OUR TIME...

Dairy for life

FONTERRA ANNUAL REVIEW 2011
FONTERRA CO-OPERATIVE GROUP LIMITED

HERE AT HOME...

& AROUND THE WORLD...

CONTENTS

DAIRY IS IN A SWEET SPOT.

DAIRY IN PHARMACEUTICALS

Lactose carries the active ingredients in medicinal inhalers and tablets. We lead the world in its supply.

AGEING POPULATIONS

The over-65 population will triple by 2050. We support healthy ageing with calcium-rich Anlene™ improving bone health and specialised dairy proteins providing quality, easily-digested nutrition.

POPULATION GROWTH

Global food demand will double by 2050. Dairy offers considerable nutritional quality and we're in key growth markets with trusted brands to meet rising demand.

THE 'ASIAN CENTURY'

Asia's growing economic wealth fuels demand for dairy. We are a trusted source of dairy nutrition in Asia, and China is now our leading market for dairy ingredients.

RISING CONSUMER INCOMES

A fast-growing Asian middle class wants to provide the best nutrition for everyone in the family. We are there with healthy, proven products suited to all of life's stages and ages.

BUSY LIFESTYLES

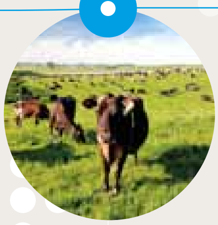
Convenience doesn't mean compromise. We work with many of the world's top foodservice businesses to bring healthy and handy options for time-short consumers.

HEALTHIER NUTRITION

Dairy has always been good. We make it even better through science, with dairy probiotics to support healthy digestive and immune systems, and dairy proteins to support weight loss and good nutrition.

CHANGING DIETS

Around the world, we turn consumer trends into market opportunities with new products tailored to busier lifestyles, broadening dietary choices and emerging health concerns.



FOOD QUALITY

New Zealand's pasture-based farms are the start of a quality chain which extends to our customers' doors and into consumers' homes. We set ourselves the highest standards of food quality.

REVENUE

$19.9b ▲19%

PROFIT

$771m ▲13%

DIVIDEND
PER SHARE

30c ▲11%

PAYOUT
BEFORE RETENTIONS

$8.25 ▲23%

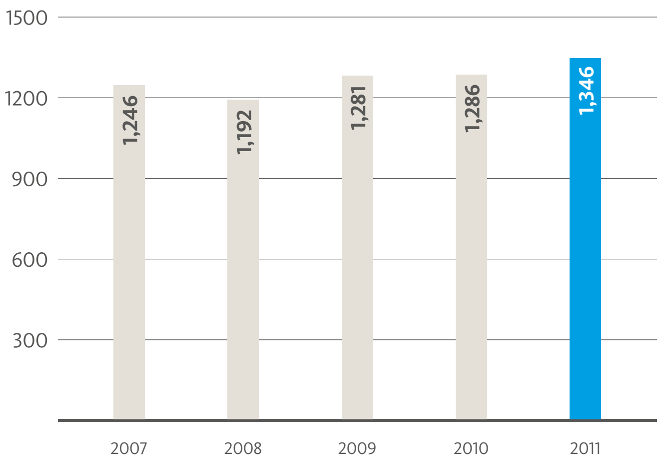
FARMGATE MILK PRICE
PER kgMS

$7.60 ▲25%

DISTRIBUTABLE PROFIT
PER SHARE

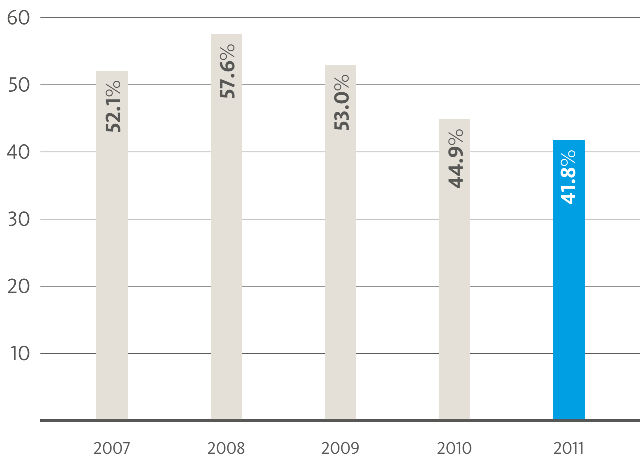
65c ▲8%

TOTAL NZ MILKSOLIDS COLLECTED[1, 2]
MILLION kgMS



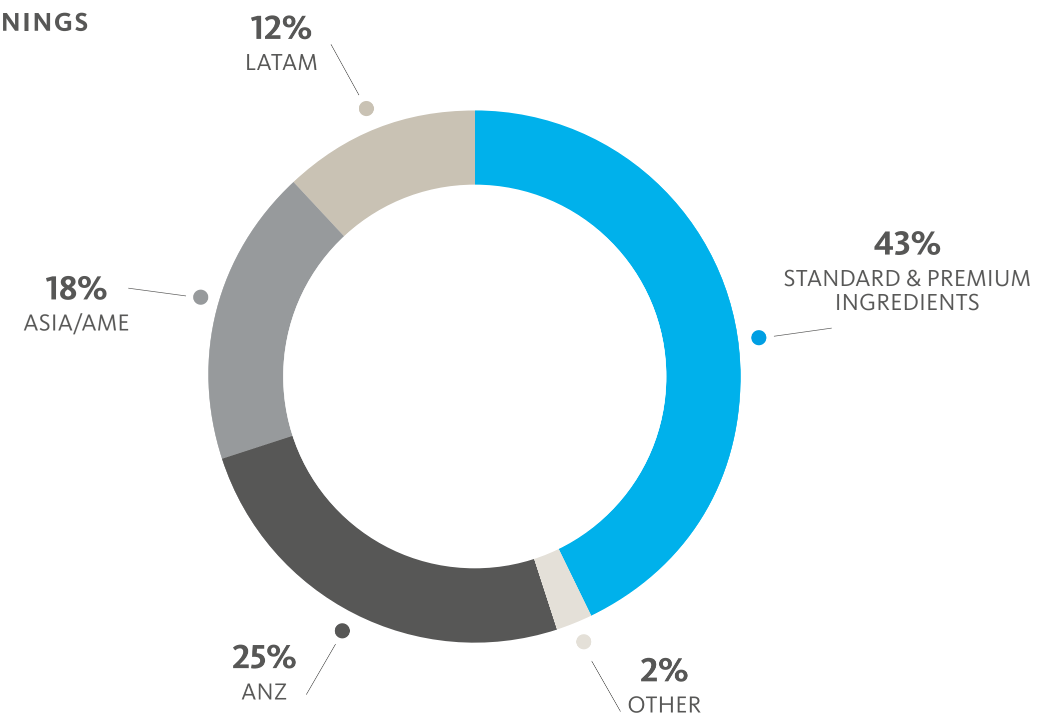
1. NZ milk collected for 12 month milk season of 1 June to 31 May.
2. 2008 affected by drought.

GEARING[1]
PERCENTAGE

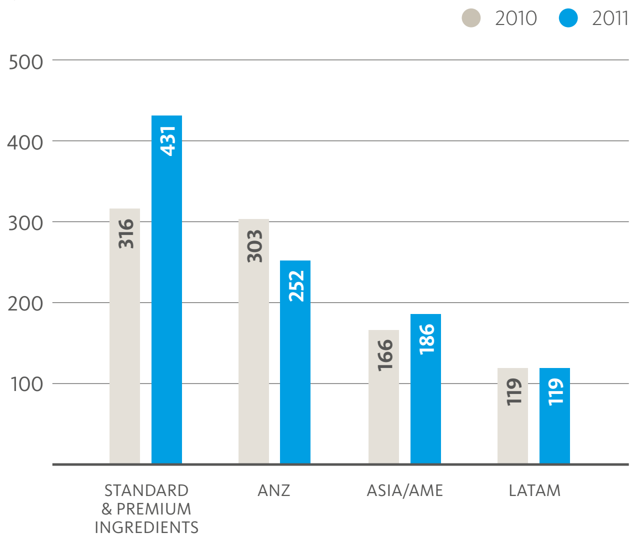


1. Gearing is measured as economic net interest bearing debt over economic net interest bearing debt plus equity (reflecting the effect of debt hedging in place at balance date). Equity excludes the cash flow hedge reserve.

SHARE OF EARNINGS
2011

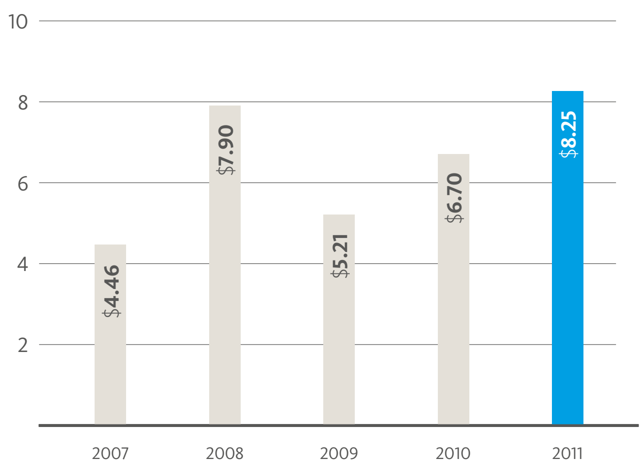


SEGMENT EARNINGS[1]
$ MILLION



1. Normalised segment earnings adjusted for non-recurring items, before impairment of equity accounted investees.

PAYOUT (BEFORE RETENTIONS)[1]
DOLLARS



1. Payout before retentions comprises the Farmgate Milk Price per kgMS for the season ended 31 May plus Distributable Profit. Distributable Profit is recognised on a dollar per share basis from the 2010 financial year. Prior to this Distributable Profit was recognised on a dollar per kgMS basis.

WE SET NEW BENCHMARKS FOR THE CO-OPERATIVE.

2011 was a year in which Fonterra set new benchmarks for the Co-operative and our Shareholders as we delivered on the mandate to be a national champion for New Zealand.

International dairy prices rose strongly for the second year running, underpinning record returns to our farmer Shareholders. Milk production in New Zealand also reached a new record, as some of the best autumn conditions in recent years offset poor weather in many regions earlier in the season.

This season, Fonterra will distribute record milk payments and dividends totalling $10.6 billion – $1.5 billion higher than our previous best. That money flows right back into the local economy as farmers reinvest in their businesses and buy more farm supplies and equipment.

2011 also marks Fonterra's 10th anniversary. Ten years ago, the New Zealand dairy industry came together to form a national champion. Our collective vision was to create a business with the scale to become a world leader in dairy ingredients and maximise dairying's contribution to the New Zealand economy.

That's exactly what Fonterra is doing. Today, we are the world's largest processor of dairy products. We invest actively in our business to achieve real efficiencies. We have effective and growing partnerships with many of the world's largest food and nutrition companies. We are helping to reshape the way dairy ingredients are traded globally. We own consumer brands businesses across key growth markets in Asia, Middle East and Latin America, as well as in Australia and New Zealand. We are at the forefront of breakthrough uses for dairy products in areas such as medical nutrition and pharmaceuticals. And while New Zealand dairying will always be our top priority, more than a quarter of our milk supply is now sourced and processed overseas.

Returns flow to our farmers by paying them a price for the milk they supply based on our Milk Price Principles, plus a dividend on the earnings Fonterra achieves. Those earnings come from processing milk as efficiently as possible and looking for the best ways to add value to it, as well as from our consumer businesses and other dairy investments.

FARMER RETURNS & PROFIT PERFORMANCE

In 2011, Fonterra achieved a Payout (before retentions) of $8.25 for share-backed production, substantially ahead of the prior period's $6.70. This Payout comprised a Farmgate Milk Price of $7.60 per kilogram of milksolids (kgMS) and a Distributable Profit of 65 cents per share, from which a dividend of 30 cents per share is being paid.

The $7.60 per kgMS Farmgate Milk Price is our highest ever and is well up on last season's $6.10 per kgMS. Its strength reflects recent

SIR HENRY VAN DER HEYDEN CHAIRMAN

"International dairy prices rose strongly for the second year running, underpinning record returns to our farmer Shareholders."

world dairy markets, with prices in some categories reaching or nearing historical highs during the past year. In addition, our hedging policy shielded farmers from the full brunt of a stronger New Zealand dollar, especially over the latter stages of the year.

The Distributable Profit of 65 cents per share is also the highest ever achieved, ahead of the 60 cents per share achieved in 2010.

The dividend of 30 cents per share is 11 per cent higher than the prior year. As the annual dividend includes an interim dividend of 8 cents per share paid in April 2011, a final dividend of 22 cents per share will be paid on 20 October 2011. Based on the current Fair Value Share price of $4.52, the dividend yield is 6.6 per cent (6.0 per cent last year).

CAPITAL STRUCTURE

We have made significant progress towards implementation of important changes to Fonterra's capital structure that will strengthen the Co-operative and improve our ability to make long-term business and investment decisions. Under Trading Among Farmers, our Shareholders will buy and sell shares from one another through a farmer-only market, rather than via the Co-operative.

At the core of Trading Among Farmers is the need for Fonterra to remain a Co-operative with 100 per cent farmer control and ownership. That is non-negotiable. While members of the public will be able to own units in a Fund that will mirror the economic benefits of Fonterra shares, neither the Fund nor individual unitholders can ever own Fonterra shares and voting rights in the Co-operative will continue to be based on share-backed production.

In accordance with the mandate from our Shareholders, we are working towards implementing Trading Among Farmers by late calendar year 2012. Much of the technical work required to develop the farmer-only share trading platform has now been completed, but we await legislative changes being approved by Parliament. We are working constructively with the Government and anticipate that the necessary changes to legislation will be introduced by early next year.

INDUSTRY ISSUES

The Government has undertaken a review of Fonterra's Farmgate Milk Price. We acknowledge and respect the right of regulatory authorities to themselves confirm that the Farmgate Milk Price methodology is robust and appropriate. But we also note that calls to change this methodology have mostly come from some of our competitors who, given the opportunity, would want to pay New Zealand farmers a lower price for raw milk.

The reality is that competition is thriving in the New Zealand dairy market, with competitors making significant investments recently in new processing plants. Fonterra has continued with its own investments and efficiency improvements. We are performing well in this competitive environment – meaning some other processors are struggling to match the returns we are achieving for our Shareholders.

GOVERNANCE

Two of our Directors, Greg Gent and John Ballard, have advised the Board that they will be retiring at this year's Annual Meeting.

Greg is one of our founding Directors and has decided not to stand for re-election. Greg has been an influential leader of the New Zealand dairy industry for 18 years and as Chairman of Kiwi Dairies played a pivotal role in the formation of Fonterra. He has always been a passionate believer of the farmer co-operative and in the ability of Fonterra to be a world leader in dairy. On behalf of my fellow Directors, I would like to thank Greg for his outstanding contribution towards shaping the success of Fonterra today and into the future.

John was appointed as a Director in May 2006 and has made a valued contribution at Board and Committee level, especially with his global perspective and insights into consumer businesses. A new appointed Director will be announced in due course.

During the year, we took steps to enhance the governance of Fonterra. The Milk Price Panel had its first year of governance oversight around Fonterra's Farmgate Milk Price. The Panel comprises five members: two Fonterra appointed Directors (one of whom must be Chairman), one farmer-elected Director and two appropriately qualified persons nominated by the Fonterra Shareholders' Council. The current Council nominees are both independent and experienced company directors.

The Board approved a formal Disclosure Policy to improve the transparency and consistency of information disclosure by Fonterra. We have also made public our full Farmgate Milk Price Manual and other disclosures on how we calculate the Farmgate Milk Price.

CEO TRANSITION

In July, we announced the appointment of Theo Spierings to succeed Andrew Ferrier, effective 26 September 2011. Andrew indicated to the Board some time ago that he wanted to move on by the end of 2011, which gave us plenty of time to embark on a global search for a new CEO and achieve an orderly transition.

We are delighted to have attracted someone of Theo's calibre to lead Fonterra into its second decade. Theo led the Dutch farmer dairy co-operative, Royal Friesland Foods, into its merger with Campina in 2008. He brings 25 years of knowledge of the global dairy industry and a wealth of experience managing dairy businesses across Asia, Latin America, Middle East and Europe. Most importantly, he has an in-built respect for the farmer co-operative structure.

Over the past eight years, Andrew has led the way in transforming Fonterra from a brave vision to a thriving international success story. He has brought together the people of Fonterra into a world class team, working to a clear strategy and with a real shared sense of purpose. Andrew's contribution was recognised recently in two prestigious industry awards: Federated Farmers' Agribusiness Person of the Year for 2011, and a Distinguished Service Award from the New Zealand Institute of Food Science and Technology. Fonterra has never been in better shape and that is a lasting credit to Andrew's leadership. I know he leaves Fonterra with the heartfelt appreciation of Directors, his colleagues and all our farmer Shareholders.

CONCLUSION/OUTLOOK

In May 2011, we announced an opening forecast Farmgate Milk Price for the 2012 season of $6.75 per kgMS and a forecast Distributable Profit range of 40-50 cents per share.

The year ahead will not be without its challenges. Volatility remains a byword not only for dairy prices and the New Zealand dollar, but also for world financial markets and the entire global economy. As we have seen with recent turmoil in financial markets, the outlook for the global economic environment remains far from certain.

Although there are many factors beyond the control of Fonterra that may affect this year's Farmgate Milk Price and profit, the efforts of the last decade have put Fonterra in a great place. The opportunities for dairy across both emerging and developed markets are immense. We have a strong business footprint across these markets and a sound strategy to build on the best opportunities for future growth.

SIR HENRY VAN DER HEYDEN
CHAIRMAN

WE GET MORE VALUE OUT OF EVERY DROP OF MILK.

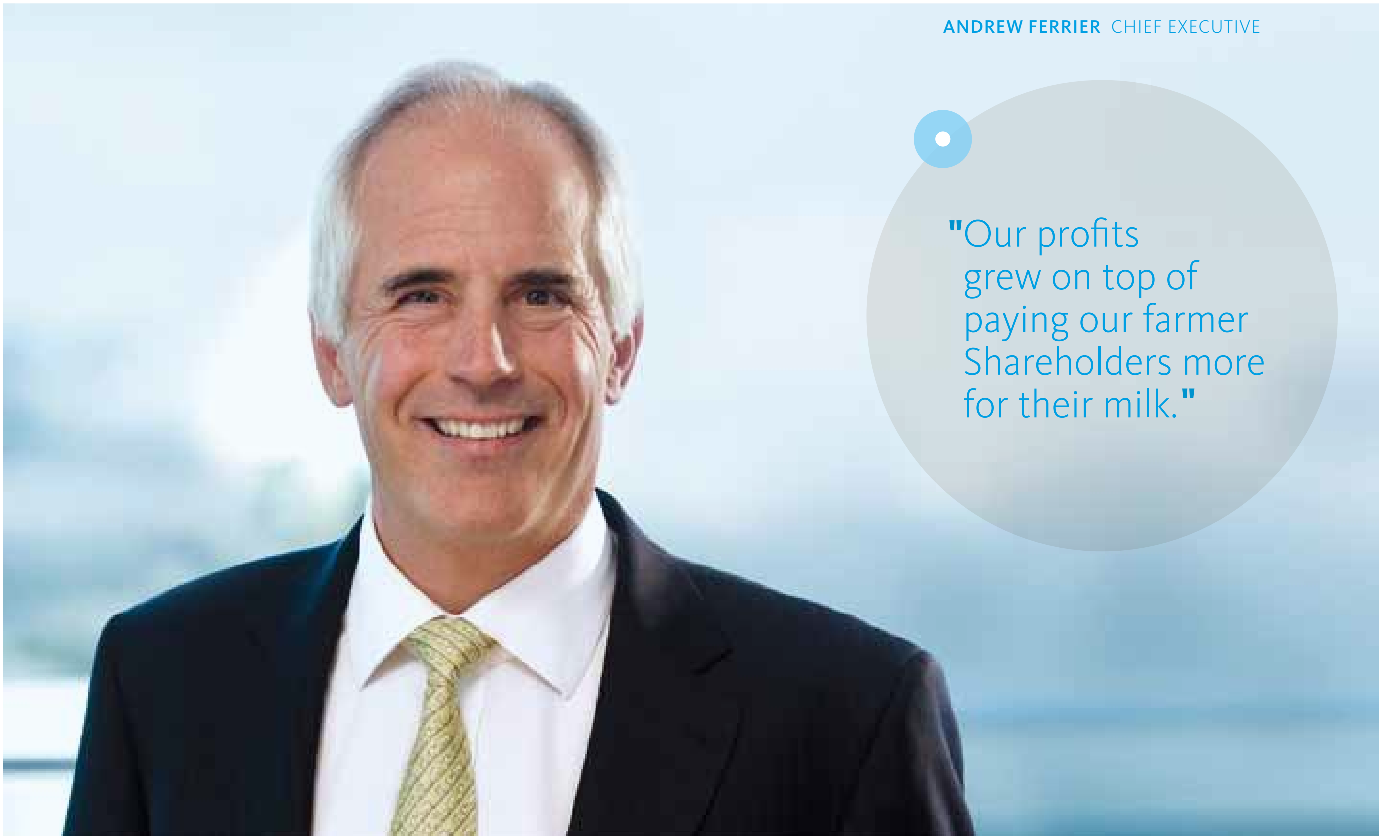
Fonterra's commitment to get more value from every drop of milk underpinned a positive year for our Shareholders:

- We posted record revenue of $19.9 billion
- We paid our highest ever Farmgate Milk Price of $7.60 per kilogram of milksolids (kgMS), despite the headwind of a stronger New Zealand dollar
- We achieved a net profit after tax of $771 million – a 13 per cent increase on the previous year, even after paying our farmers 29 per cent more for the milk they supplied last year. Similarly with last year's result, earnings benefited from some one-off gains
- Our balance sheet has further strengthened, with increased equity from farmers buying more shares and from retained earnings. Fonterra's economic gearing ratio was 41.8 per cent at 31 July 2011, compared with 44.9 per cent a year earlier.

