Long-running battle now over for Fonterra director

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With the "bruising" $73m deal to increase their shareholding in Dairy Holdings Ltd (DHL) won, Colin and Dale Armer believe staff now have some certainty and it will be business as usual at the low cost farming operation.

According to the New Zealand Companies website the Fonterra director and his wife now have a 60.74% shareholding in the South Island-based corporate dairying business that operates 72 properties, 58 of which are dairy farms milking almost 44,000 cows with the rest dairy support blocks.

The lift in shareholding from 16.6% makes them NZ's biggest dairy farming family, with 13 farms of their own in the North Island in addition to their share in DHL.

Significant capital

South Canterbury Finance (SCF) receivers announced the sale of 33.6% of DHL in early February for $56m, putting the value of shares at close to $105/share.

All up, almost $98.5m will have changed hands in the transaction, presumably soaking up a significant proportion of available agricultural investment capital.

The Armers have each lifted their shareholdings from 133,335 shares to 485,881 giving the couple a combined shareholding of 971,762 shares out of the total 1.6m shares issued in the company.

Original shareholder Alan Pye has lifted his shareholding by 66,672 shares to take a 25% stake in the company and NZ investor-backed Jagewi now has a 14.26% stake.

'We're constantly looking for continuous improvements and still driving cash out of the business.'

The couple's low input farming ethos, that's also followed by DHL, is well understood by management and staff alike but it's a system that could have faced changes had the sales process had a different result, Armer said.

Certainty welcomed

DHL chief executive, Colin Glass said the sales process had been prolonged over which time it had been difficult not to take a more short term view given the uncertainties of who would be the eventual owners. It was very much business as usual now with decisions based on the long term.

That was particularly important for the company and all its people. DHL operates with sharemilkers, contract managers and managers as well as employed farm staff and all were happy there was now certainty over the future direction of the company.

The board has remained unchanged throughout the process with Armer and Pye directors along with independent directors John Parker and Bill Bayliss who is chairman.

Armer said the board had acted professionally at all times with the disputes between other shareholders left clearly at the boardroom door so they remained at shareholder level.

That view is borne out by Glass, who said there had always been strong, clear governance from the board with the independent leadership and input from independent directors an asset throughout the sales process.

In early February the Armers were feeling a bit battered after their encounter with SCF receivers and their fellow shareholders, who had joined together to offer their shares in the company for sale and wanted the Armers to do the same.

Last year the Armers filed a High Court action to try to protect their pre-emptive rights, which they said were set down in the

Colin and Dale Armer in 2006 – investing and reinvesting.

company's constitution and a shareholders agreement. Under those protections they said they should have been given the first right to purchase any shares put up for sale.

Court battles

Instead, court documents and the statement of claim by the Armers reveal a host of allegations that questionable tactics were used, including blackmail.

The couple contend attempts were made to railroad them into signing a new shareholders' agreement and constitution that would limit their rights.

Armer said threats were made that if they didn't sign he could face investigation by the Serious Fraud Office (SFO). The threat related to a $14.5m loan he'd taken from SCF in 2009 and then on-lent to DHL.

He claimed attempts were made to make it difficult for him to repay the loan so he would be forced to default, but those creating the difficulties underestimated their resources and resolve, he said.

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But the couple had the right protections in place and they weren't going to be bullied into giving them up. He believed the push came because would-be purchasers didn't want a minority shareholder left in the company.

"In the end common sense prevailed and they had to deal with us per our contractual arrangements."

Long view

Right from the outset of their investment back in 2001 when they joined Allan Hubbard and large scale potato grower Pye to form DHL, they were in it for the long haul, Armer said.

"We saw our investment as inter-generational and we still do."

In late 2010 when it became apparent the receivers of SCF would sell the company's 33.6% stake in DHL, the Armers said they made it clear they wouldn't be selling. Other shareholders became willing sellers leaving the Armers on their own.

