FONTERRA CO-OPERATIVE GROUP LIMITED

PROGRESS

INTERIM REPORT 2015

PRIORITIES

POTENTIAL

PERFORMANCE

STRAIGHT **AHEAD**

TO A PROGRESSIVE, GLOBAL CO-OPERATIVE

We have a clear strategy.
We've strengthened the core and built the right foundations. Now we're focused on driving performance to achieve a higher Farmgate Milk Price and earnings. Looking ahead, we aim to set a platform for wider growth, with new milk partnerships and powerful brands that take our dairy nutrition to the world. Clear **priorities** that will drive **performance** and make the most of our combined **potential**.

PRIORITIES

POTENTIAL

PERFORMANCE

LETTER FROM THE **CHAIRMAN AND CHIEF EXECUTIVE**

Our Co-operative's strategy is designed to increase volume and value so that we can maximise our Farmgate Milk Price and earnings on a sustainable basis.

With the lower forecast Cash Payout this season compared to last year's record returns, farmer shareholders and investors want to know two things at the half year: where we stand on our forecast Farmgate Milk Price and what we are doing to pay the best dividend.

Our forecast Farmgate Milk Price is $4.70 per kgMS. Given the results achieved in the first half of the year, and the continued volatility in international prices, we are lowering our forecast dividend to 20-30 cents per share. The Board has declared a 10 cent interim dividend. This reflects the results achieved to date.

Fonterra is offering a dividend reinvestment plan for the first time. Shareholders who want to participate for the interim dividend need to submit a notice of participation by 13 April 2015.

In total, we have a forecast Cash Payout of $4.90 – $5.00 for the current season.

The half-year results to 31 January 2015 are below expectations in a period when the Farmgate Milk Price was low and we are reducing the forecast dividend range. They are a snapshot of variable conditions for production, demand and pricing and the volume of carryover inventory.

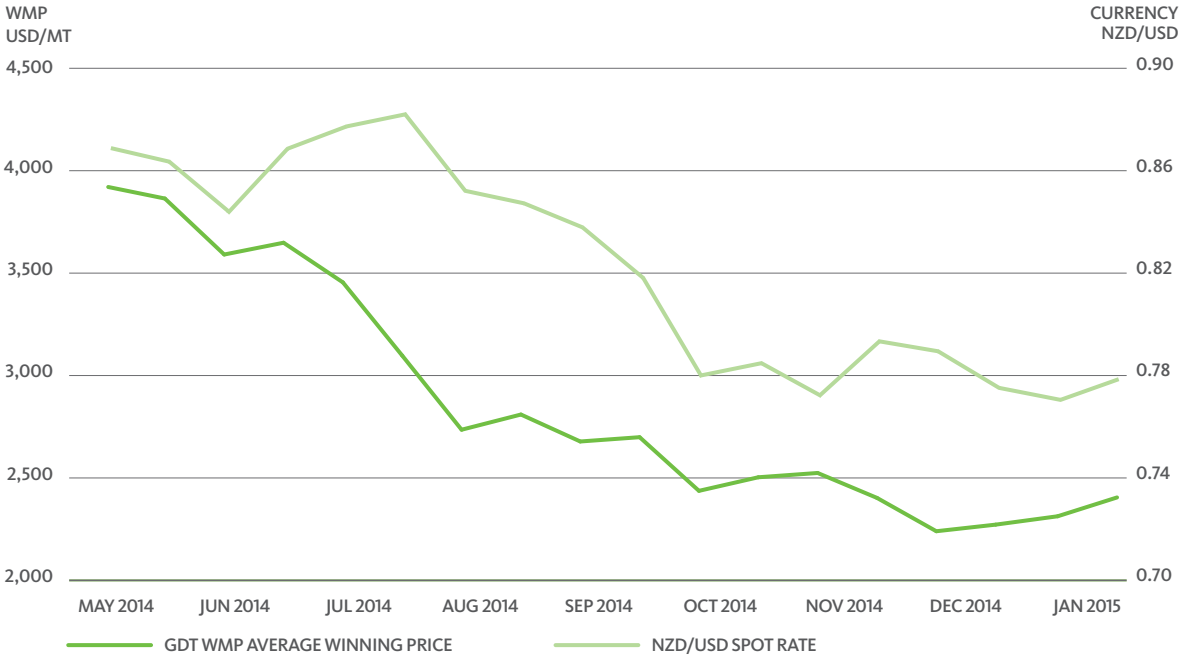
Our half year was a period of two distinct quarters, both influenced by market dynamics, production conditions for milk and the cost of raw milk last season and this season.

VOLUME

In New Zealand, milk production got off to an excellent start in the first quarter with warm, wet conditions and good pasture growth. By November, season-to-date production was four per cent ahead of the comparable period last season. A very dry summer in most regions curtailed production in the last three weeks of January, leading to a reduction in our milk volume forecast to slightly below last season's production.

A recovery in New Zealand milk production is unlikely in the second half, with farmer

WHOLE MILK POWDER PRICE AND CURRENCY



shareholders opting to dry off herds early in some regions because current farm budgets do not support the use of supplementary feed.

Oversupply from dairy producing regions around the world in the early months of the financial year saw the trade-weighted GlobalDairyTrade™ (GDT) price index hit a five-year low in December. When supply outweighs demand, buyers undervalue milk, and that is reflected in prices that declined to unsustainable levels.

As global milk production growth eased back in the second quarter, sales volumes began to build as a result of improved demand. Pricing sentiment also improved and this has been reflected in the GDT prices for Whole Milk Powder (WMP) and Skim Milk Powder (SMP). From December 2014 to 17 March 2015, WMP prices have risen by 31 per cent and SMP by 13 per cent.

The lower commodity prices placed downward pressure on our Farmgate Milk Price in the first half. This was partially offset by currency, with a benefit of approximately 30 cents per kgMS to the forecast Farmgate Milk Price as at 31 January 2015. Our NZD/USD average conversion rate for the period was approximately 80 cents.

VALUE

Across the first half, total sales volumes of 2.2 million MT were 10 per cent ahead of the same period last financial year. Revenue, at $9.7 billion, was 14 per cent lower for the comparable period, reflecting lower global prices for dairy ingredients.

Normalised earnings before interest and tax (EBIT) for the six-month period to 31 January 2015 was $376 million compared to $403 million in the prior period, a reduction of seven per cent.

The Co-operative recorded a net profit after tax of $183 million for the period, a reduction of 16 per cent. In reviewing our previous year's performance, it is important to note that last year, in order to protect the Co-operative, the Board decided to pay a lower Farmgate Milk Price than the price calculated under the Farmgate Milk Price Manual.

In the first quarter, opportunities to improve ingredients, consumer and foodservice gross margins were restricted until inventory from the prior year was cleared.

WE ARE THE **WORLD'S LARGEST DAIRY EXPORTER**

FARM SOURCE

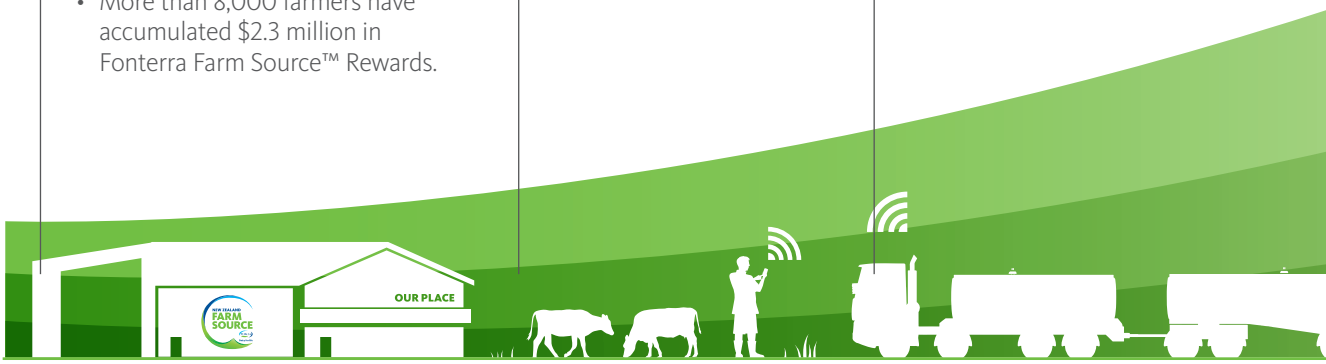
- Fonterra Farm Source™ launched as a comprehensive package of regional advice, digital tools, competitive discounts on farm necessities and financial options for managing farmers' businesses.
- More than 8,000 farmers have accumulated $2.3 million in Fonterra Farm Source™ Rewards.

WELL CONNECTED

- The Fonterra Farm Source™ app delivers milk data and business information to farmers' smartphones. It has 3,500 users.

EFFICIENCY

- The Estimated Tanker Arrival (ETA) app was launched. It helps farmers plan their day with more accuracy, enabling more efficiency on farm.



There is often a lag between when product is produced and when it is sold. During the first quarter, the value of our ingredients inventory was relatively high as it was mostly produced when WMP prices were higher, ranging between USD2,700 and USD4,700 per MT. However, these higher inventory costs were not recovered due to rapidly falling WMP prices in the first quarter of this financial year which dropped to a low of around USD2,400 per MT.

This gap between the value of inventory and selling prices in the first quarter created a margin squeeze. This contrasts with the first quarter last year when the value of inventory was based on a lower milk cost and was sold at a higher price. In the second quarter this year, earnings for ingredients improved benefiting from the lower cost of milk.

The majority of the half-year normalised EBIT was earned in the second quarter and this is expected to carry over into the second half of the financial year.

Our consumer and foodservice businesses in Asia and China source all of their milk from New Zealand and benefited in the second quarter from the lower cost of milk. Our Australian and Chilean consumer and foodservice businesses source their milk in-market.

Earnings were significantly impacted by higher milk prices within each of these milk pools, which squeezed margins. In Australia, Chile and Brazil, the prices paid for milk are influenced by in-market dynamics rather than global prices, so our businesses in these markets have faced higher input costs. Meanwhile, our Sri Lanka business has turned around, with improved earnings in the first half, after rebuilding the market share lost following the temporary suspension of our operations last financial year.

Despite some market challenges, our consumer and foodservice business overall achieved volume growth and improved pricing, together delivering a $91 million increase in our gross margin. Normalised EBIT in consumer and foodservice for the first half was $116 million, an increase of 23 per cent on the prior period.

OUTLOOK

Our first half results combined with the current market conditions mean that our expectations for the full year have resulted in an updated forecast dividend range of 20 to 30 cents per share (based on our policy of paying 65 to 75 per cent of net profit after tax). We are maintaining our current forecast Farmgate Milk Price.

CAPACITY

- $555 million investment under way to build a further dryer at Lichfield in South Waikato and to install three plants at Edendale in Southland.

GLOBAL BRANDS

We know that our farmer shareholders are looking to us to deliver sustainable earnings in a volatile market.

We have a single-minded focus on delivering results: increasing sales volumes, reducing complexity, and taking out costs to maximise returns. To accelerate delivery on strategy, the management team is leading a comprehensive business transformation programme. It will firmly embed the best features of entrepreneurial thinking, such as effectiveness, efficiency and agility.

This will require some tough decisions, but we are committed to improving performance. We have made good progress so far but we need to increase the pace of change.

We remain strongly committed to the V3 Strategy we formulated three years ago, which has been a huge change for the Co-op. The strategy is creating sustainable returns through the integration of our ingredients multi-hubs and targeted consumer and foodservice positions in our key markets. We remain uniquely placed in the world with our global reach, asset footprint, and integrated grass-to-glass supply chain.

But the change so far has not been easy. Capital structure change was a necessity. However, the precautionary recall last year, and recent contamination threat have been unwelcome distractions. These events remind us that the world is constantly changing and we have to be agile and responsive so we can remain ahead. We have the building blocks in place to deliver on our vision and strategy for the long term and the determination and aggressive plan to accelerate performance improvements.

John Wilson
Chairman

Theo Spierings
Chief Executive

UNITY GIVES US **SCALE, STRENGTH AND INTEGRATION**

It enables us to execute our strategy and secure the **best Farmgate Milk Price and earnings**

2012 – 2014 SET STRATEGY STRENGTHEN CORE

COMPLETE

2015 – 2017 DRIVE PERFORMANCE

IN PROGRESS

To achieve global relevance we need to put the stepping stones in place today.

From 2012 to 2014, we developed our V3 strategy, strengthened the core of the business and put in place a secure capital structure.

Our strategy is designed to grow Cash Payout by converting more of the milk we source into higher-returning products, especially through our consumer and foodservice operations. The more progress we make, the more we turn the value wheel. We have made good headway globally, setting the stage for consumer and foodservice growth in Latin America, China and Asia, and growing both volume and value in our key markets.

We continue to build on our strengths with the ultimate goal of being a truly global co-operative by 2025.

The success of the V3 strategy can only be measured by how much value has been captured through a higher Cash Payout and other tangible benefits such as increased value of the Co-operative and our farmers' dairy assets.

Now we are continuing to push forward with the aim of maximising performance so we can increase our Cash Payout.

Work mapped out over the next two to three years includes investments to increase our capacity in New Zealand so we can make better choices around what we make with our farmer shareholders' milk. Better choices mean better returns, so the capital outlay now is important to set ourselves up for sustainable returns to farmer shareholders over the long term. We also have a clear path ahead to grow value via our consumer and foodservice businesses, especially in Latin America, Malaysia, Indonesia, China and Sri Lanka. Success here will flow through to our dividends.

Our business transformation programme will ensure we continue to deliver on our strategy, with velocity.

2025 SCALE UP TO GLOBAL CO-OPERATIVE

Establishing partnerships with A-ware, Beingmate, Dairy Crest and Abbott, and redefining our relationship with Nestlé is setting us up for volume and value performance to fund growth.

Importantly, these relationships are giving us access to the high-quality milk pools that are also crucial to global relevance and growing returns for our farmer shareholders.

Ultimately, we want to grow milk volumes to 30 billion litres from New Zealand and from five other secure milk pools in key geographies around the world by 2025. These milk pools are our defence against becoming a regional player with our opportunities defined by milk produced in New Zealand.

