

Murray Creek Dairy Farm Limited

ANNUAL REPORT 2015/2016



ROGER DICKIE
NEW ZEALAND

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DIRECTORS ANNUAL REPORT

The 2015/2016 season saw our Variable Order Sharemilkers Jason & Sandy Herrick achieve production of 372,154kgMS. This production was up 4.8% on the 355,000kgMS target and 9% ahead of the previous year. Despite the challenges this season presented this is an excellent achievement and is the second highest production the farm has achieved. It should be noted that the farm record was set while 1,300 animals were being milked at Murray Creek, significantly higher than the 995 peak milked cows Jason & Sandy milked this season. This production equated to 374 kgMS/cow.



The final payout announced by Open Country Dairy (OCD) was \$3.90/kgMS, slightly higher than the \$3.66 that was originally forecast. Jason & Sandy this year achieved excellent milk quality and received a Milk Quality Certificate with an average Somatic Cell Count of 139,000, which is a very good achievement for a large herd. They also completed the season grade free and were awarded a Grade Free Certificate. This achievement meant that we were guaranteed all eight cents of the quality portion of the payout.

As at balance date, the term loan had a balance of \$2,729,802, and the interest rate for the term loan was 3.69%. Though there is an overdraft facility available to Murray Creek at an interest rate of 7.67%, the directors resolved to operate at a zero balance and take advantage of the more favourable term loan interest rate, by drawing down from the available funds when needed. This policy meant that there was \$245,500 in total drawn down from the term loan at the end of the season.

A valuation of all land and buildings and stock were completed by Logan Stone Limited and Progressive Livestock Limited for the financial year and summary documents are included in this annual report. Murray Creek was given a total value of \$11,307,020, being made up of land and buildings of \$10,680,000 and all stock at \$1,627,020. It should be noted that this is a drop in value of \$824,730 from the previous financial year. This decline in values can directly be attributed to the fall in dairy prices over the past two seasons. As the dairy industry begins to recover we are confident that the asset value will increase.

The share value for Murray Creek from the current accounts gives a net asset backing value of \$1.08 per share.

With the dairy payout continuing to be low, Jason & Sandy and our administration team have continued to work hard to minimise costs without impacting milk production. For the 2015/2016 season the farm working expense (FWE) were \$4.13/kgMS, which was below the original budget figure of \$4.33/kgMS.

The total capital expenditure for the year was \$124,829. This was comprised of the purchase of LIC (formally Livestock Improvement) shares \$1,782, work to the cowshed totalling \$79,139, which included new milk filters, new cowshed gland, platform and beam

and vacuum pump, new water system at \$40,745 and \$3,163 for a colostrum tank and stirrer for calf milk.

Repairs and maintenance for the year came in under budget with a total spend of \$74,462. The major expenditure items were for the workers dwellings where we had to replace the spouting and installed insulation in one of the dwellings, which was having a damp issue.

I would like to take this opportunity to thank my fellow Directors Jeff Whitlock and Stephen Barr, our Variable Order Sharemilkers Jason & Sandy Herrick and farm consultant Jack Ballam for their contributions over the past year.

Farm Update – Current Season

The production forecast for the 2016/2017 season has been set at 365,000 kgMS. Spring in Southland is one of the best for a number of years. Jason & Sandy have the cows milking exceptionally well and are currently 19% ahead for the season.

For the current season, Open Country Dairy has forecast a milk price for the 2016/2017 season of \$4.90. As prices begin to show signs of recovery, we need to remember that prices are still not entirely stable. As we proceed into this season, we continue to work with our sharemilkers to create the most efficient cost structure. As a result we have worked hard to minimise costs and have budgeted a FWE of \$3.81/kgMS.

In a move to minimise the impact on the farm business the directors have agreed to continue no principal payments for the 2016/2017 season and stay with interest only repayments. We have also re-negotiated new interest rates for the loan of 3.67% floating. The directors have also resolved to continue to operate at a zero balance and take advantage of the more favourable term loan interest rate, by drawing down from the available funds if needed.

I look forward to seeing you at the AGM.