The 2011 financial year was marked by the business impact of higher dairy ingredients prices and a fragile global economy. However, our normalised profitability showed solid growth over last year due to improved efficiencies within our ingredients businesses and the strength of our consumer brands. We continue to receive the distinction of being the world's largest milk processor.

Normalised earnings before net finance costs and tax from our Standard & Premium Ingredients (SPI) segment was 36 per cent higher than the previous year. This was despite the fact that, for the second year running, market prices for the standard dairy ingredients that feed into Fonterra's Farmgate Milk Price rose significantly.

Our consumer businesses faced a challenging year as margins came under pressure from the rise in commodity prices. Despite these challenges, in Asia, Africa and Middle East we had another good year of growth and normalised earnings before net finance costs and tax rose 12 per cent. We continue to focus on high-quality nutritional and foodservice solutions that leverage our trio of power brands – Anchor™, Anlene™ and Anmum™.



In our Latam segment, normalised earnings before net finance costs and tax was unchanged from the previous year, with both our Chilean business Soprole and the Dairy Partners America (DPA) joint venture performing solidly.

In ANZ, normalised earnings before net finance costs and tax fell 17 per cent. Margins were compressed as a fiercely competitive market environment in both Australia and New Zealand made it harder to fully reflect higher commodity costs in consumer pricing. Our market leadership positions across most categories mean we are in a sound position to work through the current market challenges.

HITTING THE SWEET SPOT FOR DAIRY

Any single year's financial performance should not be viewed in isolation. The bigger perspective is what we are doing to achieve quality growth in earnings and shareholder returns on a sustainable basis over the longer term.

We are shaping the business to capture the best opportunities for dairy in a fast-growing, fast-changing world. For example, around the world, more and more people are looking for nutritious food choices for themselves and their families – and more and more have the money to pay for them. They want the assurance of quality brands and increasingly are prepared to pay a premium for them.

> We are shaping the business to capture the best opportunities for dairy in a fast-growing, fast-changing world.

Things are also changing in the established markets. Busier lifestyles mean people want more convenient food options and products to help them manage their weight. Others are looking for healthier foods containing probiotics and other nutritional ingredients. An ageing population is increasing demand for specialised medical-nutrition products. All these needs and more can be fulfilled through emerging uses for specialised dairy ingredients.

Fonterra is in a great place to make the most of these trends. Our vision is to be the natural source of dairy nutrition for everybody, everywhere, every day.

INVESTING TO ACHIEVE REAL EFFICIENCIES

This all starts on every farm, even before the Fonterra milk tanker shows up. New Zealand is blessed with a climate perfect for turning the finest green grass into high-quality milk. That's a powerful competitive advantage for Fonterra, both financially and reputationally. But it's one we must work hard to preserve. That's why our efforts to ensure our farmers adopt best practice in sustainable dairying are so important.

Once that tanker enters our factory, our goal is to make a range of dairy products as efficiently as possible, that get the most value out of that milk. Although our manufacturing flexibility will always reflect the realities of factory capabilities and capacities, as well as commitments we have in place with long-term customers, even incremental improvements are aimed at better earnings over time. We are also continuing to manage our sales book, including the volume of product subject to fixed-price contracts, to better manage the impact of market volatility.

We have streamlined our supply chain through initiatives such as new warehousing hubs, greater use of rail and consolidated port operations to give us access to more frequent, flexible and reliable shipping operations.

RESHAPING THE WAY DAIRY INGREDIENTS ARE TRADED GLOBALLY

Back in Fonterra's earlier years, global dairy trading was not nearly as sophisticated as it is now. But since we launched online trading via the GlobalDairyTrade™ (GDT) platform in July 2008, international dairy pricing has become much more transparent and competitive. GDT has grown to offer seven product categories and in 2011 accounted for around a quarter of our dairy ingredients sales volumes. The platform has now been opened up to other dairy vendors, with DairyAmerica the first to join from October 2011.

As we have sold more standard ingredients via GDT, our sales teams have been freed up to focus more on premium ingredients – working to achieve better product margins and optimise our overall product mix.

EFFECTIVE AND GROWING CUSTOMER PARTNERSHIPS

Fonterra is well placed to be the dairy supply partner of choice for leading companies in the food and nutrition industries. We can offer them security of supply, technological leadership and an efficient global supply chain. The deeper we build these partnerships, the more opportunity we have to provide these customers with higher-value dairy solutions customised to their needs.

The increasing value of our customer partnerships was demonstrated by two key customer segments, Formulated Foods, and Foodservices, building on their $1 billion revenues in 2011.

> Fonterra is well placed to be the dairy supply partner of choice for leading companies in the food and nutrition industries.

AT THE FOREFRONT OF BREAKTHROUGH USES OF DAIRY

Our commitment to innovation, as one of the world's largest investors in dairy-based research, is also a driver of earnings growth. We are leading the way in areas such as new generation cheese technologies and the use of dairy proteins in sports bars and beverages, medical-nutrition, and weight management products. As well as leveraging innovations in high-value ingredient sales to customers, we seek to commercialise new technologies in products ourselves – such as cheese manufactured using our proprietary CHEDDAR*plus*™ ingredient at a leased plant in the United States, which in its first full year generated sales of around $50 million during 2011.

CONTINUING TO BUILD STRONG-PERFORMING CONSUMER BRANDS

This year, our consumer business represented 55 per cent of normalised earnings and over the past four years their profit growth has averaged 11.1 per cent annually. Increasingly, our focus is on growth markets within Asia, Middle East and Latin America, while maintaining our strong market positions in Australia and New Zealand.

We have highly talented people running these businesses who really know how to make the most out of brands. In key Asian markets, we are positioning our brands in response to specific concerns such as osteoporosis, pregnancy and childhood development. We have also invested significantly over recent years in advertising and promotion to make our brands resonate better with Asian consumers.

CHIEF EXECUTIVE'S REPORT CONTINUED

DEVELOPING THE CHINA OPPORTUNITY

No assessment of Asia can ignore China. In 2011, China ranked as our number one market for ingredients. And while our brands are relatively new to the China market, they have been growing quickly. We recognised early on that China is a market in massive transition, with a rapidly emerging middle class and expanding appetite for fresh dairy. However, local milk supply is not growing as fast as the market, is fragmented, and has had serious quality issues to confront over recent years. That creates opportunities for Fonterra and is why we are establishing our own farms and milk supply chain in China. During 2011, we confirmed plans for our second and third Chinese farms and outlined a vision to develop more farms to play a bigger role in the development of the Chinese dairy industry. The farms will give us the ability to source high quality local milk both for our customers and potentially over time for our own branded products.

MANAGING RISK, GENERATING VALUE

Good financial management is vitally important at Fonterra. Managing the costs and risks associated with the vast flows of money through the business can generate real value to Shareholders. Through increased equity from our farmer Shareholders, together with improved working capital and balance sheet management, we closed out the 2011 financial year with the strongest balance sheet in our history.

Our finance team's expertise was acknowledged when our Chief Financial Officer, Jonathan Mason, was named New Zealand CFO of the Year for 2011.

MOVING FORWARD

I made it clear to the Board some time ago that I thought that the end of 2011 was a good time to 'pass the baton' on to a new CEO. I have had 17 years as a CEO, including eight years at Fonterra, and I am looking forward to more flexibility in my life and choosing from a number of less strenuous business interests that are available to me.

I would not have missed a minute of the past eight years. I have truly developed 'milk in my veins' in my time at Fonterra. But I know with the Co-operative and the industry in good shape, this is the best time for the transition to a new CEO. My successor, Theo Spierings, will inherit a world-class team of dedicated men and women and a business poised for even greater success.

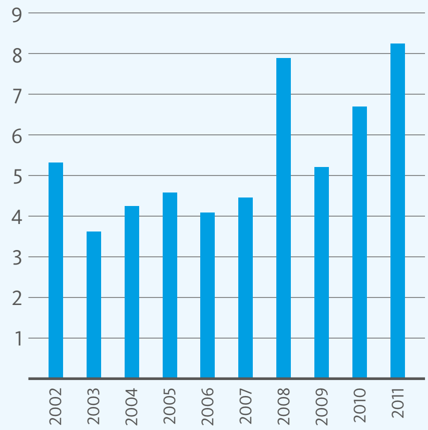
I sincerely thank all our farmer Shareholders for the support they have consistently given to my colleagues and me. It has been a privilege to work on your behalf.

ANDREW FERRIER
CHIEF EXECUTIVE

10 YEARS OF FONTERRA

FARMER RETURNS OVER 10 YEARS[1]

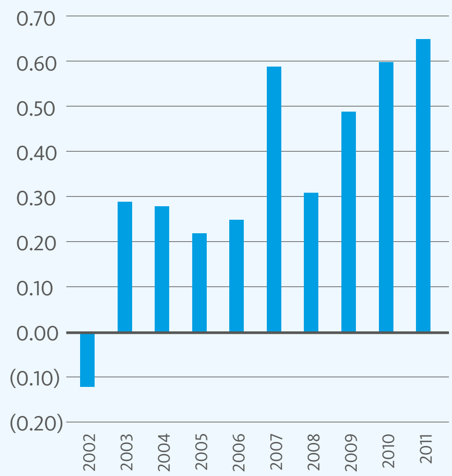
PAYOUT (BEFORE RETENTIONS) $



1. Payout before retentions comprises the Farmgate Milk Price per kgMS for the season ended 31 May plus Distributable Profit. Distributable Profit is recognised on a dollar per share basis from the 2010 financial year. Prior to this Distributable Profit was recognised on a dollar per kgMS basis.

VALUE RETURN / DISTRIBUTABLE PROFIT[1]

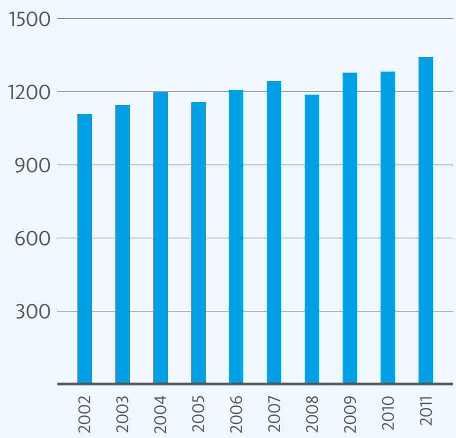
$ PER kgMS / SHARES



1. Distributable Profit is recognised on a dollar per share basis from the 2010 financial year. Prior to this Distributable Profit was recognised on a dollar per kgMS basis.

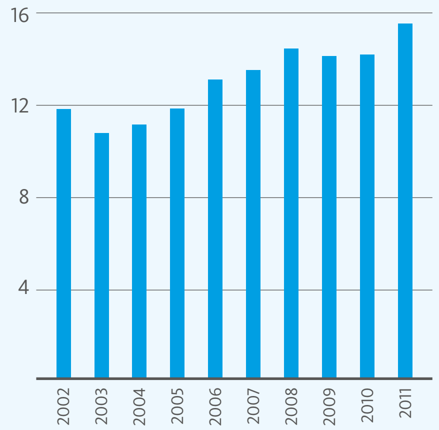
TOTAL NZ MILKSOLIDS COLLECTED[1]

MILLION kgMS



1. NZ milk collected for 12 month milk season of 1 June to 31 May.

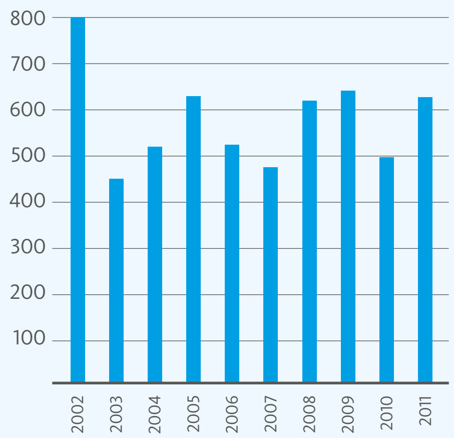
GROWTH OF BALANCE SHEET[1,2]
TOTAL ASSETS ($ BILLIONS)



1. Total assets for 2011, 2010, 2009 and 2008 are as at 31 July. Total assets for 2007, 2006, 2005, 2004, 2003 and 2002 are as at 31 May.

2. 2007-2011 figures are prepared under NZ IFRS, with 2002-2006 figures prepared under previous NZ GAAP.

CAPITAL INVESTED[1,2]
PP&E AND INTANGIBLE ASSET ADDITIONS ($ MILLIONS)



1. Property, plant and equipment (PP&E) and intangible asset additions represent cash additions for the period. On 24 January 2008 the Board resolved to change the Company's balance date to 31 July from 31 May, and therefore additions for 2008 are for the 14 month period to 31 July 2008.

2. 2007-2011 figures are prepared under NZ IFRS, with 2002-2006 figures prepared under previous NZ GAAP.

10

10 YEAR TIMELINE

2001

- New Zealand Dairy Board, New Zealand Dairy Group and Kiwi Co-operative Dairies combine to form Fonterra Co-operative Group in October.

2002

- Fonterra and Bonlac Foods form New Zealand Milk (Australasia), combining consumer operations in Australia. With a brand portfolio including Mainland, Tip Top, Bega, Perfect Italiano and Western Star, this set the stage for growth in the Australian dairy consumer market.

2003

- Fonterra Customer Service Centre in Auckland takes first calls in October. Its around-the-clock, and around-the-world service simplifies our customers dealings with us with a one stop shop for ordering.

2004

- Fonterra delivers full merger benefits ahead of schedule, with annualised savings of more than $310 million confirmed by Deloitte.

2006

- Fonterra acquires Kapiti Fine Foods business.
- DMV Fonterra Excipients joint venture formed.

2008

- Fonterra increases Soprole shareholding to 99.8 per cent.
- Fonterra launches world's first online trading platform for dairy commodities – GlobalDairyTrade™.
- Fonterra acquires Nestlé's dairy dessert business in Australia and the licence for Ski™ yoghurt brand.
- Fonterra begins developing a 35 hectare farm in China where dairy consumption is growing in excess of 10 per cent per annum.

2009

- World's biggest milk drier commissioned at Edendale – capable of producing one tonne of milk powder every two minutes.
- Fonterra's Anmum Materna™ becomes the leading maternal milk in five markets across Asia.
- Fonterra becomes supplier to all five of the world's largest infant formula companies.

2010

- Highest ever daily volume collected in one day – 76.8 million litres.
- Consumer businesses hit 65 per cent of Group's normalised earnings.
- Shareholders vote in favour of Trading Among Farmers capital structure changes.

2011

- Biggest ever milk payments and dividends totalling $10.6 billion.
- Record 1346 million kilograms of milksolids collected.

MAKING THE MOST OF EVERY DROP.

Our vision is to be the natural source of dairy nutrition for everybody, everywhere, every day. Our business is organised to do that. It all starts with collecting fresh milk – about 22 billion litres a year. Our sites work to extract every drop of value from it.

The quality of our dairy ingredients opens doors to many of the world's leading food companies. The quality of our brands opens doors to consumers' fridges and pantries in New Zealand, Australia, Asia, Africa, Middle East and Latin America. Our research and development opens more opportunities to make milk even better.

None of this would be possible without our people and our belief in doing what's right in the communities where we operate.

WE COLLECT IT

OUR BUSINESS STARTS WITH HIGH QUALITY MILK. MOST IS SOURCED IN NEW ZEALAND. WE WORK HARD TO BE FARMERS' PROCESSOR OF CHOICE.

Fonterra's business is founded on a secure, high quality source of milk. Most of that milk comes from New Zealand and we aim to be the processor of choice for New Zealand farmers.

With large international customers wanting the confidence of year-round global supply, we are increasingly looking to complement New Zealand-sourced milk with overseas supply.

In the 2011 season, Fonterra and its business partners sourced around 22 billion litres of milk globally. In New Zealand, we collected 15.4 billion litres, representing around 89 per cent of the country's milk production.

In Australia, we have been sourcing milk directly from farmers since 2005 and this season collected 1.8 billion litres, representing around 20 per cent of Australia's milk production.

In Chile, Fonterra-owned Soprole collected around 440 million litres of milk, representing about 24 per cent of Chile's milk production. Elsewhere in Latin America, our joint venture with Nestlé, Dairy Partners Americas, sourced about 2.6 billion litres of milk in the 12 months to 30 June 2011.

We also aim to develop our own milk production capabilities in key growth markets as we seek to play an active role in local dairy industry development. In China, we have one farm operational and two more in the pipeline, while in Brazil we have announced plans to develop a pilot farm. We continue to explore opportunities in other markets such as India.

WE PROCESS IT

SCALE, EFFICIENCY, FLEXIBILITY – THAT'S WHAT OUR MANUFACTURING OPERATIONS ARE ALL ABOUT. THAT WAY, WE'RE FAST TO RESPOND WHEN CUSTOMER NEEDS OR MARKET DYNAMICS CHANGE.

Fonterra's manufacturing operations combine world-class scale and efficiency with the flexibility needed to respond to customer needs and changing market dynamics.

In New Zealand, a fleet of 480 tankers delivers raw milk for processing at 76 plants across 26 sites. A large global team evaluates the market to decide exactly what mix of ingredients is made from month to month.

We continue to expand our New Zealand manufacturing capabilities to improve overall efficiency and ensure we have the capacity for growing milk supply. At an expected total capital investment of around $450 million over two stages, our first greenfields processing site in about 14 years is under development at Darfield, Canterbury.

A sophisticated international sales and marketing network is complemented by the GlobalDairyTrade™ online platform, which now accounts for around one-quarter of total ingredients sales. Our streamlined supply chain efficiently gets products to customers: every hour of the year, we close the doors on an average of 12 containers with over 90 per cent of them making their way across the equator to destinations far and wide.

In 2011, Fonterra traded approximately 2.5 million tonnes of dairy ingredients in world markets, of which around 2.1 million tonnes came from New Zealand.

