



cutting through complexity

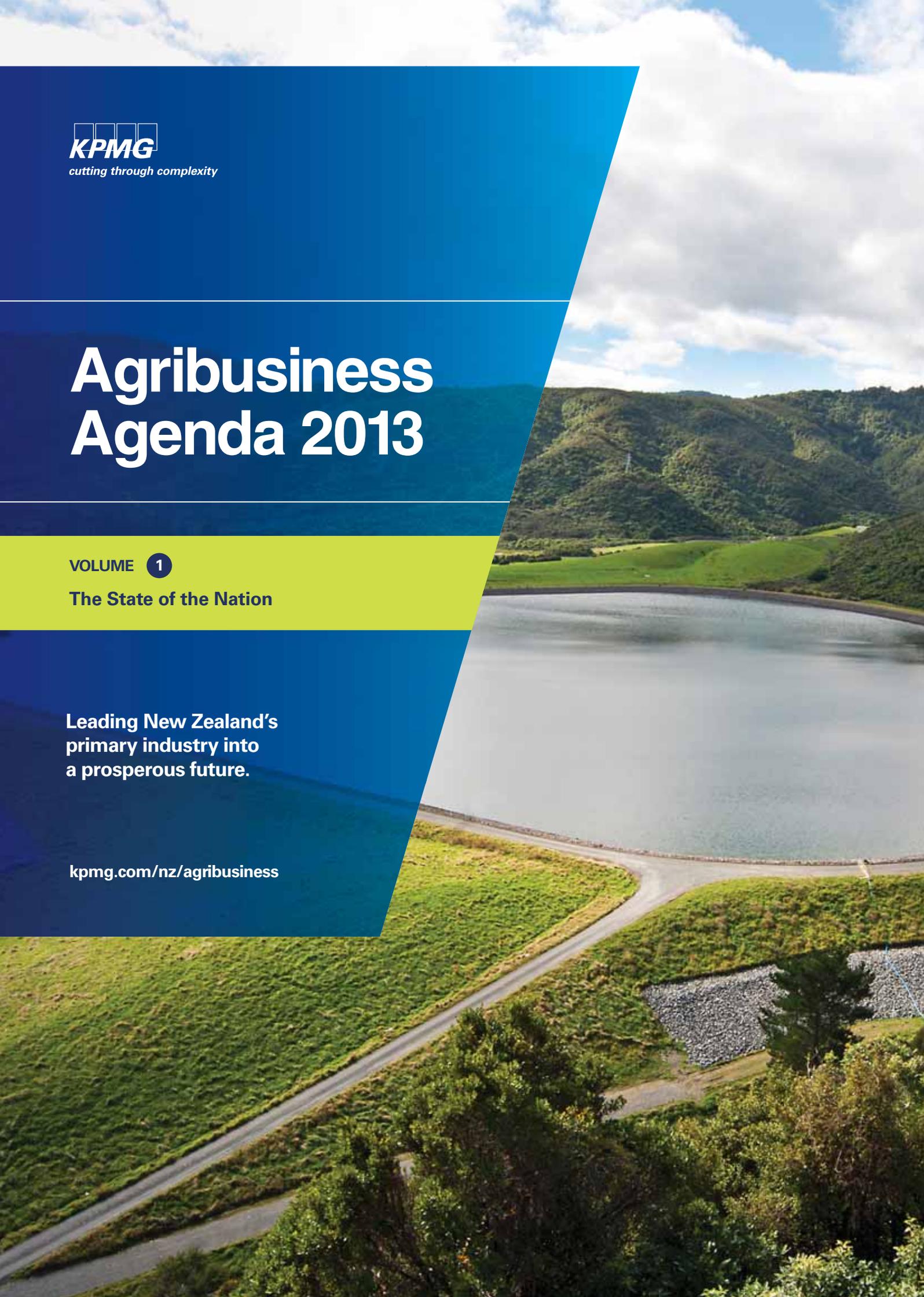
Agribusiness Agenda 2013

VOLUME 1

The State of the Nation

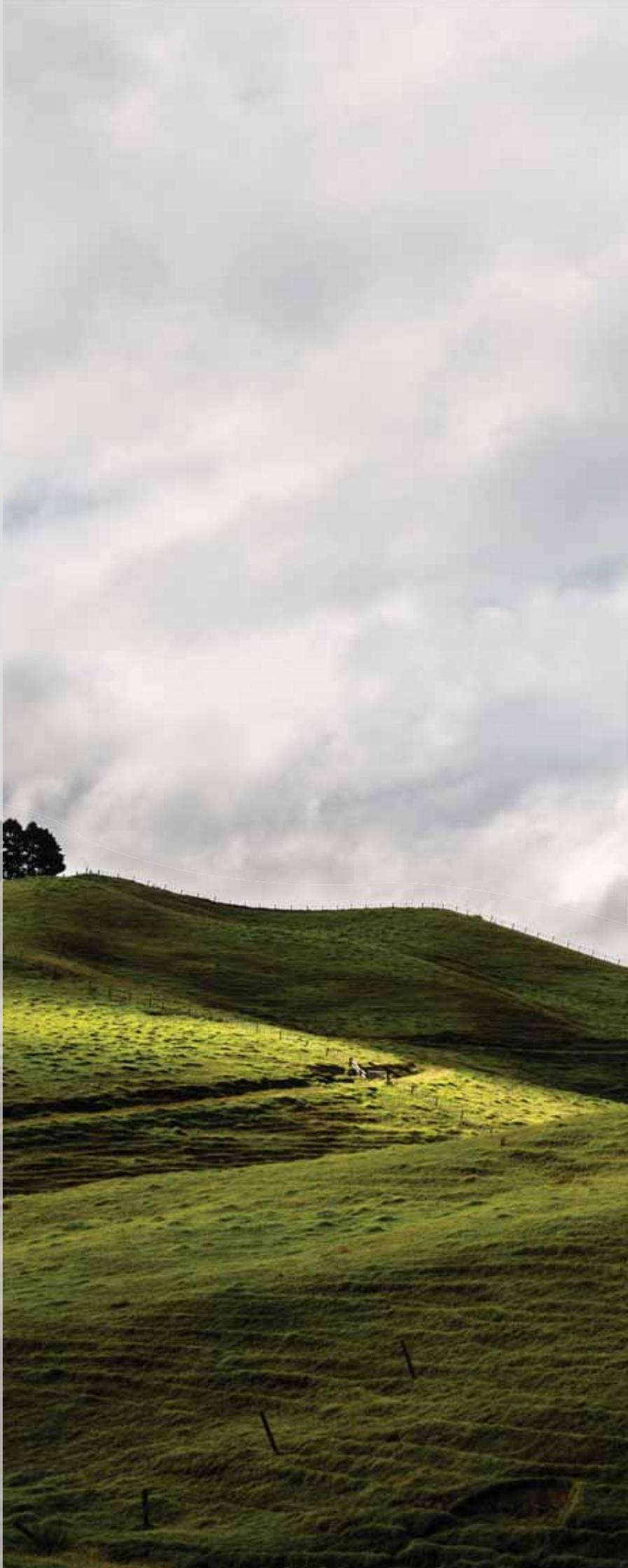
Leading New Zealand's
primary industry into
a prosperous future.

kpmg.com/nz/agribusiness



CONTENTS

- 4 Foreword
- 5 Preparing the agenda
- 6 Highlights of 2012 / 2013
- 8 'Why' the industry must stand up
- 12 Industry priorities
- 19 Biosecurity
- 22 Winning in markets
- 26 Potential of water
- 30 People deliver the future
- 33 Looking for common ground
- 36 Viewpoint: red meat
- 38 A sustainable future
- 41 Challenging piecemeal regulation
- 44 The challenge of capital
- 47 Acknowledgements
- 48 Fuelling New Zealand's Prosperity



WELCOME

The annual KPMG Agribusiness Agenda is a bold platform. We're proud of the fact our expert commentators are prepared to go where others don't.

Our goal is to delve into the sector's most critical issues, and bring them to a central forum. This Agenda provides you with a seat at the discussion table – as our leaders highlight the issues, and debate the way forward for the sector.

In preparing this Agenda, we held Roundtable discussions around the country, gaining the perspectives of more than 100 of the sector's most influential people.

In 2013, the major focus of agribusiness leaders remain the critical issues of biosecurity, water, people, value-added production, and the desire for greater collaboration across the industry. It is pleasing to see progress in these areas over the last year.

Thought leadership of this nature is an investment in the sector's future. Our objective is to stimulate debate – and crystallise the most important issues – in order to map out a way forward. Collectively, we can act upon what we know will further the prosperity of the agribusiness sector. This will contribute significantly towards our ultimate goal, which is to fuel prosperity for all of New Zealand.

This year the Agribusiness Agenda has a slightly different format. In addition to this State of the Nation piece, we will be releasing four further volumes. This allows us to explore the sector's most critical topics in greater depth, and incorporate case studies of excellence in agribusiness.

As with previous issues, the 2013 Agenda is informed, targeted, relevant and game-changing. We hope you enjoy the read – and that it gets you thinking about how we can make New Zealand more prosperous.



Ross Buckley
Executive Chairman
KPMG New Zealand



FOREWORD

New Zealand's economic prosperity and sense of national identity are strongly linked to the performance of our primary industries.

The primary sector remains New Zealand's most productive sector and earns the majority of our merchandise export earnings, generating around \$30 billion a year.

The Ministry for Primary Industries has set an ambitious target of doubling primary sector exports by 2025. This ties in with the Government's Business Growth Agenda, which is targeting an increase in exports from 30% to 40% of GDP by 2025.

A number of the Ministry's current programmes, such as supporting irrigation and increasing innovation through the Primary Growth Partnership, will play a big part in achieving this export double.

This report provides a timely and thought provoking analysis of the factors that will influence the future growth of this sector.

The top ranking priority in this year's report is maintaining our world-class biosecurity system. I agree with the importance that industry leaders place on this, and it remains my number one priority as Minister.

Protecting what we grow from pests and diseases is essential to our future prosperity as a nation.

Our biosecurity system underpins the primary industries and helps create an environment of greater security where people can invest, take informed risks and innovate. The fact that we remain free of many pests and diseases is an important competitive advantage when accessing overseas markets. We must be vigilant in the way we manage the biosecurity system, and look for continual improvements.

I urge you to read this report and consider the insights it provides into New Zealand's most important exporting sector.



Hon Nathan Guy
Minister for Primary Industries

PREPARING THE KPMG AGRIBUSINESS AGENDA 2013

THE AGENDA THIS YEAR HAS BEEN PREPARED BASED ON A SERIES OF 15 ROUNDTABLE DISCUSSIONS WE HELD WITH INDUSTRY LEADERS ACROSS NEW ZEALAND, IN MARCH AND APRIL 2013.

These Roundtables, together with some one-on-one conversations and a quantitative survey on key priorities, have provided the data set for preparing the Agenda. In total we received contributions from 115 industry leaders. We are extremely grateful for the time they gave us.

In order to explore the issues in greater depth, we have decided to publish this Agenda as a series of five volumes over the next eight months. This first volume, titled The State of the Nation, provides an analysis of the top-of-mind issues and priorities of the industry.