Our multi-hub strategy supports our goal of leadership in dairy ingredients. It also helps protect our current leadership position in export markets. This leadership often opens up opportunities to work within borders, as we do in China, where revenue will come from exports and milk we produce in market.

WE HAVE A MULTI-HUB **STRATEGY FOR MILK GROWTH**

A-WARE, HEERENVEEN, NETHERLANDS

WE ARE COMPLEMENTING OUR NEW ZEALAND MILK SUPPLY WITH MILK POOLS OFFSHORE TO **CAPTURE VALUE AND SUPPORT OUR STRATEGY TO BECOME A GLOBAL CO-OPERATIVE**

In our milk pool strategy, our farmer shareholders' milk is targeted to the highest-returning products in New Zealand, where we have significant powders experience and global market share.

Other milk pools, such as those in Australia, Chile, China and Europe, enable us to capture the best share of market demand, especially in value-returning segments such as specialised infant formula ingredients and whey.

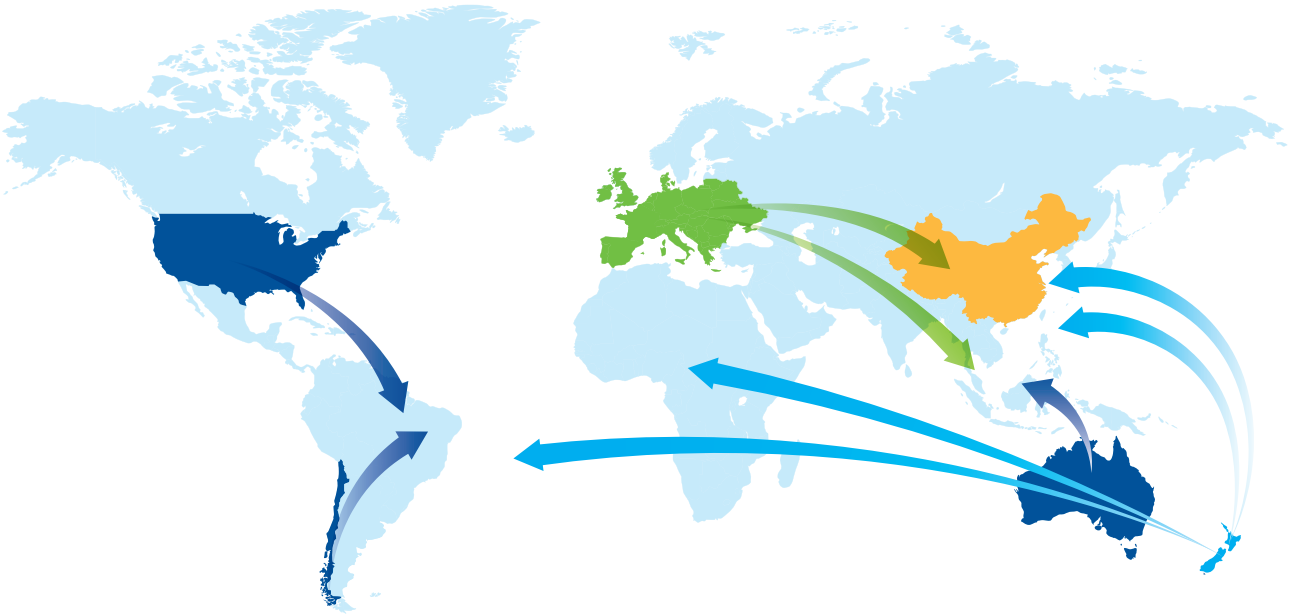
Building our New Zealand milk pool is as important as establishing global milk pools, especially as more international processors look to take advantage of New Zealand's reputation and our farmer shareholders' efficiency.

Our New Zealand ingredients business underpins the Farmgate Milk Price. Therefore, a clear priority is to increase our production flexibility in New Zealand so that we can always make the most profitable decisions about what we make, especially around the peak. In August, the Board approved a $555 million investment to build a further dryer at Lichfield in South Waikato and to install three new plants at Edendale in Southland. This investment will increase our capacity for Whole Milk Powder, Milk Protein Concentrate and Anhydrous Milk Fat.

Investments are not simply about increasing our ability to process more milk, or having more options around what we make. Each new high-volume build lifts our total asset efficiency in terms of yield, quality and cost of production, and in the long run this supports the Farmgate Milk Price.

To support growth in milk production, we rolled out Fonterra Farm Source™. This initiative is a comprehensive package of regional services and support, digital tools, competitive discounts on farm necessities and financial

GLOBAL MULTI-HUB LOCATIONS



Milk Powder / Foodservice

Whey

Cheese / Whey / Infant Formula

UHT / Foodservice

options for our farmer shareholders to help them manage their farming businesses. Fonterra Farm Source™ enables our strategy by growing the milk pool in New Zealand, which is core to the business, while protecting and enhancing our share of total New Zealand milk production.

Fonterra Farm Source™ is also a vehicle for providing financial solutions when farmers need them. Good examples are enabling farmer shareholders to defer compliance with the share standard until April, taking financial pressure off them in a tight year. We also eased that pressure by extending Fonterra Farm Source™ credit to 180 days to help farm budgets. Other financial tools include the Dividend Reinvestment Plan and Invest As You Earn, which both help farmer shareholders share up to match production as needed.

To grow our New Zealand milk pool we launched a separate milk sourcing subsidiary to attract valuable milk and provide a new pathway to membership in the Co-operative. Called **my**milk™, it is seeking to attract milk from farms in the Canterbury, Otago and Southland regions that are not currently supplying Fonterra, with no initial obligation to buy our shares. Instead, we are offering one-year contracts, renewable for a maximum of five years. After that time a **my**milk™ supplier will be encouraged to join the Co-operative and buy shares. Meanwhile, the Co-operative as a whole gains from higher milk volumes through efficient plants, which lowers our overhead costs, delivered through a profitable **my**milk™ business.

Accessing milk pools does not always need to mean creating farms as we have in China, or collecting milk from contract suppliers as we do in Australia, Sri Lanka or Chile. Increasingly access also comes via partnerships, which works well for both parties.

ACCESSING MILK POOLS DOES NOT ALWAYS HAVE TO MEAN CREATING FARMS. **INCREASINGLY ACCESS ALSO COMES VIA PARTNERSHIPS, WHICH WORKS WELL FOR BOTH PARTIES**

For example, Fonterra is the dedicated and exclusive sales channel for galacto-olgosaccharide and demineralised whey powder, both used in infant formula and made by our partner Dairy Crest in the UK.

Our partnership with Dutch cheese producer A-ware gives us access to 600 – 800 million litres of milk in the European market. During the half year, we worked toward the commissioning of our dairy ingredients plant in Heerenveen in January 2015. The Fonterra ingredients factory takes all liquid whey from A-ware's cheese production and will process this into 5,000 MT of whey protein and 25,000 MT of lactose specialty ingredients; these are used in high-value paediatric, maternal and sports nutrition products to supply Fonterra customers in Europe and Asia. This is our first wholly owned and operated ingredients plant in Europe.

Ingredients from A-ware and our Dairy Crest alliance come into play in our partnership with Beingmate Baby and Child Food Co Limited. Post balance date, Fonterra submitted a partial tender offer to acquire up to 20 per cent of Beingmate and this was completed in March. After regulatory approvals, we will set up a joint venture with Beingmate to purchase Fonterra's Darnum plant in Australia through wholly owned subsidiaries. Beingmate will own 51 per cent of the joint venture. We will also establish a distribution and licensing agreement to sell our Anmum™ brand in China.

This partnership demonstrates our multi-hub strategy and global milk pools at their best, with ingredients from our European pools going into the high-value infant formula products to be made at Darnum in Australia for China. The partnership will also see milk from New Zealand exported to China through our high-quality Anmum™ infant formula brand.

BEINGMATE GLOBAL PARTNERSHIP

After regulatory approvals, we will set up a joint venture with Beingmate to purchase Fonterra's Darnum plant in Australia and establish a distribution and licensing agreement to sell our Anmum™ brand in China.

nzmp™

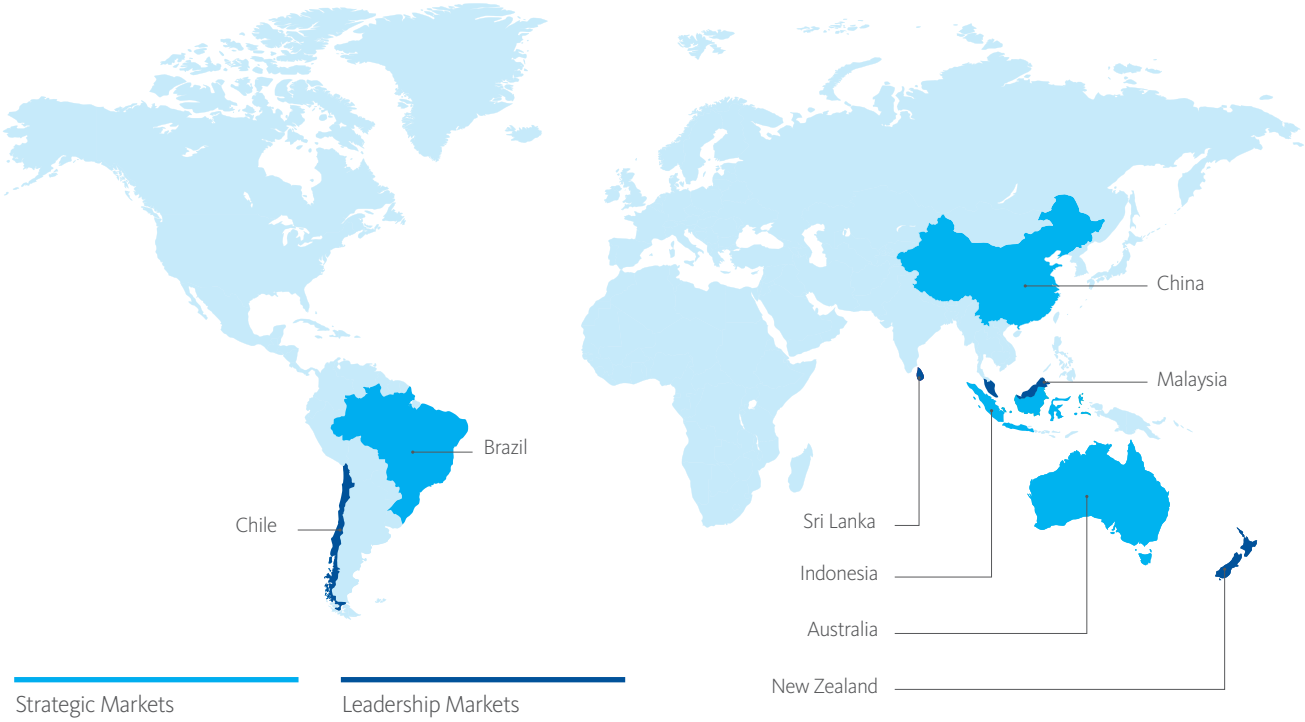
25,000 MT

LACTOSE SPECIALTY INGREDIENTS

The Fonterra ingredients factory takes all liquid whey from A-ware's cheese production and will process this into 5,000 MT of whey protein and 25,000 MT of lactose specialty ingredients.

ACCELERATE **CONSUMER AND FOODSERVICE GROWTH**

OUR EIGHT KEY STRATEGIC MARKETS



Relevance means being number one or two in our eight key strategic markets. We already have leadership positions in key dairy categories in New Zealand, Malaysia, Sri Lanka and Chile, and in China, Brazil, Australia and Indonesia we are focused on building scale operations.

We will be growing our consumer positions, continuing to maximise our foodservice potential and really backing a lean and focused portfolio of brands – the Anlene™, Anmum™ and Anchor™ brands – supported by some strong regional brands such as Soprole™, Fernleaf™, Mainland™ and Western Star™.

As we form new partnerships we are evaluating existing ones, ensuring they continue to generate value for all parties. We have completed the transformation of our Dairy Partners Americas (DPA) joint venture with Nestlé, with our new arrangement better aligned to the strategies of both companies.

We now have a majority stake in DPA Brazil, giving us the opportunity to drive strategy and accelerate growth. Together with a local partner, we have acquired Nestlé's share of DPA Venezuela and we have sold our share in DPA's milk powder manufacturing business to Nestlé. Finally, Nestlé acquired our share in DPA Ecuador.

These changes mean we can focus on building our position in everyday nutrition in the rapidly growing Brazilian and Venezuelan markets and develop foodservice opportunities that will generate higher volumes and value. We are particularly targeting volume and value growth in the yoghurt and dairy dessert categories.

As we form new partnerships we are evaluating existing ones, ensuring they continue to generate value for all parties.

In foodservice, we are exploring the implementation of our 'chef-led' foodservice strategy in Brazil. This involves our chefs working with foodservice professionals like chefs and bakers, developing recipes using our ingredients. By enabling businesses to grow through culinary innovation, we grow demand for our products and unique support offering.

In all of our markets, relevance is also measured by our customers, consumers, peers and stakeholders ranking us in the top tier for reputation. Underpinning this goal is our four-year programme to establish a global benchmark for food quality and safety, now in its second year.

In foodservice, we are exploring the implementation of our 'chef-led' foodservice strategy in Brazil.

By enabling businesses to grow through culinary innovation, we grow demand for our products and unique support offering.

BRINGING IT **ALL TOGETHER**

OUR CO-OPERATIVE IS OUR FARMER SHAREHOLDERS AND OUR PEOPLE WORKING TOGETHER FOR ONE PURPOSE: TO BRING TRUSTED DAIRY NUTRITION TO THE WORLD. OUR STRENGTH COMES FROM THIS UNITY AND OUR FUTURE DEPENDS ON IT

Global relevance is an ambitious goal but we can achieve it because we are building on a very strong foundation that has been years in the making. We have a secure base in our capital structure that gives us the balance sheet certainty to drive hard on performance and invest for growth.