In June 2011, the Germany-based International Farm Comparison Network ranked Fonterra as the world's largest milk processor.

WE SUPPLY IT TO WORLD-LEADING FOOD COMPANIES...

OUR DAIRY INGREDIENTS ARE THE FIRST CHOICE FOR MAJOR GLOBAL CUSTOMERS.

Fonterra is a supply partner to many of the world's leading food companies.

Our partnerships include global and regional agreements to supply basic dairy ingredients such as milk powder, cheese for burgers and pizzas, milk for lattes, and functional ingredients such as specialised proteins for sports and other nutritional beverages.

We partner with the five largest infant formula manufacturers in the world, providing semi- or fully-finished products, as well as including our specialised ingredients in their applications.

We supply the cream, butter and assorted dairy products used in around 45 countries by a myriad of bakery and confectionary chains, as well as by chefs in hotels and restaurants.

Our customer relationships are built around understanding how consumer lifestyles and attitudes are changing – and how this is likely to influence their appetite for dairy. These insights drive our product development and help ensure our own growth plans are aligned with those of our key customers.

...AND TO DISCERNING CONSUMERS

WE'RE BUILDING TRUSTED BRANDS IN OUR CHOSEN MARKETS, CREATING VALUE FOR OUR SHAREHOLDERS WITH EVERY SALE.

Fonterra's consumer businesses play a pivotal role in creating value for our Shareholders by building trusted brands in chosen markets.

Our fast-growing presence in Asia, Africa and Middle East, coupled with our strong businesses in Australia and New Zealand, are important to overall financial performance as well as representing a high-value channel for about 13 per cent of the New Zealand milk Fonterra collects and processes.

Across Asia, Africa and Middle East, consumers are increasingly focusing on health and wellness, and they consider milk to be a 'gold standard' for nutrition. Fonterra sells to consumers in 40 countries, with a growing portfolio of products based around the Anchor™, Anlene™ and Anmum™ brands. The Anchor™ brand proposition is trusted nutrition from New Zealand across a broad range of products. Calcium-rich Anlene™ stands for adult bone and joint health and Anmum™ represents nutrition for mothers and children.

In Australia and New Zealand, our brands hold number one or two positions in most dairy categories, including those such as yoghurts and dairy desserts which offer superior value and growth prospects.

In Chile, Soprole™ has around a quarter of the market for dairy products. During 2010, Soprole™ was named one of Chile's most respected brands by both the Marketing Hall of Fame and in an independent consumer poll. Fonterra also has a significant interest in consumer dairy across Brazil, Venezuela and Ecuador via our Dairy Partners Americas joint venture with Nestlé.

WE BRING FRESH THINKING TO MILK

DECADES OF RESEARCH AND DEVELOPMENT GIVE US THE EDGE IN INNOVATION.

Much of the respect that Fonterra enjoys around the world as a natural source of dairy nutrition can be traced back to decades of intensive research and development (R&D).

Our R&D headquarters is the Fonterra Research Centre, which has operated continuously in Palmerston North for over 85 years. The centre is supplemented by regional technical development centres in Melbourne, Amsterdam and Chicago.

Recent innovations now in commercial production with world-leading food companies include milk protein concentrates under brands such as Deluxe Protein™, Sure Protein™ and ClearProtein™, probiotic DR10™ in cultured goods and beverages, as well as low sodium cheese, CHEDDAR*plus*™ and the C21 accelerated cheese making technique.

Fonterra currently has over 600 patents and patent applications to protect our intellectual property.

In August 2010, Fonterra entered a broad research collaboration with the New Zealand Government and dairy industry partners. Fonterra is investing $47 million towards the seven year, $170 million programme and is leading post farmgate research in the areas of nutrition, food structure, and manufacturing and supply chain processes.

WE HARNESS THE TALENT OF OUR PEOPLE

WHEREVER THEY ARE IN THE WORLD AND WHATEVER JOB THEY DO, OUR PEOPLE SHARE A REAL PASSION FOR DAIRY.

Fonterra has one of the most diverse workforces of any New Zealand-based company in terms of skillsets, cultures and geographies. Almost 36 per cent of our 16,800 employees work overseas in more than 50 countries around the world.

For the past two years, Fonterra has measured employee engagement using an internationally recognised Gallup system. The second poll in 2011 showed an improvement in results, with an overall increase in the number of engaged employees. The push is now on to drive engagement right across the business.

We are also moving to the second phase of a health and safety programme which includes a clear focus on injury prevention. In 2011, the Total Recordable Injury Frequency Rate (TRIFR) was 14.8 per million work-hours, an improvement from 18.2 in the previous year. Since 2006, TRIFR has fallen by 82 per cent including a 38 per cent drop over the last three years.

We have established clear safety processes and enabling systems, and an independent review of our performance in 2010 acknowledged genuine progress. The next stage of our health and safety journey is based on achieving world-class standards across all aspects of our health and safety performance including increasing our global focus and strengthening initiatives targeted at preventing fatal and serious injury.

Fonterra won the Best Large Organisation Health and Safety Initiative category in the 2011 New Zealand Workplace Safety Awards, for a new tanker driver training programme which has led to a reduction in tanker mishaps. At the same awards, the Most Influential Employee category went to Fonterra's Greg Chaffey, from Mataura, Southland. A tanker driver and health and safety representative, Greg is actively involved in safety audits and first aid capabilities.

EVERY DAY, WE AIM TO GET THE BALANCE RIGHT...

SUSTAINABILITY IS IMPORTANT. WE AIM TO ACHIEVE THE RIGHT BALANCE BETWEEN ENVIRONMENTAL, ECONOMIC AND SOCIAL SUSTAINABILITY.

In New Zealand, Fonterra has implemented an energy efficiency programme since 2003.

This programme is based on conducting an 'energy blitz' on a selection of sites each year where projects and investments are identified and then implemented in order to reduce energy use.

In Australia, both energy efficiency and water efficiency are areas of focus. Fonterra Dennington has implemented a closed loop cooling water system for its refrigeration compressors. The upgrade saves as much as 240 megalitres of bore water a year, which is equivalent to 96 Olympic size swimming pools.

While over the past eight years great progress has been made within Fonterra's direct operations, Fonterra is now focusing on improving supplier environmental performance.

Since August 2010 Fonterra has appraised every New Zealand Shareholder's farm effluent management system identifying farms at risk of non-compliance with regional council rules. This resulted in development of 1380 Effluent Improvement Plans (EIP) by Fonterra Sustainability Advisors tailored for individual farmers. Of these, 763 have already been implemented.

Through the Primary Growth Partnership, Fonterra is partnering with DairyNZ and Government to develop and pilot an audited nutrient management system for testing with farmers in three pilot catchments around New Zealand.

Fonterra is extending the development of on-farm sustainability programmes to milk supply beyond New Zealand. The Fonterra Standard of Excellence (FSOE2) is applied as a minimum quality standard for milk across Fonterra's international supply base and suppliers are audited against this.

Sustainability for these operations, from farm to factory, is our current focus and an extended FSOE2 will be rolled out during the 2012 financial year to enable us to benchmark sustainability performance and identify areas for improvement.

We are continuing to work on reducing the carbon footprint of Fonterra's global operations. Fonterra has conducted a full lifecycle assessment of the carbon footprint of a series of our New Zealand products. This year Fonterra participated in a national study to calculate the carbon footprint of Australian dairy products. This will enhance our understanding of emissions in the Australian dairy system enabling targeted reduction programmes to be implemented.

We believe that with continued investment in research initiatives such as the Pastoral Greenhouse Gas Research Consortium, adoption of research outcomes by farmers, and initiatives such as ongoing achievements in our energy reduction programme, we can reduce the carbon footprint of each litre of milk sourced and processed in New Zealand by over 30 per cent by 2030.

...AND TO LOOK AFTER THE COMMUNITIES WHO SUPPORT US

CO-OPERATIVE SPIRIT IS ONE OF OUR VALUES. ONE OF THE WAYS WE LIVE IT IS BY HONOURING OUR LOCAL COMMUNITIES.

Fonterra aims to do what's right in the communities where we operate, recognising that a sustainable business must provide both financial and practical support to social initiatives.

As measured by the London Benchmarking Group, Fonterra's community contribution as a percentage of pre-tax profit is above the average of a benchmarked sample of around 200 companies internationally.

We partner with Sanitarium to run the KickStart Breakfast programme which provides more than 18,000 students at almost 500 schools nationwide with breakfast twice a week. The programme marked a milestone on 1 June 2011, serving its two millionth breakfast.

After the Canterbury earthquakes, we provided fresh water to Christchurch by rail and road tankers. Our emergency response team worked alongside international urban search and rescue personnel and we provided thousands of litres of milk to relief distribution centres. Fonterra, along with our Shareholders and staff, combined to contribute $5.9 million in financial support to Canterbury relief efforts.

Community support during 2011 also included donation of product to charities such as Auckland City Mission, Salvation Army and Australia's Foodbank, and financial donations to victims of the Japanese earthquake/tsunami and the floods in Queensland and Victoria, Australia.

Fonterra also invested more than $500,000 in New Zealand schools and communities through a competition that enabled Anchor™ milk drinkers to win cash for themselves and the school of their choice, with a top school prize of $50,000.

Beyond New Zealand, we are a strong supporter of programmes that reflect the importance of nutrition in health and development. Initiatives include partnering with the Soong Ching Ling Foundation, which works with mothers, their infants and health workers in rural China. Across Indonesia, the Philippines and Sri Lanka, we are partnering from 2011 with ChildFund to improve access to early childhood care and development services for children up to age five. In Chile, a Soprole programme to get students at more than 1750 schools involved in sports marked its 10th successful year. The programme is in line with Chilean Government efforts to reduce child obesity.

MANAGEMENT DISCUSSION & ANALYSIS

The Management Discussion & Analysis provides commentary on the factors affecting Fonterra's performance and to facilitate understanding of the 2011 financial results. This discussion and analysis supplements the financial information included in the Summary Financial Statements, and other financial and non-financial information elsewhere in the Annual Review.

FINANCIAL HIGHLIGHTS

The 2011 financial year was notable for a recovery in the earnings of our Standard & Premium Ingredients business (formerly called Commodities & Ingredients). Growth in our consumer businesses in mature markets slowed as higher dairy commodity prices compressed margins. In contrast, our emerging market consumer businesses continued to post strong growth.

A significant rise in international dairy prices underpinned record returns to our farmers. The Farmgate Milk Price for the 2011 season was $7.60 per kilogram of milksolids (kgMS) up $1.50 or 24.6 per cent over the same period last year. Other notable highlights include:

- Revenue for the year ended 31 July 2011 was $19.9 billion, 18.8 per cent higher than the $16.7 billion achieved in the prior year
- Earnings before interest, tax, depreciation and amortisation (EBITDA) decreased 2.9 per cent to $1.5 billion ($1.6 billion in the previous year). After adjusting for non-recurring items, normalised EBITDA was 7.6 per cent higher than last year
- Net profit after tax was $771 million, a 12.6 per cent improvement on the prior year's $685 million, driven by largely non-recurring tax items
- Earnings per share increased to 55 cents per share, a 7.8 per cent or four cents per share improvement on last year
- Dividend per share of 30 cents was three cents per share or 11.1 per cent higher than the previous year's 27 cents
- Return on Net Assets (RONA), before interest and taxes and excluding non-recurring items, was 9.3 per cent compared with 8.7 per cent last year
- Our gearing ratio (based on net interest-bearing debt to net interest-bearing debt plus equity) was 38.5 per cent as at 31 July 2011, compared with 43.6 per cent as at 31 July 2010. The economic gearing ratio (which includes the impact of debt hedging) was 41.8 per cent, compared with 44.9 per cent 12 months earlier
- Distributable Profit was 65 cents per share compared with 60 cents last year, an improvement of 8.3 per cent. Distributable Profit is used to calculate Payout, which is used to compare Fonterra's performance with that of other New Zealand co-operatives. Fonterra calculates Distributable Profit by adding to net profit after tax the additional tax credit that would be available if all current year profits were declared as a dividend.

GROUP RESULT

	2011 $M	2010 $M	CHANGE $M	CHANGE %
Revenue	19,871	16,726	3,145	18.8
Gross profit	3,010	2,751	259	9.4
Gross profit margin	15.1%	16.4%		
Earnings before interest, tax, depreciation and amortisation (EBITDA)	1,517	1,562	(45)	(2.9)
EBITDA margin	7.6%	9.3%		
Operating profit	965	1,022	(57)	(5.6)
Earnings before interest and tax	1,028	1,078	(50)	(4.6)
Net finance costs	406	313	93	29.7
Profit before tax	622	765	(143)	(18.7)
Tax credit/(expense)	149	(80)	229	286.2
Profit after tax	771	685	86	12.6
Earnings per share	55 cps[1]	51 cps[1]	4 cps[1]	7.8
Dividend per share	30 cps[1]	27 cps[1]	3 cps[1]	11.1

1. Cents per share

Our solid performance in 2011 was achieved under challenging operating conditions. This result reflects a strong improvement in the profitability of our Standard & Premium Ingredients business segment and continued growth in the Asia/AME consumer business segment. Total Group revenue grew 18.8 per cent driven by strong international dairy prices and good volume growth.

Gross profit increased 9.4 per cent to $3 billion but gross profit margin declined 1.3 percentage points primarily due to margin reduction within our consumer businesses as a result of rapidly rising dairy ingredient prices.

Operating costs increased by 6.0 per cent over the prior year. This was mainly driven by a number of significant projects across the business, increased salary costs, and higher storage expenses due to increased inventory volumes.

Normalised Group EBITDA for 2011 was $1.5 billion, which was an improvement of 7.6 per cent on last year (refer to table). Solid growth in our Standard & Premium Ingredients and continued consumer brands success in emerging markets were key factors in the increase of EBITDA.

	2011 $M	2010 $M	CHANGE $M	CHANGE %
Operating profit	965	1,022	(57)	(5.6)
Add back depreciation	414	416	(2)	(0.5)
Add back amortisation	75	68	7	10.3
Add share of profit of equity accounted investees	63	56	7	12.5
EBITDA	1,517	1,562	(45)	(2.9)
Less non-recurring items	(23)	(174)	151	86.8
Normalised EBITDA	1,494	1,388	106	7.6

Net finance costs of $406 million were $93 million or 29.7 per cent up on 2010. The increase was primarily due to the negative impact from the net change in fair value of interest rate derivatives and debt, along with higher average market interest rates. This was partly offset by lower interest costs arising from reduced levels of borrowings in 2011.

A largely non-recurring tax credit of $149 million in 2011 compared with an $80 million tax expense was mainly due to the tax effect of changes to intangibles and the recognition of New Zealand tax losses.

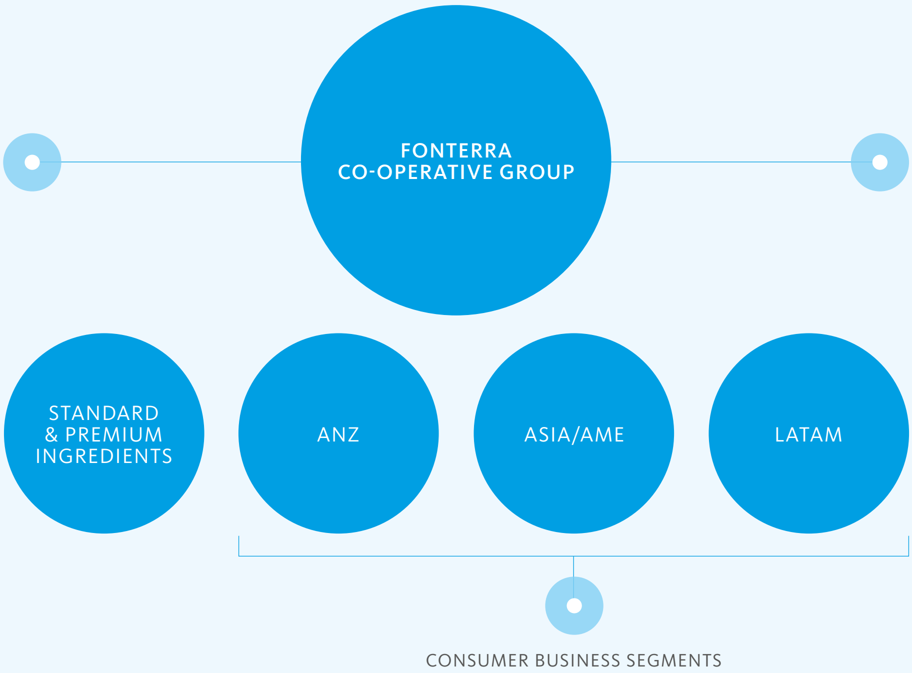
RESULTS OF OPERATIONS

Fonterra has four reportable segments that are defined by product type and geographic area to reflect how the Group's operations are managed. One segment is focused on dairy ingredients and the other three segments are primarily focused on consumer dairy products.

The performance of the Group's segments are summarised below followed by detailed commentaries.

When analysing the performance of our operations it is important to understand that these segments are interdependent and, therefore, are managed with the objective of maximising performance for the Group.

The following segment results analysis focuses on earnings before significant non-recurring items (i.e. normalised earnings).



STANDARD & PREMIUM INGREDIENTS

INTRODUCTION

The Standard & Premium Ingredients business (formerly Commodities & Ingredients) segment produces and distributes a range of ingredients made from milk that are tailored to the needs of international customers, especially food manufacturers. We work with our customers to unlock the natural goodness of dairy and provide ingredients for a range of applications. Our manufacturing operations combine world-class scale with the flexibility to respond to changing market dynamics and customer requirements.

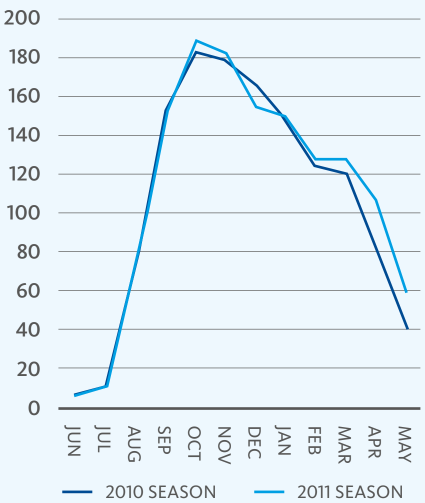
NEW ZEALAND MILK SUPPLY

The New Zealand milk production season extends from June to May with production ramping up to peak from October to December before gradually falling away through the shoulder months in late summer and autumn. This seasonal production curve requires processing and logistics capacity to handle peak milk flows while also providing flexibility to adjust product mix during the season in response to changes in relative prices and market demand. It is optimal management of these factors that enables Fonterra to extract additional value from milk processed.

Milk collection from New Zealand farmers for the 2011 season (1 June 2010 to 31 May 2011) totalled 15.4 billion litres, representing 1346 million kgMS. This included contract milk supply of 26 million kgMS. This was Fonterra's largest annual volume of milk collected and an increase of 4.7 per cent from the 2010 season. The increase was a result of favourable autumn weather conditions offset, in part, by dry conditions in many areas earlier in the season. Monthly milk collections compared with the previous year are illustrated in the graph below.