HIGHLIGHTS OF 2012 / 2013

It has been a year of dramatic contrasts. The pastoral sectors came into the 2012/13 season with stock condition and pasture cover at exceptional levels around the country. The weather during spring supported record milk production levels. However the driest summer in decades has meant much of the country ended

summer with drought conditions and concerns about the impact on next season. The Field Note headlines for the year tell stories of biosecurity challenges, inconsistent regional regulations, and receiverships; but also significant innovations, market successes and, most importantly, steps towards greater collaboration.

MAY 2012



Foreign-flagged **fishing boats** to be banned

Experts descend on Auckland to hunt **fruit flies**

New Zealand Dairies goes into receivership

JUN 2012



Fonterra purchases NZ Dairies from receivers

Fonterra shareholders vote for implementation of **Trading Amongst Farmers**

JUL 2012



Slow economy puts admission of agriculture into the **ETS on hold**

NAIT scheme goes live for cattle

Riddet institute releases 'A Call to Arms': a blue print for **increasing food exports** to \$62 billion by 2025

NOV 2012



Restrictions on some veterinary **medicines** to be reduced

Losses make the **red meat** strategy 'more relevant'

Devil in the detail for **animal welfare** reform

DEC 2012



China will be New Zealand's biggest wine market

Crafar dairy farms deal finally settled

Marlborough Sounds salmon **fish farms approved**

JAN 2013



Urgent inquiry after **horse meat found** in beef products across Europe

Farm lobby welcomes **Nathan Guy's appointment** as Minister for Primary Industries

Fears of tainted image for NZ milk over discovery of DCD residues



FIELD NOTES

fieldnotes.co.nz

**AUG
2012**



Lamb back on the menu as price slumps

Primary **sector leaders** off to Boot Camp in California

Ministry for Primary Industries (MPI) appoints a **science advisor** to support its decision-making processes

**SEP
2012**



Aussie growers target Kiwi spuds

US lowers forecast **crop yields** for a third time as record heat and drought lingers

Wool Services International board welcomes takeover offer

**OCT
2012**



Westland Milk Products plans **Canterbury** plant

Canada joins TPP talks – Agriculture protection on table

Fonterra unveils **\$500 million** NZX offer

**FEB
2013**



Chinese vegetable 'Made in New Zealand' claim rubbish

Fish exports given sustainable seal of approval

Mega rural supplies merger between **CRT and Farmlands** a step closer

**MAR
2013**



North Island declared a **drought zone**

Fonterra, Department of Conservation announce **\$20 million** waterway plan

Zespri company fined for smuggling kiwifruit into China

**APR
2013**



Surge in **log exports** gives forestry investors hope

Meat reform lobby seeks farmers mandate for change

Greens concerned at approval of use of **GE soya beans** in NZ

‘WHY’ THE INDUSTRY MUST STAND UP AND TAKE A LEAD

WHY DO WE GET UP AND GO TO WORK EVERY DAY? OR MORE FUNDAMENTALLY, WHY ARE WE DOING PRIMARY SECTOR PRODUCTION IN NEW ZEALAND?

These are deceptively simple questions. The latter question first arose during one of our Roundtable discussions. The group made the point very clearly that New Zealand’s primary sector needs to establish ‘why’ we do agriculture – if we are ever to truly understand ‘who’ and ‘what’ the industry is trying to satisfy.

Getting to the heart of the ‘why’ question could be transformational for the industry. If we can answer the question – not just from the industry’s perspective, but on behalf of wider society – then we will be taking a significant step forward.

It will be a step towards developing an accord with all New Zealanders around how the primary sector fits into and exists within our society. Having this consensus view will give our nation a solid platform to develop policy settings that meet the majority needs of both the primary sector and the wider community. We can debate the controversial issues, confident that we are taking into account the different perspectives and priorities of all New Zealanders.

This will ultimately enhance the outcomes the sector generates for its key stakeholders, as well as the wider population.

This is not a pie-in-the-sky idea. It is a proven concept that’s been adopted by progressive businesses around the world, including our own team at KPMG NZ. It has been extremely illuminating to ask ourselves ‘why we get up and go to work every day’. Getting to the heart of the question can transform the performance of a business, by increasing staff engagement around a strategy that’s focussed on where the organisation can make a real difference.¹

Let’s start by taking a closer look at the ‘why’ question.

Some possible answers

Depending on where an individual sits in our society or globally, they are likely to have different perspectives on ‘why’ we do primary sector production in this country. There are as many perspectives as there are stakeholders – whether you’re an urban family, a hobby farmer, a forestry worker, an exporter, or an offshore investor.

The graphic shows some of the possible answers to the ‘why’ question. We can start with the basic human need to eat, which is in my view, the driver of most agricultural activity around the world.

Let’s take another perspective. The land owner is investing in the sector with an intention of generating returns and growing wealth over time. This in turn requires people to be employed in the sector, creating another set of stakeholders with a different answer to the why question – being the ability to create employment opportunities.

¹ This concept was developed by Simon Sinek in the book, ‘Start with Why: How great leaders inspire everyone to take action’, released in 2009

WHY AGRIBUSINESS?

DISTILLING THE 'WHY'

To enhance the lives of New Zealanders and international consumers through utilising our **world class natural resources** sustainably to provide prosperity for our society and a commercial return to those investing capital.



01
To feed ourselves



02
To generate returns and value for investors from New Zealand and offshore



03
To create jobs and opportunities for the population



04
To generate revenues that contribute towards social assets that support our lifestyle



05
To utilise the environmental resources for the benefit of our society



06
To manage our natural environment to support other economic activities



07
To deliver safe, high quality primary products to consumers around the world

What about those New Zealanders who are not directly involved with the sector? Looking through a wider lens, investment returns and employment in the sector ultimately generate tax revenues. The Government uses these to fund the schools, hospitals, roads and other social assets that support the lifestyles we aspire to.

Sustainably managing the natural environment for agriculture also benefits other sectors of the economy – with tourism being the most significant. Without the primary sector we would unlikely have as many visitors to New Zealand as we currently do.

Many suggest New Zealand has an obligation to utilise its environmental resources for the benefit of society. Our natural environment is, after all, one of the key assets the country has. When utilised for agriculture, the resources can be managed sustainably so they can contribute benefit indefinitely.

As somebody that spends a lot of time thinking about the primary sector, the ultimate answer to the 'why' question that I settled on is:

“TO ENHANCE THE LIVES OF NEW ZEALANDERS AND INTERNATIONAL CONSUMERS THROUGH UTILISING OUR WORLD CLASS NATURAL RESOURCES SUSTAINABLY TO PROVIDE PROSPERITY FOR OUR SOCIETY AND A COMMERCIAL RETURN TO THOSE INVESTING CAPITAL.”

Using the 'why' to engage more widely with the community

The importance of the primary sector to New Zealand's economy is not well understood by wider society. New Zealand society has changed over the years – in terms of culture, ethnicity, and aspirations. We are now predominantly an urban-based population. For many New Zealanders, their knowledge of the rural sector is limited to media reports that predominantly focus on the sector's issues and failings.

If we do nothing, we risk a deepening 'them and us' divide. An important first step is to gain an understanding of why we do agriculture in New Zealand, from our many different perspectives. Then we can search out collective win/win solutions for the key issues facing the primary sector.

If we can achieve a wider accord around these key issues, it will deliver significant benefits to the country.

It has the potential to lower costs, by better defining national standards for regulations and eliminating inconsistency. A consensus view will deliver environmental outcomes that are considered by all New Zealanders to create a country we wish to live in. It will also provide a unique and 'honest' provenance story that will resonate with the premium markets we aim to succeed in.

How do we develop a consensus view around what is important to us as New Zealanders? The key areas for consensus must include:

- What lifestyles do we aspire to?
- How do we believe the environment should be used for commercial purposes?
- Where do we collectively draw the boundaries between environments we are prepared to use, and those that should be preserved in their natural condition?

How it might work in practice

What would a debate of the issues look like in practice? A good example to illustrate this is the issue around water quality. The media has made much of the impact the primary sector has had on water quality in recent years. This has convinced many New Zealanders that we have a fundamental problem with dirty dairying, in particular.

More intensive land uses have impacted the quality of water across the country. However, when compared internationally, the nutrient levels in our rivers are rated in surveys as being among the best in the world.

For the average New Zealander, their engagement with streams and rivers is limited to the summer holidays when they want to be able to take a swim. At this time they want the clean, pristine rivers that they may nostalgically recall from their childhoods.

Engaging with the community around this issue needs both the industry and the community to think about the 'why'. The sector needs to recognise that being able to swim in streams and rivers is part of the traditional Kiwi lifestyle and important to many in our community.

On the other hand, the wider population needs to recognise that retaining pristine water will result in production systems having to be redesigned, undoubtedly reducing the volume of product that can be produced. The impact of reduced production, without an alternative revenue stream, is a reduction of income available to fund social assets. New Zealanders will potentially have to reset the expectations they have around their future standard of living.

An open, fact-based conversation around issues such as water quality will likely result in both sides having to make compromises from their

preferred positions. We believe it will lead to a robust accord that preserves what is important to New Zealanders; while setting standards that generate the income to support the standard of living we aspire to.

Leading fact-based conversations

Given that the majority of the population now lives in urban centres, the direct connection many New Zealanders once had with the land is becoming increasingly remote.

As a consequence, the onus falls heavily on the primary sector to educate and inform others about the contribution the sector makes, and the resources that it uses to deliver its contribution. Every organisation and person involved in the industry needs to be prepared to become engaged in these critical conversations. At the end of the day, the outcomes will impact New Zealand's future prosperity.

Fonterra started this process in 2010, commissioning a report from the NZIER, "Dairy's role in Sustaining New Zealand".² However this was largely focused on the contribution the industry makes to New Zealand, with limited analysis of the resources consumed to deliver these outcomes.

It is important that the sector does not appear to be defensive in leading these discussions. The debate must be balanced, and based on facts (although we can, and should, highlight the many examples of best-practice across the industry). Emotion will inevitably be introduced into the conversations by those at both ends of the spectrum of public opinion. A rational, transparent approach will help counter this as we strive to reach common ground.

During the Roundtable conversations, the need for the wider sector to take leadership in discussions around a range of issues came through clearly. This is driven by the regulatory and competitive pressures that are increasingly being applied to many operators – behind the farm gate, at the processing level, and in the market.

Identifying the areas that need sector leadership is not rocket science. They include taking greater responsibility for biosecurity; water management (both usage and quality); attracting sufficient talented people into the industry; managing the sector's impact on the environment; and creating a stable platform for capital investment. These areas are explored further in this first volume of the 2013 Agenda, and many will be expanded on in more detail in the subsequent volumes.

Linking the 'why' to an industry vision and strategy

A key theme of last year's KPMG Agribusiness Agenda was the importance of having a pan-industry vision and strategy; a long-term road map for how the industry will maximise its contribution to all of its stakeholders.

Answering the 'why' question does not deliver a default industry vision. We still believe there remains a significant benefit from creating a pan-industry vision that articulates where the sector wants to be in 20-30 years time; and provides the strategic road map to achieve these objectives.

The ideal goal is to achieve both. As we work towards our pan-industry vision, we can also be working on achieving a broad accord with the New Zealand population. That way, we can ensure our sector goals are taking into account the aspirations and expectations of wider society.

