

DAIRY HOLDINGS LIMITED – COMPANY PROFILE 2016|17

1. BACKGROUND

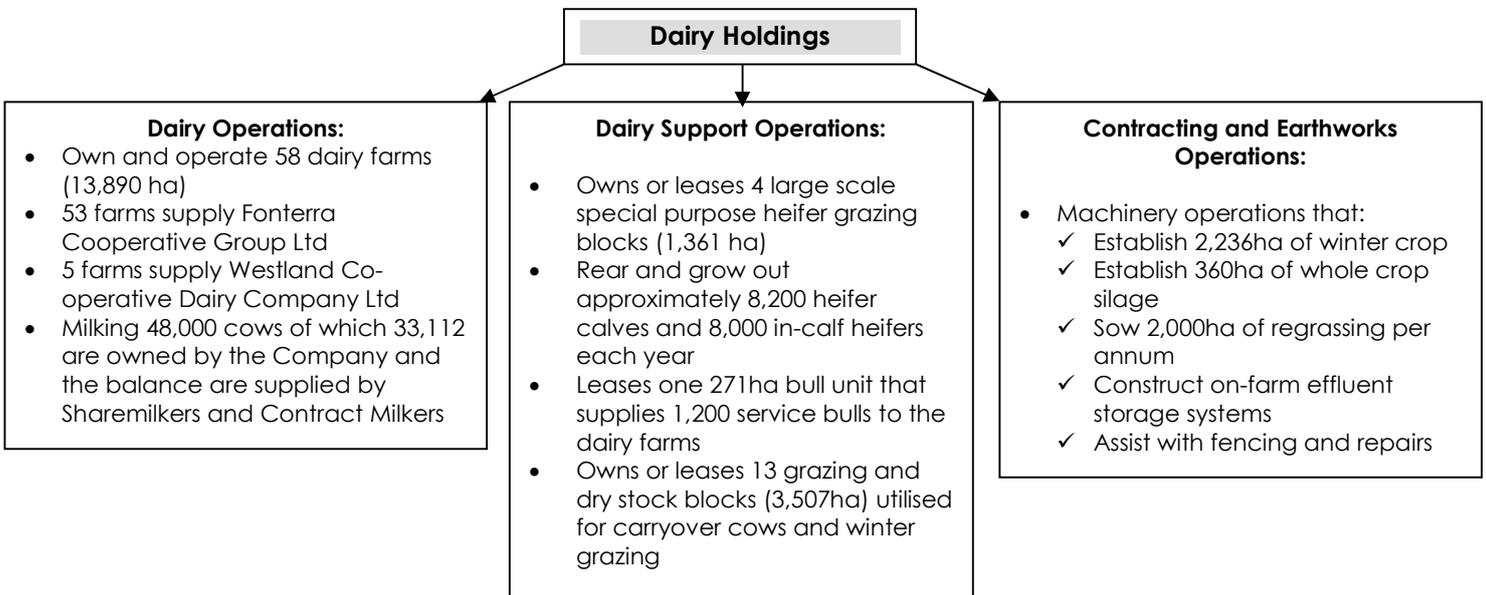
- 1.1 Dairy Holdings Limited (Dairy Holdings) is a New Zealand registered company with 100% of its farming assets in the South Island of New Zealand.
- 1.2 Dairy Holdings’ registered office is in Timaru.
- 1.3 The extensive South Island operations are undertaken through wholly owned subsidiary companies and are managed from the Group’s Timaru office. These operations commenced in June 2001 following the purchase by the Group of the major Canterbury and North Otago dairy properties from the corporate farming entities Tasman Agriculture Limited and Dairy Brands Limited.

2. OPERATIONS

2.1 Structure

Since June 2001, the South Island operations have principally been located in Canterbury and North Otago, although 8 dairy units are located in West Otago/ Southland and 5 dairy units are at Springs Junction/Murchison on the West Coast.