Kind Regards



Roger Dickie

Director

Murray Creek Dairy Farm Limited

VOSM ANNUAL REVIEW – Jason & Sandy Herrick



Over all we have really enjoyed the farm this season and the challenges it has put in front of us. The two major challenges were the failure of the vacuum pump in the cowshed in early August and a water line failure in summer. Getting to know our new office person Kate has been a pleasure and working with the directors and Jack Ballam is still a pleasure, the support has been amazing.

We believe going forward that we have the farm in a good operating position now and look forward to the next season to produce a better result than the first two seasons.

Weather conditions

The start of the season as you all may well know was a challenging wet one with the middle period being dry. Despite these weather extremes it was a good growing season. Unfortunately the wet returned for the later part as well and was a challenge getting good condition on the cows and keeping production up, while aiming to keep good grass cover going into winter.

Stock

Animal health has been really good considering the wet season we have had. Towards the end of the season with the wet conditions, lameness became our biggest problem with the end result being that we had to dry off 80 cows towards the end of the season



Fertiliser

Fertiliser has been an area where we have managed to make big savings. This season we worked with our fertiliser rep to create a cost effective plan, which involved only putting maintenance on and following milking cows with small but consistent amounts of urea to maintain the cover and quality.

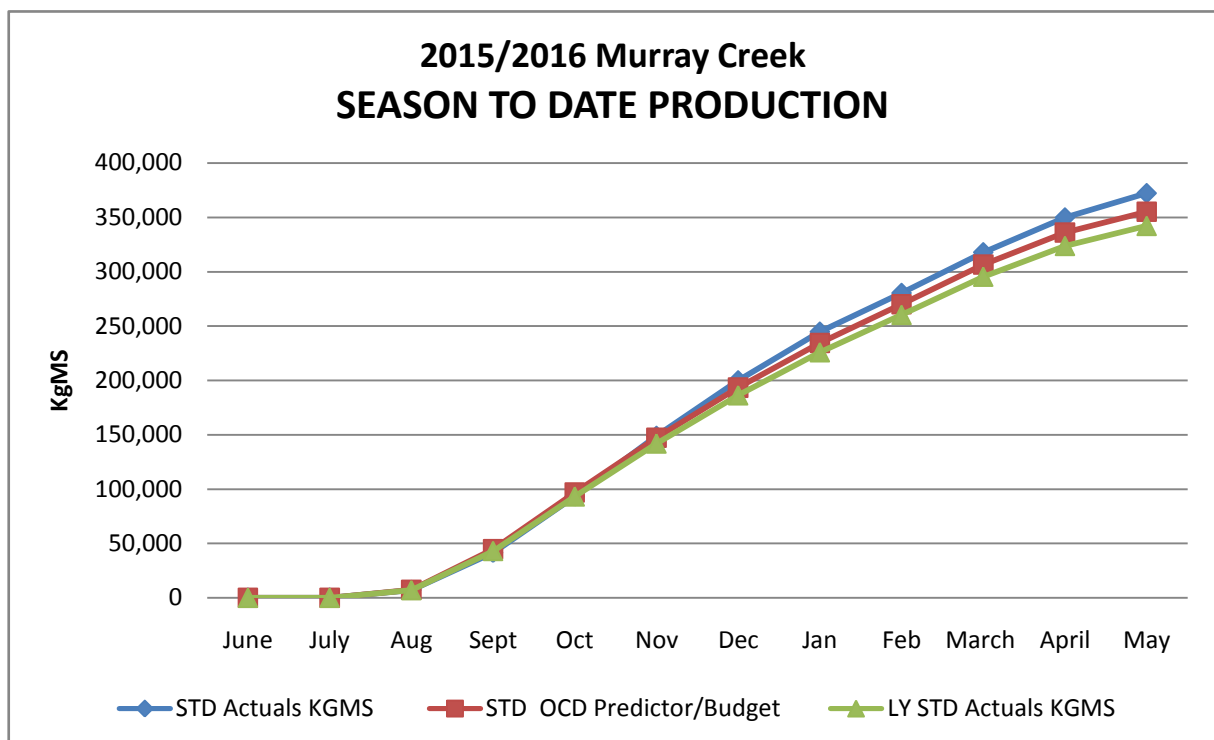
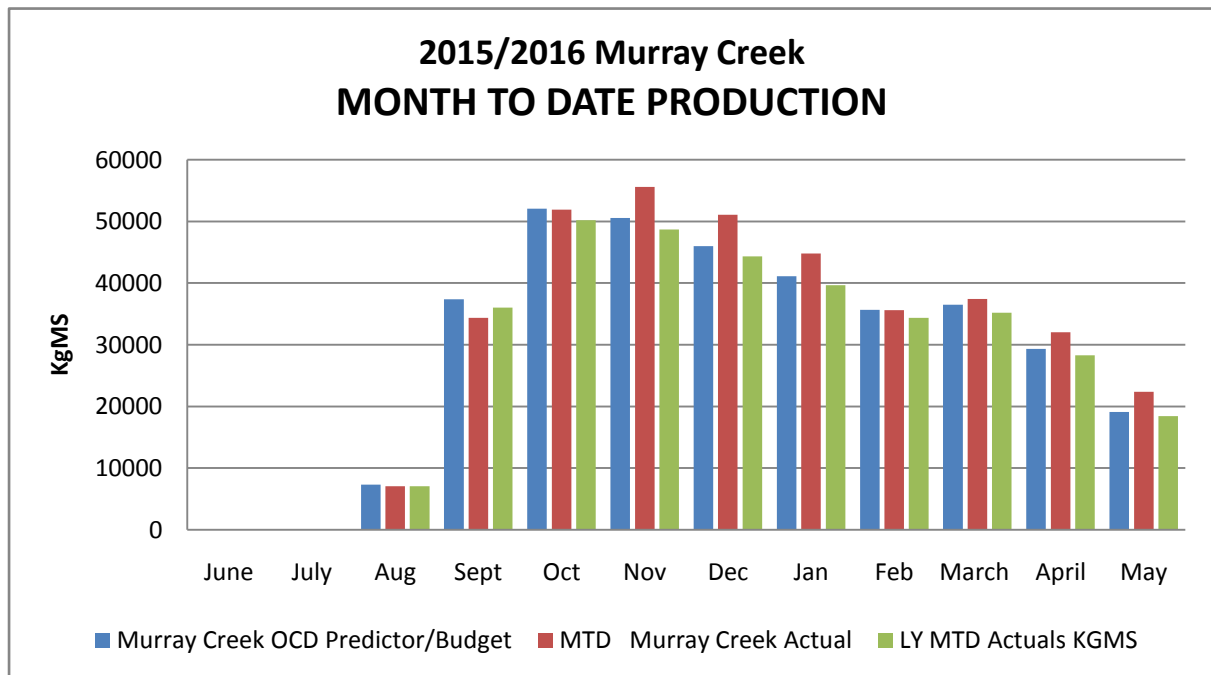
Mating