To conclude, answering the 'why' question provides an opportunity for the sector to become much more aligned with wider New Zealand society. We will have closer engagement between urban and rural populations. We will have a society that feels positively about the sector, to a greater or lesser extent. And we will have broad agreement around how New Zealand's natural assets will be managed and utilised for our collective economic and social benefit.

Doesn't that sound like a good reason to get up and go to work tomorrow?



Ian Proudfoot
Global Head of Agribusiness
KPMG New Zealand
Report Author

² NZIER – Dairy's role in sustaining New Zealand – the sector's contribution to the economy: A report to Fonterra and Dairy NZ – December 2010

INDUSTRY LEADERS HIGHLIGHT THEIR PRIORITIES

During the 15 Roundtables we held across the country, there was a high degree of consistency among industry leaders on the challenges and opportunities facing the primary sector; and the key priorities for producers, processors and marketers to focus on.

Despite a generally tougher season in 2012/13, leaders are optimistic that the sector has the potential to deliver significant value growth to the economy in the future. Realising this potential, however, is dependent on leadership and collaboration.

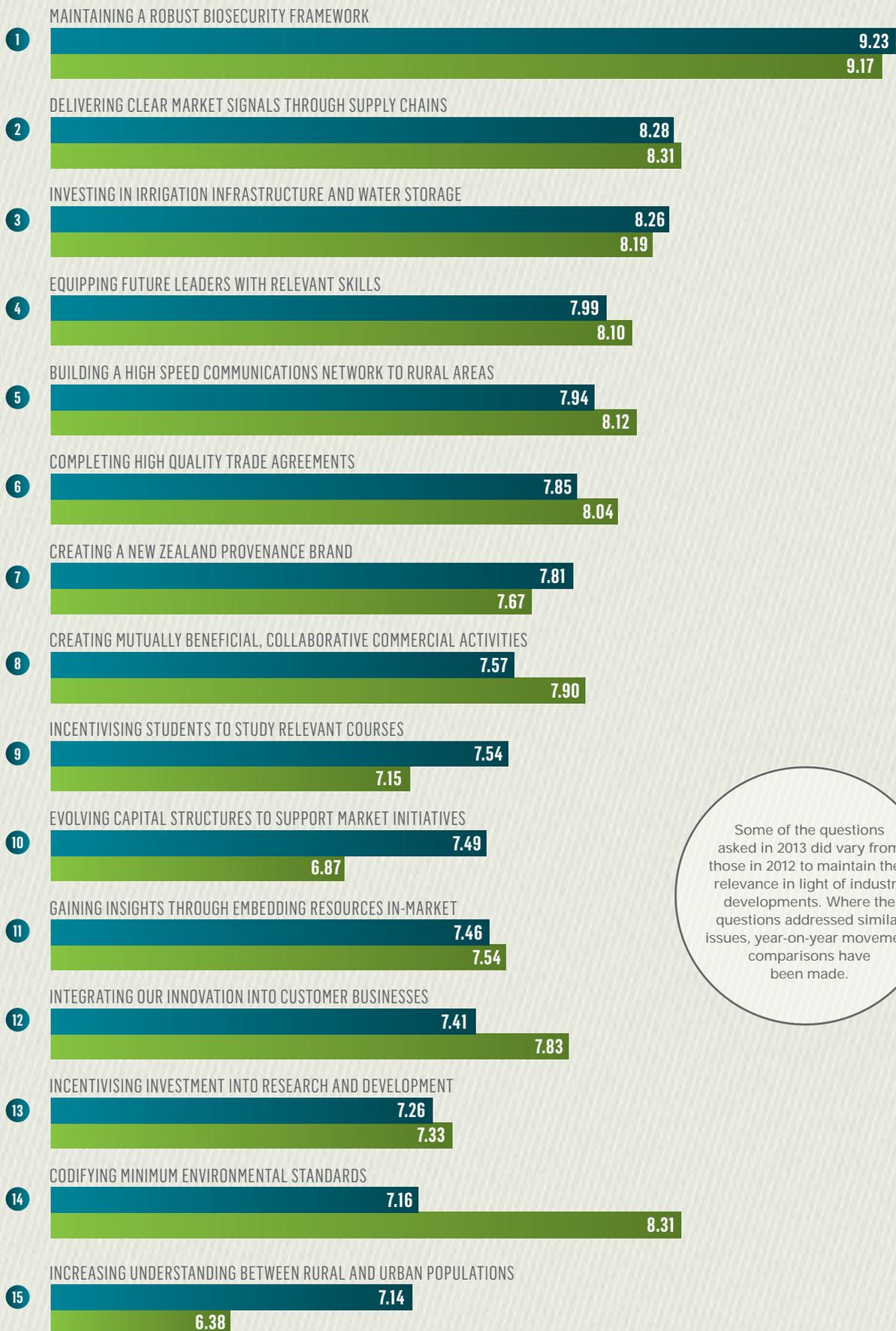
As with past Agendas, we asked industry leaders to rank a range of priorities currently facing the sector.

Respondents to the survey were invited to rank a series of industry priorities on a scale from 1 to 10 (with 1 being an issue of no priority at all, and 10 being an urgent priority requiring immediate implementation).



AGRIBUSINESS AGENDA TOP 15 RANKING

2013 2012



Some of the questions asked in 2013 did vary from those in 2012 to maintain their relevance in light of industry developments. Where the questions addressed similar issues, year-on-year movement comparisons have been made.

THIS YEAR'S SURVEY SHOWS SOME INTERESTING MOVEMENTS IN THE RANKING OF PRIORITIES, COMPARED WITH 2012.



Maintaining a robust biosecurity framework

It is not surprising that biosecurity has retained the number one priority for the third consecutive year. A number of things have focused attention on the adequacy of our biosecurity processes. These include: the impact of the Psa incursion on the kiwifruit sector; the Auditor General's report on the Ministry for Primary Industries' level of response preparedness; and recent concerns over the integrity of the processes surrounding the importation of the Palm Kernel Expeller (PKE). These issues are explored in more detail on page 19.



Equipping future leaders with relevant skills

Both the points in the survey relating to the availability and capability of people moved up the priority rankings in 2013. The issue of directing students to the most economically valuable courses for the economy was given a significant increase in priority. The theme of people came through very clearly in our Roundtable conversations; and particularly the challenge of attracting young people into university programmes that are valuable to the primary sector. The shortage of people is becoming pressing to businesses at all levels of the industry. Consequently we believe a wide-ranging initiative is required to engage widely with children and educate them about the sector.



Incentivising students to study relevant courses

Current industry leaders recognise there is also much work to be done to support the next generation of leaders, so they can gain the necessary experience to lead complex international businesses. Due to consolidation, the pathways many current leaders followed through the industry are no longer available. Therefore many believe that they are obligated to mentor and develop the next generation of leaders.

It was also noted that many companies in the sector lack a comprehensive understanding of all the skill sets required within their businesses to succeed in the Asian century. It is important that skills gaps within organisations are identified, as this can inform the kind of development and mentoring programmes that will bring the right talent into a business.



Creating a New Zealand provenance brand

We heard many anecdotes during the Roundtables about the benefits that “Made in New Zealand” brings to products. The strength of the national brand is confirmed through New Zealand’s ranking in the Anholt-GfK Roper Nations Brand Index, where we rank 16th based on New Zealand’s exports, governance, culture and heritage, people, tourism, investment and immigration in comparison to 50 countries around the world.³ However, the brand means different things to different people. To some it is clean and green, to others it is Middle Earth, and to others still it is nuclear free. An Australian design agency has recently been appointed to work on the framework for the development of a New Zealand brand story, as part of a whole-of-government project.

The core of New Zealand’s primary sector provenance story needs to be unique. It must be different from the stories that can be told by many of the countries and regions that we compete with. The natural environment, the indigenous peoples of the land, and innovation underlying production are all important attributes of our stories. However we believe that our provenance story must be centred around integrity and safety. This is something valued by customers in our growth markets in Asia; and we have the processes and systems to verify it. We hope that whatever brand story the Government produces, the primary sector still ensures its story is based around what is most important to our customers.



Evolving capital structures to support market initiatives

During the year, the launch of Trading Amongst Farmers has seen Fonterra take a significant step in evolving its capital structure to provide the co-operative with the certainty it needs to invest in market-facing initiatives. We have also seen the mergers of Farmlands and CRT to create the largest rural supplies company in the country; and Eastpack and Satara to create the largest post-harvest kiwifruit operator. There has been a significant lift in priority attached to getting capital structures aligned to opportunities in the market, so that companies have the flexibility to respond quickly.

This reflects an increased focus on grabbing the winnable opportunities. The message came through clearly in many Roundtable discussions that the industry still feels more comfortable in investing in production assets rather than market-facing initiatives. Yet we must be prepared to rebalance our investment priorities and direct capital towards the market if want to secure long term consumer relationships.



Codifying minimum production standards

The significant drop in priority attached to this question may reflect a change we made to the wording of the question. In 2012, the priority was described as “ensuring industry practice is sufficiently robust to support New Zealand’s Clean, Green image”. This year it became “codifying minimum standards of environmental protection and stockmanship to protect New Zealand’s international reputation for ethical, safe and sustainable production.”

The two key wording changes were: i) changing ‘ensuring’ to ‘codifying’, and ii) dropping the clean/green and replacing it with ‘ethical, safe and sustainable’. Many of our discussions during the year had suggested the industry should be moving away from the clean/green assertion.

Why the reduction in priority for this item? The Roundtable discussions showed that while industry leaders are strongly supportive of farming in a sustainable manner; there was limited support for achieving this by imposing standards or regulations on the sector. The strong preference was for the establishment of standards to be driven by the market, and the requirements of the customers that we choose to sell to. The switch from ‘ensuring’ to ‘codifying’ may explain the drop in priority this year.

³ Information provided by New Zealand Trade and Enterprise



Increasing understanding between rural and urban populations

There is no doubt in the minds of industry leaders that there are disconnects between the urban and rural populations; and these have the potential to drive poor regulatory outcomes for the primary sector. This lack of understanding also contributes to the challenges the industry has in securing its fair share of the best people from urban areas.

Our discussions noted that mainstream media coverage of the drought had generally portrayed a positive image of the rural sector. It had given the sector a very human face – which is something that rarely happens. The majority of mainstream coverage of the sector revolves around animal welfare issues, foreign land purchasing, and increases in farmers’ income.

It is recognised that the obligation to close the gaps between the rural and urban populations falls squarely on the sector, and everyone connected with it. The sector also recognises the need to enhance this understanding is becoming more pressing. As the sector places greater demand on the natural environment, the regulatory responses (particularly those being introduced by Regional Councils) are increasingly restricting the ‘license to operate’ that the sector has historically enjoyed.



Sourcing products globally to provide year round supply

We were surprised to see a reduction in priority being attached to this item, given the focus in the Roundtable sessions on building market positions and long-term relationships with clients. We believe that if significant investment is being put into building brands in markets, it is critical to preserve the supermarket real estate that is earned by this effort. If we fail to supply product of appropriate quality year round, there is a significant risk that the investment made will be quickly diluted.

Given our geographical location, there is a relatively limited ability to extend the season for New Zealand-produced supply; although these initiatives should continue to be explored.