MONTHLY NEW ZEALAND MILK SUPPLY

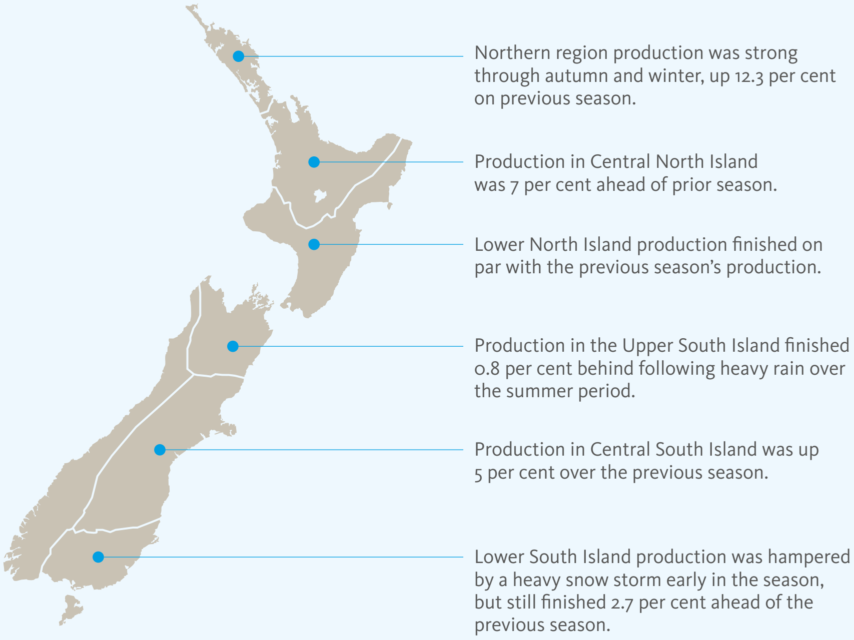
kgMS (MILLION)



Production from the North Island was 5.2 per cent higher than the previous season. This was achieved despite a tough spring and an early summer dry period.

South Island production grew 3.7 per cent as a result of mostly favourable conditions through the season and a continuation of dry-farm conversions, and recent conversions reaching full potential, in Canterbury and Southland.

New Zealand by milk supply regions



FINANCIAL PERFORMANCE

	2011 $M	2010 $M	CHANGE $M	CHANGE %
NZ sourced	11,782	9,634	2,148	22.3
Other	1,997	1,591	406	25.5
Inter-segment revenue	1,800	1,532	268	17.5
Revenue	**15,579**	**12,757**	**2,822**	**22.1**
Cost of New Zealand milk	(10,235)	(7,938)	(2,297)	(28.9)
Inventory movement	383	190	193	101.6
NZ manufacturing costs	(2,437)	(2,233)	(204)	(9.1)
Other costs of goods sold	(2,077)	(1,800)	(277)	(15.4)
Cost of goods sold	**(14,366)**	**(11,781)**	**(2,585)**	**(21.9)**
Gross profit	**1,213**	**976**	**237**	**24.3**
Normalised EBIT[1,2]	**431**	**316**	**115**	**36.4**
Normalised EBITDA[1,2]	**809**	**690**	**119**	**17.2**

1. Represents normalised segment earnings adjusted for non-recurring items.

2. 2010 has been restated to exclude indirect allocations previously recharged to ANZ, Asia/AME and Latam.

REVENUE GROWTH

Standard & Premium Ingredients achieved sales of $15.6 billion in 2011, up 22.1 per cent from 2010.

Sales for New Zealand sourced milk increased 22.3 per cent to $11.8 billion. This was due mainly to significant increases in the average US dollar denominated selling price for dairy ingredients, and volume growth from higher milk supply as noted earlier.

Most of Standard & Premium Ingredients' sales are generated from milk sourced from New Zealand. But the business is increasingly complementing New Zealand sourced milk with overseas supply to meet customer demands. This year Fonterra sourced product and processed dairy ingredients from 27 external suppliers from around the world. These sales are recorded under 'other' revenues and increased during the year due to greater volumes, and higher prices for dairy ingredients.

Inter-segment revenue is predominantly internal sales to Fonterra's consumer operations in Australia, New Zealand and Asia.

Management of Product Mix

The Standard & Premium Ingredients business processes New Zealand milk collected into a wide range of world-class dairy products.

Five reference products; Whole Milk Powder (WMP), Skim Milk Powder (SMP), Butter Milk Powder (BMP), Butter and Anhydrous Milk Fat (AMF), are used to derive the Farmgate Milk Price paid to farmers. Commentary under 'cost of goods sold' below provides a more detailed description of how these reference products inform the Farmgate Milk Price. In addition, this business manufactures a wide range of protein, cheese and cream based products.

Higher margins arise from the management of product mix and achieving prices that are above those of the five reference products informing the Farmgate Milk Price. In 2011, improved optimisation capabilities enabled us to better manage product mix by adjusting volumes during the season, having regard to manufacturing constraints and contractual obligations.

The accompanying table shows the movement between product categories.

PRODUCTION IN METRIC TONNES (MT)	2011 (MT 000)	2010 (MT 000)	CHANGE (MT 000)	CHANGE %
WMP	839	671	168	25.0
SMP	512	489	23	4.7
Cheese	202	219	(17)	(7.8)
Cream	44	62	(18)	(29.0)
Butter	195	206	(11)	(5.3)
AMF	126	136	(10)	(7.4)
BMP	35	40	(5)	(12.5)
Other	447	473	(26)	(5.5)
Total	**2,400**	**2,296**	**104**	**4.5**

Market Driven Price

Fonterra's online sales platform, GlobalDairyTrade™ (GDT) accounted for some 565,000 metric tonnes in 2011 or around 24 per cent of our total ingredients sales. The platform reached its third anniversary in July 2011 with sales to date totalling more than USD3.9 billion. During 2011, GDT increased the frequency of trading events to twice-monthly and expanded the range of products from four to seven.

The Farmgate Milk Price is informed primarily by GDT prices. To the extent that Fonterra's sales book lags GDT due to contractual arrangements with customers, earnings are exposed to pricing and margin risk. During 2011, a sharp rise in GDT prices resulted in a negative impact from longer-period fixed price contracts. Action by management to address some of these commitments helped reduce the impact of these losses.

Currency Impact

Dairy ingredient prices are denominated primarily in US dollars, which weakened against the NZ dollar in 2011. Fonterra's policy to hedge its foreign exchange exposure proved successful in reducing volatility, and yielded an effective average conversion rate of US72 cents, 5 cents lower than the average spot rate.

The impact of foreign exchange movements between the NZ dollar and the US dollar were largely mitigated by our hedging policy, and the offset between the foreign exchange impacts on revenue and cost of milk (via the impact of foreign exchange rates on prices which inform the Farmgate Milk Price). The net result was only a marginal impact on the earnings of Standard & Premium Ingredients.

COST OF GOODS SOLD

Standard & Premium Ingredients' cost of goods sold increased 21.9 per cent to $14.4 billion. The increase was primarily due to a rise in global dairy commodity prices leading to a higher Farmgate Milk Price in New Zealand, and increased volumes of milk collected in New Zealand and product sourced from overseas.

Cost of New Zealand Milk

The cost of New Zealand milk represents Fonterra's single largest cost category and in 2011 was $10.2 billion, an increase of $2.3 billion (28.9 per cent) over 2010. This includes the cost of milk supplied in the year ended 31 July 2011 (including contract-backed and share-backed milk), premiums for specialty milk, and premiums paid for winter milk. A record 1346 million kgMS of New Zealand sourced milk was supplied to Fonterra this year.

For ease of expression, the Farmgate Milk Price is described as the aggregate amount calculated in accordance with the Farmgate Milk Price Manual of $10.2 billion divided by total New Zealand milk supply, which equals $7.60 per kgMS. The average amount available to pay for share-backed supply is $7.59 per kgMS, after adjusting for winter milk premiums and contract milk discounts.

Of the $2.3 billion increase in the cost of New Zealand milk, $1.8 billion reflected higher prices, and $0.5 billion was due to growth in the volume of milksolids collected.

The Farmgate Milk Price has been derived in accordance with the Principles, methodologies and detailed rules in Fonterra's Farmgate Milk Price Manual. Because Fonterra purchases such a large proportion of New Zealand's total milk, it is not possible to distinguish a market price for milk that is independent of the price paid by Fonterra. It is therefore necessary to use a methodology such as that contained in the Farmgate Milk Price Manual.

The Farmgate Milk Price determines the amount paid for milk delivered to the farmgate by farmer Shareholders. It is calculated in accordance with the Manual by:

- Determining the revenue that the Co-operative would earn if the equivalent of all the milk Fonterra collects was converted into commodity specifications of WMP, SMP, and their by-products, which are BMP, Butter, and AMF. These products are referred to in the Manual as 'Reference Commodity Products'. Prices primarily reflect US dollar prices achieved on the twice-monthly GDT trading events, converted to New Zealand dollars using Fonterra's actual average monthly foreign exchange conversion rate
- Deducting costs, including the cost of transporting raw milk to factories, and the cost of efficiently manufacturing Reference Commodity Products and then transporting them to the point of export from New Zealand, along with selling and administration expenses. They also include amounts for depreciation of fixed assets and an appropriate return on investment, including investment in working capital. To the extent feasible and where doing so is consistent with the Milk Price Principles, costs are derived from Fonterra's actual costs associated with these activities.

The balance comprises the aggregate amount payable to farmer Shareholders. This is an aggregate amount but is usually referred to on the basis of a Farmgate Milk Price per kgMS.

For further information see the Fonterra Farmgate Milk Price Statement and Fonterra Farmgate Milk Price Manual available at *www.fonterra.com.*

Inventory Movement

The higher volumes of milk collected in the last quarter meant that 23,600 metric tonnes of additional inventory was on hand as at 31 July 2011 compared to 31 July 2010. The higher Farmgate Milk Price also meant that the value of the inventory was higher than the previous period. These factors had a positive impact of $193 million on the cost of goods sold when compared with last year.

New Zealand Manufacturing Costs

New Zealand manufacturing costs were $204 million or 9.1 per cent higher than last year. The increase in total manufacturing costs primarily reflected the combined effect of higher volumes of milk collected and processed this year, and increased per unit costs.

The key drivers behind the increase in manufacturing costs when compared with last year were:

- A $53 million increase in cheese production costs due to increased raw materials costs partially offset by lower cheese production levels compared to last year
- Higher milk collection costs of $60 million arising from the record levels of milk collected in 2011
- Other variable costs were $91 million higher due to a 4.5 per cent increase in production which contributed to additional raw materials, packaging, ingredients and lactose costs, and
- Higher unit costs for fuel and electricity.

The increase in manufacturing cost on a per metric tonne basis was 4.8 per cent.

Other Costs of Goods Sold

Other costs of goods sold mainly relate to the costs of overseas product purchases, which increased by 15.4 per cent this year primarily due to higher commodity prices.

GROWTH INVESTMENTS

Several ingredient innovations developed at Fonterra over the past few years moved beyond customer testing during 2011 and into commercial production with world-leading food companies. Examples of these innovations include the following:

- The development of new generation cheese technologies tailored to customers' requirements. In North America, cheese manufactured using our proprietary CHEDDAR*plus*™ ingredient completed its first year of production. CHEDDAR*plus*™ is manufactured at Los Banos, California
- Partnerships with the world's leading beverage manufacturers across multiple regions continued to be developed and extended. Fonterra has a wide range of functional protein ingredients that allow these manufacturers to deliver dairy nutrition to their consumers in convenient, great tasting formats. As the beverage market moves beyond traditional dairy and protein beverage applications into mainstream functional waters and sports drinks, ClearProtein™ provides a compelling solution to beverage manufacturers
- Fonterra successfully increased sales in cultured products with three new product ranges for the Japanese and South Korean markets using our DelightProtein™ ingredient.

The increasing value of our customer partnerships was evidenced by two key customer segments building on their $1 billion in revenues in 2011. In the first of these, Formulated Foods, Fonterra partners with the five largest infant formula manufacturers in the world, providing semi or fully-finished products, including our specialised ingredients in their applications. The second, the Foodservice business, is aimed at the burgeoning 'out of home eating' market. This global business now operates in around 50 countries with a portfolio of cheese, cream, butter, yoghurt, pastries and beverages, and our customers include the largest restaurant chains in the world, as well as hotels, cafés, airlines, work places, entertainment venues and institutions.

Our manufacturing capacity continues to expand to ensure capacity is in place to process growing milk supply and increase overall efficiency. The first greenfields processing site in approximately 14 years is under development at Darfield, Canterbury. The investment in stage one of around $200 million is due to be completed in 2012. It will have the capacity to convert 2.2 million litres of milk a day into milk powder for export. A further $250 million, in a stage two development, is planned that would lift daily processing capacity to 6.6 million litres. Darfield ranks among Fonterra's largest New Zealand manufacturing investments in the past five years, and reflects significant milk growth in Canterbury.

While New Zealand milk will always be our top priority, global demand for dairying is growing at a pace that New Zealand production cannot match. Prospects in key growth markets will be underpinned by Fonterra's ability to grow high-quality local milk production for customers and to play a strong role in the development of local dairy industries. During the year we announced agreements to develop second and third farms in China and a pilot farm in Brazil. Fonterra is continuing to explore opportunities in other markets such as India.

Investment continued in milk collection technology. An upgrade to add new environmentally-efficient tankers commenced and all tankers were fitted with high visibility colours to enhance road safety. Growth in milk production resulted in 50 more milk tankers operating this year compared with last year.

In 2011, we reacquired the remaining 50 per cent share of rural supplies chain, RD1, from Australian company Landmark. In August 2011, RD1 took over seven stores previously operated by Allied Farmers. The move strengthens Fonterra's presence in the rural services sector.

CONSUMER OPERATIONS

INTRODUCTION

Fonterra has three business segments that focus on fast moving consumer goods products:

- Australia and New Zealand (ANZ) represents the consumer operations in New Zealand and the consumer and manufacturing operations in Australia
- Asia/AME comprises the consumer operations in Asia, Africa and the Middle East
- Latin America (Latam) comprises the Soprole business in Chile and our joint venture in the Dairy Partners Americas (DPA) business across Latin America. It is important to note that DPA is not consolidated into Fonterra's result and Fonterra's share of DPA's earnings is treated as profits from equity accounted investees.

CONSOLIDATED CONSUMER PERFORMANCE

	2011					2010				
$M	REVENUE[1]	SEGMENT NORMALISED EBIT[2]	OPERATING MARGIN[3]	NORMALISED EBITDA[4]	EBITDA MARGIN	REVENUE[1]	SEGMENT NORMALISED EBIT[2,5]	OPERATING MARGIN[3]	NORMALISED EBITDA[4,5]	EBITDA MARGIN
ANZ	4,360	252	5.8%	333	7.6%	3,803	303	8.0%	385	10.1%
Asia/AME	1,687	186	11.0%	195	11.6%	1,537	166	10.8%	175	11.4%
Latam	830	119	14.3%	140	16.9%	738	119	16.1%	138	18.7%
Consumer Total	6,877	557	8.1%	668	9.7%	6,078	588	9.7%	698	11.5%

1. Includes inter-segment revenue: ANZ $781 million, Asia/AME nil, Latam $4 million; (2010: ANZ $570 million, Asia/AME nil, Latam $7 million).

2. Normalised segment earnings before net finance costs and tax, and including share of profit of equity accounted investees.

3. Segment normalised EBIT as a percentage of revenue.

4. Normalised earnings before interest, tax, depreciation and amortisation, and including share of profit of equity accounted investees.

5. 2010 has been restated to exclude indirect allocations previously recharged from Standard & Premium Ingredients.

The consumer businesses collectively achieved sales of $6.9 billion in 2011, up 13.1 per cent. Sales growth was driven by price rises and volume growth in most regions.

Total consumer EBITDA of $668 million was 4.3 per cent lower than last year, reflecting difficult trading conditions. However, EBITDA margin compression in those more mature markets was offset in part by solid growth from our Asian operations where margins were sustained despite higher commodity prices.

The ANZ and Asia/AME consumer operations source some products from the Standard & Premium Ingredients segment. A transfer pricing regime based on market prices governs the price charged for dairy products manufactured for our consumer businesses.

AUSTRALIA/NEW ZEALAND

	2011	2010
Total revenue growth[1]	14.6%	(0.4%)
External revenue growth	10.7%	3.8%
External volume growth	0.7%	3.6%
Total gross profit growth[1]	(4.1%)	5.3%
Normalised EBIT[2] growth	(16.8%)	22.2%
Normalised EBITDA[2] growth	(13.5%)	19.6%
Sales & marketing as a percentage of revenue[3]	4.3%	4.9%

1. Includes inter-segment transactions.

2. Adjusted for non-recurring items.

3. Calculated as percentage of total external segment revenue.

PERFORMANCE

The ANZ business had a challenging year. Although revenue grew 14.6 per cent to $4.4 billion, normalised EBITDA of $333 million was 13.5 per cent lower than last year.

The trading environment was impacted by a combination of local factors in the Australia and New Zealand retail markets and the indirect impact of global dairy ingredients prices on input costs. Consumers remained cautious in their food shopping behaviour with increasing focus on value and promotional initiatives.

Focus on higher margin products in Australia like cheese, butter and yoghurt, has helped the business support profitability. In New Zealand, the consumer products are more diversified with Fonterra Brands New Zealand (FBNZ) holding strong market positions across all dairy categories including liquid milk. The New Zealand operations experienced a decline in volumes resulting from price increases that reflected the cost of higher commodity prices. In February 2011, FBNZ froze the price at which it sells liquid milk to retailers, absorbing any further cost increases until January 2012.

Tip Top is a division of ANZ specialising in ice cream manufacture and is one of New Zealand's most trusted brands. Tip Top lifted its performance to deliver strong sales growth and an improvement in its operating EBIT before a $3 million impact from product losses arising from the Christchurch earthquake (some of which are the subject of ongoing claims).

The ANZ segment includes a division that collects milk from Australian farmers and manufactures dairy ingredients primarily for the export market. This division performed strongly, exceeding the prior year's earnings on the back of higher dairy ingredients prices.

ANZ is a success story for Fonterra with a cumulative average growth rate in normalised EBIT of 11.5[1] per cent over the past three years. As a result, Fonterra has one of the largest dairy consumer businesses in Australia and New Zealand with leading market shares in its target product categories. Given its primary exposure to mature markets and the particularly difficult conditions this year, ANZ has done well relative to some of its peers in Australia and New Zealand.

1. Calculated using unaudited management results for the 12 months to 31 July 2008.

CORE MARKETS AND NEW PRODUCTS

In Australia and New Zealand, our brands hold leading positions in cheese, spreads, yoghurts and dairy desserts, as well as leading positions in milk, flavoured milk and ice cream in New Zealand. Many of our brands are household names. Our businesses build on this success by adding innovative products in faster-growing, higher margin categories and by creating new brands that fill gaps in the market.

Recent new product launches have exceeded expectations with further range and geographical extensions under development.

Highlights include:

- The launch of Kapiti Yoghurt, which was a successful entry into gourmet yoghurts in New Zealand
- Ski® Activ® yoghurt introduced in March 2011, the first product of its kind in Australia containing a unique combination of a prebiotic plus a probiotic, proven to help manage and prevent digestive discomfort. The new product is a result of 25 years research by Fonterra scientists to perfect the probiotic strain
- The launch of the Mammoth Supply Co.™ brand, positioned at supplying 'real man food' for New Zealand men.

ASIA/AFRICA, MIDDLE EAST

	2011	2010
Total revenue growth[1]	9.8%	(9.9%)
External revenue growth	9.8%	(7.7%)
External volume growth	2.2%	3.1%
Total gross profit growth[1]	1.9%	9.1%
Normalised EBIT[2] growth	12.0%	38.3%
Normalised EBITDA[2] growth	11.4%	35.7%
Sales & marketing as a percentage of revenue[3]	15.6%	18.2%

1. Includes inter-segment transactions.

2. Adjusted for non-recurring items.

3. Calculated as percentage of total external segment revenue.

PERFORMANCE

Over the past five years the Asia/AME businesses have focused on profitable high growth categories that meet key consumer needs. This year's results reflect further progress with Asia/AME delivering a 9.8 per cent increase in sales to $1.7 billion and a continued improvement in gross profit despite the challenging operating environment.

Most of Asia/AME's sales are in local market currencies, and some of these weakened against the New Zealand dollar during the year. Asia/AME achieved a 17 per cent improvement in sales recorded in local currencies, before translation to the New Zealand dollar.

