

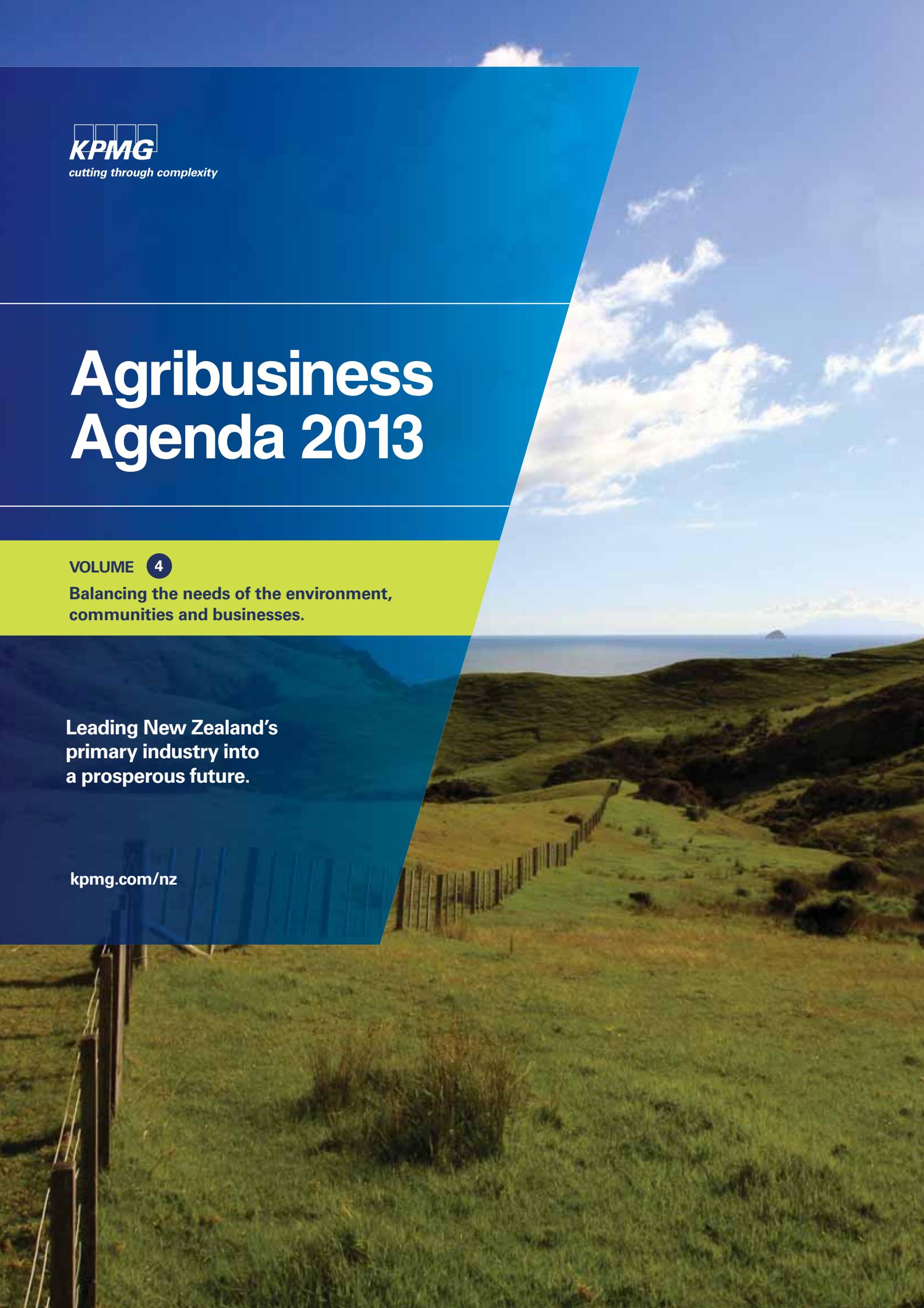
Agribusiness Agenda 2013

VOLUME 4

Balancing the needs of the environment,
communities and businesses.

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

kpmg.com/nz



KPMG IS HELPING TO FUEL THE PROSPERITY OF NEW ZEALAND'S PRIMARY SECTOR DESIGNED TO ASSIST IN CREATING A MORE SUSTAINABLE INDUSTRY...

KPMG supported the production of the Vision 2050 report by the Sustainable Business Council, to provide a vision of how New Zealand could evolve as a sustainable economy.

KPMG supports the development of governance skills in the irrigation sector, to promote the effective development and management of sustainable irrigation schemes.

KPMG has a Sustainability team that works with companies to develop leading edge integrated reports.

Through pro bono work and staff volunteer days, KPMG has contributed more than \$1.3m to communities we work in around New Zealand.



**FUELING
PROSPERITY**

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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.



In order to explore the issues in greater depth, we are publishing the 2013 *Agenda* as a series of five volumes. This fourth volume, titled *Balancing the needs of the environment, communities and businesses*, explores the need to develop a truly sustainable primary sector in New Zealand.

FOREWORD

SUSTAINABILITY IS A TERM OFTEN USED IN THE PRIMARY SECTOR TO REFER TO PRACTICES THAT HELP CREATE ENDURING OUTCOMES.

But sustainability has a deeper meaning than that. It is more than a means to an end.

I draw from the Māori concept of kaitiakitanga, where we see ourselves as guardians – as part of nature, not outside of it. Through kaitiakitanga we protect the environment and manage resources in a manner that meets the expectations and responsibilities of our ancestors, without compromising the opportunities for future generations. It is a deeply ingrained respect for the land and nature, and the associated responsibility to those who have gone before us and those who will follow. As we face constraints from growing our productive capacity, this concept is particularly relevant for Māori, who have significant amounts of underdeveloped land and a growing capacity to develop it.

We have massive opportunities ahead in the primary sector for all New Zealanders, as the sector will continue to be New Zealand's principal growth engine. However, we need to walk the talk when it comes to sustainability. One of the attributes of brand Aotearoa that will enable us to be successful in high value markets is the genuine assurance that we can deliver on sustainability. The New Zealand public, our trading partners, and the world's discerning consumers will demand credibility in this respect.

In this complex world, we often face competing objectives. We feel the tension between primary sector growth and environmental concerns. The tremendous opportunities we have, and the special resources we are privileged to manage, require us to make the right choices as guardians. We need to lead from the edge in today's changing environment with regard to consumer expectations and attitudes. Critically, a sustainability agenda is congruent with a successful primary sector.



Jamie Tuuta

The Māori Trustee and CEO of Te Tumu Paeroa





THE LICENSE TO OPERATE – ONLY AS STRONG AS THE WEAKEST LINK

THE PRIMARY SECTOR IN NEW ZEALAND IS A 'BROAD CHURCH'.

Its members are active in diverse industry groups that manage livestock, crop the land, harvest fish; and grow grass in pastures, plants under glass, fruit in orchards, or trees in forests. However they all are linked by a common thread. Their businesses utilise the world-class natural resources that we have in New Zealand to produce high-quality food, fibre or timber.

Utilising natural resources is at the core of the primary sector's ability to contribute to New Zealand's prosperity. Yet this consumption of natural resource also represents the most significant potential threat to the future of the industry. In preparing this Agenda, a message came through very clearly during our Roundtable conversations. Growing regulatory uncertainty, urban perceptions of the sector's use of natural resources, and some own goals from industry participants are placing increasing pressure on the sector's continued 'license to operate'.

The reputation of the primary sector lives or dies on the actions of every participant in the industry every day. It only takes one weak link – a single operator that fails to meet a recognised production standard – for another story to be splashed across the media; thus fuelling the resolve of regulators and risking access to markets. Regulatory obligations are becoming ever more onerous; but the increasing regulatory and compliance burden does not necessarily progress New Zealand towards a truly sustainable primary sector.

What is a sustainable primary sector? How will we know when we have a sustainable sector? It has been apparent to us over the last four years in preparing the *Agendas* that there is limited consensus among industry leaders over the answer to these fundamental questions. While for many, sustainability is solely about conserving the environment, most literature argues for a wider perspective both in terms of dimensions and timeframe. The Financial Times Lexicon provides the following definition:

"Business sustainability represents resiliency over time – businesses that can survive shocks because they are intimately connected to healthy economic, social and environmental systems. These businesses create economic value and contribute to healthy ecosystems and strong communities".¹

It is our view that New Zealand is unlikely to grow sustainable businesses via a growing web of regulations and rules. Consequently, the onus falls on the industry to slow the encroachment of legislation; by standing up and demonstrating the contribution it is making to our economy, to our communities, and to our environment. As we advocated in the first volume of this year's *Agenda*, the sector needs to take the lead in engaging with the wider community; understanding their requirements, and reaching an integrated, consensus vision on the sector's future within wider New Zealand.

Too often, we hear the commentary that New Zealand's primary sector appears to outsiders as an amalgam of companies, entities and people lacking common goals. They are seen to be running in different directions and making the case to protect their patch. Although the primary sector is a significant contributor to New Zealand's wealth, it cannot expect special treatment from the wider population. Some leaders suggested during our Roundtables that the sector often appears to be self-interestedly whinging, while lacking recognition of the bigger picture.

The bigger picture, of course, is that the urban population will be a significant constraint on the sector if it is not properly engaged with and informed. The urban population generally favours green philosophies, and expect businesses to take this into account. Debate on primary sector issues is often led by interest groups with a perspective on sustainability that focuses narrowly on environmental issues. To counter these arguments, the primary sector has some compelling stories to tell about the contribution it makes to the many dimensions of life that are important to New Zealanders.

Most New Zealanders are open to a wider discussion on what will make this country a truly sustainable, prosperous nation that will guarantee a world-class lifestyle for many generations to come. We believe the key to delivering a sustainable future for New Zealand lies in achieving consensus over how the needs of our environment, our communities and our businesses are balanced. Importantly, this will require everybody in the primary sector to do the right things. We have successful models to learn from, most notably, as we highlighted in Volume 3 of the *Agenda*, the Māori principal of Kaitiakitanga, an approach to managing the environment in balance with restoring and maintaining culture.

If the industry is to retain the confidence of the wider community, we can no longer tolerate the weak links in our systems. The only license to farm in the future will be a license to farm sustainably.



Ian Proudfoot
Global Head of Agribusiness
KPMG New Zealand
Report Author

THE VIEWS OF THE MAN (OR WOMAN) IN AN AUCKLAND COFFEE SHOP

IN BRITAIN, THE HYPOTHETICAL REASONABLE PERSON (KNOWN AS “THE MAN ON THE CLAPHAM OMNIBUS”) IS CONSIDERED TO ACCURATELY REPRESENT MAINSTREAM VIEWS OF THE WIDER POPULATION.

Interestingly, during the Roundtable discussions, industry leaders believed it was the perspective of “the Auckland latte drinker” that will determine the future of the primary sector.

They expressed the view that the rural/urban divide is effectively becoming an Auckland/rest of New Zealand divide. As political parties need to win in Auckland to secure the government benches, they will increasingly present policy platforms that appeal to and reflect the views of Aucklanders. Consequently, the environmentally-focused Auckland latte drinker will influence the thinking of politicians on how they propose to manage the primary sector.