We are focused on governance that combines the right mix of skills and experience required for a global company that has the interests of our New Zealand farmer shareholders in mind. We have a very clear strategy with clear priorities and it is delivering results.

These results are being achieved because as a co-operative we are confident in who we are and what we stand for. Our values and our identity are strong and our people are aligned to our purpose to be the world's most trusted source of dairy nutrition.

These values are demonstrated in our sustainability and social responsibility programmes where we work within our communities around the world. In New Zealand, our Fonterra Milk for Schools programme is now operating nationally with 1,498 participating schools and 170,000 children receiving a free serving of Anchor™ UHT milk every school day. The programme ensures good nutrition is now part of the school day, thanks to the support of our farmer shareholders. It is in addition to our KickStart Breakfast partnership with Sanitarium, which provides more than 100,000 breakfasts each week to around 800 schools in New Zealand.

Fonterra Milk for Schools has served as a model for a pilot to provide free milk for schools in Sri Lanka. Announced in November 2014, it is part of a wider programme to encourage the development of Sri Lanka's dairy industry where we source milk from around 4,000 farmers.

170,000

GOOD NUTRITION FOR OUR CHILDREN

The number of children receiving a free serving of Anchor™ UHT milk every school day. The programme ensures good nutrition is now part of the school day, thanks to the support of our farmer shareholders.

1,498

PARTICIPATING SCHOOLS

The Fonterra Milk for Schools programme is now operating nationally with 1,498 participating schools.

We continue to make progress with our 10-year programme with the Department of Conservation (DOC), focused on improving water quality in key dairy regions in New Zealand. Under the Living Water partnership, DOC and Fonterra, along with local communities, iwi and farmers, are working together to improve the health of five catchments. These are Hikurangi in Northland, three Waikato peat lakes – Areare, Ruatuna and Rotomānuka, Miranda/Pūkorokoro on the Firth of Thames/Tikapa Moana, Te Waihora/Lake Ellesmere in Canterbury and Waituna in Southland.

Work includes planting native trees alongside streams and rivers to improve water quality, managing animal pests and weeds, and making sure the right habitats are in place to enhance biodiversity and provide homes for native fish and birds. This complements the significant investments of time and money our farmer shareholders have put into fencing waterways on farms, riparian planting and upgrading effluent systems so they are fully compliant, and help improve on our already highly productive farm systems.

Fonterra has also linked up with Westland Milk Products, Tatua, Open Country and Synlait to commit $5 million to accelerate research and development in improved ways to remove rats, stoats and possums from large areas of land in New Zealand. This funding will add to the investment by NEXT Foundation and DOC into the Zero Invasive Predators (ZIP) programme last year and is targeting new tools in addition to existing control methods such as 1080.

Our Co-operative is our farmer shareholders and our people working together for one purpose: to bring trusted dairy nutrition to the world. Our strength comes from this unity and our future depends on it.

PROGRESS UPDATE

Our progress in achieving our potential can be grouped under two headings: cash generators and growth generators. Cash generators finance our growth today, while growth generators are our source of future cash. Cash generator priorities are to optimise New Zealand milk and to lock in the competitive positions of our consumer businesses in mature markets, especially in Australia and New Zealand.

This graphic shows progress this year.

CASH GENERATORS

OPTIONALITY

INVESTING IN INGREDIENTS ASSETS TO IMPROVE FLEXIBILITY, MAXIMISING MILK PRICE AND EARNINGS

NEW ZEALAND

- Pahiatua dryer and distribution centre: $235 million invested, increases capacity by **2.4 million litres** per day. Completion date: September 2015.

FIX UNDERPERFORMING BUSINESSES

SRI LANKA

- Sri Lanka market share rebuilt following the temporary suspension of our operations last financial year.

GROWTH GENERATORS

MULTI-HUBS

CONNECT GLOBAL MILK POOLS TO CAPTURE VALUE AND SUPPORT OUR GOAL OF BECOMING A GLOBAL CO-OPERATIVE

NETHERLANDS: A-WARE PARTNERSHIP

- Plant commissioned and ready to process 5,000 MT of whey protein and 25,000 MT of lactose specialty ingredients.
- A-ware provides us access to **600 – 800 million litres** of milk.

ACCELERATE CONSUMER AND FOODSERVICE

CHINA: BEINGMATE PARTNERSHIP

- Investment in one of the largest infant formula brands in China.
- Growth of Anmum™ brand in China via licensing arrangement.

TRUST IN SOURCE

THIS IS FONTERRA

- Year two of our programme to establish a new global benchmark for food safety and quality.
- This is Fonterra brings together people, who we are and what we stand for and our strategy.

COMPLETED

WORK IN PROGRESS

Our consumer and foodservice businesses in priority markets, including China, ASEAN and Latin America, are the growth generator priorities. Progress across all priorities is supported by our programme to establish a new benchmark in food safety and quality, building trust in Fonterra as a source of dairy nutrition.

- Lichfield dryer project - $398 million investment, adds some **4.4 million litres** per day to capacity. Completion date 2016.
- Edendale expansion, three plants, AMF, MPC and reverse osmosis. Increases capacity by **1.4 million litres** per day. Commissioning 2015.
- Initial consultation for two dryers at Studholme, capable of delivering **nine million litres** more capacity.

AUSTRALIA

- Australian costs down 21 per cent over two years.
- Strategies in hand to combat intense competition and achieve greater use of Australian assets.
- Grow infant formula exports.
- Grow specialty cheese.
- Improve returns from yoghurt.

UK: DAIRY CREST

- Fonterra is the dedicated sales channel for Dairy Crest's ingredients used in infant formula.

CHINA: ABBOTT

- Agreement in place to jointly develop a dairy farm hub in China. Antitrust approval received from Chinese Government.

AUSTRALIA/NZ: BEINGMATE

- Partnership designed to grow ingredients exported from New Zealand and Australia to China, including infant formula.

LATIN AMERICA: DAIRY PARTNERS AMERICAS

- Revised joint venture to better reflect strategy for Nestlé and Fonterra.
- Retains Nestlé as partner in Brazil, with Fonterra owning a 51 per cent controlling stake.
- Enables volume and value growth in foodservice and everyday nutrition in all dairy categories in Latin America.

All come together for our purpose:

TO BE THE WORLD'S **MOST TRUSTED SOURCE OF DAIRY NUTRITION.**

FINANCIAL **HIGHLIGHTS**

NORMALISED EBIT (NZD)

$376M

LOWER PRICES FOR GLOBAL DAIRY COMMODITIES IN THE FIRST HALF RESULTED IN LOWER INPUT COSTS. HOWEVER, THESE COST BENEFITS ONLY CAME THROUGH IN THE SECOND QUARTER AS MARGINS IN THE FIRST QUARTER WERE CONSTRAINED BY THE HIGHER-PRICED OPENING INVENTORY PRODUCED USING PRIOR-SEASON MILK

FORECAST CASH PAYOUT PER KGMS

$**4.90** TO $**5.00**

MILK COLLECTION

1,150M KGMS

VOLUME ('000 MT)

2,189MT

REVENUE (NZD)

$9,746M

NET PROFIT AFTER TAX (NZD)

$183M

INTERIM DIVIDEND PER SHARE

10CPS

Fonterra refers to normalised EBIT when discussing financial performance.
Refer to page 53 for further details on non-GAAP financial measures.

GROUP **OVERVIEW**

2%

INCREASE IN VOLUME

The impact of consolidating DPA Brazil and our Venezuela consumer business for the first time was an additional 160,000 MT of sales in the first half relative to the prior period. Excluding this, volumes increased by two per cent.

AS PART OF OUR COMMITMENT TO ONGOING IMPROVEMENTS IN OUR DISCLOSURE, **WE HAVE ENHANCED THE COMMENTARY IN THE BUSINESS REVIEW SECTION TO ALIGN WITH OUR GLOBAL STRATEGY**

The purpose of this improvement is to provide more clarity on the ingredients, consumer and foodservice, and international farming businesses, and the key drivers of earnings in each.

To ensure continued transparency and consistency, we have retained the standard segment note disclosure of the regional business units in the financial statements and added an additional table disclosing the performance of the regions within the consumer and foodservice segment.

Volumes increased by 10 per cent to 2.2 million MT. During the period, we reorganised our DPA alliance with Nestlé in Latin America. We gained management control of DPA Brazil and a consumer business in Venezuela, and sold our share in DPA Manufacturing and DPA Ecuador. The impact of consolidating DPA Brazil and our Venezuela consumer business for the first time was an additional 160,000 MT of sales in the first half relative to the prior period. Excluding this, volumes increased by two per cent. Other drivers of volume growth were China farms, which increased due to farm expansions, and our consumer and foodservice business in China.

Group normalised EBIT of $376 million in the first half was $27 million lower than the prior year.

Lower prices for global dairy commodities in the first half resulted in lower input costs, however, these cost benefits only came through in the second quarter as margins in the first quarter were constrained by the higher-priced opening inventory produced using prior-season milk.

Our ingredients business was up $7 million compared to the same period last year. Although the ingredients business benefited from positive product mix returns and higher price premiums, earnings were impacted by a lower return from powder products (which inform the Farmgate Milk Price) and an unfavourable product mix in Australia, which impacted margins.

Our consumer and foodservice business was $22 million higher than the prior period as a result of a recovery in Sri Lanka and a good performance across Asia, in New Zealand and to a lesser extent in Greater China. This was partially offset by lower earnings from Soprole, where higher milk costs were not fully recovered.

Earnings from our international farming business were down $29 million due to lower milk prices in China and the livestock revaluation gain from the prior period that was not repeated in the current period.

Operating expenses were 15 per cent higher, with the largest driver being the newly acquired Latin American businesses.

NZD million	Six months ended 31 January 2015	Six months ended 31 January 2014	Change
Total volume ('000 MT)	2,189	1,988	10%
Sales revenue	9,746	11,292	(14%)
Gross margin	1,552	1,407	10%
Gross margin percentage	15.9%	12.5%	
Operating expenses	(1,337)	(1,159)	15%
EBIT	483	416	16%
Normalised EBIT	376	403	(7%)
Net finance costs	(303)	(147)	106%
Tax credit/(expense)	3	(52)	
Net profit after tax	183	217	(16%)
Earnings per share (cents)	10	13	(23%)
Economic debt to debt plus equity ratio	51%	45%	

Excluding that impact, operating expenses were up three per cent. This was due to the expansion of our China business and investment in brands, growth in China Farms, increased storage and distribution costs in the ingredients business, and higher group costs required to execute key aspects of our strategy. This includes set-up costs related to recent acquisitions. This was offset to some extent by savings in Australia and most markets across Asia.

Net finance costs for the first half were $156 million higher than the prior period. This was mainly due to lower unrealised fair valuations of long-dated interest rate swaps used for hedging purposes. Actual cash and accrued interest was also higher, as borrowings increased due to higher working capital requirements to support our farmers during a low milk price season and higher capital spend to execute our strategy.

Tax in the first half was lower than the prior period due to a higher tax credit as a result of the higher interim dividend.

Our gearing ratio is up at 51 per cent as a result of lower equity retentions, higher capital expenditure and increased business funding requirements compared to the first half last year. This is in line with our expectations.

INGREDIENTS

Price premiums achieved above dairy commodity prices for ingredients and value-added services were $90 million higher than the first half last year.

CONSUMER AND FOODSERVICE

Greater China delivered strong volume growth of 36 per cent, driven primarily from our foodservice business and China brands.

INTERNATIONAL FARMING

Farming hubs are a key part of our strategy to be a more integrated business in China and milk production volumes increased significantly to over five million kgMS for the half year.

INGREDIENTS

The Ingredients segment represents the ingredients businesses in New Zealand, Australia and Latin America. This segment also includes the Co-operative's corporate activities and Farm Source (formerly RD1), a rural supplies retailer in New Zealand.

OUR INGREDIENTS BUSINESS BENEFITED FROM IMPROVED PRODUCT MIX RETURNS IN NEW ZEALAND AND INCREASED PRICE PREMIUMS

Milk collection across New Zealand for the season to 31 January 2015 was 1,150 million kgMS, up three per cent on the same period last season. Milk collection in Australia, which is our second largest milk pool, was 82 million kgMS, up six per cent.

Ingredients sales volume was flat, with lower New Zealand-sourced sales to China offset by higher sales in other regions. Revenue was 23 per cent down, reflecting the 45 per cent lower dairy commodity prices during the first half compared to the same period last year.

Normalised EBIT for the first half was $299 million, up two per cent relative to the comparable period.

Our ingredients business benefited from higher product mix returns in New Zealand and increased price premiums, with margins improving in the second quarter.

Positive returns from product mix drove a $71 million improvement in gross margin compared to the first half last year. Product mix is made up of the return from both powder and non-powder products (refer to the chart on the right).

The return from powder products was $182 million lower than the first half last year. There is often a lag between when product is produced and when it is sold, and this sales phasing varies by product type. In the first quarter the value of inventory sold was relatively high as it included a proportion of the previous season's product, which was produced when Whole Milk Powder (WMP) prices and hence milk prices were higher. However, selling prices achieved fell rapidly in the first quarter of this financial year with WMP falling to a low of around USD2,400 per MT.

This gap between the value of inventory and selling prices created a margin squeeze in the first quarter. This is a reversal of the same period last year, when the value of inventory was based on a lower milk cost and sold at a higher price.

In the second quarter this year, earnings from powder products improved, benefiting from the lower cost of milk.