Revenue growth mainly reflected increased prices, roll-out of higher value products under the Anmum™ and Anlene™ brands in selected markets, and strong performance in the Foodservices division that markets to hotels, restaurants and bakeries. Higher market shares in fast-growing emerging markets in Asia also helped boost volumes, which were up 2.2 per cent over the previous period.

Normalised EBITDA improved 11.4 per cent to $195 million reflecting significant growth across all of our core brands. This growth was underpinned by increased concerns among consumers about bone health, and the impact of rising consumer incomes on demand for dairy products.

Anlene™ recorded an overall market share of 62 per cent of the high-calcium milk powder category and is the number one high-calcium brand across Asia. Anmum™ and Anchor™ also continue to perform strongly in their markets following strong marketing campaigns this year.

CORE MARKETS AND NEW PRODUCTS

Asian markets remained very strong with double digit sales growth in Sri Lanka, Middle East, Malaysia, Thailand, Hong Kong and Taiwan. One of the main drivers of growth is Asia/AME's leadership in nutritional dairy and foodservice solutions.

In the markets of Malaysia, Indonesia, Philippines and Thailand we are a clear leader in adult nutrition through our bone health brand, Anlene™. Over recent years, intensive research and marketing has positioned calcium-rich Anlene™ as a key adjunct to the prevention of osteoporosis (bone mass loss) due to age. In 2011, we expanded the Anlene™ proposition to include joint health by launching Anlene Total™ which includes glucosamine, an amino sugar essential for joint cartilage. Glucosamine is usually sold in tablet form but was developed as an ingredient at Fonterra's Research Centre in Palmerston North. Anlene Total™ was launched in Indonesia and Taiwan in April 2011.

In Malaysia and Indonesia, all added sugar was eliminated from our flagship premium nutritional powder Anmum Essential™ for children, while ensuring that the taste Asian consumers enjoy was not compromised. We have also reduced sugars in other 'Growing Up Milk' categories in line with our objective of improving the nutritional value of products we sell.

Asia/AME's expansion continued into new geographical areas with sales in China increasing by 77 per cent and sales in Vietnam up 39 per cent, creating a promising platform for future growth.

LATIN AMERICA

	2011	2010
Total revenue growth[1]	12.5%	(7.5%)
External revenue growth	13.0%	(2.4%)
External volume growth	0.6%	0.3%
Total gross profit growth[1]	13.8%	9.1%
Normalised EBIT[2] growth	–	12.2%
Normalised EBITDA[2] growth	1.4%	9.5%
Sales & marketing as a percentage of revenue[3]	10.3%	10.1%

1. Includes inter-segment transactions.

2. Adjusted for non-recurring items.

3. Calculated as percentage of total external segment revenue.

PERFORMANCE

The Latam segment includes Soprole, an integrated dairy business in Chile majority owned by Fonterra, and Dairy Partners Americas (DPA), a joint venture with Nestlé covering several markets in Latin America. Fonterra's share of DPA's profit is treated as profit from equity accounted investees.

Soprole's revenue grew 12.5 per cent to $830 million compared to the previous year, driven by growth in key categories like yoghurt, milk, cheese and dessert categories. During the same period, Latam's normalised EBITDA increased 1.4 per cent to $140 million.

DPA had a challenging year driven by static volumes and higher cost of milk and other input costs which were not fully recovered through price increases. Fonterra's earnings from its investment in DPA include royalty income from its consumer operations, share of profit, and a return on the capital invested in manufacturing assets. Key areas of exposure for DPA are volatility of foreign exchange rates and inflation, particularly in markets such as Venezuela.

Earnings from the DPA manufacturing business were broadly similar to the prior year.

CORE MARKETS AND NEW PRODUCTS

Soprole is the market leader in Chile and was recognised as the 2010 Signature Chilean Corporate Brand by the Marketing Hall of Fame. Continued innovation, together with increased marketing, helped consolidate Soprole's leadership in the consumer market, where it maintains the number one or two position across all major dairy categories.

In 2011, Soprole developed the Next Tránsito and Gold Creme yoghurt brands, expanded the impulse desserts range through products like Manjarate® Frutired and Manjarate® Tofee and launched sparkling juid Frutix.

During the year, Soprole completed the construction of its Margarine and Dairy Blends plant, and expanded capacity at its San Bernardo site.

Fonterra confirmed in March 2011 that Soprole had withdrawn a proposal to merge its business with Nestlé Chile's liquid and chilled dairy business. The application was withdrawn by the parent companies Nestlé S.A. and Fonterra after having assessed the conditions to continue with the application were not appropriate, and there are no plans to present a new application to the Chilean authorities.

Soprole has continued to focus on growing its consumer business in Chile where it already has a very strong position in the market and has been posting strong growth in local currency in recent years.

DPA's performance was mixed across its priority markets of Brazil, Venezuela, Ecuador, Argentina and Columbia.

GROUP CASH FLOWS

	2011	2010	CHANGE $M	CHANGE %
Net cash flows from operating activities	1,184	1,479	(295)	(19.9)
Net cash flows from investing activities	(488)	(354)	(134)	(37.9)
Net cash flows from financing activities	(433)	(1,154)	721	62.5

Net operating cash flows were $1.2 billion in 2011 compared with $1.5 billion in 2010. Lower operating cash flows reflect a larger increase in working capital requirements than last year, with more inventory on hand at the end of the year. Payments to suppliers also increased, reflecting a higher Farmgate Milk Price and greater volume of milksolids. This was partially offset by higher revenue from dairy ingredient prices during the year.

Net cash outflows from investing activities were $488 million or $134 million higher than last year. Capital expenditure (including property, plant and equipment, and intangibles) was $623 million, compared with $492 million in the prior year. Investments mainly related to expanded production capacity in our primary markets of New Zealand and Australia, along with supply chain and systems improvements. Investments were also made to improve manufacturing flexibility and to acquire more efficient tankers. Strategic investments in equity accounted investees and subsidiaries were $55 million compared with $62 million last year. This year included the acquisition of the remaining 50 per cent of RD1. The largest divestment during the year was the sale of our Western Australia dairy operations.

Financing cash flows were an outflow of $433 million which was $721 million lower than the previous period. The lower cash outflow was largely attributable to the first full year effect of the dividend policy which was introduced in 2010.

CAPITAL EMPLOYED AND DEBT TO DEBT PLUS EQUITY RATIO

	2011	2010	CHANGE $M	CHANGE %
Average net assets[1]	10,772	10,433	339	3.2
Equity attributable to Shareholders	6,503	5,631	872	15.5
Net interest bearing debt	3,766	4,268	(502)	(11.8)
Return on net assets	9.3%	8.7%	-	0.6 pts
Economic net interest bearing debt	4,331	4,494	(163)	(3.6)
Equity less cash flow hedge reserve	6,025	5,526	499	9.0
Debt to debt plus equity ratio	38.5%	43.6%	-	5.1 pts
Economic debt to debt plus equity ratio	41.8%	44.9%	-	3.1 pts

1. 13 month average net assets excluding net debt and deferred tax.

Group equity attributable to Shareholders was $6.5 billion as at 31 July 2011, compared with $5.6 billion as at 31 July 2010. The improvement in equity was due to higher retained earnings ($396 million), net share subscriptions ($245 million) and an increase in the cash flow hedge reserve ($375 million), partially offset by negative movements in the foreign currency translation reserve of $144 million. Net share subscriptions resulted from $404 million new equity issued and $159 million equity surrendered.

The Group's gearing ratio (based on net interest-bearing debt to net interest-bearing debt plus total equity excluding the cash flow hedge reserve) was 38.5 per cent as at 31 July 2011, compared with 43.6 per cent as at 31 July 2010. The economic gearing ratio (including the impact of debt hedging) was 41.8 per cent, compared with 44.9 per cent 12 months earlier.

Total borrowings decreased from the previous year primarily due to a combination of cash raised from share issues and retained earnings.

RETURNS TO FULLY SHARED UP FARMERS

DIVIDEND

In March 2011, the Board declared an interim dividend of 8 cents per share (totalling $110 million), that was paid on 20 April 2011 on all shares held on 31 March 2011. A final dividend of 22 cents per share was declared on 21 September 2011, payable on 20 October 2011. The total annual dividend of 30 cents per share is 3 cents per share higher than in 2010.

Fonterra's dividend policy targets a payout ratio of 65-75 per cent of adjusted Distributable Profit (after taking into account non-recurring items and other factors). The policy also gives the Board discretion to have regard to other commercial considerations it considers to be relevant. The dividend of 30 cents per share is consistent with this policy, and reflects 69 per cent of an adjusted Distributable Profit of 44 cents per share. This amount is considered by the Board to be an appropriate measure of sustainable normalised earnings per share after taking into account non-recurring items, non-cash adjustments (such as the tax effect of retentions) and other factors as provided for in Fonterra's dividend policy.

PAYOUT

As a co-operative, Fonterra refers to the total returns to its farmer Shareholders as Payout. Fonterra's Payout comprises a Farmgate Milk Price per kgMS and Distributable Profit per share. Payout is used as a comparison with returns from other New Zealand dairy co-operatives. It assumes a Fonterra farmer Shareholder is 100 per cent shared up for the season (i.e. owning one share for each kgMS produced).

Payout (before retentions) was $8.25 in 2011, $1.55 or 23.1 per cent higher than in the 2010 season. Cash Payout, defined as Farmgate Milk Price plus Dividend, was $7.90 in 2011, $1.53 or 24.0 per cent higher than 2010.

	2011			2010		
	$M	MILLION	$	$M	MILLION	$
Profit attributable to Shareholders	754	1,377 Shares	0.55	669	1,343 Shares	0.50
Add tax effect of retentions	146	1,377 Shares	0.10	131	1,343 Shares	0.10
Distributable Profit	**900**	**1,377 Shares**	**0.65**	**800**	**1,343 Shares**	**0.60**
Farmgate Milk Price	10,035	1,320 kgMS	7.60	7,664	1,256 kgMS	6.10
Payout (before retentions) to farmers[1]	**10,935**		**8.25**	**8,464**		**6.70**
Distributable Profit	900	1,377 Shares	0.65	800	1,343 Shares	0.60
Less retentions	(487)	1,377 Shares	(0.35)	(438)	1,343 Shares	(0.33)
Annual Dividend	**413**		**0.30**	**362**		**0.27**
Farmgate Milk Price	10,035	1,320 kgMS	7.60	7,664	1,256 kgMS	6.10
Cash Payout to farmers[1]	**10,448**		**7.90**	**8,026**		**6.37**

1. For a 100 per cent shared-up farmer (i.e. owns one share for each kgMS produced).

CO-OPERATIVE SHARES

Fonterra farmer Shareholders purchase or redeem Co-operative shares at a price determined annually by the Board. For the 2011 year, the price was unchanged from 2010 at $4.52 per share. For more information on the valuation method used to determine the Co-operative share price, see Note 7: Capital and Reserves in the Financial Statements, or Note 5: Co-operative Shares in the Summary Financial Statements.

INTRODUCTION

The Board and management of Fonterra are committed to achieving the highest standard of corporate governance and leadership.

To support our role as a Board, we have developed governance systems that reflect Fonterra's unique characteristics and requirements as a significant New Zealand based co-operative competing in the global dairy market.

WE FOCUS ON GOVERNANCE IN A WAY THAT PROMOTES:

- the interests of our supplying Shareholders
- transparency, giving our supplying Shareholders and other stakeholders the information they need to assess our performance
- effective risk management to ensure that Fonterra meets its business objectives and all legal requirements
- a good balance between the roles and functions of the Board and management, and
- communication with important stakeholder groups, including employees, customers, farmers, governments and the communities within which Fonterra works.

OUR BOARD

The Board has 13 members – nine elected from the Shareholder base and four appointed by the Board and ratified at the Annual Meeting by Shareholders.

The Appointed Directors are selected to ensure that the Board has the full complement of skills and competencies needed to lead an enterprise of Fonterra's size, sophistication and complexity. They bring to the Board perspectives and experience to augment the direct industry knowledge and other expertise provided by the Elected Directors.

As the Elected Directors must be Shareholders, they will have a supplier relationship with Fonterra and generally will not be classified as independent under best practice definitions. The Appointed Directors, however, do meet the NZX criteria for independence – and are expected by Fonterra to maintain independence for the length of their term.

All Directors comply with the legislative requirements for disclosing interests and with Fonterra's in-house Securities Code of Conduct which regulates both Directors and management in their personal dealings with Fonterra securities and those of related companies. Fonterra does not have executive Directors.

BOARD EFFECTIVENESS

It is important that all members of the Board are appropriately informed of the Group's activities and have access to operations and management.

Directors are supplied with detailed monthly performance reports and analysis in advance of all Board meetings, together with papers on any significant commercial initiatives, and information on the Group's competitive position and general economic indicators.

The Board also makes a point of meeting away from head-office on a semi-regular basis so that our Directors can broaden their understanding of the business through direct contact with managers and customers. Directors also regularly visit key markets to gain a better understanding of the global dairy market.

Following appointment to the Board, Directors undertake an induction programme to familiarise themselves with the Group. Areas covered include:

- the Fonterra Constitution
- business strategy and planning
- an overview of key financial metrics to monitor business performance, and
- an overview of material areas of the Fonterra business, through meetings with key executives.

All Directors have access to Fonterra's General Counsel, who is responsible for advising the Board on all governance matters. The Board can also seek external advice as required.

BOARD ROLE AND CHARTER

Our Board is responsible for leadership, direction and oversight of the Group and is accountable to Shareholders for overall performance of the Co-operative. Specific functions in the discharge of this responsibility are:

- review of the dividend policy and declaration of the interim and final dividend
- declaration of the Farmgate Milk Price and Distributable Profit
- declaration of the actual co-operative share price from the commencement of each season (the Fair Value Share price)
- reviewing and approving the Group strategy and business plans
- appointing the CEO and reviewing the CEO's performance
- delegating authority to management, and monitoring the exercise of that authority
- engaging in the development of the strategic plan and setting the strategy for the Group and for the major business units within the Group
- approving significant acquisitions and disposals outside management's delegated authorities, and
- overseeing the Board Committees and the areas covered by each of those Committees.

The Board Charter outlines the key values and practices of Fonterra and provides a reference point for the Board as a whole, and for individual Directors, in the execution of their duties. The Charter is reviewed regularly, as are the Committee Charters (see *www.fonterra.com* for the Charter documents).

Board meetings

The Board meets formally at least seven times a year and calls additional meetings to deal with specific issues as they arise. Between full Board meetings, the Board uses Committees and Working Groups to advance its work programme and to enhance the efficiency and effectiveness of its decision-making. The Board also this year held a special two day planning and strategy session.

BOARD COMMITTEES

COMMITTEE	MEMBERSHIP	PURPOSE
Audit, Finance and Risk Committee (AFRC)	David Jackson (Chair) Colin Armer Malcolm Bailey Ian Farrelly Greg Gent John Waller	To assist the Board in fulfilling its corporate governance responsibilities in relation to Fonterra's risk management and internal control frameworks, financial reporting, audit activities and treasury matters.
Appointments, Remuneration and Development Committee (AR&D)	Sir Henry van der Heyden (Chair) Colin Armer John Ballard Ian Farrelly John Monaghan Ralph Waters John Wilson David Jackson (observer)	To assist the Board in fulfilling its corporate governance responsibilities in relation to the recruitment, retention, remuneration and development of Directors, executives and other employees, and to promote a safe and healthy working environment.
Supplier Relations Committee (SRC)	Colin Armer (Chair) Malcolm Bailey Ian Farrelly Nicola Shadbolt Jim van der Poel	To assist the Board in fulfilling its corporate governance responsibilities in relation to the supply of milk from Shareholders, and to seek to resolve Shareholder complaints before reference to the Milk Commissioner.
Fair Value Share Review Committee (FVSRC)	John Waller (Chair) Greg Gent David Jackson John Monaghan John Wilson Jim van der Poel	To assist the Board in fulfilling its corporate governance responsibilities in relation to the Fair Value Share process, including the adequacy of the information provided to the Valuer and the determination of Restricted Market Value.
External Relations Committee (ERC)[1]	John Monaghan (Chair) Malcolm Bailey Colin Armer Greg Gent Jim van der Poel John Wilson	To support Fonterra management to build aspiration with stakeholders for New Zealand to be the centre of dairying excellence in the world, including regulatory frameworks and infrastructure, and creating a shared agenda for Fonterra's success.
Capital Structure Committee (CSC)[2]	John Wilson (Chair) Greg Gent David Jackson John Monaghan Nicola Shadbolt Jim van der Poel John Waller	To assist the Board in fulfilling its corporate governance responsibilities in relation to the implementation of Trading Among Farmers.

1. Formerly the Government and Trade Relations Committee.

2. Established as a Board Committee on 26 October 2010. Previously a sub-committee of the FVSRC.

Board and Committee attendance

	BOARD							
	REGULAR	SPECIAL	AFRC	AR&D	SRC	FVSRC	ERC	CSC
Colin Armer	7/7	3/3	6/6	7/7	1/1		2/2	
Malcolm Bailey	7/7	3/3	6/6		5/5		2/2	
John Ballard	6/7	2/3		7/7				
Ian Farrelly	7/7	3/3	6/6	7/7	4/5			
Greg Gent	7/7	3/3	6/6			6/7	2/2	7/7
David Jackson	7/7	3/3	6/6			7/7		6/7
John Monaghan	7/7	3/3		5/7		5/7	2/2	7/7
Nicola Shadbolt	7/7	3/3			5/5			7/7
Sir Henry van der Heyden	7/7	3/3		7/7				
Jim van der Poel	7/7	3/3			5/5	7/7	1/2	7/7
John Waller	6/7	3/3	5/6			7/7		6/7
Ralph Waters	7/7	2/3		7/7				
John Wilson	7/7	3/3		6/7		7/7	1/2	7/7
Total meetings	7	3	6	7	5	7	2	7

DIRECTORS' REMUNERATION COMMITTEE (DRC)

In accordance with the Constitution, Shareholders elect an independent committee of six Shareholders to consider and make recommendations to the Annual Meeting on Elected Director remuneration. The members of the DRC are Rodney Wilson (Chair), Murray Holdaway, Murray King, Scott Montgomerie, Philip Wilson and Gerard Wolvers. The Board reviews the DRC's performance against its Terms of Reference but, given the independent nature of the committee, would refer any matters of concern to an Annual or Special Meeting of Shareholders.

The Board sets the remuneration of Appointed Directors.

SHAREHOLDERS' COUNCIL

One of the Board's most important relationships is with the Shareholders' Council. The Council, which is established under the Fonterra Constitution, is independent of the Board and comprises 35 Shareholder-elected councillors, each representing a different ward. The Council reviews the Board's statement of intentions for the performance and operations of the Group and publishes an Annual Report, commenting on these matters. The Council and the Board meet regularly, as do the Chairs of the Board and the Council and the Chairs of their respective Committees.

COMMUNICATIONS

Fonterra is committed to maintaining and improving dialogue with our Shareholder base to ensure that the objectives of both the Group and the Shareholders are understood. We run an extensive Shareholder and supplier relations programme, managed by the Group Director Supplier and External Relations and the Chief Financial Officer. We also provide channels for electronic communication through the *www.fonterra.com* and Fencepost websites.

Shareholder/supplier meetings

A schedule of regular meetings with Shareholders and suppliers is held across the country each year. Often these are run in conjunction with the Shareholders' Council, Area Managers and the Fonterra Farmer Network.

In addition, the Board consults with supplying Shareholders on specific issues as they arise. This year, for example, a number of special meetings were held to discuss the Trading Among Farmers initiative, reinforcing the Board's commitment to maintaining a constructive and open engagement with our Shareholders.

www.fonterra.com and Fencepost

Presentations on the development of the business are available on the *www.fonterra.com* website. The Group also uses email alerts, including regular updates from the Chairman and a monthly Shareholder Update.

The Fencepost website enables Fonterra suppliers, their employees and business partners to transact online with Fonterra and access information and tools on milk production and quality, online statements and up to the minute news and weather. This site is also used to provide information on the business to suppliers.

