certain circumstances at the election of the holder (by notice to Fonterra within 6 weeks of their issue) for cash and at a price not less than 97.5% of the market price at which they were issued. This requirement applies where Fonterra (or an associated person as defined in the DIRA or person with whom Fonterra or its associate has an arrangement in respect of acquiring Capital Notes) has acquired its Capital Notes during the month immediately before the date the Capital Notes which must be repurchased were issued.

Election Date

Fonterra has the option to redeem all or part of the Capital Notes for cash on an Election Date. This option prevails over any right of a holder in respect of any Capital Note. Further details regarding Fonterra's option to redeem Capital Notes on Election Dates are set out in the Capital Notes Trust Deed and in the Prospectus.

Redeemable Preference Shares

Redemption

Election option: At a time specified by Fonterra, but no later than 3 years after the Redeemable Preference Shares are issued, you may elect to convert your Redeemable Preference Shares into:

- Shares at least equal to the fair value of the Shares that you surrendered for the Redeemable Preference Shares issued; or
- cash or Capital Notes as determined by Fonterra.

At Fonterra's option: Fonterra must redeem each Redeemable Preference Share on the date determined by the Board at the time of its issue. That redemption date will be no later than 3 years after their issue.

The Redeemable Preference Shares are redeemable at Fonterra's option for cash for an amount, or the issue of Capital Notes, at least equal to the fair value of the Shares for which the Redeemable Preference Shares were issued.

Right to transfer

Redeemable Preference Shares may be transferred to, and held by, any person. They do not need to be a dairy farmer, or have any connection with dairy farming. Fonterra must ensure that the Redeemable Preference Shares are tradable.

As at the date of this Investment Statement, Fonterra has not issued any Redeemable Preference Shares nor is there an established market for the Redeemable Preference Shares.

WHO DO I CONTACT WITH INQUIRIES ABOUT MY INVESTMENT?

Any inquiries can be directed to:

Share Registrar
Fonterra Co-operative Group Limited
9 Princes Street
Auckland
Private Bag 92 032
Auckland

Telephone: 0800 65 65 68

Inquiries about Capital Notes can also be directed to:

Link Market Services Limited
Level 16, Brookfields House
19 Victoria Street West
Auckland 1010

Telephone: (09) 375 5999
Facsimile: (09) 375 5990

IS THERE ANYONE TO WHOM I CAN COMPLAIN IF I HAVE PROBLEMS WITH THE INVESTMENT?

Complaints about any of the securities covered by this Investment Statement can be directed to the Share Registrar at:

Fonterra Co-operative Group Limited
9 Princes Street
Auckland
Private Bag 92 032
Auckland

Telephone: 0800 65 65 68
Facsimile: (09) 374 9451

If a complaint in respect of the issue and surrender of Co-operative Shares or Peak Notes cannot be resolved in accordance with Fonterra's internal complaints procedure, shareholders can refer their complaint to the Milk Commissioner. The Milk Commissioner is appointed by the Shareholders' Council in consultation with the Minister of Agriculture, and is responsible for facilitating the settlement, resolution or withdrawal of a shareholder's complaint by agreement. The Milk Commissioner does not have jurisdiction to bind Fonterra to its recommendations. The Milk Commissioner can be contacted at:

Peter Radich
76 High Street
Blenheim
PO Box 646
Blenheim

Telephone: (03) 577 8450
Facsimile: (03) 577 8451

Complaints about the Peak Notes and Capital Notes can also be directed to:

Chief Manager Corporate Trusts
The New Zealand Guardian Trust Company Limited
Level 7, Vero Centre
48 Shortland Street
Auckland

Telephone: (09) 909 5100
Freephone: 0800 801 135
Facsimile: (09) 969 3732

There is no Ombudsman to whom complaints can be made. There is no approved dispute resolution scheme under the Financial Service Providers (Registration and Dispute Resolution) Act 2008 under which complaints can be made about this investment.

WHAT OTHER INFORMATION CAN I OBTAIN ABOUT THIS INVESTMENT?

Further information about Fonterra, the Shares, Peak Notes, Capital Notes and Redeemable Preference Shares is contained in a registered prospectus and financial statements. Copies of the Prospectus, Constitution, the Peak Notes Trust Deed, the Capital Notes Trust Deed, financial statements and other documents relating to Fonterra may be inspected without fee during normal business hours at Fonterra's address specified above under "*Who do I contact with inquiries about my investment?".*

These documents, together with all documents that are required to be registered with the Prospectus, may be accessed on the Companies Office website at www.business.govt.nz/companies.

You are also entitled to obtain copies of the following at no cost if you make a request in writing to Fonterra Milk Supply at the address specified above under *Who do I contact with inquiries about my investment?*

- the Constitution;
- the Capital Notes Trust Deed, and the Deeds of Modification and Supplemental Deed;
- the Peak Notes Trust Deed, and the Deeds of Modification and Supplemental Deeds;

- Fonterra's most recent annual report;
- Fonterra’s most recent annual financial statements;
- the Terms and Conditions of Supply; and
- the most recent registered prospectus and investment statement for the Shares, Peak Notes, Capital Notes and Redeemable Preference Shares.