To read the pulse of Auckland latte drinkers, KPMG surveyed more than 100 members of the team in our Auckland office, seeking their views on a range of environmental regulatory issues currently facing the primary sector. While this is neither a scientific survey nor representative of Aucklanders, it does give an indication of how (predominately) young urban professionals think about some of these major issues:

- The good news for the sector is that there is little support for restricting the construction of water storage and irrigation schemes (only 15% support); or allowing councils the freedom to determine local policies in relation to water quality, environmental resources and farming practices (26% support). There is also strong support for utilising taxpayer funds to develop a New Zealand integrity brand backed by robust accreditation standards (66% support and only 15% opposed).
- Opinions are more balanced in relation to the issue of requiring resource consents for farming activities. Around 42% of our latte drinkers oppose the introduction of consents; however a sizeable minority of 27% support such an initiative. This may reflect the fact that consents are required to do virtually anything in the city and they believe the same approach should apply in rural areas.
- We asked the latte drinkers whether agriculture should be included in the ETS scheme, so that the sector pays the cost of the greenhouse gas emissions it generates. We were surprised that more than half our survey population supported the introduction of agriculture into ETS, given the current challenges the scheme faces with the collapse in the price of New Zealand carbon units.
- The results for the other questions we asked were less surprising, but still noteworthy. They give an indication of the baseline requirements the urban population has of the primary sector. For instance, there was 91% support for the preservation of the pristine nature of New Zealand’s waterways and landscape. There was a sizeable majority (72%) who support continuing the limits on the use of genetically-modified plant cultivars in day-to-day food production.
- Interestingly, the majority of our sample (58%) supported legislation to limit the use of indoor animal housing facilities to intensify farm production. This could reflect the traditional view of agriculture in New Zealand, as well as recent high-profile advertising in Auckland against the use of ‘factory farming’ practices.

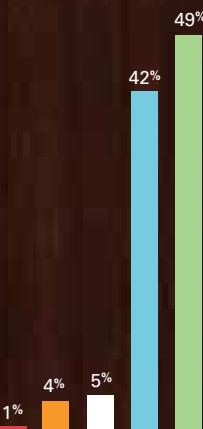
Overall, our team’s responses to the questions were relatively closely aligned with the way industry leaders described their perception of the ‘urban mindset’ during the Roundtable conversations.

This anecdotal survey confirms the task that lies ahead for the primary sector. The sector needs to balance the views that gain most traction in the mainstream media, and explain why sustainable use of the environment is critically important to a prosperous New Zealand.

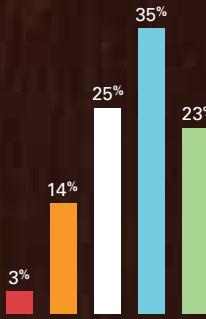
KPMG'S AUCKLAND LATTE DRINKERS VIEWS ON KEY RURAL SECTOR ISSUES.



Strengthening legislation to protect and conserve the pristine nature of New Zealand's waterways and landscape.



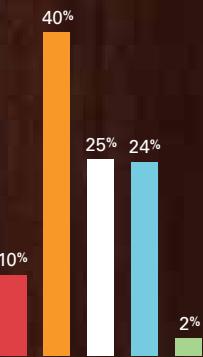
Legislating to limit the use of indoor animal housing facilities to intensify farm production.



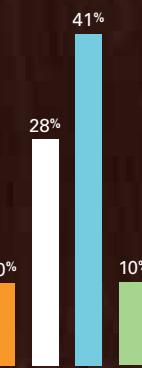
Limiting the construction of water storage and irrigation schemes that have a primary purpose of increasing the productivity capacity of land.



Allowing councils freedom to determine local policies in relation to water quality, environmental resources and farming practices.



Including agriculture in the ETS scheme so that the sector pays the cost of the greenhouse gas emissions it generates.



Using tax payer funds to develop a New Zealand integrity brand backed by robust accreditation standards.



- Strongly oppose
- Oppose
- Neutral
- Agree
- Strongly agree

% = percentage of people interviewed

DESIGNING LONG-TERM, SUSTAINABLE PRIMARY SECTOR BUSINESSES

**INDUSTRY LEADERS
UNDERSTAND THE MODERN-
DAY REALITY: THE PRIMARY
SECTOR HAS NO CHOICE
OTHER THAN TO DEVELOP
SUSTAINABLE LONG-TERM
BUSINESSES BALANCING
ECONOMIC RETURNS,
COMMUNITY BENEFITS AND
ENVIRONMENTAL IMPACT.**

Failure to follow this course risks key customer relationships and the continued license to operate.

So what are the challenges to designing long-term, sustainable business models? During the Roundtable discussions, several key themes became apparent.

01

Understanding customer requirements

Premium customers are demanding to know the products they purchase are being produced sustainably. Industry leaders noted that retailers are setting production standards on behalf of the end consumers. Therefore delivering assurance over sustainable production in order to provide consumer confidence is critical to the future. This assurance will need to be increasingly robust – and will require the industry to think beyond self-regulation and audited self-assessment to build confidence and trust of consumers.

02

Reflecting extensive community contact

All businesses exist within communities. Globally, around 38% of land is used for agriculture² – which means the primary sector has more direct contact with the communities it operates within than almost any other industrial sector. As a consequence the view is increasingly expressed that a charitable donation or sponsorship is no longer an adequate return to the communities that an organisation engages with. Corporate Social Responsibilities must be designed to use the skills and capabilities of an organisation in a constructive, mutually beneficial way to deliver value to the wider community.

04

Accelerating speed of land use change

A common theme during Roundtable conversations was the speed with which the face of New Zealand's environment is changing. It was suggested that the primary sector is currently in a 'two speed mode' – with dairy profitable and growing through continuing conversions; while many other sectors face a variety of headwinds leaving them unable to match dairy returns. For the first time in Roundtable discussions, concerns were raised about the loss of biodiversity and the impact this could have on long-term ecosystem health.

03

An inconsistent regulatory environment

As discussed in Volume 1 of the 2013 *Agenda*, inconsistent and poorly designed regulations from local government bodies are limiting the growth of the primary sector and its potential to contribute to New Zealand's prosperity. The view was expressed that too many important policy areas are devolved to local councils. Many of these bodies lack the resources and funding to appropriately research and implement sound regulation in areas such as water quality, nutrient management and environmental protection; thus adding cost to businesses.

05

Intensification of production systems

Increasing primary sector export revenues can be achieved by volume, or by value growth. Growing volume in any material way will likely require more intensive production systems to be adopted. Achieving this without impacting the environment will require innovation throughout production systems and a willingness to challenge traditional practices, some of which are viewed as New Zealand's core competitive advantages. It was noted during the Roundtables that volume growth in the primary sector cannot be at the expense of the environment.

FOCUS ON SOLUTIONS: A SUSTAINABLE PATHWAY TO A PROSPEROUS PRIMARY SECTOR

06

Suboptimal production practices

It was suggested during the Roundtables that 80% of producers consider themselves to be in the top 20% of performers. The reality is that most systems are suboptimal, and fail to maximise the economic and environmental performance of the underlying assets. The primary sector has delivered greater productivity increases over the last 30 years than most other industries in New Zealand. The differing speeds at which producers are adopting innovation is growing the performance gap between strong and weak performers. This gap creates a risk to the sector's license to operate.

08

Under-investing in science programmes

Another concern was raised relating to whether sufficient science work is being done to provide producers with the sustainable solutions required in their production systems. This work is needed to ensure robust environmental policy settings; and to generate new, sustainable product solutions. R&D needs to push the boundaries of environmental performance on-farm, so that more can be produced from the same or a smaller environmental footprint. Environmental considerations are not a fluffy add-on; organisations need to ensure they are central to all technical decisions.

07

Recognising the importance of water quality

Fresh water is an increasingly scarce resource globally, while New Zealand has a huge renewable water supply (75.6 million litres per capita²). Concern was expressed during the Roundtables that the primary sector has potentially taken the resource for granted. Water quality is one of the most significant points of friction between the urban and rural communities, and the debate goes to the heart of the industry retaining its right to operate. Lack of national policy standards around water quality has created an uncertain investment environment.

09

Other discussion themes on sustainability

Other issues relevant to development of a sustainable primary sector in New Zealand were raised during the Roundtables. The continued lack of a mature conversation on genetic modification continues to be highlighted as an issue that needs resolution. Although climate change is unlikely to impact New Zealand significantly, the need for production systems that are sufficiently robust to withstand adverse weather events was highlighted as a priority; together with addressing the regulatory environment that surrounds carbon trading.

Industry leaders recognise that the primary sector must meet the needs of all its key stakeholders – the customers supplied, the communities that operators exist within, the regulators, the Tangata whenua, and wider New Zealand society. While these groups have different expectations on producers, they are all looking for continuing improvement in environmental performance.

The following sections explore some of the ideas and opportunities identified to lead the sector towards a sustainable future. Over time, they could create long-term improvements in environmental outcomes; more prosperous businesses; and more engaged, aligned communities.

² UN Food and Agriculture Organisation; Agricultural Land Use Statistics; 2012

³ ANZ Insight: Greener Pastures: The Global Soft Commodity Opportunity for Australia and New Zealand - A Report from Port Jackson Partners Commissioned by ANZ – October 2012

01

DELIVERING DEEP ASSURANCE TO CONSUMERS

THEME

Understanding customer requirements

- 01 Premium consumers are looking to purchase sustainably-produced products
- 02 A lack of trust in many markets means robust assurance systems are a critical requirement

As we noted in Volume 3 of the *Agenda*, the world's largest retailers all share a strategic focus on reducing the environmental impact of their businesses.

As part of demonstrating their commitment to sustainable sourcing, it was noted that 19 of the 20 largest food retail chains in the USA have representatives from non-governmental organisations (NGOs) on their procurement committees. These representatives help to define what the end consumers of our products consider to be an environmentally sustainable product.

The challenge for our primary sector producers is that this definition is something of a moving feast. Retailers are continuing to evolve procurement requirements in response to their assessment of consumer perceptions. This is best demonstrated by the response of European retailers to the horsemeat scandal earlier in the year, which has seen significant changes to the supply chain and traceability requirements imposed on producers.

Unsurprisingly, there was very little debate in the Roundtables around the need for industry sectors to have comprehensive ethical food production systems. Indeed it was suggested our companies are unlikely to compete in premium markets without such a system. Customers want assurance that the food, fibre or timber they are purchasing has been produced correctly with respect to various factors. These include: product efficacy and quality, environmental impact, labour management, water utilisation and food safety.



**NEW ZEALAND HAS
THE 16TH LARGEST
AREA OF FOREST**

CERTIFIED BY THE FOREST
STEWARDSHIP COUNCIL AT
15 OCTOBER 2013

**1.49
MILLION
HECTARES**



**THE FOREST STEWARDSHIP
COUNCIL CERTIFIES
180.5 MILLION HECTARES
OF FOREST AREA IN TOTAL
ACROSS 80 COUNTRIES.
NEW ZEALAND ACCOUNTS FOR
0.83% OF CERTIFIED AREA.**

Source: Forest Stewardship Council;
Facts and Figures November 2013: www.fsc.org

Our industry leaders recognise there is a need to 'up the ante' when it comes to on-farm assurance programmes in New Zealand. One idea mooted was to follow the Origin Green system being adopted in Ireland.

The view was consistently expressed during the Roundtables that companies must be active in tracking market developments and interpreting future procurement standards that are likely to be introduced by customers. It was also suggested the industry should be prepared to move to implement these higher standards before they are required by customers, as this creates an opportunity to secure a premium for going beyond the baseline. The domestic Quota Management System for fisheries provides assurance to customers over the management of New Zealand production. As we have noted in previous *Agendas*, the system could be enhanced in the eyes of customers by establishing an independent commission to set total allowable catches, to counter any perception that the system is subject to political influence.

There was concern during the Roundtables that the industry is overly dependent on self regulation, in a global sector which is becoming less trusting as a result of food scares. Some sectors have the ability to link with globally recognised, auditable standards. Companies in the forestry sector can have their production certified under global Forest Stewardship Council standards, for instance; while the fishing industry has sought to have some fisheries certified as sustainable under Marine Stewardship Council standards.

The challenge for the primary sector is to keep ahead of global competitors, without adding significant extra cost that cannot be recovered. If New Zealand companies have a vision to be suppliers of premium products to the most valuable customers, they need to be prepared to invest in better aligning their production system with a customer's understanding of sustainability. Regulation will not deliver success. It relies on deep relationships and customer insights to deliver the product quality required backed by credible, internationally recognised assurance.