Annual Meeting

The Board views the Annual Meeting of Shareholders, which is held at a different venue around New Zealand each year, as an opportunity to communicate directly with Shareholders and ensures that adequate time is provided at these meetings for Shareholders to raise issues or ask questions from the floor.

Annual Report

The Group's Annual Report including financial statements, and Annual Review, together with the half-year reports and other material announcements, are designed to present a balanced and clear view of Fonterra's activities and prospects and are available on the website, *www.fonterra.com*.

Other disclosures

Information on the Group's performance and the expected Payout, the Fair Value Share, annual and half-year financial results, Director changes, and other significant matters is advised to the market through NZX in accordance with the Disclosure Policy. Shareholders and other stakeholders receive regular updates on these and other issues relevant to them.

Fonterra also makes presentations to the Valuer (appointed by the Shareholders' Council to determine the Fair Value range for the Co-operative share price), analysts, rural professionals and financial commentators to coincide with the publication of the Group's half-year and full-year results.

MILK PRICE PANEL

The Board has created the Milk Price Panel for the purpose of providing assurances to it as to the governance of the Farmgate Milk Price and the proper application of the Farmgate Milk Price Manual and the Milk Price Principles.

The Panel does not determine the Farmgate Milk Price as this is a decision for the Board.

The Panel's composition is designed to ensure a large measure of independence. It consists of two Appointed Directors, one Elected Director and two appropriately qualified persons nominated by the Shareholders' Council, at least one of whom must be independent. The Chair must be one of the Appointed Director members.

The Panel is currently chaired by John Waller. Other Board members are David Jackson and John Wilson. The Shareholders' Council appointees are Richard Punter and Patrick Boyle.

KEY POLICIES

Disclosure Policy

The Board affirmed Fonterra's commitment to promoting a well-informed and efficient market in its listed debt securities by signing off a new Fonterra Group Disclosure Policy in December 2010.

The Policy applies to all Directors and Officers of Fonterra and its subsidiaries, all Shareholders' Councillors and all employees (including contractors, consultants, advisers or secondees).

The objectives of the Policy are to ensure Fonterra continues to provide timely and accurate information and fully comply with the NZX continuous disclosure regime and with the Securities Markets Act and applicable market rules.

Audit independence policy

The auditor is appointed by the Shareholders at the Annual Meeting. Fonterra encourages the rotation of the lead external audit partner in the relationship in accordance with best practice. AFRC approval is required, under the Group's auditor independence policy, for certain activities the auditor may undertake for the Group. The AFRC will not approve the auditor performing any tasks which have the potential to create a conflict except in exceptional circumstances and then only if appropriate safeguards are in place.

Ethics framework

The Board is committed to maintaining high ethical standards across the Group, in all aspects of the business in all parts of the world. Fonterra's Code of Business Conduct – *The Way We Work* – provides practical guidelines on how to apply Fonterra's values in everyday work situations and when working with customers, Shareholders, suppliers and the wider community. This document is available in several languages, to facilitate its accessibility to Fonterra's global employee base.

During the year, *The Way We Work* was rewritten into simple, straightforward language and re-issued to employees. An independently run telephone, e-mail and web-based Hotline provides individuals with a confidential channel to raise difficult ethical issues. In the 2011 financial year, 15 calls were raised with the Hotline. All were fully investigated and appropriate action taken. None was sufficiently serious that it could not be dealt with through internal governance and disciplinary procedures.

COMPLIANCE WITH GOVERNANCE STANDARDS

As Fonterra does not list equity securities, not all of the provisions in the NZX Corporate Governance Best Practice Code are directly applicable. However, the Board recognises the Code's relevance to the Company and seeks to comply, but notes the following areas where its practices diverge from the Code.

- Appointments to the Board/Nomination Committee (paragraphs 2.2 and 3.10-3.12 of the Code). Under Fonterra's Constitution, the Shareholders' Council conducts the election process for Directors. To the extent the Board is responsible for appointing Directors the AR&D Committee satisfies the role of a nomination committee. The AR&D Committee does not have a majority of Appointed Directors due to the proportion of farmer-elected Directors on the Board
- Director Remuneration (paragraph 2.7). Fonterra does not run a performance-based equity security compensation plan. In particular, this is not possible as Appointed Directors are effectively debarred from share ownership as a usual condition of their appointment is that they do not have a supplier relationship with the Company.

The Board has also reviewed compliance with the Principles for Corporate Governance issued by the Financial Markets Authority. While the Board believes it complies with the Principles, there are some points of divergence from specific Guidelines.

- Audit Committee membership (Guideline 3.4). The majority of members are not independent, due to the proportion of farmer-elected Directors on the Board
- Management representation (Guideline 4.4). The CEO and CFO do not certify in the published accounts their compliance with generally accepted accounting practice in New Zealand. The Board is directly and legally responsible for these documents, and obtains all relevant assurances from management or other parties.

FONTERRA'S BOARD OF DIRECTORS HAS 13 MEMBERS – NINE ELECTED FROM THE SHAREHOLDER BASE AND FOUR APPOINTED BY THE BOARD AND RATIFIED BY SHAREHOLDERS AT THE ANNUAL MEETING.

SIR HENRY VAN DER HEYDEN has been Fonterra Chairman since 2002. He is also Chairman of the Appointments, Remuneration and Development Committee.

Sir Henry is a Director of Auckland International Airport Ltd, Independent Egg Producers Ltd, Elevation Capital Management Ltd, Pascaro Investments Ltd and Manuka Ltda. He is a member of Rabobank's Food Agribusiness Advisory Board of Australia, the New Zealand Business Forum and the Director Remuneration Committee of Zespri International.

COLIN ARMER was elected to the Board in 2006 and is Chairman of the Supplier Relations Committee, the International Farming Ventures Group, and Milk Payments Working Group. He also sits on the Audit, Finance and Risk Committee, the Appointments, Remuneration and Development Committee and the External Relations Committee.

Colin is a Director of Dairy Holdings Ltd. Colin and his wife, Dale, have extensive dairy farming interests in both the North and South Island.

MALCOLM BAILEY was elected to the Board in 2004, and sits on the Audit, Finance and Risk Committee, Supplier Relations Committee, the External Relations Committee and the Milk Payments Working Group. Malcolm also represents Fonterra on Dairy Companies Association NZ, and is a member of the International Food and Agriculture Trade Policy Council.

He is also a Director of Embryo Technologies Ltd, Hawke's Bay Dairies (2002) Ltd, Hopkins Farming Group Ltd, and Agrico Holdings Ltd. Malcolm's dairy farming interests are as a shareholder in the Hopkins Farming Group and he lives on a 200 hectare dairy support block near Feilding.

JOHN BALLARD was appointed in July 2006. He is an Appointed Director. He serves on the Appointments, Remuneration and Development Committee.

John has served on the Boards of several listed companies including Woolworths Ltd, CSR Ltd, Rinker Ltd, Email Ltd and Southcorp Ltd where he was CEO. He is currently Chairman of Elders Ltd, a Director of Magellan Financial Fund Ltd, a Director of International Ferro Metals Ltd and Chairman of the Advisory Board of Pacific Equity Partners. His farming interests extend to a property producing milk-fed veal in New South Wales.

IAN FARRELLY was elected to the Board in 2007 following a 20 year career in the banking industry. He is a member of the Audit, Finance and Risk Committee, the Appointments, Remuneration and Development Committee, the Supplier Relations Committee and the Milk Payments Working Group.

Ian is also a Director of First Mortgage Managers Ltd, Spectrum Dairies Ltd and F.D. Lands Ltd. He runs a 400 hectare calf rearing farm in Te Awamutu, owns a 50 per cent share in three Waikato dairy farms and also has ownership in dairy farms in Canterbury.

GREG GENT has been a Board member since Fonterra's formation. Greg is a member of the Audit, Finance and Risk Committee, the Capital Structure Committee, the Fair Value Share Review Committee, the Milk Payments Working Group, the External Relations Committee and the International Farming Ventures Group.

Greg is also Chairman of FMG Insurance Ltd, a Director of Equestrian Sports NZ Inc and a Director of the Northland District Health Board.

DAVID JACKSON was appointed to the Board in September 2007. He is an Appointed Director. David is Chairman of the Audit, Risk and Finance Committee and serves on the Fair Value Share Review Committee, the Capital Structure Committee and the Milk Price Panel. As Chairman of the Audit, Finance and Risk Committee, he is an observer on the Appointments, Remuneration and Development Committee.

David serves on the Boards of several companies including Pumpkin Patch Ltd, Nuplex Industries Ltd and The New Zealand Refining Company Ltd. He spent more than 30 years with accounting firm Ernst & Young in a variety of roles. He served as Chairman of the Board of Management for Ernst & Young Ltd New Zealand from 1999 to 2002.

JOHN MONAGHAN was elected to the Fonterra Board in 2008. John is Chairman of the External Relations Committee and is a member of the Appointments, Remuneration and Development Committee, the Fair Value Share Committee and the Capital Structure Committee. He is also a Director of CentrePort Ltd and CentrePort Properties Ltd. He has farming interests in the Wairarapa and Canterbury regions.

NICOLA SHADBOLT was elected to the Board in 2009. She serves on the Capital Structure Committee, the Supplier Relations Committee, the Milk Payments Working Group and the International Farming Ventures Group.

Nicola is also Professor in Farm and Agribusiness Management at Massey University, and co-author of *Farm Management in New Zealand*. She is a Director of five farming and forestry equity partnerships that include two dairy farms in the Manawatu. Nicola is a Fellow of the New Zealand Institute of Primary Industry Management.

JIM VAN DER POEL was elected to the Board in 2002 and serves on the Fair Value Share Review Committee, the External Relations Committee, the Supplier Relations Committee, the Milk Payments Working Group, the Capital Structure Committee and the International Farming Ventures Group.

He is also Chairman of the Spectrum Group of Companies and a trustee of the Asia NZ Foundation. Jim has won a number of industry awards including the AC Cameron Award, 2002 Nuffield Scholarship, Sharemilker of the Year and the Dairy Exporter Primary Performer Award. Jim and his wife Sue live at Ngahinapouri in the Waikato and have farming interests in Waikato, Canterbury and the United States.

JOHN WALLER was appointed to the Board in February 2009. He is an Appointed Director. John chairs the Fair Value Share Review Committee and the Milk Price Panel, and is a member of the Audit, Finance and Risk Committee, and the Capital Structure Committee.

John is Chairman of the BNZ and the Eden Park Redevelopment Board and of the Eden Park Trust Board. He is a Director of National Australia Bank Ltd, BNZ Investments Ltd, Haydn & Rollett Ltd, National Equities Ltd, Alliance Group Ltd, Sky Network Television Ltd and Donaghy's Ltd. John was a partner at PricewaterhouseCoopers for over 20 years. He was a member of their Board and led their Advisory practice for many years.

RALPH WATERS was appointed to the Board in July 2006. He is an Appointed Director, and serves on the Appointments, Remuneration and Development Committee.

Ralph also serves as Chairman of Fletcher Building Ltd and as a Director of Westpac New Zealand Ltd and Woolworths Ltd. He was Chief Executive of Fletcher Building from May 2001 until his retirement in August 2006. Before joining Fletcher Building, Ralph was Managing Director of the Australian publicly-listed company Email Ltd, and has also held a number of engineering and managerial positions in London and the Middle East.

JOHN WILSON was elected to the Board in 2003. He is Chairman of the Capital Structure Committee and serves on the Appointments, Remuneration and Development Committee, and the Milk Price Panel and the Fair Value Share Review Committee.

John is also the Chairman of South Auckland Independent Testing Society Ltd and a member of the Institute of Directors. In 2000 he was awarded the Nuffield Scholarship. John lives on his dairy farm near Te Awamutu and also manages a dairy farming business based in Geraldine, South Canterbury, which he owns jointly.

ANDREW FERRIER has been Chief Executive of Fonterra Co-operative Group since September 2003, bringing with him a background of generating stronger performances from companies in both the consumer products sector and the commodities market. He has more than 25 years experience at senior executive level, with 17 years as a Chief Executive.

GARY ROMANO joined the dairy industry in 1997 with the New Zealand Dairy Group of Companies, after working for Alcoa of Australia, The Boston Consulting Group and Dairy Partners Americas. In the dairy industry he has had significant experience in both manufacturing and supply chain where he has led teams responsible for driving to achieve world class standards of productivity, quality, safety, cost effectiveness, service and environmental performance.

JONATHAN MASON joined Fonterra in February 2009 as Chief Financial Officer (CFO). He came from US-based Cabot Corporation, where he was Executive Vice President and CFO from 2006, and also worked in a variety of financial management positions at International Paper and ExxonMobil Corporations from 1985 to 2000. Before moving to New Zealand for Fonterra, Jonathan had also worked here when he was CFO for Carter Holt Harvey from 2000 to 2005.

JENNIFER KERR has worked in senior human resources roles in the oil industry for Mobil in the US and Europe and in the leisure industry in the UK for Whitbread. On her return to New Zealand, Jennifer started up her own consultancy, Jennifer Kerr and Associates, before joining Fonterra in July 2006.

ANDREI MIKHALEVSKY joined Fonterra in February 2007. Previously he was Global President of the flavours division in the German listed company Symrise, a leading manufacturer of flavours, fragrances and sensory ingredients. Andrei spent seven years with Georgia Pacific and related companies, including heading the North American retail business, and 22 years in executive positions with the Campbell Soup Company. He resides in the United States with offices in Chicago and Auckland.

JOHN DOUMANI joined Fonterra in 2007 after a 25 year career in international business and consumer brands. Most recently he was President International of the Campbell Soup Company. Prior to joining Campbell's, John was Managing Director of Meadow Lea Foods and he had 13 years experience with Johnson & Johnson. He is based in Australia.

MARK WILSON has more than 35 years experience in the consumer goods sector in Asia, the Pacific, South America, and Europe. Before joining Fonterra in February 2008, he managed Danone's nutrition business across Asia and the Pacific. From 1995 to 1998 he was CEO of Dumex, before becoming President and Chief Executive Officer of the Danish listed East Asiatic Company from 1998 to 2007. He is based in Hong Kong.

KELVIN WICKHAM has over 22 years experience in the dairy industry. He was responsible for furthering Fonterra's overseas markets and partnerships and the development of GlobalDairyTrade™ before taking this new position on the Executive Committee. This role reflects the importance Fonterra places on delivering sustainable co-operative performance and includes Milk Supply, Sustainability, RD1 Ltd, International Farming, Corporate Marketing, Government Relations and Trade Strategy.

FROM LEFT – STANDING

MARK WILSON
Managing Director, Asia/Africa, Middle East

ANDREI MIKHALEVSKY
Managing Director, Global Ingredients and Foodservices

GARY ROMANO
Managing Director, Fonterra Trade and Operations

JOHN DOUMANI
Managing Director, Australia/New Zealand

KELVIN WICKHAM
Group Director, Supplier and External Relations

FROM LEFT – SEATED

JONATHAN MASON
Chief Financial Officer

ANDREW FERRIER
Chief Executive

JENNIFER KERR
Group Director, Human Resources

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SUMMARY FINANCIAL STATEMENTS

CONTENTS

FONTERRA SUMMARY FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 JULY 2011

The Directors hereby approve and authorise for issue the summary financial statements for the year ended 31 July 2011 presented on pages 46 to 61. For and on behalf of the Board:

SIR HENRY VAN DER HEYDEN
Chairman
21 September 2011

DAVID JACKSON
Director
21 September 2011

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 issuer for the purposes of the Financial Reporting Act 1993. Fonterra is also required to comply with the Dairy Industry Restructuring Act 2001.

These summary financial statements are those of Fonterra and its subsidiaries (together the 'Group') and the Group's interest in its equity accounted investees. They have been prepared in accordance with Financial Reporting Standard No. 43: Summary Financial Statements and have been extracted from the Group's full financial statements that have been prepared in accordance with New Zealand Generally Accepted Accounting Practice. Fonterra's full financial statements comply with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and with International Financial Reporting Standards.

The Board has elected to present summary financial statements for the year ended 31 July 2011 as part of the Annual Review sent to Shareholders. These summary financial statements include notes setting out the key information.

These summary financial statements are presented for the year ended 31 July 2011. The comparative information is for the year ended 31 July 2010.

These summary financial statements of the Group have been prepared using the same accounting policies and measurement basis as, and should be read in conjunction, with the Group's full financial statements for the year ended 31 July 2011. The accounting policies applied by the Group are consistent with those applied for the year ended 31 July 2010.

The full financial statements for the year ended 31 July 2011, approved and authorised for issue by the Board on 21 September 2011, have been audited by PricewaterhouseCoopers and given an unqualified opinion.

The Group is primarily involved in the collection, manufacture and sale of milk and milk derived products and is a profit-oriented entity. These summary financial statements are presented in New Zealand dollars ($), which is the Company's functional and presentation currency, and rounded to the nearest million.

The summary financial statements cannot be expected to provide as complete an understanding of the financial affairs of the Group as the full financial statements, which are available from the Company's registered office at 9 Princes Street, Auckland, New Zealand or on the Company's website, *www.fonterra.com*.

