

In the last year LIC has changed from being 'customer focused' to being 'customer driven'. At first glance this may seem a small change but we feel there is in fact quite a vital difference and one in which the Shareholders Council plays an important role. I will touch on this again a little later.

New Councillors

The council is made up of 21 councillors elected from wards throughout NZ. This year we welcome several new councillors, namely, Richard Syme, David Beuth and Gerard van Beek replacing Wayne Berry, Brian Aspin and John Scrimgeour in Wards 7,9 & 10 respectively. We also welcome Bede Kissick who is filling a casual vacancy created in Ward 12 when Steve Poole was elected to the LIC Board.

Councillors welcome feedback from all shareholders and to that end accessibility to the contact details for Councillors on the LIC website has been improved.

Overview of Council Activities

Sir Henry spoke at the DairyNZ Farmers Forum early in May this year. Along with other speakers over the two days he highlighted that it is important that we never lose sight of our main competitive advantage in NZ, being our grass based farming systems – if we put this at risk, he said, then our business is at risk. Sir Henry went on to say that one thing farmers can do to help in managing volatility is to focus on pasture.

Council feel that it is important therefore that the cow we are breeding for the future is one that can not only perform well but also survive and reproduce, with minimal farmer intervention, in a predominantly grass fed farming system. If we are breeding cows that are best suited to high input systems and are taking multiple farmer interventions to get back in calf, then we are breeding cows that are eroding our main competitive advantage in NZ. To that end the Shareholders Council have had discussions with LIC Livestock Selection, NZAEL, Colin Holmes, and most importantly farmers, about the type of cows that we as farmers want to be farming in the future.

We have had some constructive discussions with Bill Montgomery from NZ Animal Evaluation Unit and gave a presentation to one of their User Group meetings on the type of cow we would like to farm. The Shareholders Council is supporting a call for a review of the National Breeding Objective.

We have talked to Livestock Selection within LIC to understand how they select our bulls and what is driving their decisions. Our ultimate goal is to ensure that when LIC is out in the marketplace they are not just selling semen and products but they are providing a path to a herd that is tailored for, and ideal to, NZ farming systems and conditions and providing not just products but solutions for our businesses. That, to us, is being customer driven, giving the customer what they want and need not just trying to market a product.

Dairy Core Database Review

The other big agenda item for us in the last year has been the Dairy Core Database Review. As was reported at last year's Annual Meeting, DairyNZ initiated a review of the Dairy Core Database by the Anderson Committee.

Dairy NZ have now formed an industry project team to translate the Anderson recommendations into a business case for consultation. Council were updated in June 2010 and a subcommittee of the council has been briefed twice since. At this point in time the project team have prepared a concept which has been shared with the farmer forum and shortly a consultation document will be available for farmers and other industry stakeholders to comment on. Council are supportive of the concept but need to be convinced that the benefits for us as dairy farmers exceed the additional costs we will have to fund, either by levy payments or in the purchase of products and services. Council view their involvement in this industry review as critical and will discharge our duties diligently.

Genomics

This is an exciting area that we believe will enable even more rapid rates of genetic gain and result in ultimately more profitable farms. However, as with all new science Council understands that it is an evolving technology and continues to be briefed at each meeting by the appropriate experts. It is important that in our excitement we do not get ahead of the science in this very fast moving area of technology.

The recent announcement by NZAEL regarding concern over the BW of Bulls with only DNA information, and as yet no daughter proofs, highlights some of the issues we will face. Councils overriding view is that co-operative shareholders have products and services made available to them that improve their overall profitability. Where there are risks these need to be made clear to shareholders together with the ways these things are minimised.

Appointed Director

As required under Section 25 of the constitution the council carefully considered the re-appointment of Phil Lough as an appointed director. We had discussions with the Chairman of the Board, sought clarification on a number of points and endorsed the re-appointment with all voting councillors in favour.

It is vital to the future of the co-operative that we have a very high level of skill and strategic ability in our boardroom. I have no hesitation in recommending Mr Lough to you in Resolution #5.

The working relationship that the Shareholder Council has with the LIC Board and Management continues to be excellent and is based on mutual trust and respect and a willingness to share information. Regular formal and informal contact between Council, the Board and Management has been beneficial to all parties.

Company Performance

The last year was certainly a jolt back to the reality of doing business in a volatile international dairy market from the heady highs of a payout over \$7 kg/ms to an opening forecast for the season closer to \$4 kg/ms.

In looking at the performance of the company the Shareholders Council noted several things.

1. Although revenue and subsequently profit were down when compared to the 08/09 year, with underlying net earnings dropping by 43% to \$9.1 million - we need to remember that 08/09 was an outstanding year in dairy farming for both cash flow and optimism. The accounts when compared with the 07/08 year, which was a more normal average, we see underlying net earnings

have increased by 5% or \$415,000. Not a large increase, but nevertheless we feel a pleasing result given the tough economic climate. LIC also increased discounts to support farmers. Our bottom line was achieved without unduly compromising our research and development and with only a slight softening of our equity ratio.

2. Costs were controlled across the organisation very well. We would like to acknowledge our appreciation to staff that had nil wage increases. We appreciate that those at the lower end of the pay scale were hit the hardest by this decision and thank everyone for their loyalty and commitment to the company and their support of farmers who were mostly in shock having to adjust to operating in a different economic environment where the goal posts seemed to have been moved overnight.

3. Credit control and inventory were exceptionally well managed. This is an area that can tie up a lot of working capital and the company showed commitment and focus to save costs in this area.

4. Further impairment of \$1.905 million in Tru Test. LIC worked with Tru Test over a number of years before extending that relationship and buying a 19.9% stake in the company in the 06/07 year. At the time this alliance lined up nicely with our farm automation strategy. The performance of Tru Test over the following years has certainly not been outstanding. LIC recognised a loss of over \$3 million in each of the 2008 and 2009 years and this year sold its shares in the company sustaining a further \$1.905 million loss.

The Shareholders Council has been monitoring the company's investment in Tru Test with regular updates from the Board. The resulting loss on exiting this business is certainly disappointing. We are however confident that at the time of purchase, appropriate due diligence was undertaken and the investment aligned nicely with the company's strategy as signed off by the Board and Council. Council are happy that LIC actively managed the investment with Mark Dewdney being appointed to the Tru Test Board of Directors. When it was clear there was a divergence of strategy the company decided to sell its shares, which as far as the Shareholders Council was concerned was the right, but not necessarily the easy, decision.

Appreciation

I would like to thank the Board and Management for their openness and timeliness in supplying the Shareholders Council with any information we have requested during the year. And once again our thanks must go to the staff of LIC who are the cornerstone of the company and whose passion and hard work continue to keep LIC the choice of on farm partners in the quest for more profitable breeding and businesses solutions.

Thank you also to each of the farmers on the Shareholders Council for your insight and commitment to the role.

Overall the Shareholders Council are pleased with the results of the company in what was an extraordinary year and we will continue working on your behalf to ensure this co-operative continues to service your needs.