We had an 11% empty rate in the cows and 5% empty rate for the heifers and have culled all empty cows. We have 72% in calf to artificial insemination so we should expect a high heifer replacement rate next spring.

Production

Production was a challenge earlier on with the wet weather conditions during spring. We reached a peak milk production of 2.25kgMS/cow/day. We have been slightly up on monthly targets throughout the season and have produced the 2nd highest production for the farm with a lot less cows.

We also achieved a grade free season with an average SCC of 139,000 which is a very acceptable level for large herd status.



2017 SHAREHOLDER FARM VISIT



The date for the next bi-annual shareholder visit to Murray Creek has been set for Saturday 18th March 2017. Further detail to follow early in the new year.

RESOLUTIONS

Appointment of Auditor

It is moved that Silks Audit Chartered Accountants of Wanganui be appointed auditors for Murray Creek Dairy Farm Limited.

Moved: Jeff Whitlock Director

Seconded: Roger Dickie Director

Appointment of Director

In accordance with the constitution Steve Barr retires as a Director and Steve is available for re-appointment. That Steve Barr is re-appointed as a Director.



**Murray Creek Limited
743 Mossburn Lumsden Highway
Castlerock
SOUTHLAND**

Desk Top Market Valuation prepared for:

Roger Dickie Limited

As at 31 May 2016



1.0 INTRODUCTION

- 1.0.1 Further to instructions from Kate Murdoch we have undertaken a 'Desk Top' market valuation appraisal on the above property in order to assess the market value for financial reporting purposes. As per instructions we have been advised not to re-inspect the property and have therefore relied on an inspection undertaken on 4 May 2015 and described in our previous full report dated 12 June 2015. We have been advised there have been no substantial changes to the property since this date and base our assessment on the property being in similar physical condition.
- 1.0.2 Due to not re-inspecting the property and not providing a full report this report does not comply with international valuation standards.
- 1.0.3 The report complies with NZ IAS 16 and can be relied upon by Silks Audit for financial reporting purposes.
- 1.0.4 Your instructions, as per our scope of work agreement, require us to make the following valuation assessments;