Sourcing controlled, quality supply from locations around the world has been an important part of Zespri’s success in growing their leadership position in the kiwifruit sector, and securing a significantly higher price than other suppliers to the same markets. We need more successful examples of market positions backed by global supply chains. Such strategies provide our companies with the opportunity to achieve a greater scale in-market than New Zealand-sourced product permits.



Initiating NZ based field trials of cisgenic GMOs

The priority attached to this item has only moved one step up the rankings. However it is apparent from our conversations that industry leaders recognise that the discussion around the use of genetically modified technologies in our agricultural system must be advanced. Globally, the perspectives on GMOs are changing; as it becomes increasingly apparent that feeding a growing population will rely on using these technologies. We have no definitive view on the track New Zealand should take in relation to the issue – given that there are opportunities associated with both our current position and an adoption strategy. However we do strongly believe that having a robust, fact-based discussion on the issue is well overdue, and should happen as a matter of urgency.

2013 RANK	2012 RANK
25	N/A

Establish an umbrella body to represent the industry

When we prepared last year's Agenda, more than 80% of industry leaders supported some form of collaborative industry initiative to develop a pan-industry sector vision and strategy. However when it comes to the establishment of an umbrella body to act as a peak industry organisation for the sector, the response is lukewarm. Our conversations indicated there is little desire to see yet more bureaucracy and cost being added to the sector. That said, it is recognised there are currently many issues that industry would benefit from being able to speak to the wider community with a single voice. Some groups are being formed to achieve this on specific matters – such as water and biosecurity – but more needs to be done.

2013 RANK	2012 RANK
28	N/A

Change monetary and fiscal policy to move the FX rate

We added a priority into this year's survey around whether fiscal and monetary policy settings should be used to manage the exchange rate. We had expected this priority would rank more highly, given the level of discussion in political and business sectors about the pressure the current level of the New Zealand dollar is placing on our export sectors. While no export-focused company likes the current levels of the exchange rate, it is widely recognised there is little that can be done to reduce it; given the structural weaknesses in many markets, the levels of quantitative easing being undertaken by countries around the world, and the strength of demand for the food products we are exporting. Industry leaders appear more focused on the steps they can take to make their businesses profitable at the current exchange rate levels. They recognise this will deliver significant benefits if the rate returns closer to historical levels, although this could be some years away.

2013 RANK	LOWEST PRIORITY FOR THIRD YEAR IN A ROW	2012 RANK
30		30

Restrict foreign investment in agricultural assets

Once again, restricting foreign investment in agricultural land and production assets ranked as the lowest priority for industry leaders. While it is recognised that there is both constructive and value-destroying foreign investment, the predominant view remains that we have always relied on foreign investment in our economy as a small trading nation and this has not changed. We should be seeking out investment partners that are looking for win-win outcomes – creating commercial returns for the investors, and value for the wider economy.

Concern was expressed over the uncertainty that has been added to the foreign investment environment in the last year. Many of the investors we need will now consider it too difficult and risky to invest in this country.

IN THE FOLLOWING PAGES, WE EXPLORE SOME OF THE MOST CRITICAL PRIMARY SECTOR ISSUES FOR 2013.

SEVERAL OF THESE TOPICS WILL BE THE SUBJECT OF A DEDICATED AGENDA VOLUME LATER IN THE YEAR.

- + Biosecurity risks
- + Winning in markets (Vol 3)
- + Realising the potential of water
- + People deliver the future (Vol 2)
- + Looking for common ground
- + Ensuring a sustainable future (Vol 4)
- + Addressing piecemeal regulation
- + The challenge of capital (Vol 5)

BIOSECURITY RISKS

ONCE AGAIN IDENTIFIED AS THE HIGHEST PRIORITY ISSUE BY INDUSTRY LEADERS, THE FOCUS ON THE ADEQUACY OF NEW ZEALAND'S BIOSECURITY INFRASTRUCTURE IS AS INTENSE AS EVER.

The limitations of our current biosecurity systems have been highlighted by the Psa incursion in the kiwifruit sector, as well as a report from the Auditor General. There is a clear view this year that the industry needs to take greater ownership of the biosecurity system to ensure that relevant risks are identified and managed appropriately.

Some leaders suggested that 2012 was a year of real progress around biosecurity. On the positive side, all major industry sectors signed Memorandums of Understanding with the Ministry for Primary Industries (MPI), as a prelude to substantive negotiations over Government Industry Agreements (GIAs). There was also an effective response to the discovery of a fruit fly in an Auckland suburb. However many believe that we struggle to score more than a 'could do better' in respect of biosecurity

The release of the Auditor General's report on MPI's preparedness for an incursion response has reinforced this view for many. The report says that insufficient priority has been given to planning and surveillance activities around potential future incursions, while also suggesting that there is scope to improve our response capability. The Auditor General notes that learning and improvements have been made from recent incursions. However the report states that "serious weaknesses remain"⁴ in plans to deal with future incursions, including an outbreak of Foot and Mouth Disease.

Government Industry Agreements

An interesting feature of the Roundtable discussions was a regularly expressed view that the time has come for farmers to truly recognise how critical a robust biosecurity framework is to their businesses. They need to step up – and take greater interest in, and ownership of, the issues and their management. Most leaders we talked to were supportive of their industry sectors seeking to achieve a comprehensive GIA with MPI. This would increase the focus and engagement around an issue that for most producers is an uninsurable risk which could have catastrophic impact on their business.

Concerns remain about the GIA process and the Government's motivations for implementing the agreements; although there was no doubt that both industry and Government are fully aligned in a desire to mitigate the risk of incursion to the maximum extent possible. We believe the GIA process provides the opportunity to significantly enhance the relevance and effectiveness of New Zealand's biosecurity processes. However the maximum benefit will only be extracted if the following areas of industry concern are addressed during negotiations:

01 / The limited scope of the areas that MPI are prepared to negotiate with individual sectors was raised on numerous occasions. A particular concern raised was that any incursion management strategies applied prior to the border are outside the scope of GIA negotiations. Given that threats by their nature come from offshore,

⁴ OAG Biosecurity report
Controller and Auditor General –
Performance Audit Report – Ministry for
Primary Industries: Preparing for and responding
to Biosecurity Incursions – February 2013





MAY
2012

**WEST AUCKLAND
LOCKED DOWN
AS MPI OFFICIALS
SEARCH FOR
FRUIT FLY**

5540

**HOMES
AFFECTED** 

YEAR IN HEADLINES

JAN
2013

**NEW PRODUCT TO FIGHT
PSA IN KIWIFRUIT
TEMPORARILY BANNED**

MAR
2013

**MINISTRY CRITICISED
BY AUDITOR GENERAL
OVER FOOT AND MOUTH
PREPAREDNESS**

MAR
2013

**COURT DISMISSES PORK
IMPORT CHALLENGE**

a critical part of risk management and mitigation occurs before arrival in New Zealand. The view was expressed that excluding pre-border activities from negotiations will constrain the ability of sectors to effect significant change to the biosecurity outcomes that are achieved.

02 / The complexity of the negotiation process was noted at many of the Roundtables, together with the challenge this is placing on resources within MPI. A high quality outcome for each sector requires MPI to appropriately analyse the issues specific to each sector. It was noted that the process towards completing GIAs is slow, with a perception that MPI is struggling to provide the resources that the process demands. Given that threats will not wait for the GIA processes to complete, it is critical that sufficient resource is allocated to this work.

03 / A major concern was expressed over the lack of clarity around the financial contributions that MPI are looking to sectors to provide. Most leaders recognise that there are 'industry good' biosecurity activities that sectors should contribute to – but there are serious concerns that MPI appears to be looking to industry good bodies to write a blank cheque should an incursion occur. It is important the parties clearly understand the financial contributions they will be required to make on an ongoing basis.

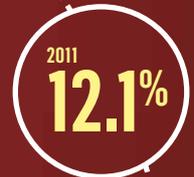
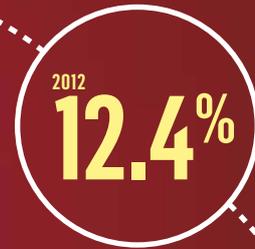
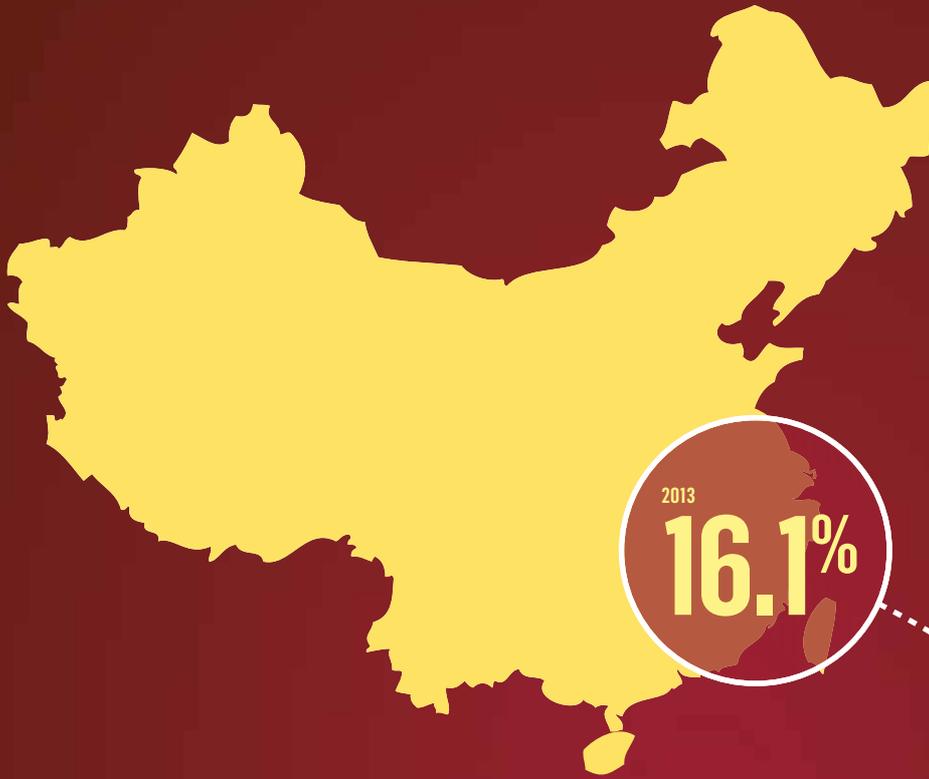
Palm Kernel Expeller

A commonly raised issue during the Roundtables related to growing level of imports of Palm Kernel Expeller (PKE), and whether these are creating a significant risk for the industry. Industry leaders recognise that the financial consequences of the Psa incursion on the kiwifruit sector could have been avoided had tighter controls existed over the importation of pollens. Accordingly, the question is being asked whether sufficient control is being exerted over the importation of PKE. It is recognised that PKE has helped to minimise animal welfare issues in the North Island over the recent summer, but questions persist as to whether the product is a ticking time bomb for a major incursion.

If the industry considers it is necessary to continue to use PKE, it is critical that appropriate investment is made into monitoring and inspection controls before the product arrives in the country. We would support consideration of a levy being charged on imported PKE to fund these inspections prior to the PKE being exported. This is preferable to placing significant trust in the authorities in Malaysia, Indonesia and other PKE-producing countries to perform the necessary inspections to protect our industry's future.

