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**NOTICE OF *SHAREHOLDER MEETING***

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**TO BE HELD 12 AUGUST 2016**



# THE PARTNERSHIP *WITH SHANGHAI MALING*

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- In October 2015 shareholders approved our partnership with Shanghai Maling by an emphatic 82% of votes cast.
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- Your Board said it would be bound by the voting outcome of the October 2015 Special Meeting.
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- Consistent with that, and subject to Overseas Investment Office approval, Silver Fern Farms is bound to complete the transaction with Shanghai Maling.
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- This meeting – whether the resolution is passed or not – cannot change that.
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- As a result, your Board recognises that some shareholders may choose not to participate in this meeting.
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- If shareholders do choose to vote, your Board encourages a vote in favour of the resolution.
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- The merits of the partnership between Silver Fern Farms and Shanghai Maling have not changed. If anything, the imperatives and potential benefits for Silver Fern Farms have increased.
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- Our disappointing financial performance this year illustrates again the volatility of the industry and the risks associated with our current capital structure.
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- We remain under lender pressure to address these issues.
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- Shanghai Maling’s investment is clearly in the best interests of the Co-operative.
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# THE SHRIMPTON/GALLAGHER *ALLEGATIONS*

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- Despite 82% of votes cast supporting the partnership, Messrs Shrimpton and Gallagher want to stop the transaction from completing.
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- Their allegations are strongly refuted by the Board, and independent bodies have found no basis for them:
    - The Financial Markets Authority has reviewed and found no issue with the 2015 Special Meeting and the information that was provided to shareholders.
    - The Registrar of Companies has found no evidence that your Directors have acted in anything other than the best interests of the Co-operative and its shareholders.
    - Independent expert Grant Samuel has reviewed our audited results for 2015 and reaffirmed its view that the transaction is fair and reasonable to shareholders.
    - Grant Samuel has also assessed the financial basis, and confirmed, the Board's assessment that the Shanghai Maling transaction is not a major transaction for Silver Fern Farms.
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- The Board believes Messrs Shrimpton and Gallagher do not appreciate, and so are not fairly or accurately representing, the prospects and risks of any refinancing and restructuring the Co-operative would need to undertake should the Shanghai Maling investment not proceed.
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- The Board believes the actions of Messrs Shrimpton and Gallagher, including in requiring this Meeting, are not in the best interests of our Co-operative.
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# CHAIRMAN'S *LETTER*

Dear Shareholder

## **THE PARTNERSHIP WITH SHANGHAI MALING REMAINS THE BEST OPTION FOR YOUR CO-OPERATIVE – THE BENEFITS RESTATED**

Your Board remains unanimous in its views that:

- **The Shanghai Maling transaction is in the best interests of shareholders and the Co-operative.**
- **The strategic rationale for the partnership has, if anything, increased since October 2015.**

### **The status quo is not an option.**

Our disappointing financial performance this year (announced in April and covered in more detail in Section Two of this Notice of Meeting) serves as a reminder of the volatility of the industry as a whole, and the risk associated with our capital structure. We remain under lender pressure to address this and permanently reduce Silver Fern Farms' reliance on debt.

The statements made by Messrs Shrimpton and Gallagher that the Co-operative is bankable without significant capital investment are wrong. They are made without the benefit of insight gained from discussions the Co-operative has had with our current lending syndicate and other potential lenders in the last 12 months, and without an understanding of the seasonal funding demands of the Co-operative. This is a fundamental issue and point of difference. I have addressed this matter in more detail later in this letter, and this is fully addressed in later Sections of this Notice of Meeting.

### **THE STRATEGIC BENEFITS OF THE PARTNERSHIP WITH SHANGHAI MALING REMAIN COMPELLING:**

- The transaction involves Shanghai Maling investing approximately \$261 million<sup>1</sup> in cash in return for a 50% stake in Silver Fern Farms' business. This investment will leave the business debt free and with cash reserves next year at Silver Fern Farms' current financial year end (i.e. 30 September 2017). Silver Fern Farms' business will be in the strongest financial position of any major company in the New Zealand red meat sector.
- The investment will provide the capital to accelerate our 'Plate to Pasture' strategy globally and to invest in technology, equipment and improving plant efficiencies.
- Our business will have a privileged position in China – the fastest growing market for red meat in the world.

1. Subject to a net tangible asset adjustment, an adjustment for advisory costs incurred by the Co-operative in connection with the transaction and for the cost of redeeming any rebate and supplier investment shares, between September 2015 and the completion date.



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- The business will retain its global focus with its existing customer base. The partnership proposal does not require Silver Fern Farms' business to supply any product exclusively to Shanghai Maling at prices set by them, nor to the China market. Any supply that is made will be on arms' length terms and will be commercially sensible for both parties.
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- Silver Fern Farms' business will continue to be responsible for its sales and marketing efforts in China - just as in other countries. We have a number of existing partners in the China market. Where it makes sense for all parties, we will be working with Shanghai Maling to create products specifically for China, and to leverage Shanghai Maling's significant wholesale and retail networks.
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- Shanghai Maling has direct control of 800 supermarket and retail stores, including 56 meat retail stores in Shanghai. Shanghai Maling's chilled and frozen meat sales network, including 19 wholesale facilities, covers large to medium sized cities in Shanghai and other Chinese provinces.
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- Shanghai Maling has committed to provide our business with China market access so that we can stock and sell Silver Fern Farms branded products in 500 retail outlets in the first year, 1,000 retail outlets in the second year and 2,000 retail outlets in the third year, following the transaction. This compares to less than 25 retail outlets that we currently supply in China after a number of years in that market.
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- Shanghai Maling wants to work with us to develop the "Silver Fern Farms" brand into the premium red meat brand in China.
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- The transaction will not have any impact on the status of our Co-operative as a co-operative company – it will remain in its current form.
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- The partnership will have a fair and appropriately balanced governance structure. The Co-operative and Shanghai Maling will be 50/50 partners in Silver Fern Farms' business. The business will have a governance structure that in the Board's view provides each party with sufficient control to ensure that neither shareholder is able to gain an advantage at the expense of the other. Silver Fern Farms' business will be managed in the best interests of both shareholders. This view is shared by Grant Samuel & Associates Limited (**Grant Samuel**) in its independent report<sup>2</sup> that accompanied the Notice of Meeting and Shareholder Information Pack for the October 2015 Special Meeting (**the previous Notice of Meeting**).<sup>3</sup>
- 
- The transaction gives the Co-operative's equity an implied value of \$2.84 per ordinary share, which compares favourably to the share price of 35 cents in July 2015 when we halted trading on the Unlisted share trading platform and the approximate \$1.00 level at which shares have traded on the Unlisted share trading platform in July 2016.
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- Subject to passing the necessary resolutions at that time, the Board's intention following completion is to use funds available to redeem all of the supplier investment shares and pay a special dividend of 30 cents per share to holders of ordinary and rebate shares in the Co-operative.
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- We have agreed with Shanghai Maling that the business will target to distribute at least 50% of its net profits (after tax) every year to the two partners, the Co-operative and Shanghai Maling. The Co-operative intends to distribute the majority of the dividends it receives to its shareholders in the form of dividends and rebates to supplying shareholders.
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2. Page 38 of Appendix Three of the previous Notice of Meeting.

3. A copy of the previous Notice of Meeting is available at [silverfernfarms.co.nz/our-co-operative/investors/](http://silverfernfarms.co.nz/our-co-operative/investors/).