- 1. Market Value as at 31 May 2016

2.0 PROPERTY CONCLUSIONS

- 2.0.1 An estate in fee simple 413.523 hectare part irrigated dairy milking platform situated in the Castlerock district of Northern Southland which has been converted some 17 years. Currently milking approximately 930 cows and producing 372,154 kg milk solids for the 2015/16 season. From a dairying perspective location is regarded as fair. Climate is suited for seasonal supply dairy land use with irrigation. The land is of flat to stronger rolling contour with a balance soils showing good fertility levels. Overall layout is good being well subdivided into 61 paddocks, reticulated water supply and well raced. Housing includes four fair to good quality dwellings; a further dwelling is warranted. The milking shed is a 50 bail rotary which is of under capacity but manageable and found in good condition. There are adequate supporting farm buildings. Overall a mid quality dairy platform being well presented and achieving improving production based on a low supplement import system. We estimate average efficient production to be 360,000 kilograms of milk solids (965 kg ms / effective ha).

3.0 VALUATION CONCLUSIONS

- 3.0.1 The appropriate valuation approaches for estimating the market value of a dairy unit (where a dairy platform is deemed the highest and best land use) are the market approach and income approach.
- 3.0.2 Under the market approach umbrella we use two main methodologies;
 - i) A summation approach on a per hectare basis. In this approach we determine the relevant classes of land at a land value level and add the added value of improvements, and chattels and plant as appropriate. This is then compared at a market value per hectare level.

- ii) A summation approach on a per kilogram of milk solids based on estimated average efficient production.

3.0.3 Under the income approach umbrella the two methodologies used are;

- i) A capitalisation of the Earnings before Interest, Tax, Depreciation and Amortisation (EBITDA) under average efficient management after an allowance for Wages of Management. This capitalized sum provides an estimate of the Total Farm Capital required to operate the business as a standalone unit. Deduction for stock, plant and Fonterra shares are required to arrive at the appropriate realty basis that as dairy units normally transact in the market. The milk price is based on the average past five year actual and current forecast under average efficient management production levels.
- ii) A multiplier of the milk price which is based on the average past five year actual and current forecast under average efficient management production levels.

3.0.4 The above approaches are supported by analysed benchmark levels from sales deemed most comparable in the market.

3.0.5 Our opinion of the quality of market evidence available is outlined in the below table:

Factor	Quality
Number of comparable sales	Poor
Recent time frame	Poor
Direct Comparability	Limited

3.0.6 When assessing the market value of the subject property we have considered the property features and compared the sales of other properties that have transacted recently and have adjusted those sales to reflect the location, standard of improvements, plantings, mixed age of plants and productive capacities compared to the subject property.

3.0.7 There have only three unconditional dairy unit sales and one near unconditional sale for 2016 to date. This is a reflection of the low confidence in the dairy sector at present due to low global commodity prices flowing through to poor farm gate returns on a historical basis. From the limited recent sales evidence there appears to be a slight drop in dairy farm values over previous years. The value drop is lower for well-located and good quality dairy units. Dairy units of lower quality with inferior locations and larger scale could find saleability and liquidity further restricted.

3.0.8 Some commentators estimate approximately 80% of dairy farm businesses have run at a cash loss over the past two years and with the forecast milk price for the 2016/2017 season only being marginally higher there will be severe financial pressure in the sector.

3.0.9 The above financial pressures could see a number of dairy units coming to the market as dairy farm businesses need to restructure their capital if there is insufficient equity to allow extended bank support. This could see an oversupply of dairy units to the market in conjunction with weak and limited buyer demand given existing industry participants have not been creating wealth and have most likely been losing money and equity over recent years.