AGENDA ITEMS

- 01 MPI must ensure the negotiation process for GIAs is appropriately resourced so that the necessary analysis can be completed and agreements concluded with sectors in a timely manner.
- 02 An accord is required over the importation of PKE to ensure robust measures are in place at loading ports to minimise the risk of a biosecurity incursion.



PERCENTAGE OF ANNUAL EXPORTS BY DESTINATION

AUSTRALIA

2008	2009	2010	2011	2012	2013
22.2%	23.2%	23.5%	22.7%	22.5%	21.1%

USA

2008	2009	2010	2011	2012	2013
10.7%	10.9%	8.9%	8.7%	8.5%	9.4%

JAPAN

2008	2009	2010	2011	2012	2013
8.7%	8.4%	7.2%	7.5%	7.2%	6.8%

KOREA

2008	2009	2010	2011	2012	2013
3.5%	2.9%	3.2%	3.4%	3.4%	3.4%

UK

2008	2009	2010	2011	2012	2013
4.2%	4.1%	4.1%	3.4%	3.2%	3.0%

Source: Overseas Merchandise Trade Statistics: Statistics New Zealand 2008 to 2013

WINNING IN MARKETS

CONSUMERS ARE SEEKING SAFE, HIGH QUALITY FOOD PRODUCTS – AND NEW ZEALAND IS A WORLD LEADER IN PRODUCING THESE.

The challenge we face is that demand significantly exceeds our supply. Exporters need to focus on selecting market niches of an appropriate scale, where we can control the value chain and utilise branding and innovation to maximise value capture.

“The potential opportunities are scary” was the comment made at one Roundtable discussion. It was a succinct summation of the scale of the markets we could potentially be marketing to. The comment also sums up our challenges. In particular, the markets with the biggest growth opportunities are in Asia. These markets are often new and quite alien to us, and their demand exceeds our supply many times over; forcing us to think carefully about who we partner with.

The key message coming out of the Roundtables was that it is critical that our exporters respond quickly to opportunities in the market, while recognising that they cannot and should not try to be everything to everybody. Winning in markets for New Zealand companies is about dominating targeted, well selected niches; even for our dairy sector.

Empathetic to Asian opportunities

The exponential growth in our trading relationship with China and the economic fallout from the GFC in traditional developed markets has led many New Zealand companies to start to explore business opportunities in Asia, and in particular China.

As a result of the China Free Trade Agreement (FTA), the Government has taken a strong position promoting the trade opportunities with China to New Zealand companies. Many have worked hard in the market to create successful businesses. Our work with companies operating in China continuously reinforces the fact that success there can take time, and cost

a lot of money. There can be as many setbacks as successes.

The view during the Roundtables was that it is important that companies take the time to think beyond China. There may be better opportunities for them in India, Indonesia, Vietnam or the Middle East – to name a few of the countries growing at a similar or faster rate to China.

The key to success in Asia is getting the right local knowledge on board quickly, so the business can interpret and understand what is happening in the market, and seek out the niche they are able to win in. The Government has an important role to play to support companies to get the right resource on the ground in-market to support their export growth initiatives; building on the work already being done by NZTE through the Beachheads programme. It would have been great to see this sort of genuine international market support receiving similar levels of funding to tourism and science in the 2013 Budget.

It is also important that our exporters take the time to understand the consumer psyche in Asia, particularly the consumer preference to buy either either ultra high end products or the cheapest option available. The absence of middle ground between branded, luxury goods and cheap, commodity products is very important for New Zealand companies to understand; as this is often the sweet spot our companies operate in successfully. The key message is that New Zealand products must be targeted at premium



AGRI SECTOR HAS
POTENTIAL TO ADD
\$550BN
OF REVENUE OVER
NEXT 40 YEARS

SEPT
2012
ASIA CAN
DOUBLE
NZ FARM
EXPORTS



YEAR IN HEADLINES

JUN
2012

MEXICO, NZ'S LARGEST LATIN
AMERICAN TRADING PARTNER
JOINS TPP NEGOTIATIONS

NOV
2012

KEY SAYS NZ WON'T SIGN
UP TO TPP UNLESS DAIRY
INCLUDED

MAR
2013

TESCO OUTLINES BRITISH
PLEDGE IN NEWSPAPER
ADVERTS

markets – and the prized attributes are quality, integrity and most significantly, safety.

The dicyandiamide (DCD) residue issue was discussed at many of the Roundtable sessions, with a wide spectrum of views expressed on how the issue was handled by Ministry for Primary Industries and Fonterra. The most significant learning that can be taken from the event is around our response to any issue which has the safety and integrity of food at its heart. The response must be quick, transparent, and from the perspective of the consumer. For a variety of reasons, the response to DCD did not appear to be consumer-focused; and this must be avoided when similar issues arise in the future.

Capturing value from markets

The biggest challenge facing New Zealand exporters is maximising the value of their production. It's easy to talk about the concept of adding value to a product, but can be very difficult to achieve. (If it were that simple, everybody would already be doing it.) Even when a company is successful in adding value, a further challenge our exporters face is capturing a fair share of the value in-market and bringing that back to New Zealand. During the Roundtable sessions, a range of strategies to achieve value creation and capture were discussed. The successful examples often required companies to secure control over more of their value chain; to have unique products with controlled intellectual property or varieties; or have the use of a recognised and powerful brand (either owned or licensed).

Currently, many exporters still focus on moving volume, rather than looking to add value through marketing and branding. This traditional trading approach is easier, and requires significantly less investment of both time and money. However this approach does mean the best a company can expect to achieve in the long run are commodity returns at, or marginally over, the global cost of production; because that is what our overseas competitors will be prepared to sell any excess production at.

Building a brand in-market takes time and requires significant investment. Investing along the supply chain requires a company to be better funded and governed due to the greater risk being assumed. We should recognise that our in-market competitors have a much greater understanding of the market dynamics and culture today than our companies could build in 10 years. They often already have well known brands. It was suggested in a number of the Roundtables that New Zealand exporters should be more willing to seek out in-market players as partners. Our companies could benefit from partnerships that offer the 'best of both worlds'. They could link a competitor's existing market position and infrastructure benefits with our attributes of safety and quality to establish value-generating products in market; with the partners sharing the returns.

Increasing the chances of success

There was little dispute during the Roundtables that achieving scale in market is a significant enabler of success. Fonterra (from its inheritance of the New Zealand Dairy Board) and Zespri have scale in the global market as a result of legislated single desk selling models. The suggestion was made during one Roundtable that the Government should be prepared to take bold moves in this direction. It could facilitate the creation of consolidated businesses with real scale in-market that can afford to make the investments in innovation and long term relationships. There was a radical but interesting proposal that this could be achieved by excluding primary sector companies from the Commerce Act, given that the parameters for assessing a combination should be the global export market.

AGENDA ITEMS

- 01 Direct Government resources towards supporting companies to have permanent in-market resources to enable them to direct their product innovation strategies.
- 02 Develop protocols to handle potential food safety issues quickly and from the perspective of the consumer, ensuring there is an information loop including all impacted organisations.
- 03 Take bold steps to facilitate the creation of businesses with real market scale, including consideration of excluding primary sector companies from the requirements of the Commerce Act.



**MORE INFO
ON THIS TOPIC
VOLUME 03**

This volume will look at export strategies being used by NZ companies and the extent to which market access is assisting market development.

REALISING THE POTENTIAL OF WATER

WATER IS NEW ZEALAND'S MOST SIGNIFICANT NATURAL ECONOMIC ASSET.

Irrigating land significantly increases productivity, but the costs are forcing many land owners to change their land use to justify their investment. We are slowly realising the potential of water; however regulation remains inconsistent and a constraint on investment propositions.

Whether the recent drought is a result of climate change, or merely a once in 50 year event; it has highlighted to the wider population that things don't grow without water. If things don't grow, our exports to overseas markets fall, impacting the economy. Increased awareness of water's central role in our economy creates an opportunity to progress some of the important discussions across the country on developing transformational water infrastructure. This greater awareness is coupled with the support the Government has pledged through the Irrigation Acceleration Fund and the Crown Irrigation Investment Company. The message from many of the Roundtables was that after years of discussion, real progress is being made in realising the potential of water.

Recent data confirms this perception, indicating that the total area of irrigated farmland has increased by 16% since 2007.⁴ The data suggests growth has mainly occurred in Canterbury and Southland, together with a significant increase in the use of precision irrigation technologies over flood systems. Delivering reliable water to land is the greatest productivity multiplier available to the primary sector. Yet despite the progress being made, the view was clearly expressed that we are failing to maximise the opportunity by accepting compromises that are strongly weighted against the productive sector.

Increasing water storage

The ANZ Insight report, *Greener Pastures*, highlighted that New Zealand enjoys an annual renewable water supply of 75.6 million litres per capita. This compares to 10.4 million litres in Europe and 3.5 million litres in Asia.⁵ Even in the last year, which has been one of the driest on record, we have had plenty of rainfall across New Zealand. The issue the sector faces is not availability of water, but one of capture and storage. This requires the construction of large-scale infrastructure, which has a significant impact on the environment and communities in which the assets are developed.

In last year's Agenda, we noted that many proposed schemes were little more than hobby businesses run by passionate farmers as a side line to their farming businesses. These lack the sophistication necessary to progress quickly or secure capital. It is apparent that the schemes making more progress have become much more corporatised. They are often being supported through the establishment process by a Council, with the Ruataniwha project in Hawkes Bay often being cited as making the most progress.

⁴ Statistics New Zealand – Agricultural Production Statistics: June 2012 (Final) – 13 May 2013

⁵ ANZ Bank – ANZ Insight Report: Greener Pastures – The Global Soft Commodity Opportunity for Australia and New Zealand – October 2012



NEW ZEALAND ENJOYS AN ANNUAL RENEWABLE
WATER SUPPLY OF 75.6 MILLION LITRES PER CAPITA ⁵



MAR
2012

**WATER KEY
TO DROUGHT-
PROOFING
AGRICULTURE**



**THE DROUGHT
HAS COST NZ
\$1BN+**

YEAR IN HEADLINES

SEPT
2012

**\$230 MILLION
RUATANIWHA WATER
STORAGE SCHEME FEASIBLE**

NOV
2012

**FRESHWATER REPORT 'ONCE-
IN-GENERATION' CHANCE TO
SETTLE WATER RIGHTS**

DEC
2012

**STUDY OF WAIRARAPA
IRRIGATION PROJECT
FUNDED**

The support of a Regional Council appears to be a key enabler to successful establishment of a scheme, given the challenges of navigating the inconsistent regional regulations around water. A critical priority raised at many Roundtables was the need to finalise the work of the Land and Water Forum, so the Government can provide consistent national guidelines to Councils around water. It was extremely positive to hear about this kind of collaborative industry initiative – as a way of enabling the wider primary sector to engage with Government, Councils and other stakeholders with a single, consistent voice.

Changing the face of farming

It is recognised that adding water to land through irrigation increases the cost of production. When water becomes available there is often a significant shift in land use. In the current economic environment this has generally been towards dairy; as it provides the stable cash flows and higher returns to justify the land-owner's investment to access and utilise water. Although it takes time for farmers to uptake water when it becomes available in a region, it was suggested that over time, post-irrigation land use change can be as high as 70%. This can place pressure on the environment if it is not handled carefully using the precision technologies now available.