AGENDA ITEMS

- 01 Define the baseline sustainability standards producers are required to meet to support the provenance story inherent within New Zealand's primary sector, so that all producers are working in accordance with the broad principles of Kaitiakitanga.
- 02 Evaluate the opportunities to implement an industry led assurance scheme relating to sustainable production techniques, similar to the Origin Green scheme, that aligns with our aspirations as New Zealanders.
- 03 Consider creating a 'customer council' for the primary sector comprising of a cross section of customers for our products, to assist in growing understanding of what is most important to them, particularly around sustainability, and how we can respond to these collectively.



ORIGIN GREEN

Ireland's food producers have launched the Origin Green programme, in response to global customers placing sustainability towards the top of their agendas.

The Irish Food Board (Bord Bia) has developed Origin Green to demonstrate the commitment of Irish food and drink producers to operating sustainably – in terms of greenhouse gas emissions, energy conservation, water management, biodiversity, community initiatives, and health and nutrition⁴.

On-farm behaviour is the foundation stone of the programme. Each producer receives an assessment of their operation's carbon footprint, and feedback on areas to further improve their environmental performance – many of which also tend to enhance the efficiency and profitability of their business. Origin Green is an industry-wide response to assuring sustainable production techniques. Could it be a model that we look to adopt in New Zealand?



⁴ Bord Bia (Irish Food Board); Origin Green Means Growth; www.bordbia.ie/origingreen/; 2013

02

GROWING SUBSTANTIVE VALUE FOR COMMUNITIES

THEME

Reflecting extensive community contact

- 01 Agriculture's land footprint gives it greater contact with the communities it operates within
- 02 Community engagement programmes need to think beyond donations and sponsorships

Companies are increasingly recognising that they have a wider role to play within the societies they operate in.

They are adopting corporate social responsibility (CSR) strategies to meet these obligations. However, there is much debate internationally about whether the traditional approach to CSR is delivering any substantive assistance to the communities it is intended to benefit. Companies are being challenged to rethink the way they meet these obligations.

The key concern around traditional CSR approaches is that they are often peripheral to a company's activities. The company may have appointed a CSR manager or a team that manage a range of projects – yet these projects may not be driving any real change to the business' operations or behaviours. The size of investment is often comparatively small to the size of the business, which may lead to claims that the initiatives amount to little more than tokenism.

In New Zealand, the primary sector has a very large footprint across the country – and companies within the industry physically interact with more communities than most other businesses. This also means companies need to be more creative in how they develop their community engagement plans if they wish to be seen as making a substantive contribution to these communities.

The view was expressed during the Roundtable conversations that carefully crafted community investments are critical to protecting the primary sector's license to operate. They can also make a significant contribution to growing strong links between rural and urban regions. The core of a well-structured programme is a systematic focus on an issue that a company can influence directly through its core operations – and one that will contribute to the development of more robust communities, ecosystems and environments.

Such initiatives are likely to be more challenging to implement than a traditional sponsorship arrangement, as it will likely require changes to the company's business model. These changes may require significant investment and partnership with others to deliver positive outcomes for a range of stakeholders. Compared with the feel-good factor a charitable donation delivers, they may also be more uncomfortable for a company. There may be a need to challenge whether their current business model creates or contributes to the issue they are seeking to influence, and is consequently part of the problem versus being integral to the solution.

We are starting to see more companies take a more holistic approach to community engagement, as token efforts are increasingly being seen for what they are. It is important that every participant in the sector recognises they have a role to play in investing into the communities they regularly interact with in a substantive manner.

The following case study profiles some of the large community investments that Fonterra has made in recent years. This volume of the *Agenda* also includes case studies on ASB's rural environmental compliance loan scheme, and the Ballance Farm Environment Awards, both of which seek to deliver more sustainable outcomes for the sector's wider communities.





WHAT IS THE SINGLE GREATEST OBSTACLE TO SUCCESS IN CSR?

- 23% LACK OF ORGANISATIONAL BUY-IN / COMMITMENT
- 16% LACK OF FINANCIAL RESOURCES
- 15% TIME CONSTRAINTS
- 12% DIFFICULTIES EVALUATING AND MEASURING CSR
- 9% LACK OF NON-FINANCIAL RESOURCES
- 8% SHORT-TERM FOCUS / RISK AVERSION

AGENDA ITEMS

01

Smaller industry sectors could consider opportunities to maximise the impact of their collective community investment and seek to work collaboratively on projects (for instance creating youth employment opportunities, enhancing waterways or developing social infrastructure).

02

Use mainstream media to communicate the impact that community investments being made by primary sector businesses are having on our country to the wider community.

Source: Australian Centre for Corporate Social Responsibility; The State of CSR in Australia and New Zealand - Annual Review 2012/2013; February 2013



TACKLING THE BIG ISSUES



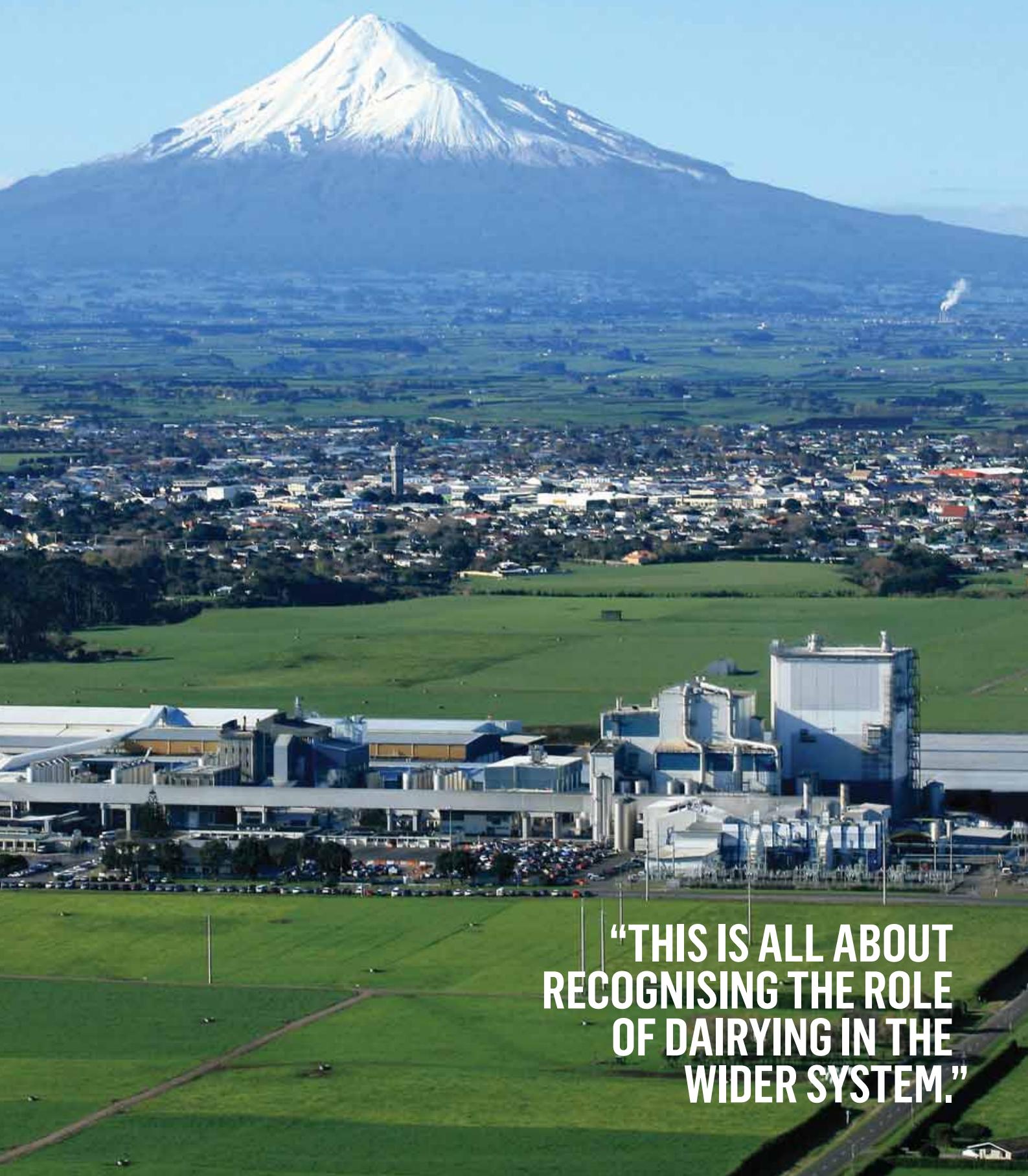
FONTERRA'S APPROACH TO SUSTAINABILITY

When it comes to corporate responsibility, there can be little doubt that Kiwis are keeping a close eye on dairy – and in particular Fonterra.

Global dairy demand is forecast to increase by 3% per annum between now and 2020, and growing demand and need for food security must be met against a backdrop of increasing competition for resources, volatility in climate, in agricultural production and in prices. Customers, consumers and communities will continue to demand high standards of sustainability and ethics for their products. On many counts, Fonterra has recognised these changes and is acting.

Carly Robinson, who leads Fonterra's Global Sustainability and Social Responsibility Group, says the Co-operative has a number of key areas of focus for sustainability.





**“THIS IS ALL ABOUT
RECOGNISING THE ROLE
OF DAIRYING IN THE
WIDER SYSTEM.”**



"WE BELIEVE FONTERA MILK FOR SCHOOLS CAN MAKE A LASTING DIFFERENCE TO HEALTH."

The first area of focus is around leading the way in dairying performance – which includes a strong focus on sustainability initiatives on-farm and throughout the value chain. A leading New Zealand-based programme in this space is Supply Fonterra, which supports farmers to identify ways to improve their on-farm efficiency and environmental performance.

"That means visiting every one of our 10,500 shareholders every year; and working one-on-one with farmers to put plans in place to ensure continuous improvement in performance."

Another key area of focus is providing the natural source of dairy nutrition to everybody, everywhere, every day. Here the organisation places emphasis on making the right type of nutrition accessible and available to all. A key programme in this area is Fonterra Milk For Schools.

"This is about sharing what we do best, which is of course, great dairy nutrition, and sharing that in a way which makes a lasting difference to our kids and to our communities." Milk for Schools offers a daily serving of milk to primary aged students at schools with students in years 1 to 6 throughout the country.

"A further area of focus for us is around creating a better world – a big part of this is acknowledging we operate and work as part of bigger social, environmental and economic systems.

"An example of this is looking at ways we can build a future where a sustainable, thriving dairy industry exists as part of healthy, functioning ecosystems," Carly says.

Fonterra's Living Water initiative pulls together a wide range of activity designed to deliver on this goal. In addition to partnering with DairyNZ on the Sustainable Dairying Water Accord, Fonterra has also launched a joint programme with the Department of Conservation (DOC) to protect the country's most sensitive waterways (see sidebar story).

Carly says it is all about finding the right balance that meets the collective needs of consumers, customers, and communities alongside those of farmers.

"There's still a perception that it's an either-or choice...that you either have economic performance, or environmental performance or something that's best for the community. But that's not the case. They're not mutually exclusive. We recognise that we have a big challenge ahead; there is a real call to action for Fonterra and the wider agriculture sector, as we continue to work to balance the global need for nutrition and food security, with the impact of agriculture on the environment. We've made a long-term commitment to ensuring an enduring Co-operative that sustains our farmers and those we touch."



SUSTAINABLE DAIRY: ONE SIP AT A TIME

Fonterra expects to invest \$15–\$20 million per year in its Fonterra Milk for Schools programme – which offers a free daily serving of milk to all primary school children.

The programme is being rolled out region-by-region, and will be available to all schools by early 2014.