## YOUR BOARD STRONGLY DISAGREES WITH THE STATEMENT PROVIDED BY MESSRS SHRIMPTON AND GALLAGHER AND THEIR NEGATIVE STANCE ON THE TRANSACTION

- The transaction is not a Major Transaction for the Co-operative under the Companies Act 1993, nor the Co-operative's constitution. Accordingly, a special resolution of shareholders was not, and is not, required. The Board took professional valuation advice from PricewaterhouseCoopers at the time. Independent expert Grant Samuel has since confirmed the view taken by the Board. Grant Samuel's opinion is included in Section Four of this Notice of Meeting.
- The previous Notice of Meeting was not misleading. The Financial Markets Authority has dismissed allegations made to that effect in its statement issued publicly on 25 May 2016.<sup>4</sup> In addition, we asked independent expert Grant Samuel to reconsider its opinion in the light of last year's actual financial results. It has done so and affirmed its views that the transaction with Shanghai Maling is fair and reasonable to shareholders, and that a financial restructuring remains critical to the Co-operative's future.
- Your directors have at all times acted in good faith and in the best interests of the Co-operative. The Registrar of Companies has dismissed allegations made to it that this was not the case.

This Notice of Meeting sets out a resolution to (re)approve the transaction that the Co-operative entered into with Shanghai Maling in September 2015.

At the Special Meeting in October 2015, shareholders overwhelmingly approved the transaction with 2,879 shareholders voting, representing over 67% of total eligible votes. The transaction received the approval of 82.22% of the votes cast – well above both the 50% level that was set by the Board, and the 75% level required to pass the "special resolution" now proposed by Messrs Shrimpton and Gallagher. Your Board is very appreciative of the support you showed.

The transaction has already been approved by our shareholders. The unnecessary reapproval proposed by Messrs Shrimpton and Gallagher can't and won't change our position.

As we said in October last year, the Board wanted you as shareholders to have your say, and we said we would consider ourselves bound by the wishes of the majority. On the basis of that very strong mandate, the shareholder approval condition in our contract with Shanghai Maling was fulfilled. Accordingly, the Co-operative is contractually bound to proceed – and what's more, the Board remains unanimously of the opinion that the partnership with Shanghai Maling is in the best interests of the Co-operative and our shareholders, and that Shanghai Maling will be an excellent partner for us.

We are frustrated and disappointed that Messrs Shrimpton and Gallagher have encouraged a small group of shareholders (together, the **Requisitioners**) to question the approval obtained last year, that they have required the Co-operative to hold this further Special Meeting, and that they are continuing to agitate for the transaction to fail.

The Board is obligated to call this Special Meeting under the Companies Act, but is unanimous in stating that this Special Meeting is of no benefit to the Co-operative or its shareholders, cannot be binding on us, can't undo the previous approval and the binding contracts we have, and is not an effective use of the Co-operative's management and financial resources.

## REVISED DATES

At this time, all conditions to the transaction have been satisfied other than Overseas Investment Office (**OIO**) approval.

The previous 30 June 2016 deadline for OIO approval was a real deadline. However, it became clear that the parties required further time to collate and deliver information required by the OIO to allow it to complete its process and provide a recommendation to the responsible Government Ministers. To accommodate this we agreed with Shanghai Maling to extend the date by which the OIO condition is required to be satisfied to 30 September 2016.

<sup>4</sup> A full copy of the FMA's announcement can be found on the Unlisted market platform for Silver Fern Farms Limited at [www.unlisted.co.nz](http://www.unlisted.co.nz).

We acknowledge the OIO's work, and are confident that OIO approval will be given within the extended timeframe that has been agreed.

In connection with that time extension, the Co-operative and Shanghai Maling have also agreed to extend the date on which Shanghai Maling will complete its investment to 4 January 2017.<sup>5</sup>

This extension gives us a firm date to plan around, reflects Shanghai Maling's desire for a start date to coincide with the intended 1 January to 31 December financial year of the partnership, and coincides with Shanghai Maling's balance date. As noted in the previous Notice of Meeting,<sup>6</sup> following completion, Silver Fern Farms' business will be consolidated for accounting purposes by Shanghai Maling and the balance date will be changed to 31 December. The Co-operative and Shanghai Maling retain the flexibility to vary the completion date, including agreeing an earlier date.

## OBLIGATION TO COMPLETE

Following receipt of OIO approval, the Co-operative will be bound to complete the Shanghai Maling transaction. If we do not honour our contractual obligations to complete:

- we will potentially have to pay substantial damages to Shanghai Maling;
- the terms of our current financing arrangements mean that we will be subject to an 'event of review' by our lenders, the outcome of which is uncertain;
- our ability to obtain financing beyond the current season will be uncertain. The current syndicate of lenders has stated in writing that they will not refinance the Co-operative without a material capital investment; and
- if significant damages are payable, or our lenders withdraw support, or a combination of both occurs, the Co-operative will be in a vulnerable position.

## GRANT SAMUEL'S VIEW

In its report that accompanied the previous Notice of Meeting, independent expert Grant Samuel concluded that the terms and conditions of the Shanghai Maling transaction were fair and reasonable to shareholders.<sup>7</sup>

As a result now of being required to hold this further meeting, the Board requested that Grant Samuel update its opinion, against the background of the audited financial results for the financial year ended 30 September 2015 and the current financial year's trading. In Section Four of this Notice of Meeting, Grant Samuel has affirmed its opinion that the transaction is fair and reasonable to shareholders and that a financial restructuring remains critical to the Co-operative's future.

The Board has also asked Grant Samuel to consider, form and express an independent opinion on the basis on which the Board concluded that the Major Transaction value threshold was not reached in undertaking the restructure referred to in the previous Notice of Meeting. Grant Samuel has independently concluded that the restructure did not constitute a Major Transaction for the purposes of the Companies Act or the Co-operative's constitution. Grant Samuel's conclusions are set out in its letter in Section Four of this Notice of Meeting.

## MEDIA STATEMENTS ON PLANT CLOSURES

There have been media reports that Silver Fern Farms' business had, at the time of the 2015 Special Meeting, committed to but not disclosed the closure of a number of processing plants. These reports are incorrect.

This is only one of a number of instances of misleading commentary or misinformation. Shareholders should be assured that the previous Notice of Meeting set out the accurate position in respect of the Co-operative and the Shanghai Maling transaction.

## THE SHAREHOLDER APPROVAL PROCESS AND THE REQUISITION

Despite the strong endorsement from shareholders at the October 2015 meeting, Messrs Shrimpton and Gallagher have encouraged the Requisitioners to exercise a power contained in the Companies Act to call, and put a resolution to, a Special Meeting of shareholders. The resolution the Requisitioners have put forward is essentially the same resolution as that which was overwhelmingly approved at the Special Meeting in October 2015. The only relevant difference is that the resolution has now been put forward as a special resolution, while the resolution in October 2015 was put forward as an ordinary resolution.

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5. At the date of printing of this Notice of Meeting these amendments remain subject to board approvals and finalising amendments to the Co-operative's facility agreement to meet lenders' requirements.

6. Page 28 of the previous Notice of Meeting.

7. Page 35 of Appendix Three of the previous Notice of Meeting.



To be passed, a special resolution requires the approval of 75% of votes cast. **Substantively the same resolution was passed in October 2015 with the approval of 82.22% of the votes cast, more than the 75% threshold required to pass the special resolution that this meeting has been called to consider.**

While the Board has a statutory obligation to call the Special Meeting requested by the Requisitioners, we are firmly of the view that the resolution is not, and will not be, binding on the Co-operative.

**Messrs Shrimpton and Gallagher have solicited and received support for the requisition on the basis that the investment needed to be “properly approved”. However, the Statement they have since provided, and their actions, make it clear that they are not seeking to simply address the alleged procedural deficiencies, but rather to stop the transaction from completing.**

Although the Board has statutory duties to act in the best interests of the Co-operative and of all shareholders, Messrs Shrimpton and Gallagher have no such obligation.

## ALLEGATIONS MADE BY MESSRS SHRIMPTON AND GALLAGHER

I encourage you to read in detail the Board's comprehensive response to the Statement provided by Messrs Shrimpton and Gallagher in Section Five of this Notice of Meeting. The Board is firmly of the view that the allegations made in that Statement are incorrect.