Irrigation is changing the face of rural New Zealand, and this creates concern in many communities. It is critically important that farmers and producers take a leadership role in engaging with their local communities to explain why irrigation is important. It needs to be recognised that the increased cost of water can have positive environmental outcomes on irrigated farms; through the consistent and precise application of water which can reduce nutrient run offs. Higher water costs also encourage land owners to explore opportunities to further minimise water use on farms through techniques such as grey water recycling.

AGENDA ITEMS

- 01 Complete and issue final decisions on a national water policy to provide a consistent regulatory framework for investors in potential irrigation schemes to work within.
- 02 A national conversation needs to occur around the pace of dairy conversion; as the impact of land use changes on the environment and communities is a concern to many industry leaders.
- 03 The wider industry needs to develop collaborative initiatives to engage with Regional Councils and communities around water and the economic contribution it can make.

PEOPLE DELIVER THE FUTURE

AFTER YEARS OF WIDELY BEING CONSIDERED TO BE A DYING SECTOR, THE PRIMARY SECTOR IS NOW STRUGGLING TO RECRUIT SUFFICIENT TALENTED PEOPLE TO FILL THE AVAILABLE OPPORTUNITIES.

The industry needs to take a proactive role in educating the wider population about the career opportunities it can provide to students, the urban unemployed, and New Zealanders returning home.

The central theme of the KPMG Agribusiness Agenda in 2012 was the role people have to play in unlocking the potential of New Zealand's primary sectors. It became very apparent from the first Roundtable session that the ability to attract and retain appropriately educated and experienced people in roles across the industry – be they on farm, in laboratories or the boardroom – has become a critical issue to a majority of industry leaders.

There is no quick fix to the people and talent issue. The sunset period of New Zealand agriculture has meant a generation of leaders have actively sought career opportunities outside of the industry. In science areas, the contestability of funding and the lack of freedom this provides researchers to undertake blue ocean experimentation was noted as a reason why we struggle to attract and retain sufficient resource. It was also suggested that intelligent people are looking to work in innovative and dynamic environments. They are not attracted to what they perceive to be staid companies doing the same stuff over and over again.

Suffering from traditional prejudices

We regularly heard that primary sector careers are simply not sexy to the young people of today. By their nature, many primary sector careers are not easy. They require students to study more difficult subjects at school and university (e.g. sciences, veterinary medicine or engineering); and many jobs involve antisocial hours and a high degree of physical labour. It was regularly highlighted that school careers advisors are failing the sector – particularly in urban areas – and have done little to address the perception that agricultural careers are for the intellectually less-able students.

There is little doubt that the primary sector and the contribution it makes to New Zealand is not given the profile it deserves in schools and universities. However the responsibility for this cannot lay solely on the careers advisors. The primary sector has the most to gain from securing its fair share of the talented people in the country, and consequently needs to take a more proactive role in telling its stories to students. The message came through loudly from the Roundtables that the onus is on the industry to take a strong lead in securing the talent it needs, by inspiring young people to explore the opportunities on offer.

What is the message we need to get through to young people more clearly? It's both simple, and powerful. There is no other industry sector in New Zealand that provides as much opportunity for globally relevant careers in science, marketing or business management.

APR
2013

**LIFE ON
THE FARM:
HIGH PAY
LOW COSTS**



AVERAGE FARM
WORKER IS NOW EARNING

\$5500

MORE PER YEAR THAN THE
AVERAGE NZ SALARY



YEAR IN HEADLINES

JUL
2012

**PRIMARY INDUSTRY
TRAINING ORGANISATIONS
TO MERGE**

MAY
2012

**PICA LAUNCHES TO PRESENT
RURAL SECTOR CAREER
OPPORTUNITIES ON A SINGLE
PLATFORM**

NOV
2012

**NUFFIELD FOUNDATION
EXPANDS TO FUND FIVE TRIPS**

Attracting a fair share of talent

The scale of the talent issue and the impact it is having on many businesses in the sector is significant. Yet it was very positive during the Roundtables to hear about some of the initiatives that are being undertaken to attract people into the primary sector. We heard about a range of school engagement programmes; cross-company graduate initiatives; and schemes to provide prospective leaders with boardroom experience earlier in their careers.

Capturing the hearts and minds of young people at an early age appears to be central to the success of any strategy. Leaders talked about their own experiences (such as taking school trips as kids, or of working with mentors) and how these ignited their passion for the primary sector. Early intervention is key. Providing young people with hands-on experiences and inspiring role models is critical to positioning the primary sector in their minds as career option.

The industry also has a lot of work to do reaching out to schools and building on the programmes already in place. A great place to start would be educating careers advisors that a job on the land is not 'just' a farm job, but an entry point to an advanced business leadership career with international prospects and potential to secure significant personal wealth.

We have argued the point strongly in past Agendas and we continue to believe that government has a role to play in directing students to economically valuable careers through reforming the student loan system. In addition, we believe that the industry needs to move quickly to introduce continuing professional education systems at the producer level. This will help to cement its position as a true profession in the minds of potential recruits.

The industry has had to fill many vacancies utilising migrant labour. While these workers are often hardworking and enthusiastic, we heard stories around the country of the negative impacts that migration can have on small rural communities. This was balanced by stories about successfully recruiting unemployed kiwis from urban areas – and New Zealanders returning home – by being open and honest about expectations and the potential the opportunity provides to them.

AGENDA ITEMS

- 01 The wider industry must take a leadership role in engaging with schools around the country. Farmers and producers, processors and suppliers of services to the industry must collaborate extensively to engage with every child and career advisor in schools as a high priority.
- 02 Directing students to economically productive careers should be a priority for government and this can be best achieved through a more targeted student funding mechanism.
- 03 Utilising unemployed people in urban areas in preference to migrant labour should be a priority for New Zealand, and a collaborative project should be developed to explore this.



**MORE INFO
ON THIS TOPIC
VOLUME 02**

This volume will explore the primary sector's people in further detail.



LOOKING FOR COMMON GROUND

FUNDAMENTALS HAVE NOT CHANGED. WE REMAIN A SMALL COG IN THE GLOBAL AGRI-FOOD SYSTEM.

The sector will maximise the value it creates by commercially collaborating to achieve scale in market. Deep collaboration is challenging and requires companies to change. Without bold steps, our relevance in global markets will fade as lack of scale leaves us unable to meet the needs of potential customers.

In July 2012 the Riddet Institute commissioned a strategic report on the agri-food sector titled 'A Call to Arms'.⁶ Its major recommendations centred on the critical importance of collaboration in meeting the aspirational export growth targets that have been adopted by the industry. Consistent with last year's Agenda, the report recognised that effective collaborations have the potential to unlock greater value from the industry; recommending a collective approach to strategy and the establishment of an industry umbrella body.

The Roundtable discussions have reinforced to us that a majority of industry leaders remain supportive of the development of a broad primary sector vision and strategy. However, they also struggle to see how such a strategy would currently be developed with meaningful buy-in across the industry. The view was expressed that while it is fashionable to talk about such collaborations, initiatives of substance remain few and far between.

Government agencies leading the way

It was apparent from our discussions that the Government, industry good bodies, research entities and the universities are being more active in seeking opportunities to work collaboratively than commercial entities. It was noted on a number of occasions that the restructuring

within MPI since its merger has created a more focused organisation, with a far greater propensity to work collaboratively to support the growth of the industry. While tensions remain around regulatory interfaces with the Ministry, its central role in key collaborative initiatives (such as the Primary Growth Partnership) is felt to have increased its alignment to the key drivers of the industry's growth.

Important examples of collaborative behaviour were also highlighted between research organisations, universities and industry good bodies. Some of these initiatives – particularly the Lincoln Hub and Massey's Food and Agricultural Innovation Hub – could potentially have a transformational impact on the country's ability to deliver innovative solutions to production and market challenges.

Core to these hub initiatives are wide groups of partners that are prepared to cede some decision-making control, as they believe this will generate better outcomes for their organisations and the wider industry. The hubs are both at a very early stage of development, but their success will require participating organisations to undergo change. The activities they are proposing to collaborate around are not peripheral – they are fundamental, core elements of their day-to-day activities. Success will require a degree of courage and a passionate belief in the objectives of the projects, and we will watch their progress with interest.

⁶ Riddet Institute, 'A Call to Arms: A Contribution to a New Zealand Agri-Food Strategy', July 2012

JAN
2013

**AVOCADO
EXPORTERS TO
COMBINE
OPERATIONS**



**PRIMOR
PRODUCE**



**SOUTHERN
PRODUCE**



TO HANDLE

70%

OF NZ AVOCADO EXPORTS

YEAR IN HEADLINES

AUG
2012

**PRIMARY SECTOR LEADERS
OFF TO BOOT CAMP IN
CALIFORNIA**

SEP
2012

**KOTAHI FREIGHT
PARTNERSHIP MAY EXTEND
TO WOOL EXPORTERS**

FEB
2013

**FARMERS ENCOURAGED TO
VOTE FOR GROWTH DRIVEN
BY BEEF+LAMB LED PGP**

Commercial collaboration moves slowly

When it comes to the desire of the commercial sector to conduct substantive collaboration to create scale in market, the jury remains out. The NZ Primary Industries Boot Camp, which saw a group of industry leaders spend a week at Stamford University last August, was viewed by the majority of the leaders we talked to as a positive initiative for the industry. It had strengthened networks and seeded a range of commercial opportunities among the attendees.

By virtue of the Boot Camp's timing – which came shortly after the release of 'A Call to Arms' – many industry commentators inadvertently believed the session was a potential forerunner of an umbrella body. This has left some leaders outside the Boot Camp group questioning the value of the programme, given the amount of public money invested, as it has not provided the industry with the leadership some expected. Although establishing an umbrella organisation was never an intended outcome of the programme, the members have continued to work on a range of joint projects which may generate wider benefits to the industry in the future. The challenge for Boot Camp members is how they continue to progress the initiative as company leaders change and new innovative agri-food companies emerge in the market.

There was limited appetite during the Roundtables for another bureaucracy being created in the sector to serve as a peak body. Yet it is hard to see how progress will be made on a collaborative vision and strategy without a person or organisation with influence assuming a leadership role. There was one idea raised which we consider to be worth exploring. That is to create a role for the primary sector which is similar to that held by Prof Sir Peter Gluckman for the science sector, in the nature of a Chief Agricultural Advisor to government. The Advisor, be they a single person or a small group, could have a clear mandate to deliver leadership to the sector and strategic guidance to the Government.

To conclude, we need to call the jury back in. We cannot afford to prevaricate much longer when it comes to the industry's desire and ability to collaborate to create scale in market.

AGENDA ITEMS

- 01 Explore the creation of a Chief Agricultural Advisor to government as an initial step to progress development of a pan industry vision and strategy.
- 02 The learnings from successful collaborative initiatives should be shared across the industry through development of case studies.





WHAT MIGHT THE FUTURE HOLD FOR THE RED MEAT SECTOR?

There are many and varied views on the root causes of the issues the sector faces, and the potential solutions. We recognise that the broad industry model is not delivering for many consumers, processors and producers. On the other hand, we also recognise there is much to celebrate in respect of the sector. We are the largest exporter of lamb, a premium red meat protein, which we deliver to customers across the world in a range of complex products. There are many companies in the sector innovating with their procurement, processing, products and marketing. They are selling into successfully created new markets, and increasing the value they deliver to their stakeholders.