"There's nothing more important than the health of our kids" says Carly Robinson. "We believe Fonterra Milk for Schools can make a lasting difference to health by providing access to great dairy nutrition."

The programme also plays an important role in urban/rural relationship-building.

"Our farmers love bringing the milk to schools. It's something really tangible that means a lot to them, and means a lot to the community. As part of our regional launch events, the kids go and watch milking on a farm. A lot of them haven't been on a farm before... it's great to be able to share that."

ON PROTECTING OUR WATERWAYS:

In March this year, Fonterra and the Department of Conservation (DOC) signed a \$20 million 10-year agreement to work together in preserving some of New Zealand's most sensitive waterways.

Carly Robinson explains the idea behind the Living Water partnership:

"Both Fonterra and DOC have a real passion for improving New Zealand's waterways – we have 10,500 farming families who have a legacy of improving their farms over time, partnering with world renowned experts in conservation – we think it's a great mix, and we're sure that we'll be able to do more together than we could have done separately."

The project is being kicked off in areas of most immediate need – the Kaipara Harbour, Waikato Peat Lakes, Firth of Thames, Te Waihora (Lake Ellesmere), and Southland's Waituna Lagoon.

"Our partnership with the Department of Conservation is about creating a future where sustainable dairying and economic success go hand in hand with healthy, resilient ecosystems."

"They are two incredibly powerful ideas in themselves – a sustainable dairy industry, and a healthy sustainable ecosystem. So to have those two things working in harmony to enrich the lives of all New Zealanders...the potential of that is huge."

**"IT'S ABOUT
CREATING A
FUTURE WHERE
SUSTAINABLE
DAIRYING AND
ECONOMIC
SUCCESS GO
HAND-IN-HAND
WITH HEALTHY,
RESILIENT
ECOSYSTEMS."**

03

ALLOCATING COSTS VIA CONSENSUS REGULATIONS

THEME

An inconsistent regulatory environment

- 01 Regulation restricts the primary sector's ability to deliver to its potential
- 02 Too many critical policy areas are devolved to under-resourced local councils

An analysis performed for KPMG International provided estimates of the direct environmental costs of production processes, and indirect upstream costs that businesses incur but do not pay for fully under current business models and legislation. The story was not a positive one for the global food production sector.

The analysis suggested that the total environmental costs for the sector amounted to 224% of the sector's US\$89 billion EBITDA, or that the sector would have reported a loss of US\$110 billion in 2010 had it been required to pay these costs in full and been unable to pass them through to customers⁵.

The nature of food production involves significant use of environmental resources for which the industry currently does not pay the full direct or indirect environmental cost. Should the industry be required to pay the full cost, it would not be financially sustainable; or be able to deliver the required community outcomes in relation to food security and cost. However, regulation is being designed to allocate more of these costs to food producers, both in New Zealand and globally.

While the environmental cost analysis has been done at a macro level and necessarily involves some significant assumptions, the core message is very relevant to New Zealand's primary sector. The sector is facing increasing regulation, as discussed in Volume 1 of the 2013 *Agenda*, when we highlighted the impact of inconsistent and inadequate local regulation on the ability of producers to commit to long-term business investments. The desire of many regulators to pass more of the environmental cost to producers has the potential to curtail the contribution the sector makes to New Zealand's economy.

During the Roundtables, the view was expressed that well-designed and consistent policy frameworks are critical to the long-term development of sustainable primary sector businesses. These need to incentivise producers to reduce consumption of environmental inputs through an

appropriate costing methodology. The view was expressed that this requires more policy setting to be handled on a national basis, rather than being left to under-funded and under-resourced local councils.

While such a shift in responsibility is desirable for the industry, it would represent a huge swing in political influence from local communities to central government. Given this, perhaps the most that industry leaders could hope for is greater use of National Policy Statements to guide the decision-making process of local councils. The collaborative work done in recent years around water policy provides a model for creating policy guidelines that result in more balanced outcomes. It acknowledges that activities beyond the primary sector have environmental consequences, while expecting the industry to make an active contribution to delivering consensus environmental outcomes.

A view was expressed that more needs to be done to enable councils to facilitate the growth of sustainable businesses. The challenges applicants are facing in securing new water allocations for aquaculture was given as one example where councils need greater specialist support from central government.

In summary, it is recognised that the primary sector must strive to reduce its environmental intensity and bear an appropriate proportion of the cost. However it is critical that regulation is appropriately measured and does not overburden the industry, rendering it uneconomic and uninvestable.



AGENDA ITEMS

01

Explore the development of a Chief Agricultural Advisor to Government as an initial step in developing a pan industry vision and strategy.

02

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) to deliver greater certainty to investors around likely regulatory outcomes.

IF INDUSTRIES HAD TO PAY THE FULL COSTS OF THEIR ENVIRONMENTAL IMPACT IT WOULD IMPACT PROFITABILITY BY:

AUTOMOBILES



BEVERAGES



CHEMICALS



INDUSTRIAL METALS



MINING



OIL & GAS PRODUCTS



FOOD PRODUCTION



= 2010 EBITDA (US DOLLARS)

= 2010 TOTAL ENVIRONMENTAL COST AS A % OF EBITDA , (US DOLLARS)

Source: Trucost 2012 for KPMG International Report 'Expected the Unexpected: Building business value in a changing world.'

04

OPTIMISING THE USE OF AGRICULTURAL LAND

THEME

Accelerating speed of land use change

- 01 Perception that industry is in a two-speed mode, attracting conversions to dairy
- 02 Concerns that excess land use change could permanently impact ecosystems

A recurring subject of discussion during the Roundtables was the speed with which land use in New Zealand has changed over the last 10-20 years.

While there is no doubt that the exponential growth of the dairy sector has created value for the New Zealand economy, many leaders are uneasy about the lack of a clear policy framework around the use of land in New Zealand. There is uncertainty surrounding the long-term impact the changes we continue to experience will have on the environment and rural communities.

The increasing cost of land in New Zealand has made the regular and more predictable returns from dairy farming more attractive to many landowners. This has resulted in a regular stream of farm conversions and growth in the national dairy herd. The concern was also raised that if irrigated water becomes more available to landowners, the incremental costs that the water will impose on farming systems will result in the land being used for the farming activity that generates the most consistent return. This has the potential to accelerate the shift to dairy to deliver an adequate payback on investment.

The risk of putting too many eggs into the dairying basket cannot be overlooked, particularly as more customers include biodiversity within their purchasing criteria. International companies, such as Unilever, are placing greater weight on the maintenance of strong, healthy ecosystems in selecting their suppliers.

We cannot afford to overlook this trend in New Zealand. Concern was expressed that conversion of New Zealand into a large dairy farm would reduce ecosystem diversity, and leave the country exposed to the disease incursions that monoculture farming regions are more prone to. It is consequently important that landowners think innovatively about how their land is used, including considering complementary land uses (such as infill forestry) which can deliver ecological and economic benefits.

A number of leaders attributed the country's laissez-faire approach to land use to a lack of broader vision for the primary sector in New Zealand. A suggestion was made that the policy position currently adopted is to let anybody push to secure the last short-term marginal dollar from a piece of land, without any deep assessment of the impacts this may have on the environment or our society. The response to land use changes is becoming more apparent, with the regulation being implemented by councils across the country.



KEY LAND USE CHANGES IN NEW ZEALAND: BETWEEN 1990-2008

KEY

2008 AREA HECTARES

TOTAL LAND AREA (%)	CHANGE 1990-2008
---------------------	------------------

CROPPING & HORTICULTURE

422,400

2%	+4,500
----	--------

Annual crops or land cultivated for crops. Orchards and vineyards.

HIGH PRODUCING GRASSLAND

5,803,100

22%	-53,400
-----	---------

Exotic grassland with highly productive vegetation.

LAKES & RIVERS

529,600

2%	+200
----	------

Open waters and riverbeds.

LOW PRODUCING GRASSLAND

7,705,800

29%	-311,000
-----	----------

Exotic and indigenous grassland with lower productivity vegetation.

NATURAL FOREST

8,101,900

30%	-50,700
-----	---------

Forest and shrub that is not grazed around and is, or could grow to, five or more metres tall.

NEW FOREST LAND

586,600

2%	+586,600
----	----------

Natural or planted forest present in 2008 but not in 1990.

FORESTRY LAND PLANTED BEFORE 1990

1,432,400

5%	-47,900
----	---------

Exotic forest used for either timber production or protection; eg, erosion or river control. Includes harvested areas.

SCRUBLAND

1,059,600

4%	-125,100
----	----------

Scattered scrub within or near grassland not protected or managed for regeneration.

SETTLEMENTS

206,100

1%	+2,600
----	--------

Urban areas, towns and settlements.

WETLAND

114,500

1%	-100
----	------

Wetland with vegetation.

WE NEED TO ENSURE OUR LAND USE DECISIONS ARE STRATEGICALLY MANAGED, TO ASSIST IN THE CREATION OF SUSTAINABLE PRIMARY SECTOR BUSINESSES AND LIMIT ANY THREATS TO MARKET ACCESS.

An alternative approach to land use allocation was mooted by industry leaders. This would involve developing a strategy that assesses how land would be best utilised to maximise long-term return that is generated in export markets while maximising the environmental outcomes. This may require a change in the mix of what we produce, to meet both the needs of customers and deliver the environmental outcomes the wider community is looking for.

This approach is not without challenges, however. There remains very little enthusiasm for government intervention into land use allocation decisions, given the costs that other consenting activities have imposed on the industry.

In the final analysis, we cannot afford to ignore global purchasing trends around biodiversity and healthy ecosystems. We need to ensure our land use decisions are strategically managed, to assist in the creation of sustainable primary sector businesses and limit any threats to market access. We also need to think innovatively about how the industry can benefit from using land for multiple complementary uses.

AGENDA ITEMS

- 01 Development of a vision and strategy for New Zealand's primary sector is required to help to guide decisions over land utilisation to maximise outcomes for the environment, communities and businesses.
- 02 Recognise that biodiversity is becoming a key purchasing criteria for many global businesses and explore opportunities to incorporate complementary land uses into production system models.

05

INTENSIFYING PRODUCTION WHILE TREADING LIGHTLY

THEME

Intensification of production systems

- ① Growing volume will likely require an intensification of production systems
- ② Traditional practices are often viewed as New Zealand's competitive advantage

When intensification is linked with agriculture, it is often associated in many minds with the worst excesses of factory farming and industrial food production.

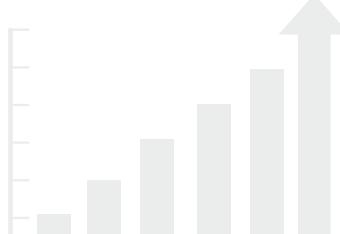
It was noted during the Roundtables that while people are not keen to see farming systems intensified, they are looking for cheaper food prices. The latter relies entirely on being able to reduce the cost of unit production.

As we discussed in Volume 3 of the 2013 *Agenda*, there are three possible strategies available to achieve the growth in exports the Government has challenged the primary sector to deliver. They are growing volume, growing value, and extracting a return from intellectual property. While there is concern that the industry remains overly-focused on growing its productive capacity rather than creating value through customer engagement, it is also recognised that volume growth is a strategic option that the sector cannot afford to ignore.

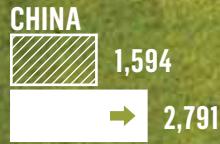
The view was expressed clearly during our discussions that while volume growth requires greater intensity of production, it cannot be delivered at the expense of sustainable environmental practices. Instead the industry needs to challenge itself to produce more production from the same or lower levels of inputs. One leader suggested the sector aim for a transformational goal over the next decade – such as tripling production while halving the inputs employed.

The current reality facing the primary sector is more pragmatic. As operating costs increase, intensification and greater production is required for many operators to stay in business. A point of significant debate among leaders centred on how far the industry should be prepared to depart from its traditional production techniques to deliver the increased production required to make a viable business. Given the role of dairy in our primary sector, this discussion often revolved around the replacement of traditional pastoral dairy systems with more intensively-housed systems.