INCOME STATEMENT
FOR THE YEAR ENDED 31 JULY 2011

	NOTES	GROUP $ MILLION 31 JULY 2011	GROUP $ MILLION 31 JULY 2010
Revenue from sale of goods		**19,871**	16,726
Cost of goods sold	1	**(16,861)**	(13,975)
Gross profit		**3,010**	2,751
Other operating income		**165**	277
Selling and marketing expenses		**(596)**	(590)
Distribution expenses		**(487)**	(474)
Administrative expenses		**(700)**	(632)
Other operating expenses		**(336)**	(303)
Net foreign exchange losses		**(91)**	(7)
Operating profit	2	**965**	1,022
Finance income		**32**	21
Finance costs		**(438)**	(334)
Net finance costs		**(406)**	(313)
Share of profit of equity accounted investees	6	**63**	56
Profit before tax		**622**	765
Tax credit/(expense)		**149**	(80)
Profit for the year		**771**	685
Profit for the year is attributable to:			
Shareholders of the Parent		**754**	669
Non-controlling interests		**17**	16
Profit for the year		**771**	685

	GROUP $ 31 JULY 2011	GROUP $ 31 JULY 2010
Earnings per share:		
Basic and diluted earnings per share	**0.55**	0.51

The accompanying notes form part of these summary financial statements

STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 JULY 2011

	GROUP $ MILLION	
	31 JULY 2011	31 JULY 2010
Profit for the year	**771**	685
Cash flow hedges:		
– Net fair value gains	**1,384**	584
– Transferred and reported in revenue from sale of goods	**(863)**	(631)
– Tax (expense)/credit on cash flow hedges	**(146)**	18
Net investment hedges:		
– Net fair value gains on hedging instruments	**49**	65
– Tax expense on net investment hedges	**(14)**	(19)
Foreign currency translation losses attributable to Shareholders	**(164)**	(150)
Foreign currency translation reserve transferred to income statement	**(15)**	19
Foreign currency translation attributable to non-controlling interests	**(4)**	(2)
Share of equity accounted investees' movements in reserves	**7**	–
Other comprehensive income/(expense) recognised directly in equity	**234**	(116)
Total comprehensive income for the year	**1,005**	569
Attributable to:		
Shareholders of the Parent	**992**	555
Non-controlling interests	**13**	14
Total comprehensive income for the year	**1,005**	569

The accompanying notes form part of these summary financial statements

STATEMENT OF FINANCIAL POSITION
AS AT 31 JULY 2011

	NOTES	GROUP $ MILLION	
		AS AT 31 JULY 2011	AS AT 31 JULY 2010
ASSETS			
Current assets			
Cash and cash equivalents		**785**	559
Trade and other receivables		**2,279**	2,088
Inventories		**3,277**	2,870
Tax receivable		**29**	18
Derivative financial instruments		**1,100**	488
Other current assets		**90**	64
Total current assets		**7,560**	6,087
Non-current assets			
Property, plant and equipment		**4,326**	4,356
Equity accounted investments	6	**429**	458
Intangible assets		**2,748**	2,756
Deferred tax asset		**116**	100
Derivative financial instruments		**154**	214
Other non-current assets		**197**	198
Total non-current assets		**7,970**	8,082
Total assets		**15,530**	14,169
LIABILITIES			
Current liabilities			
Bank overdraft		**23**	25
Borrowings	8	**444**	902
Trade and other payables		**1,350**	1,251
Owing to suppliers		**1,679**	1,138
Tax payable		**19**	33
Derivative financial instruments		**58**	113
Provisions		**67**	92
Other current liabilities		**6**	4
Total current liabilities		**3,646**	3,558
Non-current liabilities			
Borrowings	8	**4,206**	4,022
Derivative financial instruments		**718**	496
Provisions		**106**	110
Deferred tax liability		**295**	293
Other non-current liabilities		**18**	23
Total non-current liabilities		**5,343**	4,944
Total liabilities		**8,989**	8,502
Net assets		**6,541**	5,667
EQUITY			
Co-operative shares		**5,261**	5,016
Retained earnings		**943**	547
Foreign currency translation reserve		**(217)**	(73)
Cash flow hedge reserve		**516**	141
Total equity attributable to Shareholders of the Parent		**6,503**	5,631
Non-controlling interests		**38**	36
Total equity		**6,541**	5,667

The accompanying notes form part of these summary financial statements

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 JULY 2011

	ATTRIBUTABLE TO SHAREHOLDERS OF THE PARENT						
GROUP $ MILLION	CO-OPERATIVE SHARES	RETAINED EARNINGS	FOREIGN CURRENCY TRANSLATION RESERVE	CASH FLOW HEDGE RESERVE	TOTAL	NON-CONTROLLING INTERESTS	TOTAL EQUITY
As at 1 August 2009	4,557	26	12	170	4,765	40	4,805
Profit for the year	–	669	–	–	669	16	685
Other comprehensive expense for the year	–	–	(85)	(29)	(114)	(2)	(116)
Total comprehensive income/(expense) for the year	–	669	(85)	(29)	555	14	569
Transactions with Shareholders in their capacity as Shareholders:							
Dividends paid to Shareholders of the Parent	–	(107)	–	–	(107)	–	(107)
Co-operative shares issued	617	–	–	–	617	–	617
Co-operative shares surrendered	(158)	–	–	–	(158)	–	(158)
Purchase of non-controlling interest	–	(41)	–	–	(41)	(6)	(47)
Dividend paid to non-controlling interests	–	–	–	–	–	(12)	(12)
As at 31 July 2010	5,016	547	(73)	141	5,631	36	5,667
As at 1 August 2010	**5,016**	**547**	**(73)**	**141**	**5,631**	**36**	**5,667**
Profit for the year	**–**	**754**	**–**	**–**	**754**	**17**	**771**
Other comprehensive income/(expense) for the year	**–**	**7**	**(144)**	**375**	**238**	**(4)**	**234**
Total comprehensive income/(expense) for the year	**–**	**761**	**(144)**	**375**	**992**	**13**	**1,005**
Transactions with Shareholders in their capacity as Shareholders:							
Dividends paid to Shareholders of the Parent	**–**	**(365)**	**–**	**–**	**(365)**	**–**	**(365)**
Co-operative shares issued	**404**	**–**	**–**	**–**	**404**	**–**	**404**
Co-operative shares surrendered	**(159)**	**–**	**–**	**–**	**(159)**	**–**	**(159)**
Dividend paid to non-controlling interests	**–**	**–**	**–**	**–**	**–**	**(11)**	**(11)**
As at 31 July 2011	**5,261**	**943**	**(217)**	**516**	**6,503**	**38**	**6,541**

The accompanying notes form part of these summary financial statements

CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 JULY 2011

	GROUP $ MILLION	
	31 JULY 2011	31 JULY 2010
Cash flows from operating activities		
Cash was provided from:		
– Receipts from customers	19,490	16,549
– Dividends received	63	55
– Tax received	5	32
Cash was applied to:		
– Payments to creditors and employees	(7,528)	(6,784)
– Payments for milk purchased	(10,780)	(8,322)
– Tax paid	(66)	(51)
Net cash flows from operating activities	1,184	1,479
Cash flows from investing activities		
Cash was provided from:		
– Proceeds from disposal of property, plant and equipment	9	22
– Proceeds from settlement of net investment hedges	20	50
– Proceeds from sale of Group entities and other business operations	184	222
Cash was applied to:		
– Acquisition of property, plant and equipment	(488)	(437)
– Acquisition of intangible assets	(135)	(55)
– Outflows on settlement of net investment hedges	(23)	(39)
– Acquisition of Group entities and other business operations	(55)	(14)
– Purchase of non-controlling interests	–	(48)
– Advances made to equity accounted investees	–	(50)
– Acquisition of other non-current assets	–	(5)
Net cash flows from investing activities	(488)	(354)
Cash flows from financing activities		
Cash was provided from:		
– Proceeds from borrowings	3,648	2,960
– Proceeds from issue of Co-operative shares	368	590
– Proceeds for Co-operative shares not yet issued	25	20
– Proceeds from settlement of borrowing derivatives	21	13
– Interest received	32	21
Cash was applied to:		
– Interest paid	(397)	(304)
– Repayment of borrowings	(3,548)	(3,549)
– Outflows on settlement of borrowing derivatives	(46)	(37)
– Surrender of Co-operative shares	(160)	(158)
– Dividends paid to non-controlling interests	(11)	(12)
– Dividends paid to Shareholders of the Parent	(365)	(107)
– Value Return paid to Shareholder Suppliers	–	(591)
Net cash flows from financing activities	(433)	(1,154)
Net increase/(decrease) in cash and cash equivalents	263	(29)
Cash and cash equivalents at the beginning of the year	534	542
Effect of exchange rate changes on cash balances	(35)	21
Cash and cash equivalents at the end of the year	762	534
Reconciliation of closing cash balances to the statement of financial position:		
Cash and cash equivalents	785	559
Bank overdraft	(23)	(25)
Closing cash balances	762	534

There were no material non-cash transactions during the year ended 31 July 2011, or the year ended 31 July 2010.

The accompanying notes form part of these summary financial statements

NOTES TO THE SUMMARY FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 JULY 2011

1 COST OF GOODS SOLD

	GROUP $ MILLION	
	31 JULY 2011	31 JULY 2010
Opening inventory	**2,870**	2,656
Cost of Milk:		
– New Zealand sourced	**10,235**	7,938
– Non-New Zealand sourced	**1,272**	1,029
Other purchases	**5,761**	5,222
Closing inventory	**(3,277)**	(2,870)
Closing balance	**16,861**	13,975

The cost of New Zealand sourced milk includes milk supplied by Shareholders, Supplier Premiums paid, and milk purchased from contract suppliers during the financial year. Prior periods have been restated on a consistent basis. This had no impact on the total cost of goods sold. Cost of non-New Zealand sourced milk, previously disclosed as other purchases, has been included in the Cost of Milk.

2 OPERATING PROFIT

		GROUP $ MILLION	
	NOTES	31 JULY 2011	31 JULY 2010
The following items have been included in arriving at operating profit:			
Auditors' remuneration to the auditors of the Parent:			
– Audit fees		**4**	4
– Other audit related services[1]		**1**	2
– Other services[2]		**1**	1
Operating lease expense		**64**	54
Restructuring and rationalisation costs		**10**	9
Research and development costs		**90**	98
Gain on acquisition of business	7	**(23)**	–
Net gain on disposal of equity accounted investments	6	**–**	(127)
Net gain on disposal of business[3]		**(26)**	–
Net loss on disposal of property, plant and equipment		**–**	3
Receipt for amendments to equity accounted investee arrangements		**–**	(41)
Donations[4]		**6**	–
Government grant income		**(6)**	(6)
Total employee benefits expense		**1,549**	1,460
Included in employee benefits expense are:			
– Contributions to defined contribution plans		**51**	42

1. Other audit related services include services for financial and information technology controls assurance and other attest services.
2. Other services include financial reporting and advisory services.
3. On 21 March 2011, Fonterra completed the sale of its Western Australia dairy business. The transaction resulted in a pre-tax gain on sale of $26 million, which was recognised in other operating income, as part of the ANZ segment result. It also resulted in a tax credit of $26 million due to the derecognition of the net deferred tax liability associated with the assets and liabilities that were disposed of, which was recognised as a reduction to the tax expense for the year.
4. Group donations paid of $6 million includes $2 million received from employees and Shareholders by the Fonterra Communities Assistance Trust (an entity controlled by Fonterra Co-operative Group Limited) and paid by the Fonterra Communities Assistance Trust to charities associated with the Christchurch earthquake.

3 SEGMENT REPORTING

The Group operates predominantly in the international dairy industry.

The Group has four reportable segments that are defined by product type and geographic area to reflect how the Group's operations are managed.

The reportable segments presented reflect the Group's management and reporting structure as viewed by the Fonterra Executive Committee, which comprise the Group's chief operating decision makers.

Transactions between segments are based on estimated market prices.

REPORTABLE SEGMENT	DESCRIPTION
Standard and Premium Ingredients (formerly described as Commodities and Ingredients)	Includes New Zealand Milk Supply, New Zealand Manufacturing, Global Portfolio Optimisation, Global Trade (including the China Ingredients business), Global Supply Chain, Global Ingredients and Foodservices operations in North Asia, North America and Europe (including equity accounted investments and Global Formulated Foods), and Corporate.
ANZ	Represents Fast Moving Consumer Goods (FMCG) operations in New Zealand (including export to the Pacific Islands) and all FMCG and Ingredients operations in Australia (including Milk Supply and Manufacturing).
Asia/AME	Represents FMCG operations in Asia (excluding North Asia), Africa and the Middle East.
Latam	Represents FMCG operations in Chile and equity accounted investments in South America.

3 SEGMENT REPORTING CONTINUED

$ MILLION	NOTES	STANDARD AND PREMIUM INGREDIENTS	ANZ	ASIA/AME	LATAM	ELIMINATIONS	TOTAL GROUP
Segment income statement							
Year ended 31 July 2011							
External revenue		13,779	3,579	1,687	826	–	19,871
Inter-segment revenue		1,800	781	–	4	(2,585)	–
Revenue from sale of goods		15,579	4,360	1,687	830	(2,585)	19,871
Cost of Milk – New Zealand sourced		(10,235)	–	–	–	–	(10,235)
Other cost of goods sold		(4,131)	(3,451)	(1,088)	(558)	2,602	(6,626)
Cost of goods sold		(14,366)	(3,451)	(1,088)	(558)	2,602	(16,861)
Segment gross profit		1,213	909	599	272	17	3,010
Selling and marketing expenses		(93)	(154)	(264)	(85)	–	(596)
Distribution expenses		(155)	(244)	(35)	(53)	–	(487)
Administrative expenses		(415)	(164)	(88)	(46)	13	(700)
Other operating expenses		(203)	(99)	(25)	(17)	8	(336)
Segment operating expenses		(866)	(661)	(412)	(201)	21	(2,119)
Other operating income		118	39	2	27	(21)	165
Net foreign exchange losses		(75)	(13)	(3)	–	–	(91)
Share of profit of equity accounted investees		40	–	–	23	–	63
Segment earnings before net finance costs and tax		430	274	186	121	17	1,028
Non-recurring items		1	(22)	–	(2)	–	(23)
Normalised segment earnings before net finance costs and tax		431	252	186	119	17	1,005
Non-recurring items							23
Finance income							32
Finance costs							(438)
Tax expense							149
Profit for the year							771
Profit for the year includes the following amounts:							
Depreciation		(316)	(72)	(6)	(20)	–	(414)
Amortisation		(62)	(9)	(3)	(1)	–	(75)
Royalty income from equity accounted investees		–	–	–	21	–	21
Non-recurring items consist of the following amounts:							
Impact of Christchurch earthquakes and Japan earthquake and tsunami		14	4	–	–	–	18
Gain on disposal of Western Australia dairy business	2	–	(26)	–	–	–	(26)
Gain on acquisition of RD1	7	(23)	–	–	–	–	(23)
Impact of 2010 Chilean earthquake		–	–	–	(5)	–	(5)
Other		10	–	–	3	–	13
Total non-recurring items		1	(22)	–	(2)	–	(23)
Segment asset information:							
As at and for the year ended 31 July 2011							
Equity accounted investments		216	–	–	213	–	429
Capital expenditure		470	135	17	22	–	644

3 SEGMENT REPORTING CONTINUED

$ MILLION	NOTES	STANDARD AND PREMIUM INGREDIENTS	ANZ	ASIA/AME	LATAM	ELIMINATIONS	TOTAL GROUP
Segment income statement							
Year ended 31 July 2010							
External revenue		11,225	3,233	1,537	731	–	16,726
Inter-segment revenue		1,532	570	–	7	(2,109)	–
Revenue from sale of goods		12,757	3,803	1,537	738	(2,109)	16,726
Cost of Milk – New Zealand sourced		(7,938)	–	–	–	–	(7,938)
Other cost of goods sold		(3,843)	(2,855)	(949)	(499)	2,109	(6,037)
Cost of goods sold		(11,781)	(2,855)	(949)	(499)	2,109	(13,975)
Segment gross profit		976	948	588	239	–	2,751
Selling and marketing expenses		(79)	(158)	(279)	(74)	–	(590)
Distribution expenses		(149)	(244)	(31)	(50)	–	(474)
Administrative expenses		(360)	(162)	(83)	(41)	14	(632)
Other operating expenses		(177)	(95)	(25)	(10)	4	(303)
Segment operating expenses		(765)	(659)	(418)	(175)	18	(1,999)
Other operating income		265	8	2	20	(18)	277
Net foreign exchange (losses)/gains		(3)	2	(6)	–	–	(7)
Share of profit of equity accounted investees		33	–	–	23	–	56
Segment earnings before net finance costs and tax		506	299	166	107	–	1,078
Non-recurring items		(190)	4	–	12	–	(174)
Normalised segment earnings before net finance costs and tax		316	303	166	119	–	904
Non-recurring items							174
Finance income							21
Finance costs							(334)
Tax expense							(80)
Profit for the year							685
Profit for the year included the following amounts:							
Depreciation		(317)	(74)	(6)	(19)	–	(416)
Amortisation		(57)	(8)	(3)	–	–	(68)
Royalty income from equity accounted investees		3	–	–	20	–	23
Non-recurring items consist of the following amounts:							
Receipt for amendments to equity accounted investee arrangements		(41)	–	–	–	–	(41)
Gain on sale of Arla	6	(127)	–	–	–	–	(127)
Impact of Chilean earthquake		–	–	–	12	–	12
Other		(22)	4	–	–	–	(18)
Total non-recurring items		(190)	4	–	12	–	(174)
Segment asset information:							
As at and for the year ended 31 July 2010							
Equity accounted investments		231	–	–	227	–	458
Capital expenditure		378	74	13	27	–	492

3 SEGMENT REPORTING CONTINUED

$ MILLION	31 JULY 2011	31 JULY 2010
Entity wide products and services:		
Consumer goods	**5,248**	4,908
Ingredients and other revenue	**14,623**	11,818
Revenue from sale of goods	**19,871**	16,726

$ MILLION	EUROPE	CHINA	ASIA	AUSTRALIA	NEW ZEALAND	USA	REST OF WORLD	TOTAL
Geographical segment external revenue:								
Year ended 31 July 2011	**1,269**	**1,877**	**5,735**	**2,664**	**1,560**	**1,566**	**5,200**	**19,871**
Year ended 31 July 2010	1,287	1,227	4,952	2,387	1,337	1,622	3,914	16,726

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

$ MILLION	AUSTRALIA	NEW ZEALAND	USA	REST OF WORLD	TOTAL
Geographical segment reportable non-current assets:					
As at 31 July 2011	**1,011**	**4,901**	**124**	**1,664**	**7,700**
As at 31 July 2010	1,077	4,790	136	1,765	7,768

$ MILLION	AS AT 31 JULY 2011	AS AT 31 JULY 2010
Reconciliation of geographical segment non-current assets to total non-current assets:		
Geographical segment non-current assets	**7,700**	7,768
Deferred tax asset	**116**	100
Derivative financial instruments	**154**	214
Total non-current assets	**7,970**	8,082

4 CONTINGENT LIABILITIES

The Group has no contingent liabilities as at 31 July 2011 (31 July 2010: nil).

In the normal course of its business, Fonterra, its subsidiaries and equity accounted investees are exposed to claims, legal proceedings and arbitrations that may in some cases result in costs to the Group. The Directors believe that these have been adequately provided for and appropriately disclosed by the Group and that there are no additional legal proceedings or arbitrations that are pending at the date of these summary financial statements that require provision or disclosure.

5 CO-OPERATIVE SHARES

	CO-OPERATIVE SHARES (THOUSANDS)
Balance at 1 August 2009	1,251,291
Issued	136,415
Surrendered	(34,863)
Balance at 31 July 2010	1,352,843
Balance at 1 August 2010	**1,352,843**
Issued	**89,458**
Surrendered	**(35,356)**
Balance at 31 July 2011	**1,406,945**

Co-operative shares

Each Shareholder supplying milk to the Company in a season is required to hold one Co-operative share (share) for each kilogram of milksolids obtainable from milk supplied to the Company by that Shareholder, excluding milk supplied by that Shareholder under contract supply or as unshared supply, in that season. This is known as the share standard. A Shareholder supplying under contract must hold at least 1,000 shares.

In addition, each Shareholder is able to hold further shares up to 20% of the share standard, so that they can hold shares of up to 120% of the number they are required to hold under the share standard.

The rights attaching to shares include:

- voting rights on a poll or postal ballot of one vote per 1,000 kilograms of milksolids obtainable from milk supplied to the Company by a Shareholder during the season preceding that in which a poll or postal ballot is taken, less milksolids supplied under contract supply or as unshared supply;
- rights to any dividends declared by the Board; and
- rights to share in any surplus on liquidation of the Company.

Shares are valued on the basis of a Restricted Share Value. The value of Fonterra shares is determined by the Board on an annual basis, for each season, after having regard to a value range determined by an independent valuer.

The use of a Restricted Share Value represents a constitutional change to the fair value method used before the 31 May 2009 valuation and was expected to result in a lower share valuation. To recognise the impact on the share price from such a change in valuation approach, there is a transition period to the new Restricted Share Value approach, during which the share is valued separately under the Restricted Share Value approach and the Fair Value approach. During the transition period the share price cannot fall below a base price. The current base price is $4.52 per share, but this could fall if the mid-point of the range determined by the Fair Value approach falls below $4.52. If the Restricted Share Value is less than the base price, then the base price at that time will be used as the share value. Once the Restricted Share Value is greater than the base price, the transition period is deemed to have ended and the Restricted Share Value will be used from that point onwards.

The Restricted Share Value for the 2011/12 season has been set by the Board at $4.52 per share (2010: Restricted Share Value of $4.52 per share).

Shareholders may elect, within the application period (which must run, as a minimum, from 15 December to 28 February) to purchase and surrender shares. Shareholders may also elect to purchase additional shares over and above the share standard during a period set by the Board (which is currently from 1 June to 30 September). Shareholders may elect to transact at the June price, which is the share price for the coming season, or under the default price mechanism. This mechanism sets a price range of +/-7.5% of an interim share price set by the Board in the prior December. If the June price falls within the +/-7.5% price range, Shareholders will transact at the June price. If the June price is above or below the price range, Shareholders will transact at the upper or lower limit of the price range respectively.

If a Shareholder decreases supply during a season, the number of shares held will be re-apportioned between the number of minimum required shares (calculated using the share standard) and the number of any additional shares that may be held.

Shares held in excess of the number required to be held by the share standard can be surrendered at the election of the Shareholder. However shares representing greater than 120% of the number required by the share standard will automatically be surrendered, at the then prevailing share price.