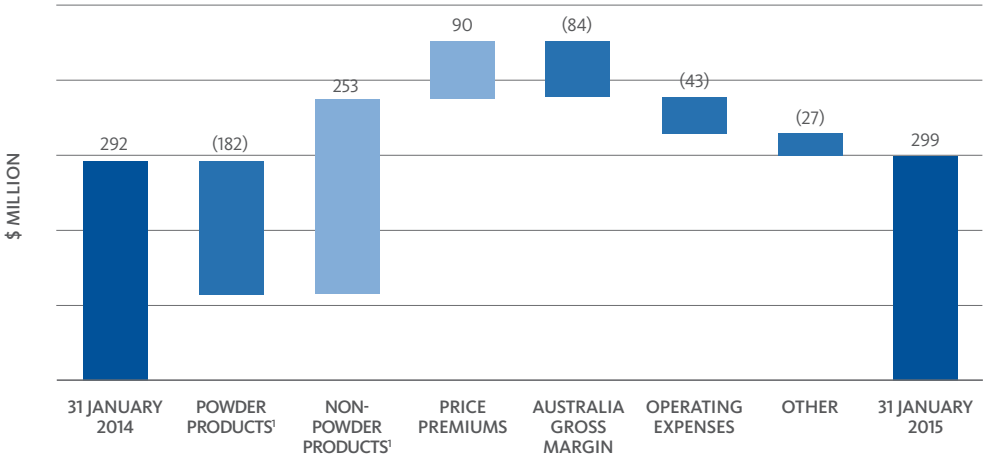
2%

NORMALISED EBIT

Normalised EBIT for the first half was $299 million, up two per cent relative to the comparable period.

NZD million	Six months ended 31 January 2015	Six months ended 31 January 2014	Change
Total volume ('000 MT)	**1,538**	**1,543**	**–**
Sales revenue	**7,617**	**9,900**	**(23%)**
Normalised EBIT	**299**	**292**	**2%**

NORMALISED EBIT: KEY PERFORMANCE DRIVERS



1 Powder products are Reference Commodity Products which inform the Farmgate Milk Price. These are currently Whole Milk Powder, Skim Milk Powder, Anhydrous Milk Fat, Butter and Butter Milk Powder.

Non-powder products also felt the first quarter margin pressure, but generated $253 million higher earnings than the first half last year. This includes a positive contribution from our long-term liquid milk contracts, which boosted returns.

Strong milk production through the peak collection period, combined with capacity constraints, resulted in some additional transport costs and inefficient processing. However, these costs were lower than the comparative period, driven by investment in operational efficiencies, which delivered additional capacity of around 1.9 million litres per day compared to the peak last season.

Price premiums achieved above dairy commodity prices for ingredients and value-added services were $90 million higher than the first half last year. In volatile times, we were able to offer our customers value under the relaunched NZMP™ brand, leveraging off an understanding of their needs. A change in global demand dynamics away from China enabled greater opportunities to sell to customers in Southeast Asia, Middle East and Africa, and increased sales of offshore government tenders.

Gross margin on ingredients manufactured in Australia was impacted by an unfavourable product mix due to lower sales of nutritionals. Gross margin was $84 million lower due to an intensely competitive market for milk supply.

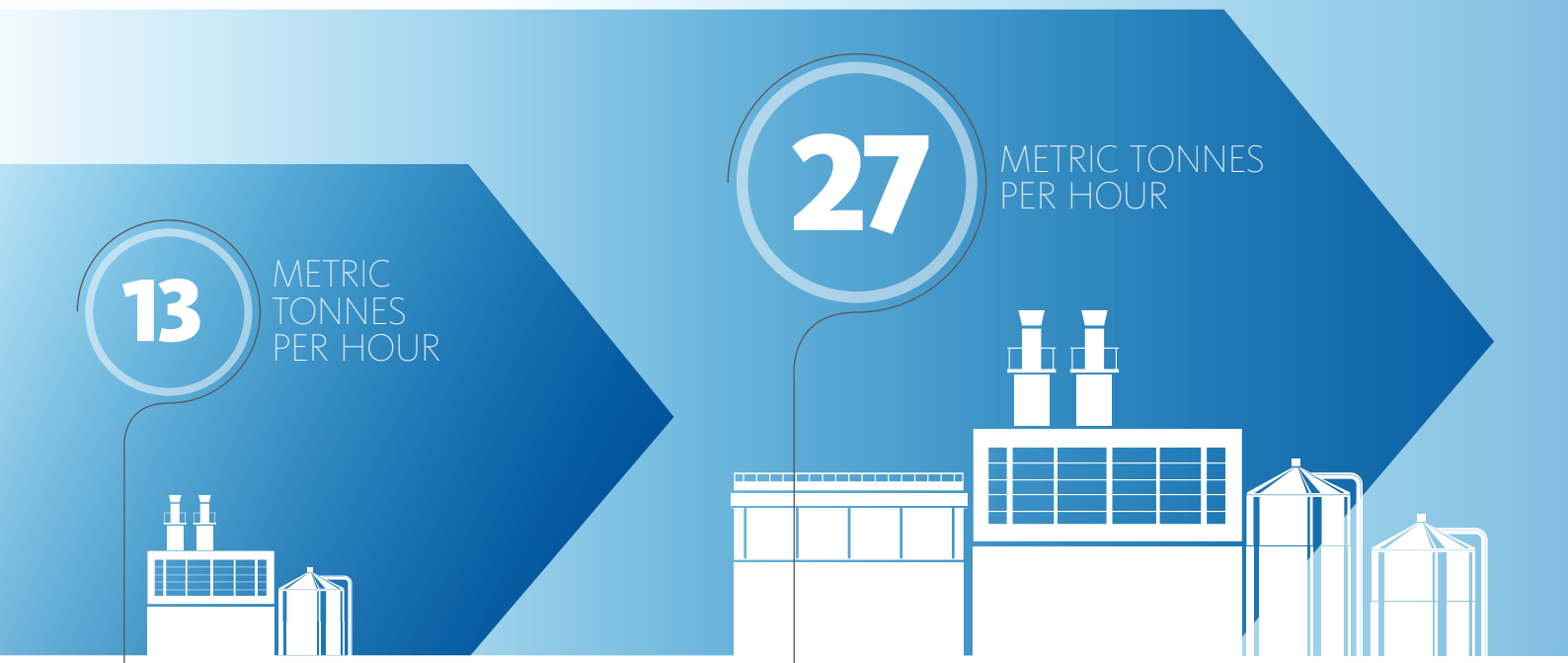
The proposed joint venture with Beingmate to acquire the Darnum plant is likely to have a positive impact on our infant formula business in Australia.

The ingredients segment includes group overheads. Operating costs were $43 million higher, mainly due to higher costs to support our global brands strategy and ensure efficient allocation of resources across our global brands portfolio, and higher storage and distribution costs in the United States and New Zealand. The benefit of the increased spend to support our global brands is starting to be realised, with the performance of our brands across Asia.

INGREDIENTS

Global relevance must include the efficient, profitable processing of the milk we produce in New Zealand. **Since 2009, some 70 per cent of capital spend has been in New Zealand to support the ingredients, and consumer and foodservice businesses.**

WHOLE MILK POWDER PRODUCTION CAPABILITY



2001. CLANDEBOYE DRYER TWO

The Clandeboye site is one of Fonterra's largest manufacturing sites in the South Island, primarily producing butter, cheese and milk powders. Dryer two was commissioned in 2001 and can process around two million litres of milk per day and produce 300 MT of Whole Milk Powder per day. Further investment at Clandeboye means that today dryer two primarily produces Milk Protein Concentrate.

2009. EDENDALE DRYER FOUR

The Edendale site, north-east of Invercargill, is New Zealand's oldest manufacturing site still in operation. Commissioned in 2009, dryer four was the world's largest and most efficient dryer, now overtaken by Darfield's second dryer. Edendale's dryer four can process around 4.2 million litres of milk and produce 630 MT of Whole Milk Powder per day.

BUILDING NEW CAPACITY

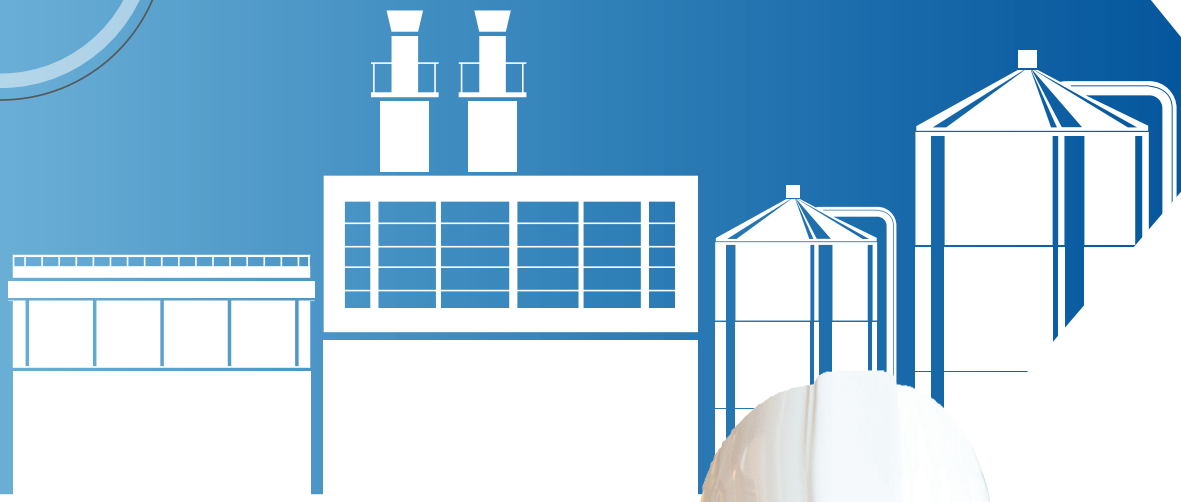
More flexibility means optimised production choices, especially at the peak, so we make the product mix that delivers the greatest returns, while meeting the needs of consumers and customers worldwide.

In addition to the Lichfield investment due for completion in September 2016, the $235 million site expansion at Pahiatua will increase North Island processing capacity by a further 2.4 million litres a day. This dryer will use the latest energy-efficient processing technology and will be the first in the country to reuse its own condensate. The first milk powder from this dryer is expected to roll out of the site by September 2015.

Also due for commissioning in 2015 are the Anhydrous Milk Fat and Milk Protein Concentrate plants, as well as a reverse osmosis plant at Edendale in the South Island. This investment increases daily capacity by 1.4 million litres and supports our strategy to increase earnings by driving more milk volume into higher-value categories.

Consultation has begun ahead of the potential lodging of consent applications for two new high-efficiency dryers at Studholme in Canterbury, delivering an additional nine million litres of capacity. If approved, the expansion will take place in two phases, with the first dryer on stream in five years and the second in 10 years.

30 METRIC TONNES PER HOUR



2016. LICHFIELD DRYER ONE

The Lichfield site, built in 1995 in the South Waikato, is the location of our next high-efficiency milk powder dryer. The new dryer will provide an additional 4.4 million litres per day of processing capacity and will be capable of producing 700 MT of Whole Milk Powder per day. This is equivalent to Darfield two, which was commissioned in August 2013.

In addition to the investment in New Zealand, we have also recently commissioned a new dairy ingredients plant in Heerenveen, in the northern Netherlands. The plant produces specialty whey and lactose ingredients which are used for high-value paediatric, maternal, and sports nutritional applications. The site has been developed in partnership with cheese manufacturer A-ware Food Group and supports our strategy in increasing the volume and value of our ingredients and branded products. The plant forms part of our fully integrated global supply chain from the farm gate direct to global consumers.

CONSUMER AND **FOODSERVICE**

The Consumer and Foodservice segment represents the consumer brands and foodservice businesses in Oceania, Asia, Greater China and Latin America.

OUR CHEF-LED APPROACH CONTINUES TO DELIVER GOOD GROWTH IN OUR FOODSERVICE BUSINESS IN ASIA DUE TO STRONG GROWTH IN THE ITALIAN KITCHEN AND ASIAN BAKERY CHANNELS

In the first half we reorganised our relationship with Nestlé in Latin America.

This will enable us to build on the success of the partnership in markets that present considerable opportunities for growth – Brazil and Venezuela. By taking management control in these markets, we can use our strengths gained in other consumer markets to deliver increased volume and value.

Dairy Partners Americas (DPA) Brazil and our consumer business in Venezuela have been fully consolidated in our accounts for the first time and this inclusion is a key reason for the increase in volume and revenue in Latin America compared to the prior period.

The consolidation has had no material impact on normalised EBIT since the equity-accounted earnings from DPA were included in EBIT in the prior period.

Volume across our consumer and foodservice businesses was up 27 per cent to 840,000 MT in the first half compared to the same period last year. Volumes for the combined DPA Brazil and Venezuela businesses in the period were 160,000 MT. Therefore, on a like-for-like basis, volume was up three per cent. Revenue was up 22 per cent to $3.3 billion and five per cent on a like-for-like basis, reflecting our ability to increase price points in some key markets.

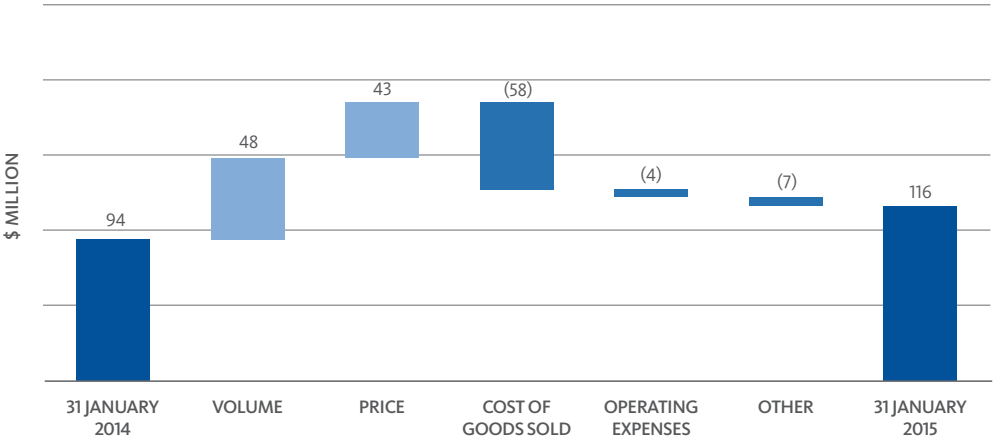
23%

NORMALISED EBIT

Normalised EBIT for the first half was $116 million, up 23 per cent relative to the comparable period.