Many passionately express the view that New Zealand cannot afford to lose the competitive advantage that pastoral farming gives us. In their opinion, the cost advantages it delivers to farmers, and the quality of the product it enables us to produce, is what makes us globally competitive. It is argued that animal housing is contrary to this competitive advantage. It is higher cost; it runs counter to the clean, green image of our pastoral system; and it would remove a key differentiator from our competitor countries.



MILK PRODUCTION PER COW IN KILOGRAMS FOR TOP 10 DAIRY PRODUCTION COUNTRIES



■ = KG's MILK PRODUCED PER COW IN 2000

■ = KG's MILK PRODUCED PER COW IN 2009

Source: Bulletin of the International
Dairy Federation 446/2010



Those prepared to explore housed systems say that the controlled environment can deliver better animal welfare and environmental outcomes; while targeted feeding can deliver significantly greater levels of output from the same genetic stock of animals. They suggest housed systems are the silver bullet for the sector - increasing production and improving environmental performance. They challenge how we can grow volume and value, without extensively degrading the environment, if we continue with pastoral farming.

Coming back to KPMG's Auckland latte drinkers, there was less than 20% support for intensifying production through use of animal housing. Thus the issue comes back, as so many do, to the perceptions society has of a particular farming system. The number of farms using a solely pastoral-based feeding system is declining in New Zealand. This will continue as farmers use supplementary feeds, such as imported Palm Kernel Expeller, to augment pasture feed and drive production growth.

The challenge for the sector is to create models that allow output to grow while mitigating environmental impacts within a particular ecosystem. The optimal model in the Waikato will not be the same as that in Southland. Industry participants will need to engage with their local communities to demonstrate how the models they are adopting deliver the sustainable outcomes that are being demanded by the wider New Zealand society.

AGENDA ITEM

01 Facilitate a mature conversation over the role of more intensive farming systems within New Zealand's primary sector, incorporating the views of customers, producers and the wider community.

“THE ISSUE COMES BACK, AS SO MANY DO, TO THE PERCEPTIONS SOCIETY HAS OF A PARTICULAR FARMING SYSTEM.”

CASE
STUDY

AN IDEA YOU CAN BANK ON



ASB'S RURAL ENVIRONMENTAL COMPLIANCE LOAN SCHEME

If you're wondering where your farming neighbour found the cash to fund that ground-breaking new effluent management system – it could be thanks to a new low-cost loan from ASB.

The ASB Rural Environmental Compliance Loan is a fee-free loan of up to \$200,000 for up to five years, that's provided on a cost-of-funding basis. (At time of writing, the interest rate is 3.8%).

Mark Heer, ASB's general manager of rural banking, explains the thinking behind it:

"We'd been having a lot of conversations with our customers – as well as Government and industry bodies such as Federated Farmers – about getting the balance right between productivity and sustainability.





**“IT’S HELPED
US TO MAKE
THE DECISION
TO DO THINGS
THIS WAY.”**



**“IT’S BEEN A
REAL POSITIVE
BOOST FOR
ANYONE
TRYING TO
DEVELOP THESE
INITIATIVES.”**

“There is plenty of opportunity for New Zealand to produce more, and grow our exports; but that increased productivity has to be balanced with the impact it has on our land and water. It’s an issue that’s impacting all of the rural sector.”

Local ASB people were also having over-the-farm-gate conversations with customers over their own challenges around sustainability, and bringing those ideas back to the head office.

“Once we’d brought all those factors together, we realised we wanted to achieve two things,” says Mark Heer.

“Firstly, we wanted to increase the level of conversation with our customers and other rural professionals – to share insights and views, and rally people. That in itself is an important element when you’ve got a big customer base. But we also wanted to provide something tangible that would be part of the solution. And as a bank, the practical thing we can do is provide a low-cost funding option to actually fund some of this investment on the farm around environmental sustainability.”

Since the launch in late February this year, ASB has provided 183 loans to both new and existing customers. The total loan value is just under \$20m, and the average loan size is around \$110,000.

The purpose of the loan can be for any on-farm initiative that has a positive impact on the sustainability of the land.

“Most have been effluent related, but there’s definitely a wide mix. We’ve funded bridges across streams, underpasses to roads, fencing of waterways and planting of trees. We deliberately went down that path because we want to engage with all farmers, not only the dairy sector.”



SO WHERE'S THE ROI?

A cost-of-funding loan isn't exactly a big earner. So what's in it for the bank?

As Mark Heer explains, there are other kinds of returns.

"We've started talking to farmers around the country who weren't necessarily ASB customers before, and we've been able to generate some new business from that, albeit not revenue-generating. But the bigger picture is that this initiative is supporting the good of the industry. And that's the return for us, from a brand and corporate responsibility perspective."

He says the reaction from industry has been "one of surprise, and a little bit of excitement."

"We've had a lot of positive feedback from industry, and that extends through to the service industries that are providing sustainability services on-farm. It's been a real positive boost for anyone trying to develop these initiatives."

"At the end of the day, it's great if we get some business out of it, it's great if it's good for our brand... but it's also very, very important to the industry."

ON PROJECTS AROUND THE COUNTRY:

From planting the banks of our waterways – to creative new ways of processing effluent – the ASB loan is being put to various uses around the country.

Tirau goat farmers Riemer Loonstra and Kylie Van Bysterveldt are cleaning up swampy wetlands to preserve the natural springs and waterfalls on their property on the shores of Lake Karapiro.

"Sustainability is a big part of what we're doing here," says Riemer. "The land we are on is right up against the lake. It's a beautiful area of the country and we really want to preserve that."

The Bennett family of Matamata have a purpose-built 'HerdHome' shelter to accommodate an additional 250 cows. By draining effluent through floor slats, it forms a dry material that can be removed once a year for spreading on pasture.

Waikato dairy farmer Kevin Ferris, who runs a 440-head herd at his property near Te Awamutu, has also invested in a unique new effluent system that will future-proof his farm's requirements for the next few decades.

"The ASB loan has made a tremendous difference. It's helped us to make the decision to do things this way, and I'm sure it's helping people to put in systems where they otherwise wouldn't have."

"IT'S AN ISSUE THAT'S IMPACTING ALL OF THE RURAL SECTOR."

06

ACTIVELY DEVELOPING BEST-PRACTICE OPERATORS

THEME

Suboptimal production practices

- 01 Too many operators deliver suboptimal returns from their asset base
- 02 The gap between the best and weakest operators continues to grow

Poorly designed and operated production systems present one of the most significant risks to the primary sector's continued license to operate.

The most profitable operators have the capacity to effectively balance their system - to optimise output, quality and environmental impacts - while delivering a strong earnings outcome. The operator of a suboptimal system, however, will do whatever they need to do (even if it is at the expense of quality or compliance with accepted standards) to make a dollar and survive. It is when operators are fighting for survival that the reputation of the industry is most put at risk. Environmental management and animal welfare are two areas where failure most often attracts adverse headlines to the industry.

During the Roundtable conversations, there was much talk around the need to improve the average operating standards across the primary sector. The focus was on the personal responsibility of every operator to do the right thing. Leaders also discussed how operators could be incentivised to make the necessary changes to their business, and the appropriate mechanisms that need to be adopted to actively deliver improvements in average production standards.

The challenge many operators currently face is that the compliance environment is fragmented and inconsistent. This increases the risk that operators only understand or comply with some rather than all of the rules.

Some leaders also argued that the current rules do not go far enough. They are insufficient to support the claims we ought to be making in market around the sustainable production practices used to produce our food, fibre and timber products.

Industry good organisations have a key role to play here. Firstly, they can maintain a full schedule of compliance requirements for operators in their sector to ensure they are clear on the rules they need to follow. Secondly, by liaising with market participants, they can ensure these requirements are sufficient to deliver the assurance demanded.

It was widely recognised that a mechanism is needed to recognise those operators who do the right things – while countering those who are unwilling to comply with minimum baseline operating standards. In Volume 3 of the 2013 *Agenda*, we reviewed the Sustainable Winegrowing initiative which requires mandatory compliance if a producer wishes to be involved in New Zealand Winegrowers' events and promotions, thus providing operators with a carrot to participate. Although a carrot is a preferable to a stick, the view was expressed that there should be financial consequences to those farmers who break the rules; such as non-collection of milk, fines or reparation payments.

Discussion also highlighted the need for any compliance mechanism to be more substantive than a self-audited, tick-the-box framework. It was suggested that any framework should ensure that operators are 'acting as if the customer is watching over the fence, all day every day'. It highlights the need for increased professional standards across the industry. In our view, increasing on-farm standards creates another burning platform for establishing a comprehensive Continuing Professional Development (CPD) programme across New Zealand's primary sector.





BY THE
END OF JUNE 2013
CHORUS HAD LAID

**2150 KM
OF FIBRE**

AS PART OF THE
GOVERNMENT'S
RURAL BROADBAND
INITIATIVE

THIS HAD BROUGHT

**51,200
CUSTOMERS**

WITHIN REACH
OF BETTER
BROADBAND

Above Source:
Chorus Limited; Annual Report 2013

IT HAS BEEN RECOGNISED BY INDUSTRY LEADERS THAT THE SECTOR IS A SLOW ADOPTER OF TECHNOLOGY SOLUTIONS.

Technology

It was also recognised that technology has an important role to play in accelerating the development of best practice operators. While the primary sector has continually outperformed the New Zealand economy in respect of the productivity improvement, it is recognised by industry leaders that it has been a slow adopter of technology solutions.

There are many reasons proffered for the slow adoption of IT; including the average age of farmers, inadequate communications infrastructure, and the lack of easy-to-use applications. Yet there are many good examples among producers who are using technology to collect and analyse data, and use this information to inform decisions that deliver superior outcomes for their businesses.

Work needs to continue at pace to address the infrastructure issues that will improve the speed and reliability of technology solutions. However an extensive education programme is equally important – to help producers understand how they can use technology in their businesses, and train the skills needed to capture its benefits.

AGENDA ITEMS

- 01 Work is needed to define and codify what constitutes acceptable production standards for each sector of our primary industries, along with mechanisms to ensure baseline standards are met.
- 02 Continuing professional development and learning (both formal and informal) should be an expectation on every person working in the sector to ensure practice around 'mission critical' areas such as environmental protection and biosecurity are kept up-to-date.

07

RESPECTING OUR VALUABLE WATER RESOURCES

THEME

Recognising the importance of water quality

- ① Extensive water supply in New Zealand has meant it has been taken for granted
- ② Water quality is one of the significant friction points between urban and rural populations

We have written about water extensively in our *Agenda* publications over the years, recognising the strategic importance of New Zealand's most critical natural asset.

Much of our past commentary has been on the need to make infrastructure investments to enable better capture and storage of water, increase irrigated land area, and deliver significant productivity improvements. The slow progress of many irrigation schemes reflects the challenge of developing major infrastructure projects, including the need to engage extensively with communities to assess the social impacts any scheme may have.