- 3.0.10 Our income based valuation methodologies are based on a an average of the five past seasons milk prices and the current forecast milk price which currently gives an average milk price of \$5.48 per kg milk solids. The resultant estimate of market value from these approaches is lower than the more traditional comparable sales summation approaches. Given the current Fonterra forecast for the 2016/17 season milk price is \$4.25, some \$1.23 per kg milk solids lower than the average, we are placing more weight on the income based approaches as a guide to market, especially where good comparable market evidence is limited, and influences our inputs for the summation approaches.
- 3.0.11 In the Southland dairy property market it is our observation that there are generally three categories of dairy unit which have broad ranges of value bands. These bands are mostly influenced by quality of property and infrastructure, location and production per hectare. We have graded these properties as A, B, and C. 'A' type properties are quality, good soil and contour units in the Central Southland and Southland Plains districts which generally show good consistent production per hectare. 'B' type units are basic, reasonably well located properties with Southland average type production. 'C' type units are poorer dairy units which may have issues with buildings, location, contour and shape etc.
- 3.0.12 In our opinion we assess the subject property as a B category.
- 3.0.13 Below is a summary of our market analysis and market value estimates under each approach:

Valuation Approach	Market Value Estimate
Per Hectare	\$9,680,000
Per kg Milk Solids. Average Efficient	\$9,720,000
Income Capitalisation	\$9,132,000
Multiplier of Milk Income	\$9,470,000

- 3.0.14 Our preferred valuation approach is the summated valuation approach based on establishing the land value and summing the added value of improvements and associated chattels and plant as outlined as we consider this a more accurate approach to factor all the attributes of the subject property.
- 3.0.15 In assessing the value of the property we have undertaken an analysis of the property in the market particularly looking at the strengths and weaknesses specific to this property and how this relates to the wider market and economic conditions prevailing at date of the valuation and over the short term that may influence the demand and value levels.

Strengths & Opportunities	Weaknesses & Threats
• 167 hectares irrigated with centre pivoting K-Line irrigation systems • Majority flat contour • Good races, fencing and water • Ability to increase production with supplementary feeding and management of irrigated pastures	• Limited capacity milking shed for this size property • Location • One dwelling short • Climate • Environmental regulations • Volatile Milk Price pay-out • Softening Real Estate Market • Consent to take water for irrigation has expired. New application not yet granted.

4.0 MARKET VALUATION

- 4.0.1 After examining all factors and subject to the overriding conditions we conclude the market value of the property as at 31 May 2016 is:

NINE MILLION SIX HUNDRED AND EIGHTY THOUSAND DOLLARS
(\$9,680,000)

Apportioned as follows:

Value of Improvements	
– Residential Improvements	\$694,000
– Productive Buildings	\$626,000
– Other Improvements	\$680,000
	\$2,000,000
Land Value	
	\$7,060,000
Realty Value – Land & Buildings	
	\$9,060,000
Household & Farm Chattels	\$30,000
Milking & Effluent Plant & Equipment	\$200,000
Irrigation Plant	\$390,000
Market Value	
	\$9,680,000

The above valuation assessment is plus Goods and Services Tax (if any).

- 4.0.2 Unit analysis

Area	413.523 ha	(373 ha effective pasture)
Ave Efficient Production	360,000 kg milk solids	(965 kg ms / effective ha)
Land Value	\$17,073/ha	\$19.61/kg ms
Market Value (net of shares)	\$23,409/ha	\$26.89/kg ms

- 4.0.3 Fonterra Shares are not included.

- 4.0.4 Qualification to Valuation; The above market value assessment is based on a new water permit being issued for a groundwater take for the irrigation water on no less favourable

terms than the old water permit which has expired. If such a permit is not issued this may materially negatively affect the market value assessment.

4.2 Certification

Experience

- 4.2.1 'The principal signatory has a minimum of five years' experience in valuing the subject class of asset, has all appropriate qualifications and registrations enabling them to practice as a Valuer and has not been subject at any stage to disciplinary action by the relevant professional governing body to prevent them acting as a Registered Valuer.'

Independence

- 4.2.2 The signatories have no direct or indirect pecuniary or other interests in the property being valued and are not aware of any other potential conflicts of interest.

Professional Indemnity Cover

- 4.2.3 We certify that Logan Stone Limited hold professional indemnity insurance for an amount of up to \$3 million and note this may be less than the requirement for insurance cover as set by the lender.