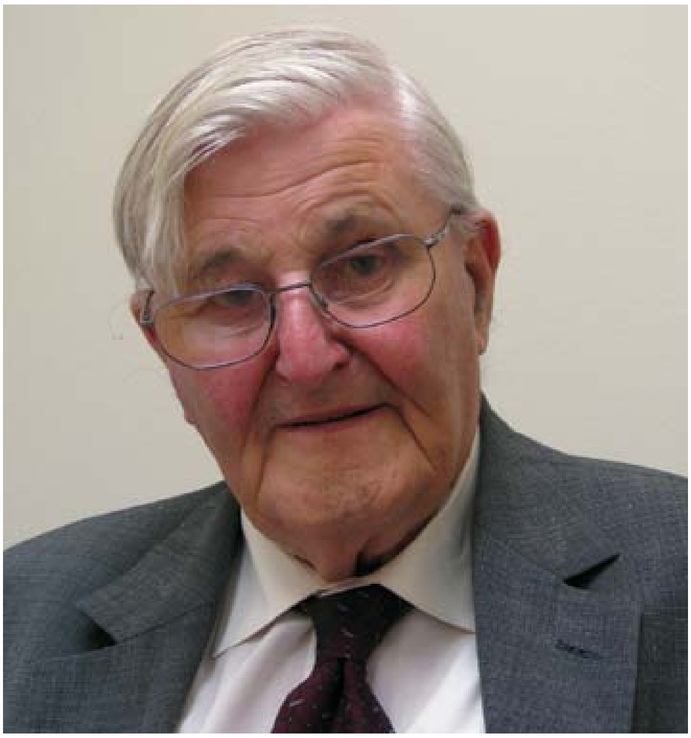
"We were happy to stay with our stake and work with the incoming new shareholders and we reiterated that on several occasions," Armer said.

As it turned out they were in a position not just to hold their shareholding but to increase it.

Along with Pye, who had a change of heart in terms of selling, and new Kiwi-based investors, they were able to negotiate a deal to buy SCF's stake as well as the 8.33% held by each of three US-based investors and the 3.91% held by Christchurch-based shareholder, businessman Humphry Rolleston.

The new shareholders, including DairyNZ chairman John Luxton, took over Rolleston's company Jagewi and now own 14.26% of DHL. Jagewi is now a wholly

Colin Glass – strong clear governance.



The late Allan Hubbard who the Armers joined in business back in 2001.

owned subsidiary of Hybrid Dairies which has two shareholders.

One is Penrith Holdings owned by Wellington-based families and the other is JD and RD Wallace which has nine shareholders including Luxton's family and wellknown Waikato farming family, the Wallaces.

Their purchase of the Jagewi shares and increased stake will have cost more than $23m while Pye will have had to pay close to $7m for his extra shares.

Traditional path

The Armers story of progress through the dairy industry is one typical of many, albeit that their success is at a scale few have achieved.

Armer mortgaged his prized Valiant V8 car at the age of 19 to get enough money together to go sharemilking, to long hours spent milking cows and his wife's hours running the administration side of their North Island business, as well as rearing a large family – it's been a story of hard work rather than good luck.

But they've been prepared to take risks and always saw the value in trying to increase scale in their operation.

"Our focus has always been to be cash driven and any capital growth that came along was a bonus," he said.

"Being cash motivated – that's how you end up with a big business."

The cash coming out of the business was always reinvested. Growth was and apparently still is the aim.

"But if you're growth orientated you have to have a business that's robust enough to stand up to the shocks along the way and we've been through those," he said.

Growth focus

They've seen the highs and the lows of payout fluctuations and battled the vagaries of the weather, particularly in the North Island with little insurance through irrigation. Back in 2001 they were looking at a way to invest further in the South Island that wouldn't mean a big commitment in their already stretched management time.

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Hubbard was aware of their interest and invited them to join himself and Pye in buying Tasman Agriculture Farms (TasAg) being sold off as a result of Brierley Investments having to free up cash.

They were joined by US investors and together they formed DHL.

Armer said the high standard of management and administration already in place at TasAg impressed and they engaged general manager Glass along with several supervisors.

By the end of the second year DHL had bought 30 farms – a mixture of TasAg farms, corporate dairy farmer Dairy Brands' properties, existing farms and some conversions. It was rapid fire purchasing but always with an eye to improving the profitability of the enterprise.

Basic principles

In 2001 cost structures in New Zealand were noticeably rising and higher input systems were gaining traction.

Glass said DHL farms' systems were scrutinised and returned to the "tried and true" grass-based principles exhorted by C. P. McMeekan, Arnold Bryant and the Ruakura Number 2. Dairy Farm. It was back to basics then and remains so today, he said.

Over the latter years the company has sought to insulate itself from market vagaries by owning support land to winter cows, rear youngstock, graze service bulls and grow supplement.

"We're constantly looking for continuous improvements and still driving cash out of the business."

The Armers are a strong supporter of cooperatives in both who they supply and who they buy from. Their own farming enterprise in the North Island continues to grow with two dairy farm conversions being carried out this season.

"We've got a very strong business," he said.

"We've been investing and reinvesting for a long time now."

It's a pattern that looks set to continue.