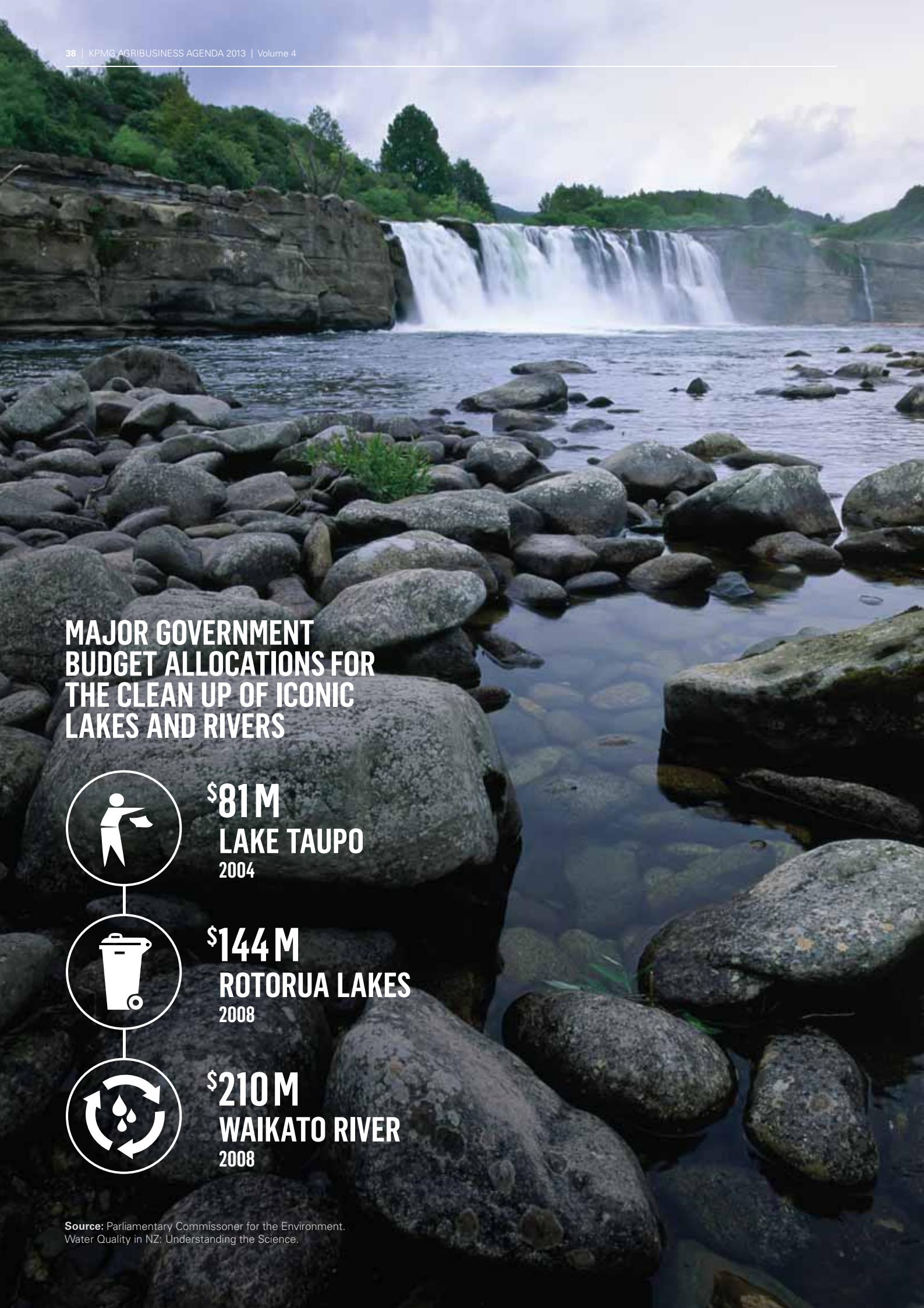
At its core, the discussion over water for agricultural purposes in New Zealand is fundamentally about the sector's license to operate. For most of the population, the discussion is not about the incremental productivity that can be derived from irrigating additional land – but is very much about the quality and safety of our rivers, lakes and streams. The public wants to be able to use these waterways for swimming, fishing and other leisure pursuits that are core to the Kiwi way of life. This is clearly demonstrated in KPMG's survey of Auckland latte drinkers, which indicated 91% support for strengthening legislation to protect and conserve the pristine nature of New Zealand's waterways and landscape.

While New Zealand generally ranks well in global surveys of water quality, there is evidence to suggest water quality across many regions of the country has deteriorated in recent decades. It is very apparent that this deterioration is unacceptable to the majority of the population. As a consequence, it poses a significant risk to the primary sector's license to operate.

The recently announced Sustainable Dairying: Water Accord represents a collaborative industry response to wide public concern over the impact of dairy production on water quality. The initiative which involves the majority of dairy processors, DairyNZ, the fertiliser co-operatives, Federated Farmers, Irrigation New Zealand and the NZ Institute of Primary Industry Management. These groups have collectively committed to enhance the overall performance of dairy farming as it impacts on freshwater. Commitments under the Accord include: delivering on targets to exclude stock from waterways, bridging streams and culverts, implementing riparian management plans, compliance with water regulations, and closer monitoring of nutrient levels on-farm. This requires the farmer, the fertiliser co-operatives, and the milk processor to work co-operatively with authorities to deliver a significant improvement in water quality.

The Accord enables each farmer to develop a response that addresses the factors applicable to their property, and thus avoids the one-size-fits-all regulatory approach. Importantly, the involvement of the dairy processing companies make it enforceable, as compliance can be incorporated into their terms and conditions of supply.





MAJOR GOVERNMENT BUDGET ALLOCATIONS FOR THE CLEAN UP OF ICONIC LAKES AND RIVERS



\$81M
LAKE TAUPO
2004



\$144M
ROTORUA LAKES
2008



\$210M
WAIKATO RIVER
2008

It was also suggested that using water in a responsible and efficient way can over time contribute to the improvement of water quality. In previous *Agendas* we have commented on the need to treat water as a scarce resource, given the freshwater water shortages that many of the countries we sell products to live with day-to-day. This means there is a need to make a greater investment in developing grey water recycling techniques, and technologies that can better manage the environmental outcomes from used water. It was also highlighted that the consistent, precise application of water would deliver the twin benefits of enhancing productivity and improving water quality.

The sector cannot afford to ignore the perspective of the wider population on water quality, and must be active in achieving measureable improvements. The very nature of river systems means solutions must be collaborative, and the dairy industry's Water Accord is a leading example of the type of initiatives the sector will need to adopt.

It may be worth the industry taking some time to reflect on the perspective Māori have towards New Zealand's freshwater resources. The rivers and mountains of a region are as core to the identity of many tribes as their ancestors. Rivers were considered taonga, being a source of food, a facilitator of early cultivation and a mechanism for navigating the country. As a consequence, an affinity with water runs to the heart of Māori culture and its preservation is central to many agricultural initiatives being developed by Māori organisations across the country. The concept of developing a farming system that results in a deterioration of a natural treasure runs counter to the principal of kaitiakitanga, which expects that the economic and social needs of a community will be developed in balance with the environment.

The dairy conversion project being developed by Ngāi Tahu in Canterbury is an example of business being developed using best practice knowledge to produce a sustainable farming model with a low environmental footprint. Key to the development of the farms has been ensuring that the farming operation is developed in a manner consistent with the tribe's values, objectives and expectations including those around the use of natural resources such as water.* It is an important demonstration of how a clear set of values can inform and guide the development of a sustainable business and highlights again the critical importance of reaching a consensus on the core values we stand for as New Zealanders.

AGENDA ITEMS

- 01 Continue to work to fully implement the National Policy Statement on Water, to provide a consistent regulatory framework that meets the needs of communities and provides certainty for business investment.
- 02 Increase the interaction between mainstream and Māori agribusiness activities to ensure best practices and perspectives, around issues such as water use and management, are shared for the wider benefit of the country.

* Te Rūnanga o Ngāi Tahu; Aoraki Matatu – Annual Report 2012; 2012



GREEN AT THE GRASSROOTS



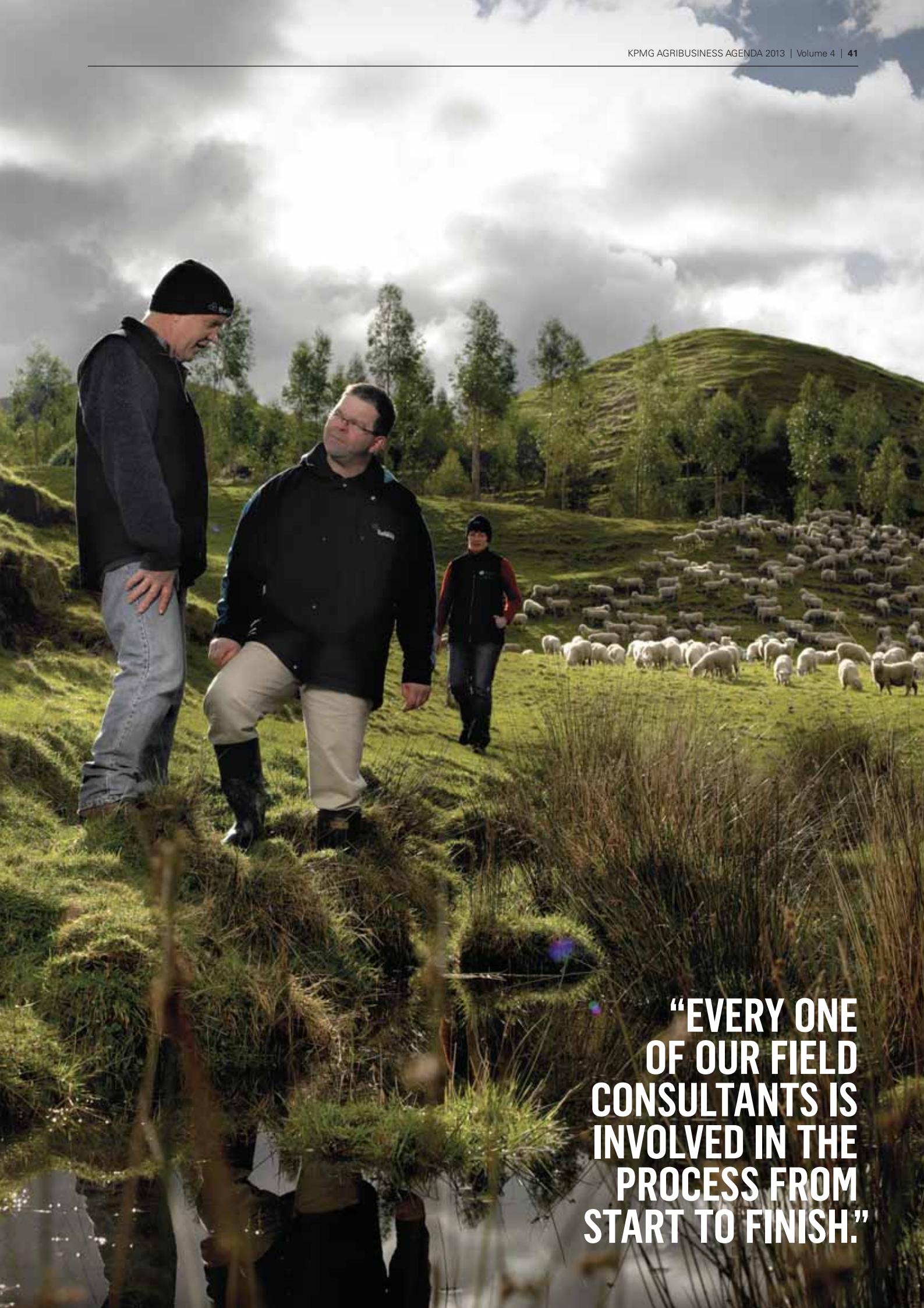
THE BALLANCE FARM ENVIRONMENT AWARDS

'Greenwashing' is the term used to describe corporates who cynically cash in on the environmental bandwagon – and it's a concept that's firmly rejected at Ballance Agri-Nutrients.

The company's long-standing sponsorship of the Ballance Farm Environment Awards is not just about having their logo on a large screen at the annual awards dinner. According to Chief Executive Larry Bilodeau, it's more of a total immersion experience.

"Ballance gets a great deal of mileage out of this sponsorship, and at many different levels. It's not just money we put into it – there's a huge amount of time, effort, support and advice of our employees. We have people on each regional committee, and out there judging. Every one of our field consultants is involved in the process from start to finish."