In essence, the Statement provided by Messrs Shrimpton and Gallagher has three key themes:

- 1 Allegation: Shareholders were, in approving the transaction, misled as to the financial position of the Silver Fern Farms group.**

**Board's response:** This is not correct. The Financial Markets Authority (the Government body charged with regulating New Zealand's financial markets), in its public statement issued on 25 May 2016,<sup>8</sup> vindicates the Board's position on this.

A related allegation has been made that Shanghai Maling was given materially different financial information to that included in the previous Notice of Meeting. This is addressed in detail in Section Five of this Notice of Meeting.

- 2 Allegation: Shareholders were, in approving the transaction, misled as to the likelihood of receivership if the Shanghai Maling transaction did not proceed.**

**Board's response:** This is not correct. Shareholders were not misled and the Co-operative's prospects of future financial support from its lenders was far from certain or secure. My Chairman's Letter accompanying the previous Notice of Meeting, said *“if the Proposed Transaction is not approved, some or all of the members of the banking syndicate could elect not to provide debt facilities”*.<sup>9</sup> I stand by that statement and statements to the same effect made by Grant Samuel in its independent report that accompanied the previous Notice of Meeting.<sup>10</sup>

Messrs Shrimpton and Gallagher ignore the very challenging financial history of the Co-operative in recent times, and the excessive debt levels borrowed from this same syndicate of banks as recently as the 2013 financial year (with peak debt at over \$580 million) despite debt having been as low as \$130 million in August 2010.

The Board and the Co-operative's lenders have for some time been in agreement that Silver Fern Farms' needs to address its capital structure. In this regard, the Co-operative's lenders have made it very clear that they are concerned at the extent of risk they carry given the Co-operative's existing capital structure, our history of being unable to raise sufficient new equity from existing shareholders, the volatility of our earnings and the significant working capital requirements of Silver Fern Farms' business.

In this context, at the date of the previous Notice of Meeting the Co-operative had received correspondence from the syndicate of banks which included the following statements:

28 May 2015:

*“For the avoidance of doubt, the Lenders want the Board to understand that they will not under any circumstances provide ongoing financing to the Company if the shareholders do not approve a material capital transaction that is recommended to them [by the Board].”*

16 June 2015:

*“The only firm statement in this regard is that the Lenders are in no circumstances prepared to refinance the Company if shareholders do not approve a Capital Structure Transaction put to them [by the Board].”*

<sup>8</sup>. A full copy of the FMA's announcement can be found on the Unlisted market platform for Silver Fern Farms Limited at [www.unlisted.co.nz](http://www.unlisted.co.nz).

<sup>9</sup>. Page 2 of the previous Notice of Meeting.

<sup>10</sup>. Pages 34 and 35 of Appendix Three of the previous Notice of Meeting.



As a result of the Co-operative's disappointing financial performance this year (see Section Two of this Notice of Meeting), the Co-operative has not met a number of the financial covenants under our debt facility agreement. The lenders have, to date, not sought to exercise any rights in relation to the areas of non-compliance and have continued to support the Co-operative. We appreciate their support.

However, we are under no illusion that if the partnership proposal with Shanghai Maling was not progressing to implementation, we would be having very different conversations with our lenders. Even if we had their continued support in the face of a failed transaction (support which we believe cannot be relied upon, given their previous comments), we think it would be at an even higher cost, include greater financial constraints and very likely require asset and business restructure, disposal and or heavily discounted recapitalisation.

This is in stark contrast to the financial certainty and business opportunity provided by the Shanghai Maling investment.

**3 Allegation: The transaction was not properly approved at the October 2015 shareholder meeting as it is a Major Transaction under the Companies Act and so required a special resolution to approve it.**

**Board's response:** This is not correct. The Board acted in accordance with all relevant laws, best practice governance and with regard to the principles of our Co-operative in seeking shareholder approval.

No special resolution is or was required. Messrs Shrimpton and Gallagher are not correct to state that 100% of the Co-operative's assets have been sold as a part of the transaction. The Co-operative's shares in its subsidiary that holds its beef business (the group's most valuable business, and the subsidiary that will become the 50:50 partnership entity), were not sold or transferred as part of the restructure. Less than 50% of the value of the Co-operative's assets were transferred to that subsidiary. Grant Samuel has independently reviewed this calculation and concluded that the restructure did not constitute a Major Transaction for the purposes of the Companies Act. Grant Samuel's conclusions are included in its letter in Section Four of this Notice of Meeting.

Messrs Shrimpton and Gallagher now also allege that an approval should have been obtained for what they call "an essential change in the Co-operative's business". There is no such legal test and, in any event, we did ask for shareholder approval to the transaction, and received 82.22% support.

The leadership of the political party NZ First complained to the Registrar of Companies stating that your directors had breached their duties under the Companies Act by failing to obtain approval of the Shanghai Maling transaction as a Major Transaction. NZ First also alleged that your directors deliberately structured the transaction to avoid the application of the Major Transaction provision of the Companies Act. The Board utterly rejects those allegations. We have been transparent with shareholders, putting the transaction before you in October 2015 with substantial Shareholder Information provided at the time to allow you to form a judgment. The Registrar of Companies has also rejected NZ First's allegations stating: "*the Registrar has not identified any evidence of a breach of s 138A of the Companies Act 1993 (relating to criminal breaches of directors duties). This investigation is complete...*".

In summary, the Board strongly disagrees with the Statement provided by Messrs Shrimpton and Gallagher. The Board considers that their allegations are legally and factually wrong, that many elements of their allegations are misleading, and that Messrs Shrimpton and Gallagher are now attempting to usurp the wishes of the majority of the shareholders and the recommendation of the Board.

**MORE ON THE POSITION WITH OUR LENDERS**

The Board and the Co-operative's lenders agree that Silver Fern Farms' business has carried, and continues to carry too much debt relative to its assets and average earnings, that it needs to address its capital structure and that it cannot rely on operating profits to do this.

The lenders remain very concerned in relation to the unsustainable nature of our existing capital structure, our history of being unable to raise sufficient new equity from existing shareholders and our resulting need for significant new equity capital. Since 2013, these concerns have resulted in:

- 
- our seasonal facilities only being provided on an annual basis; and
- 
- the lenders advising us formally that their continued financial support would be conditional on the Co-operative undertaking a robust process that culminated in an investment, such as that now agreed with Shanghai Maling.
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In their recent correspondence with the Co-operative, the lenders have stated:

*“The Lenders reiterate their view that should the [Shanghai Maling] investment fail to complete, they will not, and cannot be reasonably expected to, continue to provide financial support to the Group if their long standing concerns with the Group’s capital structure are not addressed.”*

Further, the lenders have made it clear that any new banking facilities for the period from expiry of the existing facilities on 31 October 2016 until the revised completion date of 4 January 2017 should not be assumed. They have also expressed their view that the Board should be considering all options as a contingency should the Shanghai Maling investment fail to complete, including the sale of 100% of Silver Fern Farms business and 100% of the beef business.

We are confident that the revised timetable agreed with Shanghai Maling can be achieved. We are also confident that if we achieve OIO approval by 30 September our financing requirements through to completion of the Shanghai Maling transaction will be made available by our current lenders.

However, it is clear to us that continued interference with the process by Messrs Shrimpton and Gallagher, and any escalation of agitation challenging the legitimacy of the transaction and your prior approval, risk putting the Co-operative and the Board in an untenable position with our lenders.

## SHOULD SHAREHOLDERS VOTE?

The Board is conscious, from feedback already received, that many shareholders are questioning why the Co-operative is required to call this Special Meeting and why they should vote at all – having already voted on the resolution.

We can appreciate shareholder frustration. We do expect that those in the Shrimpton and Gallagher camp will turn out in force to vote, while the silent majority may feel that they have already voted and the Co-operative should just get on with completing the deal. We respect that sentiment.