NZD million	Six months ended 31 January 2015	Six months ended 31 January 2014	Change
Total volume ('000 MT)	**840**	**662**	**27%**
Sales revenue	**3,256**	**2,671**	**22%**
Normalised EBIT	**116**	**94**	**23%**

NORMALISED EBIT: KEY PERFORMANCE DRIVERS



Note: The impact on volume and revenue due to the consolidation of DPA Brazil and Venezuela is not reflected in the price, volume and cost of goods sold columns of the chart, but included in other to ensure those reflect underlying performance of the business.

NORMALISED EBIT

Normalised EBIT for the first half was $116 million, up 23 per cent relative to the comparable period.

VOLUME

Volume growth contributed to an increase in gross margin of $48 million, mainly due to Greater China, which delivered strong volume growth of 36 per cent. The recovery in Sri Lanka after the temporary suspension of our operations in the first half of last year was reflected in volume growth of four per cent in Asia. Volumes in Australia were higher in spreads and cheese categories and New Zealand delivered volume increases across most of the consumer brands domestically together with improved supply chain management.

In Greater China growth in foodservice was supported by our successful chef-led approach and the launch of our new foodservice application centre in Shanghai in November. The foodservice rollout continued into three new cities, taking the total to 29.

Our brands business in China continues to make good progress and is well positioned both in store and in the top e-retailers like T-mall. The rollout of Anchor™ in China continues with market share growth in the Yangtze River Delta region and in the North, which is a new region for the Anchor™ brand. Anmum™ infant formula is performing as per plan in selected markets.

WE HAVE HAD SOLID REVENUE GROWTH ACROSS OUR KEY MARKETS OF INDONESIA AND SRI LANKA

PRICE MANAGEMENT

Improved pricing management resulted in a gross margin increase of $43 million compared to the same period last year. In Asia, this had a positive impact, reflecting our ability to manage price points across a number of dairy categories including foodservice, despite the lower commodity prices. In Latin America we took price increases in Chile without losing volume and while maintaining market share.

We have had solid revenue growth across our key markets of Indonesia and Sri Lanka. The business maintained growth in everyday nutrition and foodservice with a strong performance from our Fernleaf™ brand in Malaysia.

Our chef-led approach continues to deliver good growth in our foodservice business in Asia due to strong growth in the Italian kitchen and Asian bakery channels.

DRIVING VALUE

Driving value through winning brands such as Kapiti Kahurangi blue cheese.

PRICE MANAGEMENT

Improved pricing management resulted in a gross margin increase of $43 million compared to the same period last year.

$43M

FOODSERVICE BUSINESS

Our chef-led approach continues to deliver good growth in our foodservice business in Asia due to strong growth in the Italian kitchen and Asian bakery channels.

COST OF GOODS SOLD

Input costs increased significantly across the consumer and foodservice business with higher cost of goods sold impacting gross margin by $58 million. This was mainly due to the higher cost of milk in Australia and in Chile in the first half compared to the same period last year.

Movements in raw milk prices in Chile tend to lag global commodity prices. As a result milk was relatively more expensive in the first half as costs did not drop in line with key international benchmarks. This is in contrast to the prior year, where the rapid increase in global prices did not take hold until the second half, resulting in a strong first half earnings performance.

In Asia, first-quarter margins in the consumer brands business remained under pressure as a result of last season's high cost inventory flowing through and this is reflected in the higher input costs. However, margins improved in the second quarter compared to the same period last year as the benefits of the lower dairy commodity costs started to come through. The higher input costs were offset to a small extent by the New Zealand consumer business where cost decreases came through relatively more quickly due to the higher proportion of fresh dairy products.

OPERATING EXPENSES

Operating expenses were $4 million higher mainly because of increased investment in our China consumer business. Operating expenses in China were $25 million higher mainly due to increased advertising and promotional spend to support business growth. In Latin America, expenses were higher due to increased storage and distribution costs in Chile. This was offset by Asia and Australia, where continued focus on costs led to further reductions in operating expenses.

INTERNATIONAL **FARMING**

International Farming represents the international farming operations in China.

FUTURE INVESTMENTS IN CHINA FARMS MAY INCLUDE FUNDING FROM STRATEGIC PARTNERS AS WELL AS FROM FONTERRA.

OUR GROWTH STRATEGY ADOPTS A HUB APPROACH, LEVERAGING ECONOMIES OF SCALE AND MITIGATING BIOSECURITY RISKS

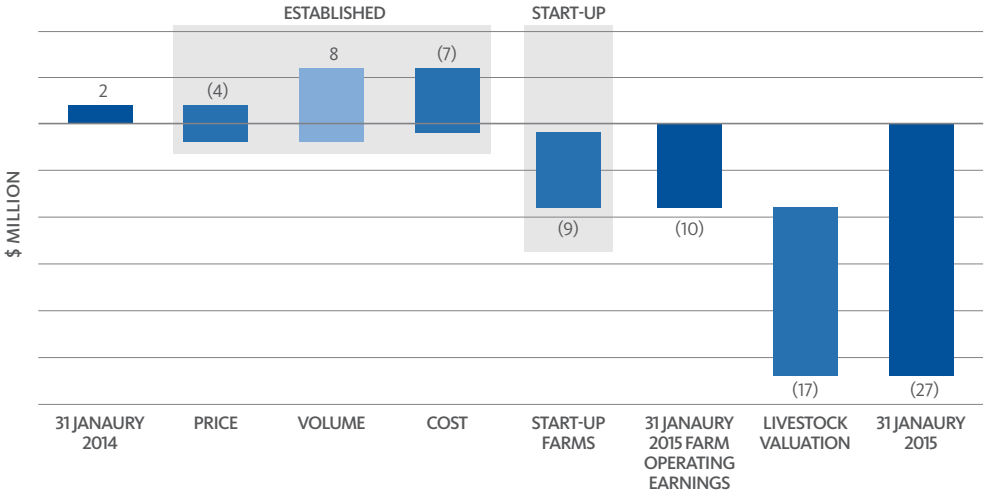
97%

VOLUME

Milk production volumes increased significantly to 67,000 MT for the first half as a result of the new farms that have come on stream since the first half last year (Yutian 3 in the Yutian hub) and the increased volume from Hangu, Yutian 1 and Yutian 2.

NZD million	Six months ended 31 January 2015	Six months ended 31 January 2014	Change
Total volume ('000 MT)	**67**	**34**	**97%**
Sales revenue	**66**	**37**	**78%**
Normalised EBIT	**(27)**	**2**	

NORMALISED EBIT: KEY PERFORMANCE DRIVERS



Farming hubs are a key part of our strategy to be a more integrated business in China, contributing to the growth and development of the local dairy industry and helping to meet Chinese consumers' need for safe, nutritious dairy products.

We now have two farming hubs with a total of nine productive farms. A single farm has capacity for around 3,200 – 3,500 milking cows and a double farm has around 6,500 milking cows. In total we have 24,000 milking cows plus 25,000 heifers and calves, across our farms to support our growth.

Milk production volumes increased significantly to 67,000 MT for the first half as a result of the new farm that has come on stream since the first half last year (Yutian 3 in the Yutian hub) and the increased volume from Hangu, Yutian 1 and Yutian 2. This equates to over five million kgMS of milk produced for the six months.

Normalised EBIT in the first half was $29 million lower than the same period last year due to the higher livestock revaluation in the first half of last year not being repeated this year. In addition we had a lower milk price in China as a result of increased local supply surplus, accentuated by lower global dairy commodity pricing, and higher year-on-year start-up costs as we accelerated the pace of farm development.

Livestock valuations include consideration of the age of the herd on farm and the medium-term view of milk prices in China. In the prior period the livestock revaluation saw a significant uplift reflecting milk price and the herd profile assumptions at the time. The revaluation gain in the prior period was not repeated in the first half this year.

Future investments in China farms may include funding from strategic partners as well as Fonterra. Our growth strategy adopts a hub approach, leveraging economies of scale and mitigating biosecurity risks. A typical hub accommodates approximately 16,000 milking cows, consisting of three to five farms in one region.

While growing a dairy business has its challenges, the opportunity is significant in China. As we develop the new hubs we will not compromise on milk quality, sustainability and high standards and this positions the business well for future growth.

INTERIM
FINANCIAL STATEMENTS

FOR THE SIX MONTHS ENDED 31 JANUARY 2015

DIRECTORS' STATEMENT

FOR THE SIX MONTHS ENDED 31 JANUARY 2015

The Directors of Fonterra Co-operative Group Limited (Fonterra or the Company) are pleased to present to Shareholders the financial statements for Fonterra and its subsidiaries (together the Group) and the Group's interest in its equity accounted investees for the six months ended 31 January 2015.

The Directors are responsible for presenting financial statements for the six months which give a true and fair view of the financial position for the Group and of the financial performance and cash flows for that period.

The Directors consider the financial statements of the Group have been prepared using accounting policies which have been consistently applied and supported by reasonable judgements and estimates, and that all relevant financial reporting and accounting standards have been followed.

The Directors believe that proper accounting records have been kept which enable, with reasonable accuracy, the determination of the financial position of the Group and facilitate compliance of the financial statements with the NZX Listing Rules.

The Directors consider that they have taken adequate steps to safeguard the assets of the Group, and to prevent and detect fraud and other irregularities.

The Directors hereby approve and authorise for issue the financial statements for the six months ended 31 January 2015 presented on pages 34 to 52.

For and on behalf of the Board:

JOHN WILSON
Chairman
24 March 2015

DAVID JACKSON
Director
24 March 2015

INCOME STATEMENT

FOR THE SIX MONTHS ENDED 31 JANUARY 2015

		GROUP $ MILLION		
		SIX MONTHS ENDED		YEAR ENDED
	NOTES	**31 JAN 2015 UNAUDITED**	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Revenue from sale of goods		**9,746**	11,292	22,275
Cost of goods sold	1	**(8,194)**	(9,885)	(19,813)
Gross profit		**1,552**	1,407	2,462
Other operating income		**188**	98	139
Selling and marketing expenses		**(356)**	(307)	(593)
Distribution expenses		**(318)**	(251)	(499)
Administrative expenses		**(444)**	(391)	(762)
Other operating expenses		**(219)**	(210)	(356)
Net foreign exchange gains		**51**	32	39
Share of profit of equity accounted investees		**29**	38	73
Profit before net finance costs and tax		**483**	416	503
Finance income		**20**	7	13
Finance costs		**(323)**	(154)	(379)
Net finance costs		**(303)**	(147)	(366)
Profit before tax		**180**	269	137
Tax credit/(expense)		**3**	(52)	42
Profit after tax		**183**	217	179
Profit after tax is attributable to:				
Equity holders of the Parent		**165**	206	157
Non-controlling interests		**18**	11	22
Profit after tax		**183**	217	179

	GROUP $		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Earnings per share:			
Basic and diluted earnings per share	**0.10**	0.13	0.10

The accompanying notes form part of these interim financial statements.

STATEMENT OF COMPREHENSIVE INCOME

FOR THE SIX MONTHS ENDED 31 JANUARY 2015

	GROUP $ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Profit after tax	**183**	217	179
Items that may be reclassified subsequently to profit or loss:			
Cash flow hedges:			
– Net fair value (losses)/gains	**(957)**	276	732
– Transferred and reported in revenue from sale of goods	**128**	(179)	(505)
– Tax credit/(expense) on cash flow hedges	**232**	(27)	(63)
Net investment hedges:			
– Net fair value (losses)/gains on hedging instruments	**(81)**	3	25
– Tax credit/(expense) on net investment hedges	**23**	(1)	(7)
Available-for-sale investments:			
– Net fair value gains/(losses) on available-for-sale investments	**3**	(2)	(1)
Foreign currency translation gains/(losses) attributable to equity holders	**235**	(98)	(207)
Foreign currency translation reserve transferred to income statement	**78**	–	–
Hyperinflation movements attributable to equity holders	**4**	–	–
Share of equity accounted investees' movements in reserves	**7**	(7)	(11)
Total items that may be reclassified subsequently to profit or loss	**(328)**	(35)	(37)
Items that will not be reclassified subsequently to profit or loss:			
Foreign currency translation gains/(losses) attributable to non-controlling interests	**5**	(2)	(4)
Hyperinflation movements attributable to non-controlling interests	**3**	–	–
Total items that will not be reclassified subsequently to profit or loss	**8**	(2)	(4)
Total other comprehensive expense recognised directly in equity	**(320)**	(37)	(41)
Total comprehensive (expense)/income	**(137)**	180	138
Total comprehensive (expense)/income is attributable to:			
Equity holders of the Parent	**(163)**	171	120
Non-controlling interests	**26**	9	18
Total comprehensive (expense)/income	**(137)**	180	138

The accompanying notes form part of these interim financial statements.

STATEMENT OF FINANCIAL POSITION

AS AT 31 JANUARY 2015

	NOTES	GROUP $ MILLION AS AT 31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
ASSETS				
Current assets				
Cash and cash equivalents		**266**	812	340
Trade and other receivables		**2,461**	2,653	1,950
Inventories		**4,651**	6,617	3,701
Tax receivable		**36**	32	20
Derivative financial instruments		**265**	203	303
Assets held for sale		**–**	–	58
Other current assets		**364**	60	112
Total current assets		**8,043**	10,377	6,484
Non-current assets				
Property, plant and equipment		**5,778**	4,917	5,091
Equity accounted investments		**298**	445	388
Livestock		**264**	159	202
Intangible assets		**3,354**	2,799	2,791
Deferred tax assets		**555**	156	231
Available-for-sale investments		**76**	72	74
Derivative financial instruments		**335**	188	154
Other non-current assets		**93**	158	114
Total non-current assets		**10,753**	8,894	9,045
Total assets		**18,796**	19,271	15,529
LIABILITIES				
Current liabilities				
Bank overdraft		**13**	3	21
Borrowings	8	**2,660**	2,107	1,534
Trade and other payables		**1,997**	1,664	1,638
Owing to suppliers		**978**	4,216	1,771
Tax payable		**17**	20	18
Derivative financial instruments		**973**	76	30
Provisions		**49**	47	47
Other current liabilities		**32**	50	74
Total current liabilities		**6,719**	8,183	5,133
Non-current liabilities				
Borrowings	8	**4,840**	3,966	3,364
Derivative financial instruments		**492**	369	415
Provisions		**185**	75	65
Deferred tax liabilities		**121**	5	5
Other non-current liabilities		**17**	10	13
Total non-current liabilities		**5,655**	4,425	3,862
Total liabilities		**12,374**	12,608	8,995
Net assets		**6,422**	6,663	6,534
EQUITY				
Subscribed equity		**5,807**	5,807	5,807
Retained earnings		**1,151**	1,192	1,059
Foreign currency translation reserve		**(200)**	(362)	(455)
Cash flow hedge reserve		**(515)**	(12)	82
Other reserves		**6**	(2)	(1)
Total equity attributable to equity holders of the Parent		**6,249**	6,623	6,492
Non-controlling interests		**173**	40	42
Total equity		**6,422**	6,663	6,534

The accompanying notes form part of these interim financial statements.