A photograph of three people in a rural, hilly landscape. In the foreground, a man in a black beanie and dark jacket stands on the left, looking down. Next to him, another man in a black jacket and glasses walks towards the camera. In the background, a woman in a dark jacket and red vest walks away from the camera. A large flock of sheep is grazing in a field to the right. The background features rolling green hills and a cloudy sky.

**“EVERY ONE
OF OUR FIELD
CONSULTANTS IS
INVOLVED IN THE
PROCESS FROM
START TO FINISH.”**



"THE BIG PICTURE IS THAT MOST FARMERS ARE ACTUALLY DOING THE RIGHT THING FOR THE LAND."

And it's doing the hard yards that provides Ballance with the real payback – a genuine understanding of the environmental challenges facing farmers around the country.

"It's allowed us to develop relationships that will endure for a long time; as well as showcasing to the rest of the industry what best practice looks like," says Larry Bilodeau.

"We're certainly not just putting our name on an environmental award for the public perception. I'd say if you were doing it for those reasons, you shouldn't be involved."

Likewise, with the applicants themselves, there's definitely no window-dressing.

"There's not one person who's entered this to win prizes...in most cases, they've been arm-twisted to enter."

"Most of them don't see that they're doing anything special. They see it as their job to be good stewards of the land, and to know they're leaving the land in better condition for the next generation."

"The other consistency is that they're all commercially-savvy operators. They're not tree-huggers...they're trying to run a commercially sound business in a sustainable manner. Sometimes the best decision for sustainability is not the cheapest decision, so you have to have a financially viable model to do that."

And according to Larry Bilodeau, it's never too late to turn the environmental juggernaut around.

"I remember one guy stood up in Napier and said 'the best time to plant a tree was 20 years ago, but the second best time to plant a tree is tomorrow'. I think we need to recognise that whatever's gone on in the past; we can stop it, change it or fix it. It's never too late to start."



ON SPREADING THE GOOD NEWS STORIES:

If perception is reality, then the farming sector needs to shout a little louder about its good news stories.

"The big picture is that most farmers are actually doing the right thing for the land," says Larry Bilodeau.

"But like any industry, there's a few ratbags out there and they let the industry down."

There's been strong growth in the number of dairy participants in the awards – partly in response to the public perception of dirty dairying. Larry Bilodeau believes the mantle is unfair to the vast majority of good operators out there.

"We've had many regional winners from the dairy industry who are doing the right thing. You don't see that on the six o'clock news or the front page of the newspaper, because they're good news stories. But get one cow in a stream and you'll hear all about it."

A major driver for the awards is about having a platform to showcase what best-practice looks like.

"A key audience for us is the urban population, and politicians, and regional councils – all of those interested parties that don't necessarily see the good work that's being done by farmers around the country."

PROVIDING A PICTURE OF BEST PRACTICE:

Brother and sister farming partners Shayne and Charmaine O'Shea are two of the country's rock stars of sustainable farming practices.

The Northland Supreme Award winners have been recognised for their immaculate showcase dairy farm in Kokopu, with judges describing their operation as an "aesthetically-pleasing, well-presented property that achieves excellent production at minimal cost to the environment."

They're no slouches when it comes to business performance either – with a stocking rate that's 50% higher than the area average, and 1698kg/milk solids per hectare in the 2011/12 season.

And although their 380-head Jersey farm has consent to discharge into a local waterway, the O'Sheas go to great lengths not to do so.

According to Shayne: "Our sustainability practices simply stem from best management practices and understanding what is best for the environment and ourselves."

The O'Shea vision is to operate a "financially, environmentally and socially sustainable business" – covering everything from water quality and effluent management, to riparian planting and staff development.

"All these things I can control from within the boundary fence of the business."

"THE O'SHEA VISION IS TO OPERATE A FINANCIALLY, ENVIRONMENTALLY AND SOCIALLY SUSTAINABLE BUSINESS"

08

USING SCIENCE TO DELIVER SUSTAINABLE OUTCOMES

THEME

Under-investment in science programmes

- 01 Concern that science is being underutilised throughout the primary sector
- 02 R&D needs to push boundaries of on-farm environmental performance

This Government has set the primary sector the significant challenge to grow exports to more than \$60 billion by 2025.

This is an achievable challenge, but one that relies on transformational thinking. As was highlighted in "A Call to Arms: A contribution to a New Zealand Agri-Food strategy" from the Riddet Institute, this is highly dependent on increasing the amount and effectiveness of investment in innovation, research, development and extension supporting the agri-food industry.⁶

The view was expressed in the Roundtable discussions that we must place a greater focus on increasing the value generated from our production systems. The following case study profiles some of the innovative work being done by Scion for the forestry sector to add value to non-core components of a tree, creating new revenue streams from innovative products and intellectual property.

It was suggested that perhaps it is time to set a bold, aspirational challenge for the industry; such as becoming the global leader in producing zero carbon proteins. This could create a unique, premium market niche for the New Zealand primary sector – but would rely heavily on using science more extensively throughout the supply chain to generate a step change in export earnings. Such a challenge would require dramatic changes in thinking about products and businesses.

Industry leaders consistently expressed the view that the sector continues to under-invest in science – and not only for achieving transformational outcomes, but also in addressing the day-to-day challenges faced by the sector. Insufficient research is being done to verify policy settings being imposed on industry sectors, for instance, or to support producers in delivering increases in productivity while reducing their environmental footprint.

It was suggested that science is the only effective response the industry has to some of the blunt regulatory tools being implemented around the country, with specific focus placed on the need to invest heavily in the science of nutrient management.

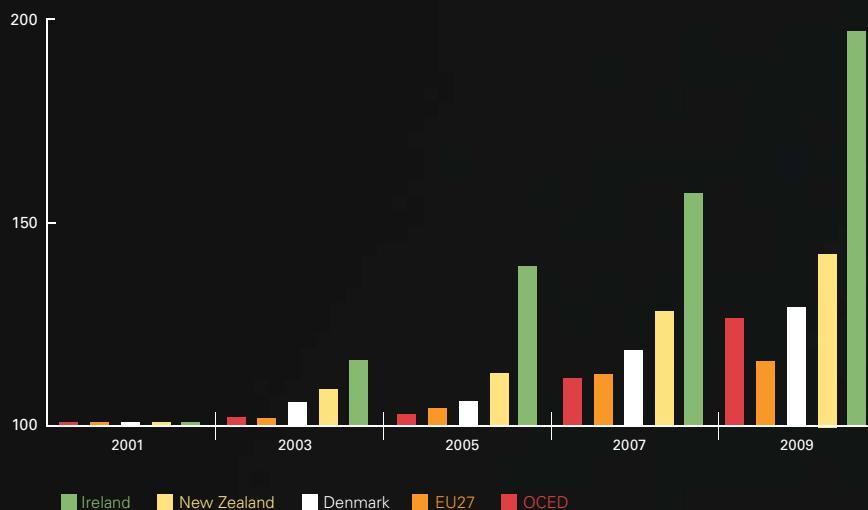
The use of Overseer as a regulatory tool, with the potential to deliver policy settings that do little to contribute towards the development of a truly sustainable primary sector, was raised during many discussions. It appears the industry is being left to work out the science around nutrient loadings and allocations within an ecosystem, and then challenge the regulations; rather than the work being done upfront to set appropriate rules.

It is also recognised that some industry sectors are more exposed to challenges around their environmental impact than others. The wild harvest fishing sector was highlighted as one which has had its sustainable credentials challenged over time. The sector is making collective investment in reducing the environmental impact of fishing through the precision seafood harvesting PGP programme, which is also intended to improve the condition of the fish when they are landed to increase their value.

The fishing sector's collective goal to deliver improved sustainability outcomes and increase profitability demonstrates how science can be effectively utilised to improve businesses. During our conversations, there were other examples of companies utilising technology to create market differentiators and demonstrate the integrity of production systems. The Just Shorn wool carpet range that Elders Primary Wool is taking to market uses a science solution to demonstrate to consumers that their carpet has been produced by a farmer that has passed an auditable integrity programme.

6 The Riddet Institute; A Call to Arms: A Contribution to a New Zealand Agri-Food strategy; July 2012

GROSS DOMESTIC EXPENDITURE ON R&D (2001 =100)



AGENDA ITEMS

01

Investigate consolidation of all government investment in primary sector innovation under a single management structure, controlled by the Ministry for Primary Industries and directed at building the most sustainable primary sector in the world.

02

Commercial organisations need to commit a higher percentage of revenue to investment in innovation programmes to match or exceed the investment that is being made by other countries reliant on the primary sector for their wealth.

Source: OECD; OECD Factbook 2013: Economic, Environmental and Social Statistics - Expenditure on R&D; 2013