The decision of whether or not you vote is yours to make. Obviously, you should also feel free to seek independent professional advice.

For those shareholders that do wish to vote, the Board encourages you to vote in favour of the resolution. However, we reiterate that the results of the vote will, for the reasons set out above, have no bearing on the transaction whether or not the resolution is passed.

Shareholders can vote online or appoint me or any other person as a proxy to vote on their behalf.

Yours sincerely,



**Rob Hewett**  
Chairman of Directors, Silver Fern Farms Limited  
14 July 2016



# KEY STEPS *AND KEY DATES*

## KEY STEPS

The purpose of this Notice of Meeting is to provide you with information regarding the resolution that has been proposed by shareholders in order to assist you to make an informed decision. There are three steps for you to take:

### 1 **READ**

this Notice of Meeting and the previous Notice of Meeting and Shareholder Information Pack (a copy of which is available on Silver Fern Farms' website at [www.silverfernfarms.co.nz](http://www.silverfernfarms.co.nz)).

### 2 **ATTEND**

your nearest Roadshow Meeting (if you are able), ask questions and, if you wish, seek independent professional advice. Details of the Roadshow Meetings will be announced by the Co-operative in due course.

### 3 **VOTE**

If you wish to vote on the resolution, you can do so by internet, post or fax (see the Postal / Internet / Fax Voting Form that accompanies this Notice of Meeting) or, if you would like to, by attending the Special Meeting in person or by proxy or corporate representative (see the In Attendance / By Proxy Voting Form that accompanies this Notice of Meeting).

## KEY DATES

TIME	DATE	ACTION
5.00pm	15 July 2016	Record date for determining the shareholders that are eligible to vote on the resolution
1.00pm	10 August 2016	Last time and date by which internet votes must have been made and proxy, postal voting and fax voting forms must have been received by the Co-operative
1.00pm	12 August 2016	Time and date for Special Meeting

# NOTICE OF *SPECIAL MEETING*

Notice is given that a Special Meeting of shareholders of Silver Fern Farms Limited will be held at:

**Silver Fern Farms' Dunedin Corporate Office,  
283 Princes Street, Dunedin,  
at 1.00pm on Friday, 12 August 2016.**

Scan the code at right to save this date to your calendar.



## SPECIAL BUSINESS

### Resolution

To consider the following resolution put forward by Messrs Shrimpton and Gallagher, and other shareholders (together, the **Requisitioners**):

**Resolution:** Put forward by the Requisitioners as a special resolution:

*That the shareholders of Silver Fern Farms Limited (the Company) hereby approve the proposed partnership of the Company with Shanghai Maling and the restructure described in the Notice of Meeting and Shareholder Information Pack dated 28 September 2015 by way of this special resolution of shareholders.*

### Other Business

*To consider any other business which may properly be brought before the Special Meeting.*

**Note:** All matters of business at this Special Meeting are discussion points only and there will be no binding vote in relation to any matters.

### Eligibility to Vote

All shareholders are welcome to attend the Special Meeting. However, only the holders as at the record date of 5.00pm on 15 July 2016 of:

- fully paid ordinary shares; and/or
- rebate shares who are Current Suppliers (see below),

are entitled to vote on the resolution.

Holders of partially paid ordinary shares, rebate shares that are not Current Suppliers and supplier investor shares will **not** be entitled to vote at the Special Meeting.

The following table sets out which shareholders are eligible to vote at the Special Meeting:

Shares held in Silver Fern Farms Limited	Voting Rights
Fully paid ordinary shares	<b>Yes</b>
Partly paid ordinary shares	<b>No</b>
Rebate shares held by a Current Supplier	<b>Yes</b>
Rebate shares held by a non-Current Supplier	<b>No</b>
Supplier investment shares	<b>No</b>

For the purposes of the resolution, “**Current Supplier**” means a holder of rebate shares or fully paid ordinary shares (as applicable) who has supplied livestock to Silver Fern Farms Limited since 1 September 2014.

### Voting

Whilst the Co-operative is not, and will not be, bound by the voting outcome of the resolution, the Board encourages all eligible shareholders who wish to vote, to vote in favour of the resolution.

The resolution has been put forward by the Requisitioners as a special resolution, the threshold for which to be passed is seventy five percent of the votes of:

- the fully paid ordinary shares; and
- the rebate shares held by Current Suppliers,

voting on the resolution, which must include a majority of the votes of Current Suppliers voting on the resolution.

Under the Co-operative's constitution the holders of:

- fully paid ordinary shares who are "Qualifying Shareholders" (see below); together with
- rebate shares who are Current Suppliers,

will be scaled (if necessary) to have not less than 60% of the votes cast on the resolution.

The holders of fully paid ordinary shares who are not "Qualifying Shareholders" (see below) will be scaled (if necessary) to have the lesser of one vote per ordinary share, or 40% of the votes cast on the resolution.

For the purposes of the resolution, a Qualifying Shareholder is the holder of a fully paid ordinary share that has supplied Silver Fern Farms Limited with not less than 400 "Production Equivalents" (as that term is defined in the Co-operative's constitution) in each of the two 12 month periods ending on 31 July 2016.

## CASTING YOUR VOTE

You can vote on the resolution in one of five ways:

- 1 Internet voting – [www.silverfernfarms.com](http://www.silverfernfarms.com)**

You can follow the link and the instructions on Silver Fern Farms' website to cast your vote. This link takes you to the secure internet voting site provided by electionz.com and is not part of the Silver Fern Farms' website. You will be asked to provide your unique PIN number and password set out in the **Postal / Internet / Fax Voting Form** (accompanying this Notice of Meeting).
- 2 Postal voting**

You can vote by posting your completed **Postal / Internet / Fax Voting Form** (accompanying this Notice of Meeting) in the reply envelope accompanying this Notice of Meeting. Shareholders are encouraged to post their completed **Postal / Internet / Fax Voting Form** no later than Wednesday, 3 August 2016 to ensure that it is received **no later than 1.00pm on Wednesday, 10 August 2016**.

- 3 Fax voting**

You can vote by faxing your completed **Postal / Internet / Fax Voting Form** (accompanying this Notice of Meeting) to **03 377 1474**.

- 4 In Person**

You can attend the Special Meeting and vote. You should bring your **In Attendance / By Proxy Voting Form** (accompanying this Notice of Meeting) with you to the Special Meeting.

- 5 Proxy or corporate representative**

You can appoint a proxy or corporate representative (if the shareholder is a body corporate) to attend the Special Meeting and vote on your behalf. A proxy or corporate representative need not be a shareholder or Current Supplier. You may appoint the Chairman or another Director of the Co-operative as your proxy. If you do not direct the Chairman or Director how to cast your vote the Chairman or Director will cast your vote in favour of the resolution.

Please note that the **In Attendance / By Proxy Voting Form** (accompanying this Notice of Meeting) must be signed by the shareholder or the shareholder's attorney duly authorised in writing or, if the appointor is a corporation, by an officer or attorney duly authorised. Where there are joint shareholders entitled to vote, the **In Attendance / By Proxy Voting Form** must be signed by a majority of the joint owners.

The completed **In Attendance / By Proxy Voting Form** must be received **no later than 1.00pm on Wednesday, 10 August 2016** by post in the reply envelope accompanying this Notice of Meeting or fax to **03 377 1474**.