STATEMENT OF CHANGES IN EQUITY

FOR THE SIX MONTHS ENDED 31 JANUARY 2015

	ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT							
GROUP $ MILLION	SUBSCRIBED EQUITY	RETAINED EARNINGS	FOREIGN CURRENCY TRANSLATION RESERVE	CASH FLOW HEDGE RESERVE	OTHER RESERVES	TOTAL	NON-CONTROLLING INTERESTS	TOTAL EQUITY
As at 1 August 2014	**5,807**	**1,059**	**(455)**	**82**	**(1)**	**6,492**	**42**	**6,534**
Profit after tax	–	165	–	–	–	165	18	183
Other comprehensive income/(expense)	–	7	255	(597)	7	(328)	8	(320)
Total comprehensive income/(expense)	–	172	255	(597)	7	(163)	26	(137)
Transactions with equity holders in their capacity as equity holders:								
Dividend paid to equity holders of the Parent	–	(80)	–	–	–	(80)	–	(80)
Acquisition of subsidiaries	–	–	–	–	–	–	120	120
Dividend paid to non-controlling interests	–	–	–	–	–	–	(15)	(15)
As at 31 January 2015 (unaudited)	**5,807**	**1,151**	**(200)**	**(515)**	**6**	**6,249**	**173**	**6,422**
As at 1 August 2013	5,807	1,249	(266)	(82)	–	6,708	40	6,748
Profit after tax	–	206	–	–	–	206	11	217
Other comprehensive (expense)/income	–	(7)	(96)	70	(2)	(35)	(2)	(37)
Total comprehensive income/(expense)	–	199	(96)	70	(2)	171	9	180
Transactions with equity holders in their capacity as equity holders:								
Dividend paid to equity holders of the Parent	–	(256)	–	–	–	(256)	–	(256)
Dividend paid to non-controlling interests	–	–	–	–	–	–	(9)	(9)
As at 31 January 2014 (unaudited)	5,807	1,192	(362)	(12)	(2)	6,623	40	6,663
As at 1 August 2013	5,807	1,249	(266)	(82)	–	6,708	40	6,748
Profit after tax	–	157	–	–	–	157	22	179
Other comprehensive (expense)/income	–	(11)	(189)	164	(1)	(37)	(4)	(41)
Total comprehensive income/(expense)	–	146	(189)	164	(1)	120	18	138
Transactions with equity holders in their capacity as equity holders:								
Dividend paid to equity holders of the Parent	–	(336)	–	–	–	(336)	–	(336)
Dividend paid to non-controlling interests	–	–	–	–	–	–	(16)	(16)
As at 31 July 2014 (audited)	5,807	1,059	(455)	82	(1)	6,492	42	6,534

The accompanying notes form part of these interim financial statements.

CASH FLOW STATEMENT

FOR THE SIX MONTHS ENDED 31 JANUARY 2015

	GROUP $ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Cash flows from operating activities			
Profit before net finance costs and tax	**483**	416	503
Adjustments for:			
Foreign exchange losses/(gains)	**5**	(1)	11
Depreciation and amortisation	**283**	273	538
Movement in provisions	**80**	313	132
Other	**(140)**	(62)	(41)
	228	523	640
(Increase)/decrease in working capital:			
Inventories	**(1,012)**	(3,853)	(757)
Trade and other receivables	**40**	(729)	(111)
Amounts owing to suppliers	**(793)**	3,505	1,060
Payables and accruals	**95**	176	111
Other movements	**(23)**	(24)	(28)
Total	**(1,693)**	(925)	275
Cash generated from operations	**(982)**	14	1,418
Net taxes paid	**(32)**	(33)	(51)
Net cash flows from operating activities	**(1,014)**	(19)	1,367
Cash flows from investing activities			
Cash was provided from:			
– Proceeds from sale of business operations	**62**	11	46
– Proceeds from disposal of property, plant and equipment	**5**	5	12
– Other cash inflows	**54**	–	21
Cash was applied to:			
– Acquisition of business operations	**(162)**	(18)	(18)
– Acquisition of available-for-sale investments	**–**	(78)	(78)
– Acquisition of property, plant and equipment	**(584)**	(394)	(791)
– Acquisition of intangible assets	**(54)**	(47)	(102)
– Other cash outflows	**(68)**	(1)	(99)
Net cash flows from investing activities	**(747)**	(522)	(1,009)
Cash flows from financing activities			
Cash was provided from:			
– Proceeds from borrowings	**3,120**	2,093	4,241
– Proceeds from settlement of borrowing derivatives	**35**	4	–
– Interest received	**3**	7	13
– Other cash inflows	**–**	2	8
Cash was applied to:			
– Interest paid	**(262)**	(154)	(332)
– Repayment of borrowings	**(1,098)**	(638)	(3,894)
– Settlement of borrowing derivatives	**(36)**	(10)	(24)
– Dividends paid to non-controlling interests	**(15)**	(9)	(16)
– Dividends paid to equity holders of the Parent	**(80)**	(256)	(336)
Net cash flows from financing activities	**1,667**	1,039	(340)
Net (decrease)/increase in cash and cash equivalents	**(94)**	498	18
Cash and cash equivalents at the beginning of the period	**319**	329	329
Effect of exchange rate changes on cash balances	**28**	(18)	(28)
Cash and cash equivalents at the end of the period	**253**	809	319
Reconciliation of closing cash balances to the statement of financial position:			
Cash and cash equivalents	**266**	812	340
Bank overdraft	**(13)**	(3)	(21)
Closing cash balances	**253**	809	319

The accompanying notes form part of these interim financial statements.

CONDENSED STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

FOR THE SIX MONTHS ENDED 31 JANUARY 2015

a) General information

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

These consolidated interim financial statements of Fonterra, as at and for the six months ending 31 January 2015, comprise Fonterra and its subsidiaries (together the Group) and the Group's interest in its equity accounted investees.

The Group is primarily involved in the collection, manufacture and sale of milk and milk derived products and is a profit-oriented entity.

b) Basis of preparation

These consolidated interim financial statements comply with New Zealand Generally Accepted Accounting Practice (NZ GAAP). They have been prepared in accordance with New Zealand Equivalent to International Accounting Standard 34: Interim Financial Reporting and International Accounting Standard 34: Interim Financial Reporting. They should be read in conjunction with the consolidated financial statements for the year ended 31 July 2014.

These consolidated interim financial statements are presented in New Zealand dollars ($), which is the Company's functional currency. All financial information has been rounded to the nearest million, except where otherwise stated.

Interim income tax is calculated based on the best estimate of the full year effective tax rate taking into account profit before tax, the tax effect of distributions to farmer shareholders and the impact of recognition and de-recognition of deferred tax.

The preparation of interim financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates. In preparing these consolidated interim financial statements the significant judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty were the same as those applied to the consolidated financial statements for the year ended 31 July 2014.

c) Comparative figures

Where a change in the presentational format of the financial statements has been made during the period, comparative figures have been restated accordingly. Where material, additional disclosure has been provided in the notes to these consolidated interim financial statements.

d) Accounting policies

The same accounting policies are followed in these consolidated interim financial statements as were applied in the Group's financial statements for the year ended 31 July 2014.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE SIX MONTHS ENDED 31 JANUARY 2015

1 COST OF GOODS SOLD

	GROUP $ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Opening inventory	**3,701**	3,078	3,078
Cost of Milk:			
– New Zealand sourced	**5,057**	9,519	13,226
– Non-New Zealand sourced	**617**	714	1,192
Other purchases	**3,470**	3,191	6,018
Closing inventory	**(4,651)**	(6,617)	(3,701)
Total cost of goods sold	**8,194**	9,885	19,813

2 SEGMENT REPORTING

The Group operates predominantly in the international dairy industry.

a) Operating segments

The Group has five reportable segments that reflect the Group's management and reporting structure as viewed by the Fonterra Management Team, which is the Group's chief operating decision maker.

During the year ended 31 July 2014, transactions between segments were based on estimated market prices adjusted for the difference between the Farmgate Milk Price calculated in accordance with the Farmgate Milk Price Manual and that determined by the Board. During the six months ended 31 January 2015, transactions between segments were based on estimated market prices.

REPORTABLE SEGMENT	DESCRIPTION
Global Ingredients and Operations (formerly New Zealand Milk Products (NZMP))	Represents the collection, processing and distribution of New Zealand milk, global sales and marketing of New Zealand and non-New Zealand milk products (including North Asia), Global Brands and Nutrition, Co-operative Affairs and Group Services.
Oceania	Represents Fast Moving Consumer Goods (FMCG) businesses in New Zealand (including export to the Pacific Islands) and all FMCG and ingredients businesses in Australia (including Milk Supply and Manufacturing). It includes foodservice sales in Australia and New Zealand, and Farm Source stores.
Asia	Represents FMCG and foodservice businesses in Asia (excluding North Asia and Greater China), Africa and the Middle East.
Greater China	Represents FMCG, foodservice and farming businesses in Greater China.
Latin America	Represents FMCG and ingredients businesses in South America and the Caribbean. It includes farming in South America.

From 1 August 2014, Greater China has been reported separately from Asia. In addition, Fonterra's organisational structure was realigned and as a result the Taiwanese ingredients business has moved out of Greater China into Global Ingredients and Operations.

Comparatives have been restated to reflect these changes.

2 SEGMENT REPORTING CONTINUED

	GROUP $ MILLION						
	GLOBAL INGREDIENTS AND OPERATIONS	OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	ELIMINATIONS	TOTAL GROUP
Segment income statement							
Six months ended 31 January 2015 (unaudited)							
External revenue	6,124	1,476	776	425	945	–	9,746
Inter-segment revenue	805	253	92	–	1	(1,151)	–
Revenue from sale of goods	6,929	1,729	868	425	946	(1,151)	9,746
Cost of goods sold	(6,230)	(1,474)	(646)	(311)	(676)	1,143	(8,194)
Segment gross profit	699	255	222	114	270	(8)	1,552
Selling and marketing expenses	(51)	(72)	(95)	(77)	(61)	–	(356)
Distribution expenses	(106)	(87)	(16)	(5)	(104)	–	(318)
Administrative and other operating expenses	(381)	(122)	(55)	(48)	(80)	23	(663)
Segment operating expenses	(538)	(281)	(166)	(130)	(245)	23	(1,337)
Net other operating income	40	18	1	6	146	(23)	188
Net foreign exchange gains/(losses)	55	(2)	1	–	(3)	–	51
Share of profit of equity accounted investees	25	3	–	–	1	–	29
Segment earnings before net finance costs and tax	281	(7)	58	(10)	169	(8)	483
Normalisation adjustments	22	–	–	–	(129)	–	(107)
Normalised segment earnings before net finance costs and tax	303	(7)	58	(10)	40	(8)	376
Normalisation adjustments							107
Finance income							20
Finance costs							(323)
Profit before tax							180
Profit before tax includes the following amounts:							
Depreciation	(166)	(33)	(5)	(7)	(17)	–	(228)
Amortisation	(40)	(13)	(1)	–	(1)	–	(55)
Normalisation adjustments consist of the following amounts:							
Net gain on Latin America strategic realignment[1]	–	–	–	–	(129)	–	(129)
Time value of options[2]	22	–	–	–	–	–	22
Total normalisation adjustments	22	–	–	–	(129)	–	(107)
Segment asset information:							
As at and for the six months ended 31 January 2015 (unaudited)							
Equity accounted investments	248	38	–	4	8	–	298
Capital expenditure	386	39	18	210	56	–	709

1 Of the $129 million normalisation adjustment, $141 million relates to other operating income, less $4 million to cost of goods sold and $8 million to other operating expense. Refer Note 7.