IDEAS THAT GROW ON TREES

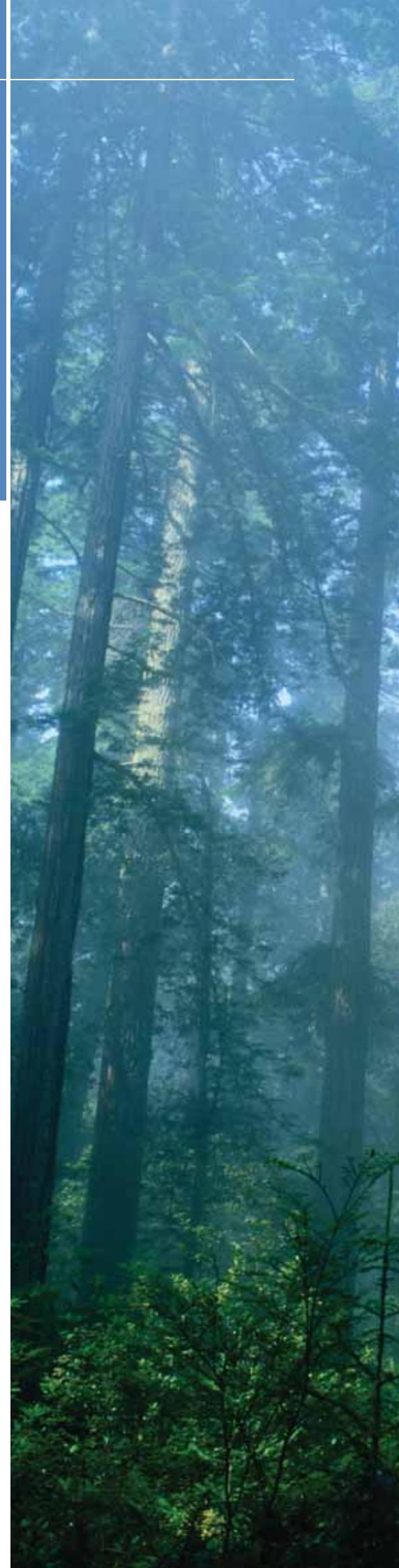


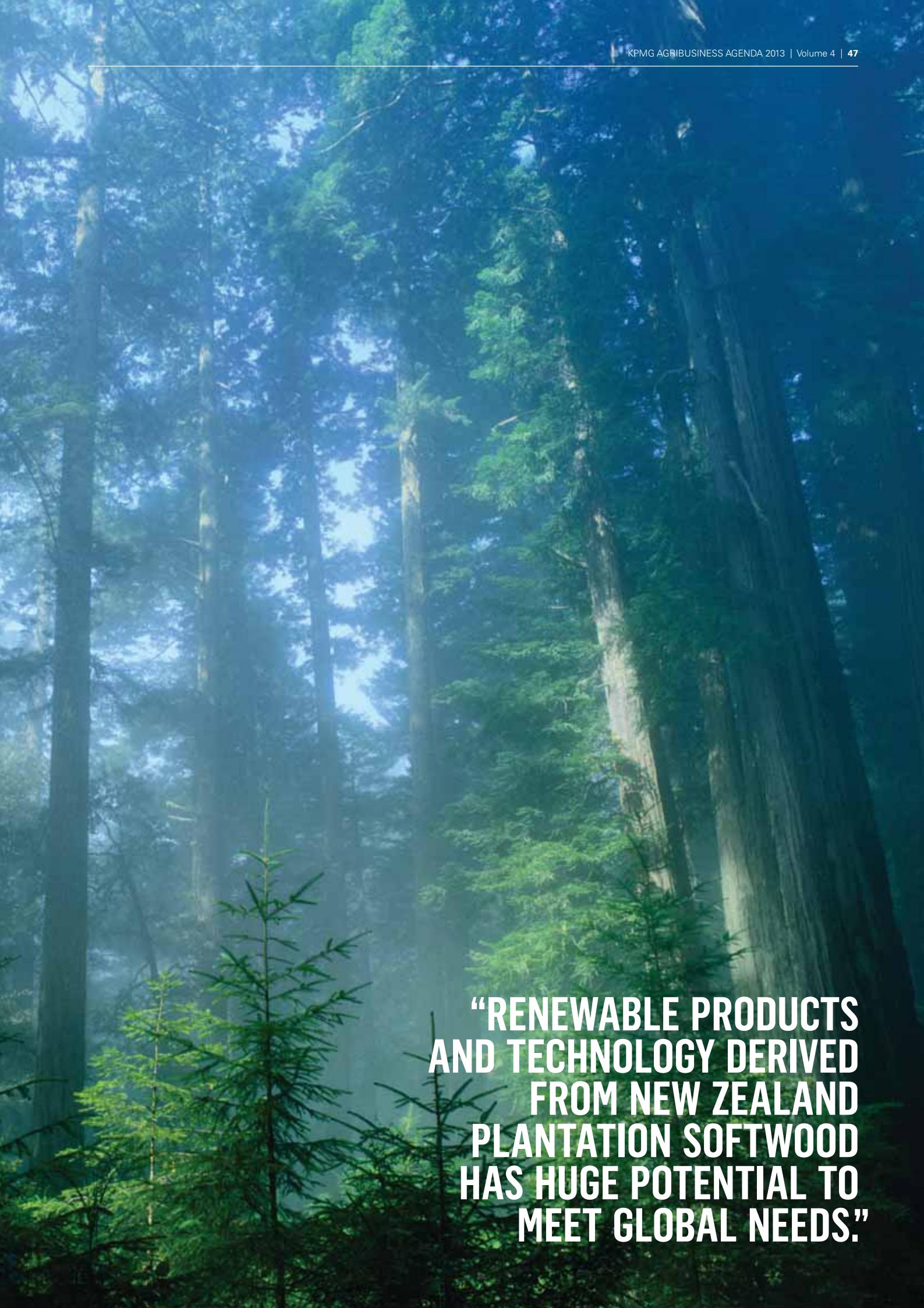
FUTURE-SCAPING NEW ZEALAND'S FORESTRY SECTOR

Start with a simple log of wood – and you never know what you might end up with.

Just some of the hundreds of possibilities include renewable energy, alternative fuels, fabrics, paints, medicines, even car bodies. All of these future technologies are on the radar of Scion, in their quest to future-proof the viability of New Zealand's forestry sector.

Scion is a Crown Research Institute (CRI) that specialises in research, science and technology development for the forestry, wood product and biomaterial sectors.





**“RENEWABLE PRODUCTS
AND TECHNOLOGY DERIVED
FROM NEW ZEALAND
PLANTATION SOFTWOOD
HAS HUGE POTENTIAL TO
MEET GLOBAL NEEDS.”**



“WE START WITH A MACRO VIEW OF THE GLOBAL DRIVERS OF CHANGE.”

As CEO Warren Parker explains, its core purpose is to drive innovation and growth within these sectors.

“Essentially we focus on the fact the world is changing rapidly, and it faces these challenges around energy security, energy supply, and climate change. Those challenges are not going to go away. Renewable products and technology derived from New Zealand plantation softwood has huge potential to meet global needs – whether they are raw materials, chemicals or fuels.”

Warren Parker draws an analogy with the evolution of the dairy industry.

“In the old days, milk was broken down to make butter and skim milk powder. We had a piece of four-by-two and some pulp residue that went to make paper. Now in both of those sectors, you’ve got a whole suite of different products – made with sophisticated technologies, and offering a range of price points and margins.”

New Zealand’s wood processing opportunities are being evaluated by Scion in a major commissioned research project called ‘WoodScape’. The project aims to determine which wood processing and complementary technologies (pulp, paper, timber, panel products, energy and chemicals) will give the best return to wood processors.

“Given that our forestry industry is strongly export-focused, we start with a macro view of the global drivers of change – identifying where our customers of the future will come from, what their needs are and who our competitors will be.”

And, as you’d expect from a research body, Scion is also keen to assess and evaluate GM technologies and non-GM new breeding techniques (NBT).

According to Warren Parker: “You’d have to be living in some kind of wonderland if you think we can increase global food production by 70% by 2050 – as well as harvesting more fibre off the same or smaller land area – without making the step change to use these technologies.”

Overall, Warren Parker says the big picture drivers for the future of New Zealand’s plantation forest industry are strongly positive.

“With an increasing harvest coming on-stream over the next decade, this will provide the basis for the industry’s goal to more than double exports to \$12 billion by 2022.”



ON THE POTENTIAL OF THE 'CORN CAR':

Car components made from wood residue? Why not – thanks to a revolutionary biomass technology being developed here in New Zealand.

The project is a collaboration between LignoTech (an Ashburton based company), research partner Scion, and US-based Fisher Composite Technologies. They've developed a patented technology which 'pressure cooks' woody residue materials such as dried distillers grains, corn fibre and sugar beet pulp.

The technology transforms biowaste (that would otherwise go to landfill or become livestock feed) into fillers used in the manufacture of plastic and composites. It creates a smooth, paintable surface – the kind that's highly desirable to the automotive industry.

Warren Parker says it's a good example of a New Zealand company using offshore partners to overcome our lack of scale.

"The reality is we need multinationals to help take these technologies to market. They can reach the big players in industrial segments that are wanting to use these new materials. And the benefit for New Zealand is that we get to create revenue streams from it to support and grow the industry here."

NZ'S CURRENT POLICY SETTINGS: HOW COULD THEY BE IMPROVED?

When it comes to creating a sustainable manufacturing sector in the forest industry, Scion boss Warren Parker reckons it's time to tweak a few macro settings.

"In New Zealand, for example, the cost of taking processed timber over the wharf is greater than it is for a log. The Chinese have a lower VAT on our logs than lumber," says Warren Parker.

"And we need to create greater certainty for investors into new plant and technology. The relatively high volatility of our exchange rate against our competitors manifests directly into log prices, and therefore profitability. This uncertainty, together with the need for long-term security of log supply, means investors into wood processing are understandably very cautious."

To empower the sector's future, Warren Parker says there are a number of initiatives that would be welcomed by both growers and processors.

Some of these include: accelerated depreciation on new plant and equipment; re-negotiating aspects of the China FTA when it is reviewed in 2014; reducing the time and cost to get building standards in place for new wood products; and supporting new plantings to assure future security of wood supply.

"THE REALITY IS WE NEED MULTINATIONALS TO HELP TAKE THESE TECHNOLOGIES TO MARKET."

09

CONVERSATIONS ON SUSTAINABILITY ISSUES

THEME

Other discussion themes on sustainability

- 01 Evaluating the adoption of GMOs
- 02 Future-proofing the industry for climate volatility
- 03 Creating an effective carbon market

Genetic modification

While industry leaders continue to discuss the adoption of genetic technologies by New Zealand primary sector companies, they recognise this is a difficult conversation to have with the wider population in an objective manner. It does not go unnoticed that while the uptake of GM technologies is increasing annually around the world, delivering yield and quality benefits to competing producers; our country continues to avoid starting a conversation on the issue.

It is unavoidable that GM technologies will be adopted globally, to enable sufficient food to be produced to meet the demand of the growing population.

There may well be a good argument for New Zealand continuing to take a GM-free position, in order to differentiate our product in premium market niches. However, if this course of action is considered to be most the appropriate strategy for the primary sector in New Zealand, we must ensure that any yield sacrifice to GM products is compensated by an ability to secure a premium price in the market.

As we have said in previous *Agendas*, the industry is currently stuck in a no-man's land between a GM and a non-GM future. This provides neither the production benefits nor the market benefits that could be derived from having a clear strategy either way. It is critical that an objective, fact-based conversation takes place on the issue to reach a consensus that New Zealanders are comfortable with. This is the only path to maximise the value of the industry into the future.

Climate change

The Intergovernmental Panel on Climate Change ('IPCC') reported in late September that the evidence supporting the warming of the global climate is unequivocal. They stated that data sets show the oceans are warming, and ice caps are shrinking; and they argue that historic carbon emissions are likely to impact the climate for centuries to come⁷.

Regardless of whether industry leaders concur with the perspectives of the IPCC, there was recognition during the Roundtables that farming systems need to be equipped to cope with weather shocks that appear to be becoming increasingly common. The drought that occurred during the first quarter of 2013 highlighted the limited reserve capacity in the current farming systems in New Zealand.

Many businesses were forced to start culling capital stock within weeks of the drought starting to bite.

Developing production systems that are better able to cope with climate variability should be on the agenda for the majority of primary sector participants. Increasing system capacity is likely to require some level of capital investment, for instance in water storage and irrigation infrastructure which requires a collaborative working relationship with the wider community.

Inconsistent carbon policy

New Zealand has introduced a range of policies that attempt to influence behaviour around carbon emissions, the flagship of which was intended to be the Emissions Trading Scheme (ETS). With the collapse of the price of the New Zealand carbon units, many investors have forestry farming propositions that are currently delivering huge unintended gains as a result of flaws in the design of the scheme creating arbitrage opportunities. This however, is contributing to a decline in forestry plantings over the last two years. While not a major subject of discussion during the Roundtables, the view was expressed that the Government needs to develop a long-term consistent approach to incentivising businesses to better manage carbon emissions. This should be achieved through a single integrated policy, to provide certainty to potential investors and incentivise a reduction in the intensity of carbon usage.

⁷ Intergovernmental Panel on Climate Change; Climate Change 2013: The Physical Science Basis – Headline Statements from the Summary for Policymakers; September 2013

GM CROPS NOW ACCOUNT FOR:

82%
OF THE GLOBAL COTTON AREA
(FOR HERBICIDE TOLERANCE AND INSECT RESISTANCE)

75%
OF SOYBEANS
(HERBICIDE TOLERANCE)

32%
OF MAIZE
(HERBICIDE TOLERANCE AND INSECT RESISTANCE)

26%
OF RAPESEED / CANOLA
(HERBICIDE TOLERANCE AND INSECT RESISTANCE)

Source: ISAAA 2012

AGENDA ITEMS

01

Establish an independent commission to lead an objective public enquiry into New Zealander's attitudes towards GM technologies and use the findings to guide a definitive vision for the future of New Zealand agriculture.

02

Industry good organisations should make funding available to develop cost effective solutions to increase the capacity of production systems to better withstand and recover from weather shocks.

ACKNOWLEDGEMENTS

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

We would like to offer special thanks to the organisations featured in the Case Studies in this volume of the Agenda:

ASB

Mark Heer

Ballance Agri-Nutrients

Larry Bilodeau and Graeme Smith

Fonterra

Carly Robinson
Emma Parsons

Scion

Warren Parker

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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.**

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- » Availability of capital, particularly in co-operative organisation structures
- » Addressing customs and quota issues and maximising the benefit of FTAs
- » Issues arising from climate change regulations, carbon trading and food miles
- » Obtaining R&D funding to support innovation in genetics, seed technology and nutrition
- » Cost management and control
- » Farming for profit
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- » Negotiating financing arrangements
- » Succession planning and future proofing your business strategy

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