In each year, shareholders will be sent a copy of Fonterra’s annual review and half-yearly report, and may request the annual report. The annual review, annual report and half-yearly report will include Fonterra's financial statements for the relevant financial year or half year; the annual report and review contain the annual full and summary financial statements respectively, while the half-yearly report contains the interim financial statements.

Under the Dairy Industry Restructuring (Raw Milk) Regulations 2001 Fonterra is required, every three months, to publish certain forecast information for the Season (including forecasts of the total payout, Fonterra’s retention, kilograms of milk solids supplied, and the additional cost of winter milk for both the North and South Islands), and the total volume of raw milk that Fonterra has contracted to supply to independent processors for the Season and the following five Seasons.

At the end of each Season Fonterra must also publish the actual figures for the forecasts referred to above, the total winter milk premium, and the cost of capital rate used in calculating the price of a Share for the Season (if any), and, after 1 June of each Season, the price and total number of Shares, and the price and total number of Peak Notes, as at 1 June in that Season.

All such information will be published on Fonterra’s website (www.fonterra.com).

You should also be aware that as at the date of this Investment Statement, Fonterra is continuing to further develop its capital structure. Please refer to page 3 for further information. As discussed on page 3, materials circulated to shareholders or presentations made to shareholders on the review will be sent to any person receiving a copy of this Investment Statement.

GLOSSARY

In this Investment Statement, unless the context otherwise requires:

Base Price means $4.52, or such other value set as the Base Price in the manner described on page 20;

Bill has the meaning given on page 9;

Board means the board of directors of Fonterra;

Constitution means Fonterra’s constitution as amended from time to time;

Contract Supply means the supply of milk to Fonterra by a shareholder pursuant to clause 3.4 of the Constitution in a Season without the milksolids obtainable from that milk being taken into account for the purposes of the share standard for that Season;

Default Price is a price for Shares determined by reference to the difference between the June Price and the Published Price as described on pages 13 and 14;

DIRA means the Dairy Industry Restructuring Act 2001;

Distributable Profit means the total profit from Fonterra’s business activities available for distribution to Shareholders by way of dividend;

Fair Value Range has the meaning given on page 20

Farmgate Milk Price means a price for milk that is calculated under the Farmgate Milk Price Manual;

Farmgate Milk Price Manual has the meaning given on pages 17 and 18;

Fonterra or the Company means Fonterra Co-operative Group Limited;

Fonterra Group means Fonterra and its subsidiaries;

June Price is the fair value Share price set by the Board on 1 June each year as described on pages 13 and 14;

NZDB means New Zealand Dairy Board;

NZX means NZX Limited.

Published Price is the price for Shares published at the beginning of the application period which may be amended during the application period as described on pages 13 to 14;

Redeemable Preference Shares means redeemable preference shares issued by Fonterra to shareholders under the Constitution in satisfaction of some or all of the surrender value of Co-operative Shares;

Restricted Market Value Range has the meaning given on page 20;

Restrictions has the meaning given on page 20;

Season means a period of 12 months ending on 31 May in each year;

Shares means co-operative shares issued by Fonterra;

Surrender Value, in respect of Shares, means the fair value of the Share for the applicable Season less any amount not paid up on that Share;

Transition Season has the meaning given on page 20;

Transitional Provisions has the meaning given on page 20;

Valuer means Grant Samuel & Associates Pty Limited or any other independent valuer appointed by the Shareholders' Council.

Fonterra Co-operative Group Limited
("Fonterra")

Directors' Statement

pursuant to clause 8 of the
Securities Act (Fonterra Co-operative Group Limited) Exemption Notice 2012

Dated: 12 **April 2012**

(a) There are no material matters relating to the offer of Co-operative Shares, Peak Notes, Capital Notes and Redeemable Preference Shares by Fonterra ("**Offer**") other than –

(i) matters set out elsewhere in the Fonterra Investment Statement dated 12 April 2012 relating to the Offer, the Fonterra Prospectus dated 14 December 2001 (as amended) relating to the Offer, or the Financial Statements of Fonterra for the year ended 31 July 2011; and

(ii) contracts entered into in the ordinary course of business of Fonterra.

(b) In the Directors' opinion, after due enquiry by them, none of the following have materially and adversely changed during the period between the date of Fonterra's most recent statement of financial position and the date of this Directors' Statement:

(i) the trading or profitability of Fonterra or the Fonterra group. The forecast distributable profit for 2012 (last reviewed on 12 March 2012 of 40-50 cents per share) is below the return of 65 cents per share achieved in 2011. This is, however, consistent with the original forecast distributable profit for 2012 advised on 24 May 2011.

(ii) the value of the assets of Fonterra or the Fonterra group;

(iii) the ability of Fonterra or the Fonterra group to pay its liabilities due within the next 12 months.

Signed by each Director of Fonterra Co-operative Group Limited (or by his or her agent who has been duly authorised in writing):

Henry William van der Heyden

Colin Charles Armer

Malcolm Guy Bailey

John Charles Ballard

Ian James Farrelly

David Alexander Jackson

David Nigel MacLeod

John Anthony Monaghan

Nicola Mary Shadbolt

Jim William van der Poel

John Anthony Waller

Ralph Graham Waters

John Speer Wilson