5 CO-OPERATIVE SHARES CONTINUED

Payment for the surrender of shares may be made at the option of the Company by:

- cash; or
- the issue of Capital Notes.

The Company also has the option to pay the surrender value in special circumstances by the issue of redeemable preference shares.

The expected cash outflow on redemption or repurchase of the shares is dependent on the share value at that time, the number of shares redeemed or repurchased and the instrument used to settle the obligation, and accordingly cannot be reliably estimated.

If a Shareholder increases supply during a season, any additional shares held will be used first to satisfy the increased minimum required shares under the share standard. If no, or insufficient, additional shares are held, the Shareholder must either:

- acquire the extra shares required under the share standard at the current season share price; or
- request unshared supply (if available).

If the Company decides to make unshared supply available, a Shareholder's entitlement to it cannot exceed 20% of that Shareholder's share standard for that season. If a Shareholder is granted unshared supply, they will not be required to purchase shares for the quantity elected. However, they will receive a lower milk payment for this unshared supply.

Shares acquired by Shareholders may be paid by:

- cash; or
- the redemption of any Capital Notes held (at the discretion of the Company).

On 30 June 2010 Shareholders approved constitutional changes that allow the Board to work towards implementation of capital structure changes which have the following key features:

- The establishment of a platform to enable share trading among Shareholder Suppliers at a well-discovered market price.
- The establishment of a Fonterra Shareholders' Fund that would acquire from Shareholders the right to receive dividends and the gain/loss from any change in the underlying value of the shares, whilst Shareholder Suppliers retain voting rights and the access to milk payments attached to the shares.

There is no current year impact to the Company's capital structure arising out of the approval granted on 30 June 2010.

Dividends paid
All shares are eligible to receive a dividend if declared by the Board. On 22 September 2010, the Board declared a dividend of 19.0 cents per share (totalling $255 million), paid on 20 October 2010 to the Shareholders on the share register at 31 May 2010.

On 23 March 2011, the Board declared an interim dividend of 8.0 cents per share (totalling $110 million), paid on 20 April 2011 to the Shareholders on the share register at 31 March 2011.

6 EQUITY ACCOUNTED INVESTMENTS

The movement in the carrying value of equity accounted investees is:

	GROUP $ MILLION	
	31 JULY 2011	31 JULY 2010
Opening balance	**458**	506
Share of profit after tax	**63**	56
Additional investments in existing equity accounted investees	**4**	14
Derecognised as a result of a business combination	**(10)**	–
Acquired as a result of a business combination	**20**	–
Impairment of equity accounted investments	**(2)**	–
Foreign currency translation	**(48)**	(63)
Dividends received	**(63)**	(55)
Share of equity accounted investees' reserve movements	**7**	–
Closing balance	**429**	458
Amount of goodwill in carrying value of equity accounted investees:		
Opening balance	**218**	241
Closing balance	**199**	218

In the year ended 31 July 2011, Fonterra completed the purchase of the remaining 50% of RD1 Limited, which resulted in RD1 Limited becoming a subsidiary of Fonterra. Further details are set out in Note 7.

In the year ended 31 July 2010, Fonterra disposed of its 25% interest in AFF P/S. Amongst the ongoing arrangements Fonterra will continue to licence the Anchor brand to AFF P/S and will continue to supply butter. The transaction and wider arrangements resulted in a net pre-tax gain of $127 million. The gain formed part of the Standard and Premium Ingredients segment and was included within other operating income for the year ended 31 July 2010.

The ownership interest of the following entities is 50% 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 (%)	
OVERSEAS EQUITY ACCOUNTED INVESTEES	COUNTRY OF INCORPORATION	AS AT 31 JULY 2011	AS AT 31 JULY 2010
DPA Manufacturing Holdings Limited[1]	Bermuda	**50**	50
Dairy Partners Americas Brasil Limitada[1]	Brazil	**50**	50
Ecuajugos S.A.[1]	Ecuador	**50**	50
DMV Fonterra Excipients GmbH & Co KG[1]	Germany	**50**	50
Dairy Industries (Jamaica) Limited[1]	Jamaica	**50**	50
Dairiconcepts, L.P.[1]	USA	**50**	50
Dairiconcepts Management, L.L.C.[1]	USA	**50**	50
Corporacion Inlaca, C.A.[1]	Venezuela	**25**	25

1. Balance date 31 December.

	OWNERSHIP INTERESTS (%)	
NEW ZEALAND EQUITY ACCOUNTED INVESTEES	AS AT 31 JULY 2011	AS AT 31 JULY 2010
International Nutritionals Limited[1]	**50**	–

1. Balance date 31 May. International Nutritionals Limited is 50% owned by RD1 Limited. RD1 Limited became a subsidiary during the year as set out in Note 7.

7 BUSINESS COMBINATIONS

On 1 July 2011, the Group completed the purchase of the remaining 50% of RD1 Limited. The Group has recorded a gain of $23 million relating to this business combination. This gain represents the difference between the carrying value of the Group's equity accounted investment in RD1 at the time of acquisition of the remaining 50%, and the fair value of that pre-existing interest. This gain was recognised in other operating income, in the Standard and Premium Ingredients segment result. This transaction is not considered material and therefore no further disclosure has been made.

There were no material business combinations during the year ended 31 July 2010.

8 BORROWINGS

	GROUP $ MILLION	
	AS AT 31 JULY 2011	AS AT 31 JULY 2010
Opening balance	**4,924**	5,794
New issues		
Bank loans	**2,298**	2,051
Finance leases	–	75
Commercial paper	**817**	612
Retail bonds	–	150
Medium term notes	**533**	72
	3,648	2,960
Repayments		
Bank loans	**(2,396)**	(2,223)
Finance leases	**(9)**	(5)
Commercial paper	**(990)**	(710)
Medium term notes	**(153)**	(611)
	(3,548)	(3,549)
Other movements		
Amortisation of discount	**7**	13
Changes in fair value	**(6)**	82
Changes due to foreign currency translation	**(375)**	(376)
	(374)	(281)
Closing balance	**4,650**	4,924

	GROUP $ MILLION	
	AS AT 31 JULY 2011	AS AT 31 JULY 2010
Net interest bearing debt position		
Total borrowings	**4,650**	4,924
Cash and cash equivalents	**(785)**	(559)
Interest bearing advances included in other non-current assets	**(122)**	(122)
Bank overdraft	**23**	25
Net interest bearing debt	**3,766**	4,268
Value of derivatives used to manage changes in hedged risks and other foreign exchange movements on debt	**565**	226
Economic net interest bearing debt[1]	**4,331**	4,494

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

	GROUP	
	AS AT 31 JULY 2011	AS AT 31 JULY 2010
Net tangible assets per security[1]		
$ per listed debt security on issue	**3.60**	2.76
$ per Co-operative share on issue	**2.70**	2.15
Listed debt securities on issue (million)	**1,053**	1,053
Co-operative shares on issue (million)	**1,407**	1,353

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

9 FINANCIAL RISK MANAGEMENT

Overview

Global financial and commodity markets remain volatile. The nature of Fonterra's business is such that managing risks in the foreign exchange, interest rate, commodity, credit and liquidity markets is critical to minimising the volatility in returns to Shareholders.

The Board has overall responsibility for the establishment and oversight of the Group's financial risk management framework. The Board:

- has established risk management policies and procedures to identify, analyse and, where appropriate, manage the risks faced by the Group;
- has approved a Treasury Policy that covers appropriate risk limits and controls (including, but not limited to, delegated authority levels and authorised use of various financial instruments); and
- monitors risks and adherence to approved limits.

The Group's overall financial risk management programme focuses primarily on maintaining a prudent risk profile that provides flexibility to implement the Group's strategies, while ensuring the optimisation of the return on assets. Risk management is predominantly carried out by a central treasury department (Group Treasury), which ensures compliance with the risk management policies and procedures set by the Board.

During the year in order to manage financial risks, the key risk management activities undertaken by the Group included, but were not limited to, the following:

Capital structure

Fonterra continues to work towards establishing trading among farmers. Should necessary changes to the Dairy Industry Restructuring Act 2001 (DIRA) to give effect to this be approved by the government, the Company's obligations under DIRA to redeem Co-operative shares will be removed. These capital structure changes are significant steps for Fonterra, and further detail is given in Note 5.

Bank facility renewal

Fonterra's banking facilities are renewed at least annually. On 31 July 2011, Fonterra had $3,715 million (31 July 2010: $3,687 million) of undrawn committed facilities.

Debt to debt plus equity ratio

For the 12 months to 31 July 2011, the Board set a target debt to debt plus equity ratio of 45% to 50%. As a result of the above activities and close management of the financial risks faced by Fonterra, the economic debt to debt plus equity ratio has reduced from 44.9% at 31 July 2010 to 41.8% at 31 July 2011.

For further details in respect of financial risks faced by the Group refer to the Group's full consolidated financial statements.

10 SUBSEQUENT EVENTS

On 21 September 2011, the Board of Directors declared a final dividend of 22 cents per share, payable on 20 October 2011 to the Shareholders on the share register at 31 May 2011.

There were no other material events subsequent to 31 July 2011 that would impact these summary financial statements.

AUDITORS' REPORT
TO THE SHAREHOLDERS OF FONTERRA CO-OPERATIVE GROUP LIMITED

pwc

INDEPENDENT AUDITORS' REPORT ON SUMMARY FINANCIAL STATEMENTS TO THE SHAREHOLDERS OF FONTERRA CO-OPERATIVE GROUP LIMITED

We have audited the accompanying summary financial statements of Fonterra Co-operative Group Limited on pages 46 to 61, which comprise the statement of financial position as at 31 July 2011, the income statement, statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and related notes, which are derived from the audited financial statements of Fonterra Co-operative Group Limited for the year ended 31 July 2011.

The summary financial statements do not contain all the disclosures required for full financial statements under generally accepted accounting practice in New Zealand. Reading the summary financial statements, therefore, is not a substitute for reading the audited financial statements for the year ended 31 July 2011.

Directors' Responsibility for the Summary Financial Statements

The Directors are responsible for the preparation of the summary financial statements in accordance with FRS-43: Summary Financial Statements.

Auditors' Responsibility

Our responsibility is to express an opinion on the summary financial statements based on our procedures, which were conducted in accordance with International Standard on Auditing (New Zealand) 810: Engagements to Report on Summary Financial Statements.

We carry out other assignments on behalf of the Company and the Group in the areas of other audit related services, international accounting standard advisory services, transaction services and taxation compliance services. Partners and employees of our firm may deal with the Company and the Group on normal terms within the ordinary course of trading activities of the Company and the Group. These matters have not impaired our independence as auditors of the Company and the Group.

Opinion on the Financial Statements

Our audit of the financial statements for the year ended 31 July 2011 was completed on 21 September 2011 and our unmodified opinion was issued on that date.

Opinion

In our opinion, the summary financial statements derived from the audited financial statements of Fonterra Co-operative Group Limited for the year ended 31 July 2011 and are consistent, in all material respects, with those financial statements, in accordance with FRS-43.

Restriction on Distribution or Use

This report is made solely to the Company's shareholders, as a body. Our audit work has been undertaken so that we might state to the Company's shareholders those matters which we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's shareholders, as a body, for our audit work, for this report or for the opinions we have formed.

PricewaterhouseCoopers

Chartered Accountants — Auckland

21 September 2011

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CURRENT CREDIT RATING STATUS

Standard & Poor's has rated the Company A+ with a rating outlook of stable. Fitch has rated the Company AA- with a rating outlook of stable. Retail Bonds have been rated the same as the Company by both Standard & Poor's and Fitch. Capital Notes which are subordinate to other Fonterra debt issued are rated A by Standard & Poor's and A+ by Fitch. The ratings were last affirmed in December 2010 by Standard & Poor's and in May 2011 by Fitch.

EXCHANGE RULINGS AND WAIVERS

NZX Limited (NZX) has ruled that Capital Notes do not constitute "equity securities" under its Listing Rules (Rules). This means that where Capital Notes are quoted on NZX's debt market (NZDX), the Company is not required to comply with certain Rules which apply to an issuer of quoted equity securities.

NZX has granted waivers from NZDX Rule 11.1.1 to enable Fonterra to decline to accept or register transfers of Capital Notes or Retail Bonds (NZDX listed debt securities FCGHA, FCG010 and FCG020) if such transfer would result in the transferor holding or continuing to hold Capital Notes or Retail Bonds with a face value or principal amount of less than $5,000 or if such transfer is for an amount of less than $1,000 or multiple thereof. The effect of these waivers is that the minimum holding amount in respect of the Capital Notes and Retail Bonds will at all times be $5,000 in aggregate and that Retail Bonds can only be transferred in multiples of $1,000.

NZX has also granted a waiver from NZDX Rule 5.2.3 in respect of Retail Bond FCG020 to enable that Bond to be quoted on the NZDX market even though it did not meet the requirement that at least 500 members of the public held at least 25% of the Bonds being issued.

FIVE YEAR SUMMARY

	JULY 2011	JULY 2010	JULY 2009	JULY 2008[1]	MAY 2007
SHAREHOLDER RETURNS					
Payout ($ per kgMS)					
Farmgate Milk Price[2]	**7.60**	6.10	4.72	7.59	3.87
Distributable Profit[3]	**0.65**	0.60	0.49	0.31	0.59
Payout (before retentions)	**8.25**	6.70	5.21	7.90	4.46
Less retentions	**(0.35)**	(0.33)	(0.01)	(0.24)	–
Payout[4,5]	**7.90**	6.37	5.20	7.66	4.46
Fair Value Share price ($) set for the next season	**4.52**	4.52	4.52	5.57	6.79
Total Shareholder return[6]	**6.6%**	6.0%	(10.2%)	(16.9%)	12.5%
OPERATING PERFORMANCE					
Average commodity prices (USD per MT FOB)					
Whole Milk Powder	**3,841**	3,313	2,379	4,605	2,687
Skim Milk Powder	**3,521**	3,020	2,205	4,325	2,748
Butter	**4,583**	3,573	2,343	3,755	1,848
Cheese	**4,285**	3,819	3,114	4,894	2,806
Source: Oceania Export Series, Agricultural Marketing Service, US Department of Agriculture					
Average NZD/USD spot exchange rate applying throughout the year[7]	**0.77**	0.71	0.60	0.77	0.68
Fonterra's average NZD/USD conversion rate[8]	**0.72**	0.67	0.67	0.74	0.67
Revenue ($ million)					
Ingredients and other revenue	**14,623**	11,818	10,987	14,267	9,755
Consumer revenue	**5,248**	4,908	5,048	5,245	3,932
Total revenue	**19,871**	16,726	16,035	19,512	13,687
Dairy ingredients manufactured in New Zealand (000s MT)	**2,143**	2,058	2,021	2,021	2,082
Total ingredients sales volume (000s MT)	**2,486**	2,392	2,310	2,633	2,458
Segment profit ($ million)[9]					
Standard & Premium Ingredients	**430**	506	584	340	918
ANZ	**274**	299	240	220	200
Asia/AME	**186**	166	63	(39)	49
Latam	**121**	107	106	129	58
Eliminations	**17**	–	(3)	(36)	41
Segment profit	**1,028**	1,078	990	614	1,266
Non-recurring items	**(23)**	(174)	(32)	145	23
Normalised segment earnings	**1,005**	904	958	759	1,289
Profit for the year attributable to Shareholders ($ million)[10]	**754**	669	599	272	862

1. On 24 January 2008 Fonterra's Board resolved to change the Company's balance date to 31 July from 31 May, consequently the financial period for 2008 was a 14 month period to 31 July 2008.
2. From the beginning of the 2009 season the Farmgate Milk Price has been determined in accordance with the Farmgate Milk Price Manual and is independently audited.
3. On 18 November 2009 Shareholders approved stages one and two of the capital structure changes. As a result of the changes to the capital structure, all shares are eligible to receive a dividend if declared by the Board. Previously, in addition to the Farmgate Milk Price, returns to Shareholder Suppliers were by way of the Value Return payment. Distributable Profit per share for the years ended 31 July 2010 and 31 July 2011 has been calculated as Distributable Profit divided by the number of shares on issue as at 31 May. For the years ended 31 July 2009 and prior, Distributable Profit was calculated per kgMS.
4. Average Payout for a 100% share-backed supplier.
5. Payout to Shareholder Suppliers for 2007 is based on the actual Payout calculation and does not incorporate subsequent adjustments relating to the transition to New Zealand Equivalents to International Financial Reporting Standards.
6. Total Shareholder return reflects movements in the Fonterra Fair Value Share (FVS) price plus a return on investment, represented by dividends paid or Value Return payments per share. In 2009, as part of the capital structure changes, the FVS price has been valued on a restricted market basis. The FVS has been held at a base price of $4.52 until the price based on a restricted market value catches up. In 2010 and 2011 this has meant that Total Shareholder Returns only reflect dividends paid and do not include any movements in the FVS.
7. Average spot exchange rate is the average of the daily spot rates for the financial period.
8. Fonterra's average conversion rate is the rate that Fonterra has converted net US dollar receipts into NZ dollars based on the hedge cover in place.
9. Represents segment profit before unallocated finance income, finance costs and tax. 2007 and 2008 have been restated to be on a consistent basis with 2009, 2010 and 2011.
10. Profit after tax attributable to Shareholders for 2009, 2008 and 2007 has been restated to recognise the tax effects of distributions to Shareholders within tax expense in the income statement. This was previously recorded directly in equity.

	JULY 2011	JULY 2010	JULY 2009	JULY 2008[1]	MAY 2007
CAPITAL EMPLOYED ($ million)					
Total assets employed	**15,530**	14,169	14,117	14,439	13,494
Average net assets[11]	**10,772**	10,433	10,975	10,702	10,333
Total equity	**6,541**	5,667	4,805	4,269	4,978
Equity excluding cash flow hedge reserve	**6,025**	5,526	4,635	4,357	4,829
Net interest bearing debt	**3,766**	4,268	5,166	5,860	4,971
Economic net interest bearing debt[12]	**4,331**	4,494	5,221	5,931	5,250
Return on net assets[11]	**9.3%**	8.7%	9.2%	7.4%	12.7%
Headline debt to debt plus equity ratio[13]	**38.5%**	43.6%	52.7%	57.4%	50.7%
Economic debt to debt plus equity ratio[13]	**41.8%**	44.9%	53.0%	57.6%	52.1%
STAFF EMPLOYED					
Total staff employed (000s, permanent full time equivalents)	**16.8**	15.8	15.6	15.9	16.4
New Zealand	**10.8**	9.8	9.5	9.5	10.0
Overseas	**6.0**	6.0	6.1	6.4	6.4

	MAY 2011	MAY 2010	MAY 2009	MAY 2008	MAY 2007
SEASON STATISTICS[14]					
Total NZ milk collected (million litres)	**15,427**	14,746	14,764	13,862	14,340
Highest daily volume collected (million litres)	**76.8**	72.3	73.7	71.6	70.5
NZ Shareholder supply milksolids collected (million kgMS)	**1,320**	1,256	1,227	1,183	1,243
NZ contract and tactical supply milksolids collected (million kgMS)	**26**	30	54	9	3
NZ milksolids collected (million kgMS)	**1,346**	1,286	1,281	1,192	1,246
Total number of Shareholders at 31 May	**10,485**	10,463	10,537	10,724	10,921
Total number of sharemilkers at 31 May	**3,928**	3,733	3,990	3,946	3,857
Total number of shares at 31 May (million)	**1,377**	1,343	1,216	1,261	1,280

11. Return on net assets (RONA) is derived by dividing profit before non-recurring items, finance costs and tax (as reported in financial statements, with exception of the 14 month period ended 31 July 2008) by 13 month average net assets (excluding net debt and deferred tax). 2008 RONA is based on unaudited management results for the 12 months to 31 July 2008.

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

13. Headline debt to debt plus equity ratio is before taking account of the effect of debt hedging. Economic debt to debt plus equity includes the effect of debt hedging.

14. All Season statistics are based on the 12 month milk Season of 1 June – 31 May.

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