**VOTES MUST BE RECEIVED NO LATER THAN 1.00PM ON WEDNESDAY 10 AUGUST 2016, UNLESS YOU ARE VOTING IN PERSON OR BY PROXY OR CORPORATE REPRESENTATIVE AT THE SPECIAL MEETING.**



**Rob Hewett**  
Chairman of Directors, Silver Fern Farms Limited  
14 July 2016



# 1

## SECTION *ONE*

FIXING OUR  
CAPITAL STRUCTURE

# SECTION ONE

## FIXING OUR CAPITAL STRUCTURE

The agreements required to give effect to the Shanghai Maling partnership were signed in September 2015, and shareholders voted to support the proposal in October 2015. In November 2015, we announced a very satisfactory set of financial results for the 2014/15 financial year (see Section Two). That has caused a level of unwarranted optimism that we can fix our capital structure requirements without a material capital injection. This Section addresses that issue.

---

### THE TRANSACTION ADDRESSES OUR CAPITAL STRUCTURE AND DEBT LEVELS

Despite having achieved improved results in 2014 and 2015, the need to address the capital structure of the business remains a high priority. This has been reinforced by our disappointing trading results in the current season. While we budgeted for an improved result based on a set of trading assumptions, actual conditions have meant that trading this season has been difficult for the Co-operative and others in the industry. Despite a number of positive initiatives, we are now expecting to make little or no headway on debt reduction and expect to finish the financial year with a similar debt level to that at the start of the year.

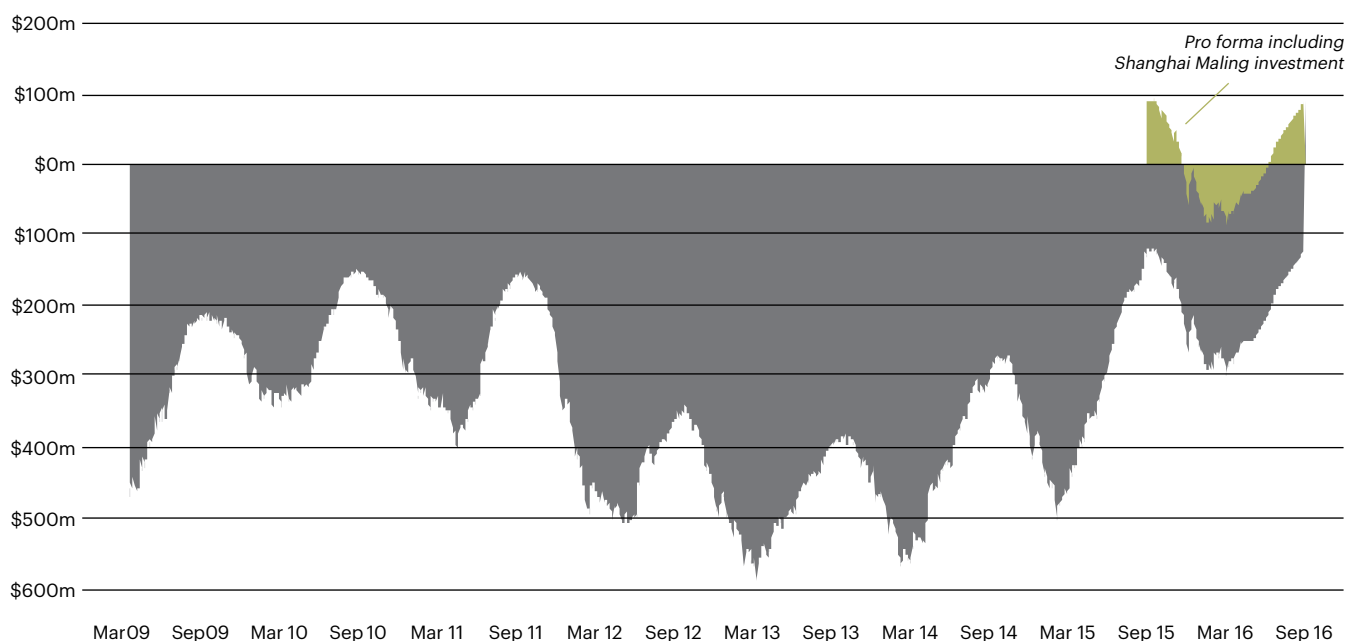
A comprehensive update on the Co-operative's financial performance and position for the six month period ended 31 March 2016 is set out in Section Two.

The Board considers that the year end debt of \$121 million for the financial year ended 30 September 2015 remains too high as:

- 
- our lenders have for some time made it clear that they are concerned at the extent of risk they carry given the Co-operative's existing capital structure, our history of being unable to raise material new equity from existing shareholders, the volatility of our earnings and the significant working capital requirements of Silver Fern Farms' business;
  - the Co-operative's need for a more sustainable capital structure has been longstanding. History has shown that similar levels of year-end debt (for instance \$130 million as at August 2010) have not adequately insulated us against unforeseen market events. The business has a limited ability to withstand financial shock;
- 
- the year end position is a point in time figure only, and typically reflects the lowest level of the business' debt throughout the financial year. It fails to reflect the true debt burden on the business over the course of a financial year resulting from the seasonal profile of stock supply – with forecast peak debt levels typically around \$200 million higher than the business' opening debt position;
  - the debt reductions during the 2014 and 2015 financial years were a significant and necessary achievement. However, as we have consistently stated, these reductions were achieved largely due to "one time events" being the release of excess working capital, the sale of surplus assets and constrained capital expenditure. Such strategies have largely been completed. That means that without a capital injection or the sale of a core asset or business, the Co-operative is reliant on retained trading profits to fund debt reductions. Net profit after tax for the 2014 and 2015 financial years was \$0.5 million and \$24.9 million respectively. The net profit before tax for this financial year is expected to be approximately breakeven. These levels of profitability – individually and in aggregate - do not allow for any meaningful debt reduction;
  - the Board and the Co-operative's lenders agree that Silver Fern Farms' business is carrying too much debt relative to its assets and average earnings, that it needs to address its capital structure and that it cannot rely on operating profits to do this; and
  - as a result of the Co-operative's disappointing financial performance this year (see Section Two), the Co-operative has not met a number of the financial covenants under our debt facility agreement. The lenders have, to date, not sought to exercise any rights in relation to the areas of non-compliance and have continued to support the Co-operative. We appreciate their support.
-



### SILVER FERN FARMS' NET DEBT (INCLUDING TRADE FINANCE) FROM 2009 – 2016



During the course of the 2015 capital raising process the Co-operative considered a number of alternatives to create a more sustainable capital structure for the Co-operative.

The Co-operative held detailed discussions with a number of banks regarding the possibility of refinancing with an alternative banking syndicate. Each of the banks approached declined, in the absence of significant new equity in the Co-operative.

It was (and continues to be) the Board's view that the required capital structure improvements could not be achieved by capital from the Co-operative's existing shareholders alone. In the past, when the Co-operative has required further capital, our shareholder base has not been in a position to meet those requirements. An example of this is the poor results of the 2:1 rights issue undertaken by the Co-operative in 2009, where the Co-operative sought to raise \$128 million from shareholders and raised only \$22 million.

In 2015, the Co-operative also advanced discussions with a consortium of third parties, including some existing shareholders, in parallel with the capital raising process to potentially underwrite a share offer by the Co-operative to existing shareholders. The underwriting commitment proposed by the consortium however was insufficient in size to gain the support of the existing or a new banking

syndicate, would have been highly dilutionary to non-participating shareholders, and required the new shares to have priority over all existing shares as to dividends.

### THE IMPACT OF DEBT BEING TOO HIGH

As can be seen from the chart above:

- the Co-operative has carried high levels of debt for a prolonged period of time;
- the September year end debt position is close to the seasonal low point (and therefore misleading as the sole basis for determining financial strength and ability to refinance);
- our peak debt in recent years has been as high as \$580m; and
- the pro forma impact of the Shanghai Maling investment would be a much lower peak debt, and a net cash positive position for much of the season.

In your Board's view, despite the recent reductions, debt levels remain considerably higher than is appropriate to achieve a strong financial position and from which sustainable returns could be delivered to our shareholders.