The corporate structure of the New Zealand operations is as follows:



2.2 Profile of Operations

The New Zealand dairy operations of Dairy Holdings are conducted through four autonomous wholly owned subsidiary groups, Dairy Farm Holdings Ltd, Clumber Farms Ltd, Livestock Holdings Ltd, and West Coast (Dairy) Ltd. For the 2016/17 season, these groups will operate 58 dairy units on 13,890 effective hectares, milking 48,000 cows to produce approximately 16.87 million kilograms of milk solids.

Of these dairy farms, 12 have been operated from 1 June 2016 under 50/50 and Variable Order Sharemilking agreements, whereby Dairy Holdings supplies the land, buildings and infrastructure, and the Sharemilker provides greater than 50% of the livestock, and all of the plant and machinery necessary to operate the farm; 2 under Lower Order Sharemilking agreements, where the Sharemilker provides the plant and machinery necessary to operation the farm and may provide some of the livestock; 44 under Contract Milking Agreements where the Milker provides the plant and machinery.

Under the 50/50 and Variable Order Sharemilking agreements, Sharemilkers are paid 42-50% of the value of milk solids produced and receive all livestock sale proceeds as the owner of the majority of the stock. The Sharemilker is responsible for 42-50% of all feed and grazing costs, all labour and dairy shed operating costs, and all repair and maintenance, insurance and ownership costs in respect of the Sharemilkers plant and machinery.

Under the Lower Order agreements, Sharemilkers are paid a fixed percentage of the value of milk solids produced and provide the labour to operate the farm and pay a fixed percentage of the milking cow feed costs. Revenue from calves over the replacement numbers, accrue to the Sharemilker, but, as owner of the livestock, Livestock Holdings retains proceeds from cull cows sold. All animal health and breeding expenses are paid by the farm owner.

Under the Contract Milking Agreement, the Milker is paid a fixed payment per kilogram of milk solids produced and provide the labour to operate the farm and pay a fixed percentage of the milking cow feed costs. Revenue from calves over the replacement numbers, accrue to the Milker, but, as owner of the livestock, Livestock Holdings retains proceeds from cull cows sold. All animal health and breeding expenses are paid by the farm owner.

On managed farms, all income accrues and all costs are borne by the farm owner.

Three Farm Operations Managers and four Farm Supervisors oversee the day-to-day farm operations and are generally responsible for about 10 farms each. Five of the Operations Managers/Farm Supervisors also operate their own dairy units, or farm under Sharemilking agreements with the Company.

Dairy Holdings dairy farms are budgeted to produce 16.87 million kilograms of milk solids in the season ended 31 May 2017 supplying the processor, Fonterra Cooperative Group Limited with 15.62 million kilograms of milk solids and 1.25 million kilograms of milk solids to Westland Co-operative Dairy Company Ltd.

In addition to its dairy farming operation, Dairy Holdings through its wholly owned subsidiary Livestock Holdings Ltd operates 17 large-scale grazing and dry-stock properties in Springs Junction, Mid-Canterbury, Northern Southland and West Otago.

The dry-stock operations are responsible for the management and return of approximately 8,000 in-calf heifer replacements to the dairy units each year. In addition to the dairy heifer operations, the grazing blocks also provide dairy cow winter grazing and carry dairy service bulls and carryover cows as seasonal conditions allow.

2.3 Business Objective

The Dairy Holdings' operations are driven by the overriding objective of maximising profitability by adopting systems that increase the quantity of pasture grown and harvested.

This business ethos is based on research conducted through Ruakura and more recently the Lincoln University Dairy Farm that provides the base system for successful and profitable dairy farming. This system initially promoted by Dr C P McMeeken and subsequently by Dr Arnold Bryant, continues to be supported through the use of high comparable stocking rate systems by DairyNZ.

Dairy Holdings' Shareholders, Directors and Management are committed to achieving consistent and repeatable levels of profitability predicated on simple, pasture based management systems.

To ensure systems are followed and that Dairy Holdings is regarded as an "employer of choice", Supervisors, Sharemilkers, Managers and Staff are interviewed annually by Investors in People NZ (IIPNZ) to ensure minimum standards are achieved or exceeded. Accredited farms are able to use the Investors in People logo when advertising for staff.