2 The $22 million normalisation adjustment relates to net foreign exchange losses.

2 SEGMENT REPORTING CONTINUED

a) Operating segments CONTINUED

	GROUP $ MILLION						
	GLOBAL INGREDIENTS AND OPERATIONS	OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	ELIMINATIONS	TOTAL GROUP
Segment income statement							
Six months ended 31 January 2014 (unaudited)							
External revenue	8,216	1,522	678	315	561	–	11,292
Inter-segment revenue	921	303	95	–	9	(1,328)	–
Revenue from sale of goods	9,137	1,825	773	315	570	(1,328)	11,292
Cost of goods sold	(8,514)	(1,481)	(584)	(230)	(422)	1,346	(9,885)
Segment gross profit	623	344	189	85	148	18	1,407
Selling and marketing expenses	(48)	(71)	(104)	(56)	(28)	–	(307)
Distribution expenses	(90)	(92)	(15)	(9)	(45)	–	(251)
Administrative and other operating expenses	(344)	(148)	(57)	(38)	(28)	14	(601)
Segment operating expenses	(482)	(311)	(176)	(103)	(101)	14	(1,159)
Net other operating income	53	11	2	32	14	(14)	98
Net foreign exchange gains/(losses)	35	–	(3)	–	–	–	32
Share of profit of equity accounted investees	26	2	–	–	10	–	38
Segment earnings before net finance costs and tax	255	46	12	14	71	18	416
Normalisation adjustments	(13)	–	–	–	–	–	(13)
Normalised segment earnings before net finance costs and tax	242	46	12	14	71	18	403
Normalisation adjustments							13
Finance income							7
Finance costs							(154)
Profit before tax							269
Profit before tax includes the following amounts:							
Depreciation	(165)	(37)	(4)	(4)	(14)	–	(224)
Amortisation	(37)	(10)	(2)	–	–	–	(49)
Normalisation adjustments consist of the following amounts:							
Time value of options	(13)	–	–	–	–	–	(13)
Total normalisation adjustments[1]	(13)	–	–	–	–	–	(13)
Segment asset information:							
As at and for the six months ended 31 January 2014 (unaudited)							
Equity accounted investments	221	33	–	–	191	–	445
Capital expenditure	252	56	11	80	18	–	417

1 The $13 million normalisation adjustment relates to net foreign exchange gains.

2 SEGMENT REPORTING CONTINUED

	GROUP $ MILLION						
	GLOBAL INGREDIENTS AND OPERATIONS	OCEANIA	ASIA	GREATER CHINA	LATIN AMERICA	ELIMINATIONS	TOTAL GROUP
Segment income statement							
Year ended 31 July 2014 (audited)							
External revenue	16,160	2,979	1,415	618	1,103	–	22,275
Inter-segment revenue	1,915	621	195	–	58	(2,789)	–
Revenue from sale of goods	18,075	3,600	1,610	618	1,161	(2,789)	22,275
Cost of goods sold	(17,032)	(3,017)	(1,224)	(436)	(894)	2,790	(19,813)
Segment gross profit	1,043	583	386	182	267	1	2,462
Selling and marketing expenses	(106)	(137)	(187)	(111)	(52)	–	(593)
Distribution expenses	(184)	(182)	(31)	(7)	(95)	–	(499)
Administrative and other operating expenses	(673)	(255)	(110)	(56)	(51)	27	(1,118)
Segment operating expenses	(963)	(574)	(328)	(174)	(198)	27	(2,210)
Net other operating income	96	18	4	22	26	(27)	139
Net foreign exchange gains/(losses)	50	(1)	(12)	–	2	–	39
Share of profit of equity accounted investees	54	5	–	–	14	–	73
Segment earnings before net finance costs and tax	280	31	50	30	111	1	503
Finance income							13
Finance costs							(379)
Profit before tax							137
Profit before tax includes the following amounts:							
Depreciation	(323)	(72)	(8)	(8)	(26)	–	(437)
Amortisation	(75)	(22)	(3)	–	(1)	–	(101)
Segment asset information:							
As at and for the year ended 31 July 2014 (audited)							
Equity accounted investments	218	36	–	–	134	–	388
Capital expenditure	602	93	32	121	44	–	892

2 SEGMENT REPORTING CONTINUED

b) Platforms

The Group also presents financial information that reflects Fonterra's strategic platforms. These strategic platforms are organised on a different basis than the Group's operating segments presented in section a) of this note. The basis of presentation is explained in the table below.

This information is presented for the first time in these interim financial statements. Comparative information is also presented. Fonterra considers this information is useful as it provides more clarity on the financial performance of the ingredients, consumer and foodservice, and international farming businesses.

PLATFORM	DESCRIPTION
Ingredients	Represents the Global Ingredients and Operations reportable segment, the ingredients businesses in Australia and South America, Farm Source stores and excludes the foodservice businesses in Asia and Greater China.
Consumer and foodservice	
– Oceania	Represents the Oceania reportable segment, excluding the ingredients business in Australia and Farm Source stores.
– Asia	Represents the Asia reportable segment and the Asia foodservice business reported in Global Ingredients and Operations.
– Greater China	Represents the Greater China reportable segment, excluding International Farming and including the foodservice business in Greater China reported in Global Ingredients and Operations.
– Latin America	Represents the Latin America reportable segment excluding the ingredients businesses in South America.
International Farming	Represents China farming operations.

	GROUP		
	VOLUME METRIC TONNE THOUSAND	SALES REVENUE $ MILLION	NORMALISED EBIT $ MILLION
Ingredients	**1,538**	**7,617**	**299**
Consumer and foodservice			
– Oceania	**310**	**1,043**	**10**
– Asia	**142**	**968**	**56**
– Greater China	**64**	**389**	**15**
– Latin America	**324**	**856**	**35**
	840	**3,256**	**116**
International Farming	**67**	**66**	**(27)**
Eliminations	**(256)**	**(1,193)**	**(12)**
31 January 2015 (unaudited)	**2,189**	**9,746**	**376**
Ingredients	1,543	9,900	292
Consumer and foodservice			
– Oceania	313	1,050	(5)
– Asia	137	886	20
– Greater China	47	295	14
– Latin America	165	440	65
	662	2,671	94
International Farming	34	37	2
Eliminations	(251)	(1,316)	15
31 January 2014 (unaudited)	1,988	11,292	403
Ingredients	3,052	19,559	354
Consumer and foodservice			
– Oceania	631	2,102	(24)
– Asia	274	1,811	51
– Greater China	92	560	8
– Latin America	328	848	94
	1,325	5,321	129
International Farming	100	103	21
Eliminations	(512)	(2,708)	(1)
31 July 2014 (audited)	3,965	22,275	503

2 SEGMENT REPORTING CONTINUED

c) Geographical revenue

	GROUP $ MILLION								
	EUROPE	CHINA	REST OF ASIA	AUSTRALIA	NEW ZEALAND	USA	LATIN AMERICA	REST OF WORLD	TOTAL GROUP
Geographical segment external revenue:									
Six months ended 31 January 2015 (unaudited)	**414**	**1,203**	**2,610**	**811**	**977**	**643**	**1,554**	**1,534**	**9,746**
Six months ended 31 January 2014 (unaudited)	584	3,149	2,755	847	1,054	609	1,038	1,256	11,292
Year ended 31 July 2014 (audited)	946	5,537	5,787	1,666	2,162	1,014	1,802	3,361	22,275

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

d) Non-current assets

	GROUP $ MILLION							
	GLOBAL INGREDIENTS AND OPERATIONS		OCEANIA		ASIA	GREATER CHINA	LATIN AMERICA	TOTAL GROUP
	NEW ZEALAND	REST OF WORLD	NEW ZEALAND	AUSTRALIA				
Geographical segment reportable non-current assets:								
As at 31 January 2015 (unaudited)	**4,421**	**447**	**1,388**	**993**	**766**	**724**	**1,124**	**9,863**
As at 31 January 2014 (unaudited)	4,201	365	1,377	1,051	714	330	512	8,550
As at 31 July 2014 (audited)	4,300	391	1,387	1,022	705	410	445	8,660

	GROUP $ MILLION		
	AS AT		
	31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Reconciliation of geographical segment non-current assets to total non-current assets:			
Geographical segment non-current assets	**9,863**	8,550	8,660
Deferred tax assets	**555**	156	231
Derivative financial instruments	**335**	188	154
Total non-current assets	**10,753**	8,894	9,045

3 CONTINGENT LIABILITIES

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

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

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

In January 2014, Danone formally initiated legal proceedings against Fonterra in the High Court of New Zealand and separate arbitration proceedings against Fonterra in relation to the WPC80 precautionary recall. The New Zealand High Court proceedings have been stayed pending completion of the Singapore arbitration.

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

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

The Group has no other contingent liabilities as at 31 January 2015 (31 January 2014: nil; 31 July 2014: nil).

4 SUBSCRIBED EQUITY INSTRUMENTS

Subscribed equity instruments include Co-operative shares and units in the Fonterra Shareholders' Fund (the Fund).

Co-operative shares, including shares held within the Group

Co-operative shares may only be held by a shareholder supplying milk to the Company (farmer shareholder) and Fonterra Farmer Custodian Limited (the Custodian). Rights attaching to Co-operative shares include:

- voting rights when backed by milk supply[1];
- the right to receive the share-backed milk price on each kilogram of milk solids produced by the farmer shareholder[1];
- rights to any distributions declared by the Board; and
- rights to share in any surplus on liquidation of the Company.

As at 31 January 2015 there are 1,597,834,000 Co-operative shares on issue. No shares have been issued or surrendered in the six months to 31 January 2015.

Farmer shareholders

The Company maintains a Share Standard that requires a farmer shareholder to hold one Co-operative share[2] for each kilogram of milk solids supplied to the Company by that farmer shareholder. This is measured as an average over the three preceding seasons production (excluding milk supplied under contract supply in that season). Farmer shareholders are permitted to hold more or fewer Co-operative shares than required by the Share Standard in certain circumstances. Farmer shareholders supplying under contract must hold at least 1,000 Co-operative shares.

In addition to Co-operative shares held under the Share Standard, farmer shareholders are able to hold further Co-operative shares up to 100 per cent of production (where production is defined as the minimum number of Co-operative shares a farmer shareholder is required to hold under the Share Standard). No farmer shareholder (including its related parties) is allowed to hold interests in Co-operative shares, not backed by milk supply, exceeding five per cent of the total number of Co-operative shares on issue.

Farmer shareholders have a number of alternatives in meeting the requirements of the Share Standard[2]. These include purchasing the required shares over a three year period, along with other flexible arrangements provided by the Co-operative.

Voting rights in the Company are dependent on milk supply supported by Co-operative shares[1]. A farmer shareholder is entitled on a poll or postal vote, to one vote per 1,000 kilograms of milk solids if that farmer shareholder holds a Co-operative share[1] for each of those kilograms of milk solids. The amount of milk solids that support voting rights are measured at 31 May, the season end date[3]. As at 31 May 2014, the aggregate milk solids eligible for voting was 1,537,000,000 kilograms of milk solids (31 May 2013: 1,424,000,000 kilograms of milk solids).

Farmer shareholders are able to buy and sell Co-operative shares directly on the Fonterra Shareholders' Market. Shareholders may elect to sell the Economic Rights of some of their Co-operative shares to the Fund, subject to an individual limit set by the Board within an overall individual limit set out in the Company's constitution. On the sale of an Economic Right of a Co-operative share to the Fund, a farmer shareholder transfers the legal title to the Co-operative share to the Custodian. Where the Co-operative share transferred was backed by milk supply, the farmer shareholder is issued a voucher by the Custodian (subject to limits).

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

2 The Fonterra Board may permit the Share Standard to be satisfied through the holding of both Co-operative shares and vouchers.

3 Aggregate milk solids eligible for voting at season end date are adjusted for farmer shareholders who have joined the Company or are no longer supplying milk to the Company and for changes in the basis of supply of farmer shareholders in the period between the season end date and the record date for the meeting at which the vote is to be held.

The Custodian

The Custodian holds legal title of Co-operative shares of which the Economic Rights have been sold to the Fund on trust for the benefit of the Fund. At 31 January 2015, 121,855,834 Co-operative shares (31 January 2014: 106,414,814; 31 July 2014: 109,777,717) were legally owned by the Custodian, on trust for the benefit of the Fund.

4 SUBSCRIBED EQUITY INSTRUMENTS CONTINUED

	UNITS (THOUSANDS)
Balance at 1 August 2014	**109,778**
Units issued	**17,984**
Units surrendered	**(5,906)**
Balance at 31 January 2015 (unaudited)	**121,856**
Balance at 1 August 2013	107,969
Units issued	5,680
Units surrendered	(7,234)
Balance at 31 January 2014 (unaudited)	106,415
Balance at 1 August 2013	107,969
Units issued	13,116
Units surrendered	(11,307)
Balance at 31 July 2014 (audited)	109,778

Units are issued by the Fund. In respect of the Co-operative shares that it holds, the Custodian is required under trust to pass to the Fund the following rights of those Co-operative shares:

- the right to receive any dividends declared by the Fonterra Board;
- the right to any other distributions made in respect of Co-operative shares; and
- rights to share in any surplus on liquidation of Fonterra.

The Fund then attaches these rights to units it issues.

A farmer shareholder who holds a unit can require the Fund to effectively exchange it for a Co-operative share held by the Custodian. The Custodian relinquishes legal ownership of that Co-operative share (provided that completion of this transaction would not put that farmer shareholder in breach of the limits on Co-operative share ownership explained above). A unit is cancelled by the Fund, as all units in the Fund must be backed by a Co-operative share held by the Custodian.

Dividends paid

All Co-operative shares, including those held by the Custodian on trust for the benefit of the Fund, are eligible to receive a dividend if declared by the Board. On 23 September 2014, the Board declared a final dividend of 5.0 cents per share (totalling $80 million), paid on 20 October 2014 to all Co-operative shares on issue at 9 October 2014.

5 PROPERTY, PLANT AND EQUIPMENT

	GROUP $ MILLION		
	SIX MONTHS TO		YEAR ENDED
	31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Additions	**659**	370	788
Disposals	**(3)**	(5)	(14)
Capital commitments	**467**	324	362

6 EQUITY ACCOUNTED INVESTMENTS

The ownership interest of the following entities is 50 per cent or less and the Group is not considered to exercise a controlling interest. These entities are therefore accounted for as equity accounted investees.

		OWNERSHIP INTERESTS (%)		
		AS AT		
OVERSEAS EQUITY ACCOUNTED INVESTEES[1]	COUNTRY OF INCORPORATION[2]	**31 JAN 2015 UNAUDITED**	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
DMV Fonterra Excipients GmbH & Co KG	Germany	**50**	50	50
Dairy Industries (Jamaica) Limited	Jamaica	**50**	50	50
DairiConcepts, L.P.	USA	**50**	50	50
DairiConcepts Management, L.L.C.	USA	**50**	50	50
Dairy Partners Americas Brasil Limitada	Brazil	**–[3]**	50	50
Lacven Corporation	Barbados	**–[3]**	25	25

	OWNERSHIP INTERESTS (%)		
	AS AT		
NEW ZEALAND EQUITY ACCOUNTED INVESTEES	**31 JAN 2015 UNAUDITED**	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
International Nutritionals Limited	**50**	50	50

1 Overseas investees have balance dates of 31 December.

2 This is also the principal place of business.

3 On 1 August 2014, the Group purchased additional voting equity interests in DPA Brazil (Dairy Partners Americas Brasil Limitada) and DPA Venezuela (Lacven Corporation). These equity accounted investments became consolidated subsidiaries from that date. Please refer to Note 7 for further information.

7 BUSINESS COMBINATIONS

On 27 May 2014, the Group entered into agreements to realign the Latin America segment's Dairy Partners Americas (DPA) joint venture arrangements.