History has shown that earnings (for ourselves and other processors) can be volatile in this industry. The Co-operative's total year end debt has been as low as \$130 million in recent times (30 August 2010) but this has not prevented the Co-operative from facing considerable financial challenges in later years.

In short, our current capital structure is not sustainable. The Co-operative has historically carried, and continues to carry, too much debt relative to its average earnings and assets which means:

- 
- it is dependent on the continued support of its lenders;
- 
- it bears high interest and financing costs;
- 
- the terms of its debt facilities are extremely restrictive;
- 
- it is unable to make material permanent debt reductions;
- 
- it is unable to pay consistent dividends;
- 
- it has limited ability to withstand the volatility of earnings inherent in the industry in which it operates and the financial shocks that this volatility can entail; and
- 
- most importantly, it is unable to invest to accelerate its growth strategies.
- 

The Board does not consider that the Co-operative is in a position to refinance its debt facilities from its existing lenders or any alternative syndicate of lenders. However, even if it was, given the peak and average debt burden on the business over the course of a financial year, the Co-operative would continue to be required to direct any cash generated in the business towards reduction of its debt and so would not be in a position to drive change and deliver sustainable returns to its shareholders. Further, the Co-operative would only be one poor season away from potential financial jeopardy.

## THE IMPACT OF THE SHANGHAI MALING TRANSACTION ON OUR BALANCE SHEET

Following completion of the Shanghai Maling transaction, the business will:

- 
- be in a net cash positive position for much of the year, with a seasonal working capital facility to fund stock and debtor build up required during the peak of the season only; and
- 
- be in the strongest financial position of any major company in the New Zealand red meat sector.
-



# 2

## SECTION *TWO*

FY2015 FINAL RESULTS AND  
CURRENT TRADING UPDATE

# SECTION TWO

## FY2015 FINAL RESULTS AND CURRENT TRADING UPDATE

This Section discusses the forecast financial results included in the previous Notice of Meeting in comparison to the actual audited results for the financial year ended 30 September 2015. It also provides a trading update for the first half of this financial year.

FY15 Financial Summary	Forecast	Actual	Difference	
	\$m	\$m	\$m	%
<b>Financial Performance</b>				
Total income	2,255.0	2,451.8	196.8	9%
Operating earnings before interest, tax, depreciation and amortisation ( <b>EBITDA</b> )	77.3	86.9	9.6	12%
Operating earnings before interest and tax ( <b>EBIT</b> )	48.9	58.0	9.1	19%
Net operating profit before tax	19.7	27.2	7.5	38%
Income tax benefit/(expense)	(6.3)	(2.3)	4.0	(63%)
<b>Net profit after tax</b>	<b>13.4</b>	<b>24.9</b>	<b>11.5</b>	<b>86%</b>
<b>Financial Position</b>				
Total assets	605.0	627.1	22.1	4%
Net working capital	154.5	136.2	(18.3)	(12%)
Net Debt	148.0	120.9	(27.1)	(18%)
Total equity including members' shares	361.2	368.4	7.2	2%
<b>Cash Flow</b>				
Net cash flow (used in)/from operating activities	111.1	152.3	41.2	37%

### ACTUAL AUDITED RESULTS FOR THE FINANCIAL YEAR ENDED 30 SEPTEMBER 2015

Messrs Shrimpton and Gallagher have expressed concern that forecast financial results for the year ended 30 September 2015 set out in the previous Notice of Meeting understated the actual results.

The previous Notice of Meeting was finalised and printed before the Co-operative's financial year end of 30 September 2015 and, therefore, included forecast information reflecting what the Board expected the financial performance and financial position of the Co-operative would be at 30 September 2015. The audited financial results were not approved by the Board until 9 November 2015, following completion of the audit.

It was not possible for the Co-operative to delay holding the previous Special Meeting until its audited financial statements had been prepared. This was because:

- the Silver Fern Farms group's bank facilities expired on 31 October 2015 and it was a condition to the provision of the new facility for the 2015/16 season that both Shanghai Maling's and the Co-operative's shareholders had approved the Shanghai Maling transaction; and
- under the agreements with Shanghai Maling, the Co-operative was contractually bound to hold its Special Meeting "as soon as practicable and in any event prior to 31 October 2015".

The Board does not consider that the differences between the forecast financial information provided and our audited results for the financial year ended 30 September 2015 were material, having regard to their amounts, their "point in time" nature and the material swings in the debt requirements of Silver Fern Farms' business through the season. The Financial Markets Authority has independently determined that the financial information provided in the previous Notice of Meeting was not misleading or deceptive.

The table opposite summarises the differences between the forecast information included in the previous Notice of Meeting and the actual audited financial results for last season.

We address below the two areas that have been the particular focus of statements made by Messrs Shrimpton and Gallagher:

### Profitability

The favourable variance in profitability was slightly under \$10 million at an EBITDA or EBIT level and was the product of a number of factors including a combination of strong beef prices, low dairy payout prices and the threat of a significant El Nino weather event (and associated drought), which encouraged farmers to send unprecedented volumes of livestock to the Co-operative and other processors. This was reflected in higher than expected beef and sheep volumes and also margins in the last two months of the year. Actual EBITDA was less than the normalised EBITDA of \$97 million included in Grant Samuel's independent report that accompanied the previous Notice of Meeting.

The favourable variance of just under \$10 million at an EBITDA and EBIT level increased to \$11.5 million at the net profit after tax (**NPAT**) level due to the tax expense only being precisely calculated based on actual results, as is normal for most companies. Whilst as a percentage of forecast NPAT the variance seems large, this is a function of the low level of profitability (which means small dollar changes create large percentage changes) rather than a misstatement of performance.

To suggest that an \$11.5 million variance in NPAT between the 2015 forecast and actual results (a) could be foreseen and (b) provides a misleading view on the true financial performance of the Co-operative fails to appreciate the dynamic nature of Silver Fern Farms' business.

The difference between the forecast and the actual net profit before tax will be one of the items accounted for in the net tangible assets adjustment to be made on completion of the transaction.

### Net debt

The forecast 30 September 2015 net debt position published in the Grant Samuel report was \$148 million. The statements by the Co-operative in the previous Notice of Meeting referred to a forecast range for net debt of \$140 million to \$160 million.

Actual year end debt turned out to be \$121 million after very strong cash receipts in the latter part of September 2015. In the month of September 2015 the Co-operative received

on average approximately \$9.1 million per day and paid out on average \$7.1 million per day, with the highest daily inflow being \$22.7 million, and highest daily outflow being \$15.9 million. In fact, the Co-operative's net debt only dropped below \$140 million some seven days before the financial year end and was back over \$140 million before the end of October 2015.

The Board considered that the final outcome of \$19 million below the expected range in the previous Notice of Meeting was not material in the context of:

- Average debt that year of approximately \$320 million; and
- Peak debt that year of approximately \$490 million.

The financial year end typically reflects the lowest point in the Co-operative's debt in a season and so does not reflect its true debt burden over the course of a financial year. Average debt and peak debt are much more relevant metrics for both the Co-operative and its lenders, and in the Board's view the variance to these metrics was not material in the context of the resolution on the proposed investment by Shanghai Maling.

## HALF YEAR ACTUAL, UNAUDITED, RESULTS

As we publicly stated in April, the Co-operative's financial performance for the six month period ended 31 March 2016 has been significantly below that budgeted for this period and when compared to the same period last year, as summarised in the table on the following page.

This disappointing financial performance is the product of an unusual combination of factors which have affected the industry in New Zealand this year, including:

- a sharp and unexpected decline in in-market prices for many beef, lamb and mutton products during the first quarter of this financial year; and
- weather patterns different to those widely forecast, leading to an unusual flow of livestock with second quarter livestock volumes being less than expected as a result of farmers holding onto stock due to good grass conditions and strong store markets, making replacements expensive relative to further finishing of existing stock. This has led to a flatter, longer supply curve than the traditional peak in supply.