5.0 OVERRIDING CONDITIONS

- Our valuation is subject to the attached Statement of General Valuation Policies.
- This valuation is current as at the date of valuation only. The value assessed herein may change significantly and unexpectedly over a relatively short period (including as a result of general market movements or factors specific to the particular property). We do not accept liability for losses arising from such subsequent changes in value. Without limiting the generality of the above comment, we do not assume any responsibility or accept any liability where this valuation is relied upon after the expiration of three months from the date of the valuation, or such earlier date if you become aware of any factors that have any effect on the valuation. Unless otherwise stated our assessments are made in New Zealand Dollar currency.

6.0 DISCLAIMER

- 6.0.1 Logan Stone Ltd prohibits the publication of this report in whole or in part, or any reference thereto, or to the valuation figures contained therein, or to the names and professional affiliations of the valuer, without the written approval of the valuer as to the form and context in which it is to appear.
- 6.0.2 Our valuation has been completed in compliance with International Valuation Standard framework. International Valuation Standards IVS 101 – *Scope of Work*, International Valuation Standard IVS 102 – *Implementation*, International Valuation Standard IVS 103 – *Reporting*. We confirm that:

- The statements of fact presented in the report are correct to the best of the Valuer's knowledge;
- The analysis and conclusions are limited only by the reported assumptions and conditions;
- The Valuer has no interest in the subject property;
- The Valuer's fee is not contingent upon any aspect of this report;
- The valuation was performed in accordance with an ethical code and performance standards;
- The Valuer has satisfied professional educational requirements;
- The Valuer has experience in the location and category of the property being valued;
- The Valuer has made a personal inspection of the property; But not re-inspected for the purpose of this report.
- The Valuer holds an Annual Practicing Certificate; and
- No one except those specified in the report, has provide professional assistance in preparing the report.

6.0.3 Should you require any further advice, do not hesitate to contact us.

Yours faithfully

LOGAN STONE LTD



Grant Barron

B Com (Ag) VFM, MBA, ANZIV, MPINZ

Mob: 027 2789 663

E-Mail: grant.barron@loganstone.co.nz

Reviewed by:



Jay Sorensen

B Appl Sc (Rural Val) Agr Bus, MPINZ, ANZIV

Cert. Adv. Sustainable Nutrient Management

Mob: 027 498 9932

E-Mail: jay.sorensen@loganstone.co.nz

31st May 2016

Cameron Town
The Engagement Partner
Silks Audit Chartered Accountants
PO Box 7144
Wanganui 4541



PROGRESSIVE LIVESTOCK LTD

DAIRY & BEEF
LIVESTOCK AGENTS

Dear Cameron

LIVESTOCK COUNT AND VALUATION

We confirm that we have attended to the count and the valuation of the Livestock held by *Murray Creek Dairy Farm Limited* as at 31/05/2016.

We confirm that we understand that this information will be used in the preparation of the Farms annual financial statements.

We can confirm the following:

Livestock Class	Verified Units on Hand	Price Per Head - \$	Total Value of class - \$
3-8 year old F & FX incalf dairy cows	731	\$1650	\$1 206 150 + GST
9 year old plus F & FX incalf dairy cows	47	\$800	\$37 600 + GST
Mixed age budget F & FX incalf dairy cows (inc 3 titters)	26	\$800	\$20 800 + GST

Herd BW 104

PW 116

RA 84%

Livestock Class	Verified Units on Hand	Price Per Head - \$	Total Value of class - \$
F & FX incalf dairy Heifers	188	\$1320	\$248 160 + GST

BW 136

PW 143

Livestock Class	Verified Units on Hand	Price Per Head - \$	Total Value of class - \$
F & FX empty R1 dairy Heifers	161	\$710	\$114 310 + GST

BW 161

PW 175

Total \$1,627,020

+ GST \$1,871,073

We confirm that we have counted and verified the units held as above.

We confirm that the value per head above is the current market value.

We confirm that the stock appeared to be in reasonable condition and health.

The overall presentation and lift in production performance in the Murray Creek Dairy Farm herd has seen it maintain value at the better end of the market. The same can be said for the R1 heifers.

We confirm that we are independent of the Farm, Farm Manager and the shareholders of the Farm.

We acknowledge that Silks Audit Chartered Accountants, as auditor of the farm, will be relying on our considerations and opinions expressed in the report.

Yours sincerely



Burke Patching

Progressive Livestock Ltd

Dairy Livestock Agent