On 1 August 2014, the Group acquired additional voting shares in DPA Brazil (Dairy Partners Americas Brasil Limitada – from 50 per cent to 51 per cent, with Nestlé holding the balance) and DPA Venezuela (Lacven Corporation – 25 per cent to 60 per cent, with a local partner holding the balance). These equity accounted investments became consolidated subsidiaries from that date.

On 1 October 2014, the Group's equity accounted investments in Ecuador (Ecuajugos S.A.) and DPA's milk powder manufacturing business (DPA Manufacturing Holdings Limited) was sold to Nestlé.

Provisional business combination accounting based on the best information available at this interim reporting date is as follows.

The fair value of consideration transferred at the acquisition date is:

	GROUP $ MILLION		
	BRAZIL	**VENEZUELA**	**TOTAL**
Carrying value of existing interest	106	23	129
Gain/(loss) on remeasuring to fair value[1]	165	(6)	159
Fair value of existing interest	271	17	288
Cash paid	2	–	2
Fair value of consideration transferred	273	17	290
Represented by:			
Share of identifiable acquired net assets	97	41	138
Goodwill on acquisition	176	–	176
Gain on bargain purchase[2]	–	(24)	(24)
Total	273	17	290

1 The gain/(loss) on remeasuring the previous equity accounted interests is with reference to the fair value determined by independent experts.

2 Gain on bargain purchase arises on the consolidation of Venezuela into the Group. The business was no longer a strategic fit for another owner, and therefore the Group was able to negotiate a favourable purchase price for the additional 35 per cent.

7 BUSINESS COMBINATIONS CONTINUED

The cash inflow on acquisition is:

	GROUP $ MILLION		
	BRAZIL	VENEZUELA	TOTAL
Net cash acquired with subsidiary	9	17	26
Cash paid	(2)	–	(2)
Net consolidated inflow on acquisition	7	17	24

The contribution of the acquired entities to the Group's revenue and profit for the six months ended 31 January 2015 is:

	GROUP $ MILLION		
	BRAZIL	VENEZUELA	TOTAL
Revenue	268	173	441
Profit after tax	3	22	25

The Group has recorded a one-off gain relating to the business combinations, sale of equity accounted investments and the settlement of other relationships with the parties.

	GROUP $ MILLION			
	BRAZIL	VENEZUELA	OTHER	TOTAL
Fair value gain/(loss) revaluing existing interest	165	(6)	–	159
Foreign currency translation reserve transferred to income statement	(39)	(15)	(24)	(78)
Gain on bargain purchase	–	24	–	24
Gain on sale of equity accounted investment	–	–	5	5
Other items	–	–	19	19
Total gain[1]	126	3	–	129

1 The gain is included in other operating income ($141 million), cost of goods sold ($4 million expense) and other operating expenses ($8 million expense).

The fair values of the major classes of identifiable assets acquired and liabilities assumed at the acquisition date are:

	GROUP $ MILLION		
	BRAZIL	VENEZUELA	TOTAL
Trade and other receivables	159	64	223
Property, plant and equipment	111	83	194
Intangible assets	328	12	340
Other assets	115	59	174
Total assets	713	218	931
Trade and other payables	(119)	(95)	(214)
Borrowings	(193)	(37)	(230)
Deferred tax liabilities	(112)	(6)	(118)
Other liabilities[1]	(101)	(10)	(111)
Total liabilities	(525)	(148)	(673)
Fair value of identifiable net assets	188	70	258

1 Provisions of $80 million have been recognised for contingencies relating to tax and legal matters arising in the normal course of business. The timing and amount of the future obligations are uncertain, as they are contingent on the outcome of a number of administrative and judicial proceedings. The amount recognised has been based on management's best estimate of the amount that will be required to settle the obligation. The outcome of most of the obligations is not expected to be determined within the next year and therefore the provisions are classified as non-current.

8 BORROWINGS

	GROUP $ MILLION		
	AS AT		
	31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Commercial paper	**504**	625	464
Bank loans	**1,874**	1,689	437
Finance leases	**178**	186	180
Capital notes	**35**	35	35
NZX listed bonds	**950**	947	948
Medium-term notes	**3,959**	2,591	2,834
Total borrowings	**7,500**	6,073	4,898

	GROUP $ MILLION		
	AS AT		
	31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Net interest bearing debt position			
Current borrowings	**2,660**	2,107	1,534
Non-current borrowings	**4,840**	3,966	3,364
Total borrowings	**7,500**	6,073	4,898
Cash and cash equivalents	**(266)**	(812)	(340)
Interest bearing advances included in other non-current assets	**(56)**	(113)	(81)
Bank overdraft	**13**	3	21
Net interest bearing debt	**7,191**	5,151	4,498
Value of derivatives used to manage changes in hedged risks and other foreign exchange movements on debt	**(57)**	219	234
Economic net interest bearing debt[1]	**7,134**	5,370	4,732

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

	GROUP		
	AS AT		
	31 JAN 2015 UNAUDITED	31 JAN 2014 UNAUDITED	31 JUL 2014 AUDITED
Net tangible assets per security[1]			
$ per listed debt security on issue	**2.91**	3.67	3.55
$ per equity instruments on issue	**1.92**	2.42	2.34
Listed debt securities on issue (million)	**1,053**	1,053	1,053
Equity instruments on issue (million)	**1,598**	1,598	1,598

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

9 FAIR VALUE

Valuation techniques for determining fair values

The fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The fair values of financial assets and liabilities are calculated by reference to quoted market prices where that is possible. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis.

If quoted market prices are not available, the methodology used to calculate the fair values of financial assets and liabilities is to identify the expected cash flows under the terms of each specific contract and then discount these values back to the present value. These models use as their basis independently sourced market data where it is available and rely as little as possible on entity-specific estimates.

The calculation of the fair value of financial instruments reflects the impact of credit risk where appropriate.

Specific valuation techniques used to value financial instruments include:

- The fair value of forward foreign exchange contracts is determined using observable currency exchange rates, option volatilities and interest rate yield curves;
- The fair value of interest rate contracts is calculated as the present value of the estimated future cash flows based on observable interest rate yield curves;
- The fair value of commodity contracts that are not exchange traded is determined by calculating the present value of estimated future cash flows based on observable quoted prices for similar instruments; and
- The fair value of borrowings and long term advances that are not exchange traded is calculated as the present value of the estimated future cash flows based on observable interest rate yield curves.

The carrying amount of the financial instruments held by the Group as at 31 January 2015 is a reasonable approximation of fair value, except for the items set out in the table below:

	GROUP $ MILLION	
	AS AT 31 JAN 2015 UNAUDITED	
	CARRYING VALUE	FAIR VALUE
Financial liabilities:		
Finance leases	(178)	(200)
NZX listed bonds	(950)	(945)
Medium-term notes	(3,959)	(4,248)

Fair value hierarchy

All financial instruments for which a fair value is recognised are categorised within level 1 or level 2 of the fair value hierarchy. The fair value of the Group's livestock is categorised within level 3. These categories are described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Inputs other than quoted prices included within level 1 that are observable for the asset or liability either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- Level 3: Inputs for the assets or liabilities that are not based on observable market data (unobservable inputs).

9 FAIR VALUE CONTINUED

The following table shows the fair value hierarchy for items that are measured at fair value on the statement of financial position:

	GROUP $ MILLION		
	AS AT 31 JAN 2015 UNAUDITED		
	LEVEL 1	LEVEL 2	LEVEL 3
Derivative assets			
– Commodity derivatives	19	1	–
– Foreign exchange derivatives	–	244	–
– Interest rate derivatives	–	336	–
Derivative liabilities			
– Commodity derivatives	(5)	(5)	–
– Foreign exchange derivatives	–	(1,019)	–
– Interest rate derivatives[1]	–	(436)	–
Available-for-sale investments	75	1	–
Livestock	–	–	264
Fair value	89	(878)	264

1 Includes cross currency interest rate swaps.

10 SUBSEQUENT EVENTS

On 24 March 2015, the Board declared an interim dividend of 10.0 cents per share, to be paid on 20 April 2015 to all Co-operative shares on issue at 10 April 2015. Fonterra has announced a Dividend Reinvestment Plan, where eligible shareholders can choose to reinvest all or part of their future dividend in additional Co-operative shares. The Dividend Reinvestment Plan will apply to this interim dividend. Full details of the Dividend Reinvestment Plan are available on the financial section of Fonterra's website.

On 16 March 2015, Fonterra acquired an 18.8 per cent shareholding in Beingmate Baby & Child Food Co., Ltd. (Beingmate) for cash consideration of $756 million. Beingmate is an infant formula business in the People's Republic of China, listed on the Shenzhen stock exchange.

There were no other material events subsequent to 31 January 2015 that would impact these interim financial statements.

NON-GAAP MEASURES

Fonterra uses several non-GAAP measures when discussing financial performance. For further details and definitions of non-GAAP measures used by Fonterra, refer to the Glossary on page 54. These are non-GAAP measures and are not prepared in accordance with NZ IFRS.

Management believes that these measures provide useful information as they provide valuable insight on the underlying performance of the business. They may be used internally to evaluate the underlying performance of business units and to analyse trends. These measures are not uniformly defined or utilised by all companies. Accordingly, these measures may not be comparable with similarly titled measures used by other companies. Non-GAAP financial measures should not be viewed in isolation nor considered as a substitute for measures reported in accordance with NZ IFRS.

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

Reconciliation from the NZ IFRS measure of profit after tax to Fonterra's normalised EBITDA

	GROUP $ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2015	31 JAN 2014	31 JUL 2014
Profit after tax	**183**	217	179
Add: Depreciation	**228**	224	437
Add: Amortisation	**55**	49	101
Add: Net finance costs	**303**	147	366
(Less)/add: Tax (credit)/expense	**(3)**	52	(42)
Total EBITDA	**766**	689	1,041
Less: Net gain on Latin America strategic realignment	**(129)**	–	–
Add/(less): Loss/(gain) on time value of options	**22**	(13)	–
Total normalisation adjustments	**(107)**	(13)	–
Normalised EBITDA	**659**	676	1,041

Reconciliation from the NZ IFRS measure of profit after tax to Fonterra's normalised EBIT

	GROUP $ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2015	31 JAN 2014	31 JUL 2014
Profit after tax	**183**	217	179
Add: Net finance costs	**303**	147	366
(Less)/add: Tax (credit)/expense	**(3)**	52	(42)
Total EBIT	**483**	416	503
Less: Normalisation adjustments (as detailed above)	**(107)**	(13)	–
Normalised EBIT	**376**	403	503

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

	GROUP $ MILLION		
	SIX MONTHS ENDED		YEAR ENDED
	31 JAN 2015	31 JAN 2014	31 JUL 2014
Profit after tax	**183**	217	179
Less: Normalisation adjustments (as detailed above)	**(107)**	(13)	–
(Less)/add: Tax on normalisation adjustments	**(6)**	4	–
Total normalised earnings	**70**	208	179
Less: Share attributable to non-controlling interests	**(18)**	(11)	(22)
Net normalised earnings attributable to equity holders of the Parent	**52**	197	157
Weighted average number of shares (thousands of shares)	**1,597,834**	1,597,834	1,597,834
Normalised earnings per share ($)	**0.03**	0.12	0.10

GLOSSARY

NON-GAAP MEASURES

Fonterra refers to non-GAAP financial measures throughout the Interim Report, and these measures are not prepared in accordance with NZ IFRS. The definitions below explain how Fonterra calculates the non-GAAP measures referred to throughout the Interim Report.

Constant currency	means a measure that eliminates the effect of exchange rate movements. Constant currency variances are calculated by taking the current period financial measure in local currency less the prior period financial measure in local currency and dividing this by prior period financial measure in local currency using the prior period local currency to the New Zealand Dollar exchange rate.
Contribution margin	is calculated as segmental gross profit less distribution, selling and marketing expenses.
EBIT	means earnings before interest and tax (EBIT) and is calculated as profit for the period before net finance costs and tax.
EBIT margin %	is calculated as EBIT divided by revenue.
EBITDA	means earnings before interest, tax, depreciation and amortisation and is calculated as profit for the period before net finance costs, tax, depreciation and amortisation.
Economic debt to debt plus equity ratio	is calculated as net interest bearing debt divided by net interest bearing debt plus equity. Net interest bearing debt includes the effect of debt hedging, and equity excludes the cash flow hedge reserve.
Farmgate Milk Price	means the price that Fonterra pays for milk supplied to it in New Zealand for a season. The season refers to the 12 month milk season of 1 June to 31 May.
Net tangible assets	means total assets less total liabilities less intangible assets.
Normalisation adjustments	means transactions that are unusual by nature and size. Excluding these transactions can assist users with forming a view of the underlying performance of the business. Unusual transactions by nature are the result of a specific event or set of circumstances that are outside the control of the business, or relate to the major acquisitions or disposals of an asset/group of assets or business. It may also include certain fair value movements created by required accounting treatments, in particular if they are non-cash movements, and will have no impact on profit over time. Unusual transactions by size are those that are unusually large in a particular accounting period. Unusually large is defined as greater than $30 million.
Normalised EBIT	means profit for the period before net finance costs, tax and normalisation adjustments.
Normalised EBIT margin %	means Normalised EBIT divided by revenue.
Normalised EBITDA	means profit for the period before net finance costs, tax, depreciation, amortisation and normalisation adjustments.
Normalised segment earnings	means segmental profit for the period before net finance costs, depreciation, amortisation, tax and normalisation adjustments.
Payout	means the total cash payment to farmer shareholders. It is the sum of the Farmgate Milk Price (kgMS) and the dividend per share. Both of these components have established policies and procedures in place on how these are determined.
Segment earnings	means segmental profit for the period before net finance costs, tax and normalisation adjustments.

OTHER

Powder Products	means the commodity dairy products used in the calculation of the Farmgate Milk Price, which are currently Whole Milk Powder, Skim Milk Powder, Butter Milk Powder, Butter and Anhydrous Milk Fat.
Non-powder Products	means all other commodity dairy products.

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