Half Year Unaudited Financial Summary	Actual 6 months to 31 March 2016	Actual 6 months to 31 March 2015	Variance (FY16 to FY15)	Budget 6 months to 31 March 2016	Variance (Actual to Budget)
	\$m	\$m	\$m	\$m	\$m
<b>Financial Performance</b>					
Total income	1,035.1	1,223.3	(188.2)	1,449.7	(414.6)
Operating earnings before interest, tax, depreciation and amortisation ( <b>EBITDA</b> )	19.9	76.5	(56.6)	65.4	(51.4)
Net operating profit/(loss) before tax	(2.6)	50.6	(53.2)	43.4	(46.0)
<b>Financial Position</b>					
Net working capital	281.1	449.4	(168.3)	387.6	(106.5)
Net Debt	277.8	453.1	(175.3)	333.8	(56.0)
Total equity including members' shares	362.8	379.8	(17.0)	392.6	(29.8)
<b>Cash Flow</b>					
Net cash flow (used in)/from operating activities	(152.3)	(166.7)	14.4	(177.3)	25.0

As the above table shows, these factors have collectively contributed to EBITDA (including share of associate earnings) for the six month period ended 31 March 2016 of \$19.9 million, compared with a budget of \$65.4 million and actual performance for this period last year of \$76.5 million. This variance has flowed through to net profit before tax where the actual result is a loss of \$2.6 million for the first six months of this financial year, against a budgeted profit of \$43.4 million and a profit of \$50.6 million for the same period last year.

Positively, the Co-operative's level of investment in working capital is also significantly less than budgeted, as both the value and volume of livestock processed was less than was expected in the first six months of this financial year. In turn, this meant that net debt at 31 May 2016 of \$278 million was \$56 million less than that budgeted. The seasonal peak debt was also lower than budgeted, as the lower than anticipated volume of livestock resulted in a lower peak debt than would be typical. With the "lower but longer" seasonal profile this year, our debt is expected to stay elevated for a longer period than was budgeted for the second half of the financial year. It does not follow, however, that year end debt will be lower than budgeted. On the contrary, due to the lower profitability this year, year end debt is expected to be higher than that budgeted and very similar to last year's closing net debt position of \$121 million.

## TRADING UPDATE – CURRENT FINANCIAL PERFORMANCE

Trading conditions have continued post the six month result period above to be more challenging than budgeted. We now expect full year net profit before tax to be only at a break even level, compared to our budget of \$61.1 million (\$46.4 million after tax). This is clearly disappointing.

The events of the first six months have been unable to be offset in a season where overall end market values for beef and sheepmeat (in New Zealand dollars) have averaged below last year, and industry volumes processed are down on last year (in the nine months this season to 26 June 2016, lamb and beef national numbers processed are down 3% and 4% respectively on the same period last year).



# 3

## SECTION *THREE*

TRANSACTION UPDATE



# SECTION *THREE*

## TRANSACTION UPDATE

In the nine months since the shareholders of the Co-operative approved the transaction, and in reliance on that approval, there has been significant progress made towards completion of the transaction with Shanghai Maling.

As outlined below, all of the conditions to completion of the transaction have been satisfied, other than receipt of OIO approval.

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### SATISFACTION OF CONDITIONS

Shareholders will recall that five conditions were required to be satisfied before Shanghai Maling would proceed with its investment in Silver Fern Farms' business, namely:

- 1 The shareholders of Silver Fern Farms approving the transaction.
- 2 The shareholders of Shanghai Maling Aquarius Co., Ltd approving the transaction.
- 3 Certain Chinese regulatory authorities approving the transaction.
- 4 Completion of the restructure of the Silver Fern Farms group.
- 5 The OIO approving the transaction.

### SILVER FERN FARMS – SHAREHOLDER APPROVAL

While no shareholder approval was legally required to undertake the transaction, the Board made it clear that shareholder approval would be a condition of the transaction proceeding. The Board saw this as fundamental, in the interests of good governance and having regard to the principles of our Co-operative. These include respect for our shareholders and an acknowledgement that many of the suppliers to the Silver Fern Farms group are also shareholders of the Co-operative – and so without their support the transaction could not be an ongoing success.

The Board was pleased that this condition was satisfied with shareholders showing their support by a strong majority of those voting approving the transaction.

### SHANGHAI MALING – SHAREHOLDER APPROVAL

In another very strong endorsement, on 30 October 2015, 99% of the votes cast by shareholders of Shanghai Maling Aquarius Co., Ltd were in favour of the transaction, so satisfying this condition.



## CHINESE REGULATORY AUTHORITIES APPROVALS

Shanghai Maling has formally confirmed satisfaction of this condition following:

- the National Development and Reform Commission providing its formal approval of the transaction on 19 November 2015;
- the Ministry of Commerce providing its approval on 30 December 2015; and
- correspondence with the State Foreign Exchange Commission, Shanghai Maling determining that formal approval from this Chinese regulatory authority was not in fact required.

## RESTRUCTURE OF THE SILVER FERN FARMS GROUP

Full details of the restructure were set out in the previous Notice of Meeting,<sup>11</sup> and a full explanation of the reasons for the restructure are set out in Section Five.

The Co-operative and Shanghai Maling have formally confirmed satisfaction of this condition.

## OVERSEAS INVESTMENT OFFICE APPROVAL

At the date of this Notice of Meeting, the only condition that remains to be satisfied is receipt of OIO approval. Following receipt of that approval the Subscription Agreement between the Co-operative and Shanghai Maling will be unconditional.

The Co-operative and Shanghai Maling have agreed to extend the date by which this condition is required to have been satisfied to 30 September 2016 (previously 30 June 2016).<sup>12</sup> The parties continue to have the ability under the agreement to vary this date. The Board remains confident that OIO approval will be given in due course and within the extended timeframe that has been agreed.

## COMPLETION DATE

In connection with that time extension, the Co-operative and Shanghai Maling have also agreed to extend the date on which Shanghai Maling will complete its investment to 4 January 2017.<sup>13</sup> This extension gives us a firm date to plan around, reflects Shanghai Maling's desire for a start date to coincide with the intended 1 January to 31 December financial year of the partnership, and coincides with Shanghai Maling's balance date.

<sup>11</sup> Pages 22-25 and 47-50 of the previous Notice of Meeting.

<sup>12</sup> The Co-operative and Shanghai Maling have agreed to extend the date by which this condition is required to have been satisfied to 30 September 2016 (previously 30 June 2016). The parties continue to have the ability under the agreement to vary this date. The Board remains confident that OIO approval will be given in due course and within the extended timeframe that has been agreed.

<sup>13</sup> At the date of printing of this Notice of Meeting, these amendments remain subject to board approvals and finalising amendments to the Co-operative's facility agreement to meet lenders' requirements.