2012 can't be ignored

There are issues with the industry's structure and performance that are highlighted by the results of 2012 – and these cannot be ignored. The sector lacks the balance sheet depth to take many more losses of a similar scale. Change must follow before the banks, and ultimately the liquidators, are called in. Part of the losses of 2012 related to market conditions, exchange rates and other external factors over which we can exercise limited control. These would not necessarily be changed by a consolidation of the industry.

Having listened to the Roundtable discussions, the central challenge facing the sector comes back to confidence and trust. Put simply, we have a view that the majority of farmers do not trust the processors behaviours and vice versa. As a consequence insufficient investments are being made by farmers and processors with both sides adopting short-term, trading behaviours in an effort to make a dollar. There is no confidence that anything will change. As a result, the more certain returns from dairy farming are attractive to land owners and land conversions continue at a good pace.

While the success of the dairy sector cannot be disputed, the vast majority of the leaders that contributed to the Agenda do not want to see New Zealand become a large dairy farm. The red meat sector provides an economic and environmental counterbalance to dairy; having different customers, nutrient demands on land, and lower water requirements. However, the sector will only survive if it generates a return on investment commensurate with the risk being taken by investors.

A silver bullet?

We are regularly asked what our silver bullet is for reviving the sector's fortunes. There is no easy answer to this question, but we are certain of one thing. An imposed, regulated solution that overrides individual property rights is not an option. Common commercial ground needs to be identified; but given the urgency of the situation, significant compromises are likely to

be required by all parties to achieve a workable deal. The size of the prize is significant, with some suggesting that collaboration around livestock supply and processing could generate annual benefits for industry participants of hundreds of millions of dollars a year.

Any change is going to require strong leadership both behind and beyond the farm gate. The industry needs leaders that can balance the commercial interests of their own organisations with a longer term perspective of what the sector needs to move forward and restore confidence. Ideas that have been considered and discarded in the past need to be reassessed, and historic disputes need to be left behind. Now is the time for current industry leaders to satisfy themselves that they are ready to commit to working through this process. There will be numerous reasons not to do a deal over the coming months – but the process needs leaders with the fortitude and willpower to keep pushing forward. We need total focus on the belief that the sector and its participants will ultimately benefit from collaborating or consolidating.

Not surprisingly, the future of the red meat sector featured prominently in discussions during many of the Roundtables.

The structural issues facing the sector were clear for all to see during 2012, with the financial results reported publicly showing much red ink.

REPORTED RESULTS IN RED MEAT SECTOR 2011/2012

COMPANY	ALLIANCE GROUP	ANZCO FOODS	BLUE SKY MEATS	SILVER FERN FARMS
LAST BALANCE DATE	SEPT 2012	SEPT 2012	MARCH 2012	SEPT 2012
REVENUE (\$ MILLION)	1,369	1,212	114	2,015
REPORTED LOSS	\$47.23 Million	\$24.51 Million	\$0.57 Million	\$33.06 Million
PERCENTAGE OF OPENING EQUITY LOSS REPRESENTS	13.7%	10.3%	2.3%	9.0%

Note: Extracted from most recent financial statements filed with the NZ Companies Office
 Other significant companies in the sector do not have filing requirements
 Reported Loss: Net loss reported for Total Comprehensive Income

ENSURING A SUSTAINABLE FUTURE

OUR CREDENTIALS AS A SUSTAINABLE PRODUCER OF FOOD MUST BE ROBUST AND AUDITABLE TO MEET INCREASINGLY STRINGENT CUSTOMER REQUIREMENTS.

The time has come to recognise this. We need to carefully define what constitutes sustainable production, by engaging the wider population in a conversation around our aspirations as New Zealanders.

What are sustainable agricultural practices? The answers to this question remain as diverse today as they were when we published our first Agenda in 2010. As New Zealanders, we have benefited from the inconsistent answers given to this question. They prevented development of a set of global standards for sustainable production, leaving us to measure our 'Clean, Green 100% Pure' messaging against our own standards.

The message from the Roundtables was very clear. If we are to continue to claim to be 'Clean, Green 100% Pure' we cannot take the risk of sweeping our problem children under the carpet. Our customers will see the bumps! The whole industry has got to walk the talk each and every day, with it being preferable that we set our standards ahead of those being demanded by the retailers today. The horse meat scandal in Europe has clearly demonstrated what happens to the brand equity of retailers that breach the implicit trust that consumers place on them to guarantee they are selling what they claim to be selling.

It was noted during a Roundtable that 19 of the top 20 US retailers now have some level of Non Governmental Organisation (NGO) representation on their procurement committees. With the events in Europe it is reasonable to assume that the demands placed on food suppliers will be further tightened in the future. Industry leaders indicated that we need to think very carefully about the standards we apply to our production systems and how these are enforced.

Defining the right thing

It is a sobering thought that in many sectors of the primary economy, each farmer and producer relies every single day on each of their peers doing the right thing to maintain the reputation of the industry. It is even more sobering when you recognise that, in many cases, we have not told them what the right things to do are. The industry is only as strong as its weakest link.

The Roundtables were broadly unanimous in recognising that the status quo cannot be allowed to continue. Some sectors have been able to adopt international standards that are clearly defined and auditable. The best examples are in the forestry and fishing sectors. The Forestry Stewardship Council and the Marine Stewardship Council have developed standards that enable New Zealand producers to have their product certified as grown and harvested in accordance with sustainable practices recognised by potential customers across the globe. New Zealand's wine industry has also taken a proactive stance in defining what it considers to be sustainable wine growing practices. Wineries must now be accredited under the Sustainable Wine programme to be able to take part in industry initiatives.



OCT 2012
CARBON CREDIT CRASH COULD FORCE LAND SALES



PRICE OF NZ CARBON UNITS DROPPED

YEAR IN HEADLINES

JUL 2012
MINISTER ADMITS DOLPHIN PROTECTION IS HURTING THE FISHING INDUSTRY

NOV 2012
UNILEVER, FRIESLAND CAMPINA BUILD ON SUSTAINABLE PARTNERSHIP DEAL

DEC 2012
DAIRY STRATEGY USES WORD 'SUSTAINABLE' IN DOCUMENT'S TITLE

Many of the other sustainability programmes have been created by a processing or marketing company, to meet the needs of their customers, rather than being applied universally across the industry. The view was expressed that processor-specific schemes enable farmers that do not wish to comply with baseline requirements to seek alternative processors with lower standards, and ignore the industry's need for everybody to do the right thing.

As we discussed in the introduction, before we can start defining what will constitute sustainable production standards for the primary sector in New Zealand, there is a need for the industry and the wider community to find common ground over a wide range of issues. These include obvious points of contention such as: the use of genetically modified technologies; the intensification of farming systems; extensive changes in land use; and expectations around the quality of water. The discussion needs to take into account the lifestyle expectations of New Zealanders, balanced against the significant contribution the industry makes to the economy.

The discussion around sustainability must be extended beyond environmental issues into a much more rounded consideration of our aspirations as New Zealanders. Addressing these issues will provide a far more robust perspective on what constitutes sustainable primary sector activities in New Zealand. It will therefore provide much more substance to our core New Zealand brand.

Carrot or stick?

While there was strong support for articulating baseline standards for sustainable production, there was a wide spectrum of opinions on how these should be implemented. The majority of leaders did not favour regulating to introduce the standards; preferring that they were subject to self-management frameworks adopted collectively by all processing and marketing companies. This ensures that there is a national baseline, but it does require the companies to police the standards. They must be prepared not to handle product from farmers who consistently flaunt the standards. The penalties for not complying must be economic. Such a mechanism could also provide an opportunity to reward those businesses that do go the extra mile to do the right thing.

In contrast, there was a sizeable minority of leaders who argue that the baseline standards can only be introduced through legislation. They argued it should not be left to processors to make decisions on whether a farmer is behaving appropriately or inappropriately, suggesting that these calls need to be made by an independent body to ensure that the industry consistently meets the highest standards. It is also suggested that an independent system provides a more effective response to some of the piecemeal regional regulation the industry currently has to deal with.

AGENDA ITEMS

- 01 A process is needed to define what constitutes acceptable production standards for each sector of our primary industries, along with identifying the most appropriate mechanisms to implement the baseline standards.
- 02 Defining sustainable production standards that align with our aspirations as New Zealanders can be used to add significant substance to the New Zealand brand story.



MORE INFO ON THIS TOPIC VOLUME 04

This volume will consider what a sustainable industry looks like from a wider perspective than solely the environment.

ADDRESSING PIECEMEAL REGULATION

INCONSISTENT REGULATIONS FROM LOCAL GOVERNMENT BODIES HAVE THE POTENTIAL TO LIMIT THE GROWTH AND PROFITABILITY OF THE PRIMARY SECTOR.

Regulators need to understand that every rule they place on the industry comes with a cost to somebody. It is critical that these costs are understood before regulations are introduced, and assessed against the benefits they deliver.

Travelling around the country for the Roundtable discussions highlighted the wide variations in regulation that rural communities are currently addressing, or may soon have to respond to, in different regions. Local government bodies are influencing the investment environment for farming businesses; yet are often being left to set complex regulations with limited or no guidance from national policy statements. Concerns were expressed about various regulations being implemented by councils around the country – particularly around the management of water resources (including aquaculture water), consenting processes, and nutrient-related regulations.

Uncertainty and cost

The loudest concern related to the manner in which some councils are proposing to use Overseer, a decision support system for nutrient use and management. It was developed as a management tool to assist farmers in optimising production and environmental outcomes. Overseer was never intended to form the basis for a regulatory framework, and attempts to use the tool in this way clearly illustrates the risk that uninformed regulation could kneecap the potential of the primary sector. Utilising Overseer – in the way that some councils propose – will require dramatic destocking of farms to comply with regulated targets at a huge cost to productive capacity and the economy.

The current framework for setting regulations is considered to be creating high levels of uncertainty for investors into agricultural production businesses. The lack of national policy statements gives councils significant freedom to develop their own regulations. A view was expressed that councils regularly appear to 'be in a hurry to do something'. The perception being they are prone to developing rules based on subjective beliefs rather than detailed scientific research and robust economic analysis. These often political perceptions and opinions are having significant effect on the regulations being set.

The sheer number of councils adds further complexity to the issue. We have 78 local government bodies across New Zealand.⁷ Around a third of the population lives in the Auckland Council region. This leaves numerous local government bodies, which lack the scale or resources to support best practice decision making processes, to regulate our rural communities.



⁷ Local Government New Zealand website: www.lgnz.co.nz



AUG
2012

POTENTIAL TO PROFIT
\$880m
OVER THE NEXT
25 YEARS



KING SALMON
APPLYING TO BUILD

09

MORE FARMS

YEAR IN HEADLINES

NOV
2012

GOVERNMENT REPORT
REVEALS ONE PLAN SLASHING
FARM PROFITS

FEB
2013

WHEELS MAY COME OFF
RURAL DELIVERY

MAR
2013

RURAL TOWNS KEY TO CITY'S
BIG GROWTH IN HOUSING

Winning hearts and minds

The challenge the industry faces is that too many New Zealanders believe its sole goal is to exploit the environment for individual profitability. The industry has not won the hearts and minds of the wider community in this respect. They are not convinced of the industry's desire to manage the natural environment in a responsible manner; nor of its ability to adequately self-manage its obligations to achieve this. In turn, the regulatory response is driven by the reaction of the local politicians to the beliefs held by their constituents.