This simple pastoral based farming approach has already enabled a significant number of the Group's 300 farm staff to progress through the Group's employment structure to Contract Milking, Lower Order Sharemilking and 50/50 Sharemilking positions, and subsequently farm ownership.

The drive to maximise shareholder profitability, while at the same time satisfying staff career progression, has resulted in approximately one-quarter of the Group's New Zealand farms being operated by 50/50 or Variable Order Sharemilkers that own greater than 50% of the herd on the farm. The balance of the farms are operated by Managers, Contract Milkers and Lower Order Sharemilkers. This structure ensures all operators remain focused and motivated while growing their businesses within the Group.

This systems based approach to dairy farming, enables the Group to now operate a significant corporate farming operation in New Zealand.

3. OUTLOOK

The Board believes the outlook for Dairy Holdings is sound.

New Zealand is an active participant in the international dairy commodity market and commodity prices for dairy products have strengthened significantly since the limitations on export subsidies under the WTO came in to being around 2000. Over the past few seasons, dairy commodity prices have been extremely volatile as reflected through the Fonterra trading platform, global Dairy Trade (gDT). However, the growth of the world's population, strong growth in Asia and an increase in dairy consumption, general increase in energy costs and the international grain shortage, which has been accentuated by the worldwide move towards ethanol and bio-diesel production, should ensure dairy commodity prices appreciate overtime. This is most evident with the growing exports of whole milk powder to China.

The New Zealand dairy industry will benefit from the structural adjustment occurring through the latest WTO round of trade negotiations. To date this has resulted in limitations on subsidised exports from Europe and the United States. This, together with other international market conditions has led to a rise in international commodity prices and an improved outlook for New Zealand's competitive position in the international dairy market. New Zealand's relative position is also assisted by its low cost pasture based systems.

As one of the largest suppliers to both Fonterra Co-operative Group Ltd (Fonterra) and Westland Milk Products Ltd (Westland), Dairy Holdings Ltd is a strong supporter of the co-operative model and the need to contract and manage the marketing of milk commodities on the international market. Dairy Holdings also promotes investment in value add initiatives that boost long term milk prices.

As a result, the Board anticipates a general firming in the New Zealand farm gate payouts over the long term.

In New Zealand the development and growth of dairying continues. Dairy Holdings is confident that the long-term prospects are positive.

4. DAIRY HOLDINGS BOARD OF DIRECTORS

- **Gregory (Greg) William Gent (Chairman)**

Greg is a dairy farmer from Ruawai, Northland. Greg was a foundation director of Fonterra and retired from that Board in 2011. His current directorships include The Southern Cross Health Care Group, rural insurer FMG, and Crown Research Institute Plant & Food.

- **Colin Charles Armer**

Colin Armer is a leading North Island based dairy farmer and, together with his wife Dale, holds extensive agricultural interests. Mr Armer brings considerable dairy farming experience to the Board having been involved in the Industry for 30 years.

- **John Suffield Parker**

John has a background in dairying and a business career with the New Zealand Dairy Board. Starting as a Consulting Officer and retiring as Deputy Chief Executive of the New Zealand Dairy Board, he has also owned dairy farms. John is currently the Chairman of Primary ITO Ltd.

- **Harold (Harry) Snell**

Harry is a Farm Consultant and serves as a Director on a number of farming companies. Harry is the Chairman of Waikato based JD and RD Wallace Ltd which is a Shareholder in Dairy Holdings Ltd via Jagewi Ltd. Harry is involved in the ownership of several dairy farms in the Te Awamutu/North King Country region.

- **Murray Turley**

Murray is involved in a large scale arable and vegetable operation with farms in South and Mid Canterbury, along with his wife, Margaret. They are involved in other value-add businesses associated with their farming enterprise.

5. **FURTHER ENQUIRIES**

Further enquiries can be directed to the following:

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