The view was regularly expressed that some of the regulatory frameworks around the country have significant cost impacts on all rural businesses. This means everyone in the industry needs to be prepared to stand up and argue the industry's case more proactively than they have done in the past.

It is recognised that Federated Farmers have taken a lead in addressing these issues, but they are working with limited resources. There is a belief that farmers, growers and other rural businesses need to collaborate closely to commission the independent research and analysis that councils are leaving undone around some of their proposals. Individual farmers and growers are also best placed to communicate directly with their communities on the economic impacts these regulations will have – and to win the hearts and minds, one person at a time. The message must be delivered loudly and clearly – that those within the primary sector have the most to lose if our natural environment and biodiversity is not protected and enhanced.

AGENDA ITEMS

- 01 The scope and coverage of national policy statements and guidelines needs to be increased to:
 - a) provide guidance within which local bodies can establish regulations relating to primary sector activities, and;
 - b) deliver greater certainty to investors around likely regulatory outcomes.

THE CHALLENGE OF CAPITAL

THE MAJORITY OF INVESTMENT IN THE SECTOR REMAINS FOCUSED BEHIND THE FARM GATE, YET THE INDUSTRY NEEDS GREATER INVESTMENT IN MARKET DEVELOPMENTS.

However securing these funds from New Zealand investors remains challenging – given the capital demands of the succession wave, the inherent volatility of the industry, and the current investment environment.

We set out in our research for this year's Agenda to challenge the often stated 'fact' that there is a shortage of capital available to the primary sector in New Zealand. During the discussions it became apparent that capital can generally be sourced for well-structured investment propositions with commercial rates of return. However, it was acknowledged that the industry is under investing – particularly in market-focused initiatives. The core reason given for this was the lack of profitability and return that primary sector investments have historically generated. The message came through in many discussions that without profitability, investors from outside of the industry have no confidence to make investments in what are inherently volatile businesses.

No shortage of land investment

That said, the demand for land has recovered this year, as have prices. We have seen a significant uplift in farm lending over the last 12 months; as those farmers and growers who have made it through the global financial crisis unscathed take advantage of opportunities to add scale to their businesses. This investment continues, despite New Zealand having some of the highest pastoral land prices in the world.

AGRICULTURAL SECTOR CREDIT (NZSBILLIONS)



Source: Monthly Agricultural Credit Series (C5) Reserve Bank of New Zealand



APR
2013

CHINESE
DAIRY FIRMS
TO SET UP TWO
PROCESSING
PLANTS IN NZ

WAIKATO
REGION

SOUTH
ISLAND

2 PLANT
DEALS WORTH
NZ\$400M+



YEAR IN HEADLINES

OCT
2012

CRAFAR FURORE SHOWED NZ
IN BAD LIGHT, SAYS EXPAT

NOV
2012

FONTERRA FUND SURGES
ON NZX LISTING

APR
2013

MĀORI LAND IS BURSTING
WITH AGRICULTURAL
POTENTIAL

The media have placed significant focus on a small number of land purchases by overseas investors in recent years. Our analysis does not indicate any real increase in the rate of foreign direct investment in land in the last few years; the key reason being that our land is expensive and the levels of return do not stack up for professional investors.

Rather than worrying about the limited amount of foreign investment that has occurred, the view was expressed that far more attention should be focused on the impact high land prices are having on the sector. The two priorities highlighted during the Roundtable sessions related to the ability of new entrants to buy into land, and the impact of the succession wave on the industry. The view was expressed that it is simply not possible for a young person to buy a farm these days without significant equity backing, which most do not have. Even traditional stepping stones to land ownership (via share milking in the dairy sector for instance) are becoming increasingly unobtainable for many as entry costs increase.

The succession issue is a major challenge that requires a significant supply of capital across the sector for the foreseeable future. Many land owners have held off selling their land during the last five years, as GFC impacts were being felt on land prices. As our land owners age, however, retirement options become more attractive and more will seek to sell their farms. As the succession wave gathers momentum, the view was expressed that the sector will potentially see gearing increase further, particularly in traditional sheep and beef areas. Purchasers will then address this by reassessing how the land is used. It is expected that succession will increase the likelihood that land use will be changed where possible to convert to dairy, to secure a more stable return to service the debt. Much work needs to be done to investigate structures that can facilitate a smooth transition of farm ownership, while retaining diversity of land use.

Investing beyond the farm gate

Without capital, it is not possible to make any meaningful investment beyond the farm gate. Creating brands, developing innovative and differentiated products and building trusted customer relationships in markets requires large amounts of investment. Despite these challenges, New Zealand-based primary sector companies have made investments in market development and brands with some notable successes being achieved in recent times. Fonterra has recognised the importance of investing in value-adding activities. During the last year it has implemented Trading Amongst Farmers to provide the co-operative's capital base with the permanence it needs to enable larger, in-market investments to be made (such as the recently announced plan to launch the Annum infant formula product in China).

There is an often expressed view that our tax system incentivises land investment over market-facing investment, as land gains are realised tax free. Debate has continued around proposals from the Labour Party to implement a Capital Gains Tax. There's a relatively widely held view that such a strategy has the potential to at least level the playing field between investment options, in front and behind the farm gate. There is no doubt that we need an investment environment that does not penalise investment directed at the market as it has the greatest potential to generate value for the sector, but there is no certainty that a Capital Gains Tax would have anywhere close to a transformational impact on investment patterns in the industry.

AGENDA ITEMS

- 01 Investigate structures that enable existing capital in succession farms to be partly retained in the business, by providing an incentive for retiring farmers to support new farmers onto their land.
- 02 Explore the full implications of a Capital Gains Tax with the intention of developing a tax structure that neutralises the tax incentives for investments in front of and behind the farm gate.



**MORE INFO
ON THIS TOPIC
VOLUME 05**

This volume will further discuss capital availability and demand, as well as the interactions with foreign and Māori capital.

ACKNOWLEDGEMENTS

KPMG WOULD LIKE TO ACKNOWLEDGE THE CONTRIBUTION OF THE FOLLOWING INDUSTRY LEADERS IN PREPARING THIS REPORT

Michael Ahie	Jeff Grant	Paul O'Brien
Steve Allen	Richard Green	Hon. Damien O'Connor
Wayne Anderson	Craig Greenlees	Warren Parker
Dacey Balle	Philip Gregan	Brian Patchett
Eric Barratt	Jim Grennell	Alison Paterson
Catherine Beard	Hon. Nathan Guy	Mike Petersen
Louise Beard	Mark Harris	Owen Poole
Larry Bilodeau	Sir Graeme Harrison	Nick Pyke
Chris Black	John Harrison	Tim Ritchie
Richard Bowman	Angus Haslett	Sam Robinson
John Brakenridge	Mark Heer	William Rolleston
Barry Brook	Simon Hegarty	Grant Rowan
Michael Brooks	David Hemara	Prof Jacqueline Rowarth
Tom Bruynel	Andrew Hill	Ben Russell
Jon Calder	Brendan Hoare	Jim Scotland
Greg Campbell	Julie Hood	Jen Scoular
Scott Champion	Gary Hooper	Peter Silcock
Peter Chrisp	Traci Houppapa	Prof Nicola Shadbolt
Mark Clarkson	Collier Isaacs	Haylon Smith
Brian Cloughley	Mark Jefferies	Graham Stuart
Keith Cooper	David Jones	Murray Taggart
Geoff Copps	Chris Kelly	Jon Tanner
Neil Craig	Max Kennedy	Geoff Taylor
Anders Crofoot	Natasha King	Nadine Tunley
Grant Cuff	Barbara Kuriger	Herstall Ulrich
Andrew Curtis	Peter Landon-Lane	Ross Verry
Jason Dale	Terry Lee	Sir James Wallace
Tony De Farias	John Loughlin	John Waller
Michael Dunbier	Hon. John Luxton	Mark Ward
Charles Eason	Bob Major	Andrew Warren
Tony Egan	Mike Manning	Donovan Wearing
Connor English	Laurie Margrain	Richard Wild
Richard Fitzgerald	Jeanette Maxwell	Murray Willocks
Eoin Garden	William McCook	Bruce Wills
Howie Gardner	Tony McCormick	Stuart Wright
Colin Glass	Paul McGilvary	Richard Wyeth
George Gould	Bill McLeod	
Prof Hamish Gow	Champak Mehta	
David Graham	Dean Nikora	

KPMG staff photo
acknowledgements:

Justine Todd
Matt Wilcox
Steve Pettigrew

HELPING THE SECTOR PROSPER

NEW ZEALAND CAN AND SHOULD BE ACHIEVING MORE WITH THE TALENT, KNOWLEDGE, NATURAL RESOURCES AND MARKET REPUTATION THE GENERATIONS BEFORE US HAVE BUILT.

We love agribusiness, and take great pride in how our roles as independent advisors, thought leaders, strategists and, in some cases, farm owners helps fuel prosperity for our great country.

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We would like to thank our many clients for the opportunities they give us to help them overcome their challenges and contribute to their successes at home and around the world. Being proudly New Zealand owned, the investment KPMG makes in producing thought leadership for the industry, and our sponsorship initiatives across the agribusiness and food sectors, is our way of saying thank you to our clients for their business. We really appreciate it.

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- » Obtaining R&D funding to support innovation in genetics, seed technology and nutrition
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- » Farming for profit
- » Valuation of brands on a local and international basis
- » Acquisition and transaction support to encourage growth in local and overseas markets
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4

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INDUSTRY
REPORTS

177

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FIELDNOTES



FIELDNOTES.CO.NZ

Contact us

Auckland – Audit

Ian Proudfoot

T: +64 (9) 367 5882

M: +64 (21) 656 815

E: iproudfoot@kpmg.co.nz

Auckland – Financial Advisory Services

Gary Ivory

T: +64 (9) 367 5943

M: +64 (21) 932 890

E: givory@kpmg.co.nz

Auckland – Sustainability Services

Jamie Sinclair

T: +64 (9) 363 3460

M: +64 (21) 475 735

E: jpsinclair@kpmg.co.nz

Hamilton – Tax

Rob Braithwaite

T: +64 (7) 858 6517

M: +64 (21) 586 517

E: rbraithwaite@kpmg.co.nz

Hamilton – Farm Enterprise Group

Hamish McDonald

T: +64 (7) 858 6519

M: +64 (21) 586 519

E: hamishmcdonald@kpmg.co.nz

Tauranga

Robert Lee

T: +64 (7) 571 1773

M: +64 (25) 511 035

E: relee@kpmg.co.nz

Tauranga

Glenn Keaney

T: +64 (7) 571 1784

M: +64 (27) 288 7555

E: gkeaney@kpmg.co.nz

Wellington

Graeme Edwards

T: +64 (4) 816 4522

M: +64 (27) 296 5050

E: gdedwards@kpmg.co.nz

South Island

Andrew Hawkes

T: +64 (3) 353 0093

M: +64 (27) 508 0135

E: ahawkes@kpmg.co.nz

kpmg.com/nz/agribusiness



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