# 4

## SECTION *FOUR*

LETTERS FROM INDEPENDENT EXPERT  
GRANT SAMUEL & ASSOCIATES LIMITED



LEVEL 31  
 VERO CENTRE  
 48 SHORTLAND STREET AUCKLAND  
 PO BOX 4306 AUCKLAND  
 T: +64 9 912 7777 / F: +64 9 912 7788  
 www.grantsamuel.co.nz

11 July 2016

The Directors  
 Silver Fern Farms Limited  
 283 Princes Street  
 PO Box 941  
**DUNEDIN**

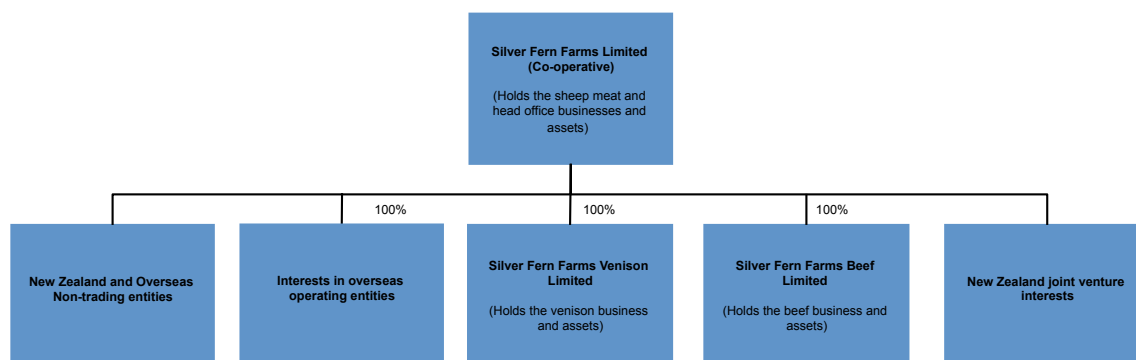
Dear Directors,

### Proposed Transaction with Shanghai Maling Aquarius Co. Ltd

#### 1. Introduction

Effective from 1 October 2015, Silver Fern Farms Limited (**SFF Co-Op**) undertook a corporate restructuring (the **Corporate Restructure**) as a pre-requisite to completing a proposed transaction involving a NZ\$261.4 million equity investment by Shanghai Maling Aquarius Co. Ltd (**Shanghai Maling**) into SFF Co-Op's operating business, Silver Fern Farms Beef Limited (**SFF**) (the **Proposed Transaction**).

#### *Silver Fern Farms Group prior to the Corporate Restructure*

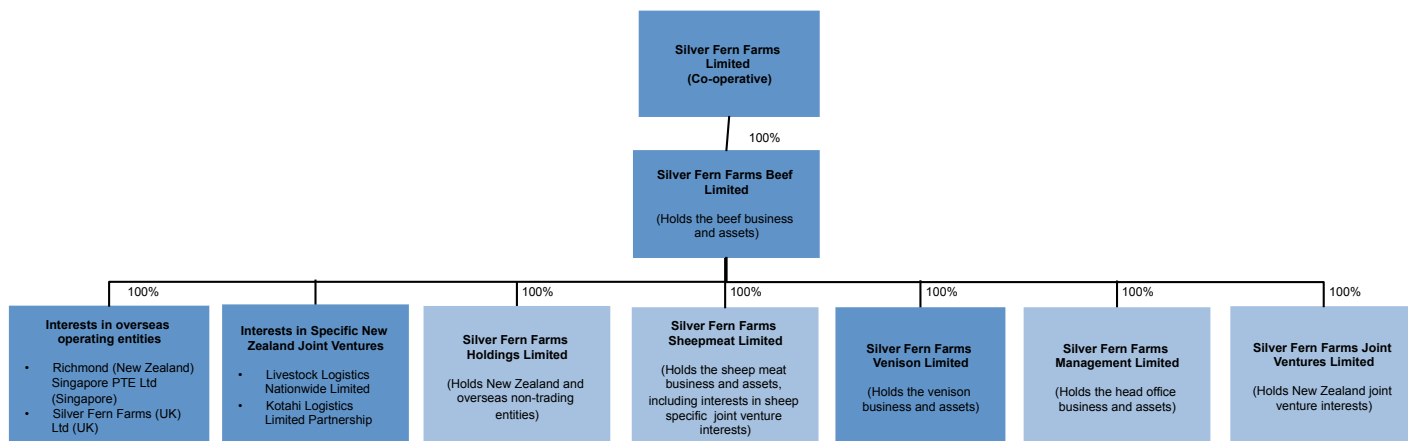


The details of the Corporate Restructure were set out in Appendix Two of the Notice of Meeting sent to SFF Co-Op shareholders in September 2015 and, in summary, involved:

- the incorporation of four wholly owned subsidiaries of SFF (being Silver Fern Farms Sheepmeat Limited, Silver Fern Farms Management Limited, Silver Fern Farms Holdings Limited and Silver Fern Farms Joint Ventures Limited);
- the sale of SFF Co-Op's sheepmeat business (including the transfer of related employees and interests in various sheep specific joint ventures) to Silver Fern Farms Sheepmeat Limited;
- the sale of SFF Co-Op's head office function (including the transfer of related employees) to Silver Fern Farms Management Limited;

- (d) the sale of SFF Co-Op's shares in Silver Fern Farms Venison Limited and interests in various joint ventures to SFF;
- (e) the sale of SFF Co-Op's interests in the remaining joint ventures (being those not transferred to Silver Fern Farms Sheepmeat Limited or SFF) to Silver Fern Farms Joint Ventures Limited; and
- (f) the sale of SFF Co-Op's various non-trading companies to Silver Fern Farms Holdings Limited.

### Silver Fern Farms Group after the Corporate Restructure



#### Newly incorporated Companies

SFF Co-Op shareholders met on 16 October 2015 and by a majority of 82% approved an ordinary resolution for SFF Co-Op to proceed with the Proposed Transaction. Subsequent to the shareholders meeting, a number of shareholders (the **Requisitionists**) queried whether the Corporate Restructure was effected in compliance with section 129 of the Companies Act 1993 (the **Act**) and the corresponding provisions of SFF Co-Op's constitution. The Requisitionists contend that the transfer of the various businesses and assets taken together comprised a Major Transaction as defined in section 129 of the Act (a **Major Transaction**). Major Transactions require the approval by a majority of more than 75% of the shareholders voting on a special resolution.

## 2. Scope of Work

Grant Samuel & Associates Limited (**Grant Samuel**) prepared an independent report in relation to the Proposed Transaction that was sent with the Notice of Meeting to SFF Co-Op shareholders in September 2015. SFF Co-Op shareholders are now meeting again on 12 August 2016 to vote on a special resolution proposed by the Requisitionists with the stated objective of approving the Proposed Transaction by special resolution as if it was a Major Transaction.

The directors of SFF Co-Op have asked Grant Samuel to provide this letter for SFF Co-Op shareholders to be sent with the Notice of Meeting for the upcoming Special Meeting in August 2016. In this letter Grant Samuel has been asked to determine whether in its opinion the Corporate Restructure was a Major Transaction. Under the Act a Major Transaction is defined as either:

- (a) the acquisition of, or an agreement to acquire, whether contingent or not, assets of the company the value of which is more than half the value of the company's assets before the acquisition; or
- (b) the disposition of, or an agreement to dispose of, whether contingent or not, assets of the company the value of which is more than half the value of the company's assets before the disposition.

"Assets" includes property of any kind, whether tangible or intangible. The legislation does not expressly state whether "assets" means the gross assets of the company before deducting liabilities (**Gross Assets**) or the net assets of the company after deducting liabilities (**Net Assets**). Subsequent court cases have concluded "assets"

means the market value of the Gross Assets of the company. Grant Samuel has adopted market value of Gross Assets as being the appropriate measure to determine whether the Corporate Restructure was a Major Transaction.

Grant Samuel was not asked to prepare a new independent report. The report was dated September 2015 and based on economic, market and other conditions at that date. The scope of work undertaken by Grant Samuel in preparing this letter has been limited to analysis of the Corporate Restructure to determine whether it met the definition of a Major Transaction at the time it was undertaken.

Preparation of its earlier report and this letter does not imply that Grant Samuel has audited in any way any information or records of SFF Co-op. Grant Samuel has not undertaken a due diligence investigation of SFF Co-Op and does not warrant that its enquiries have identified or verified all of the matters which an audit, extensive examination or a "due diligence" investigation might disclose. It is understood that, where appropriate, any information provided to Grant Samuel was prepared in accordance with generally accepted accounting practice and in a manner consistent with methods of accounting used in previous years.

### **3. The Corporate Restructure was not a Major Transaction**

**In Grant Samuel's opinion the carrying value of assets reported in SFF Co-Op's statement of financial position at 30 September 2015 is not representative of the market value of its Gross Assets. Accordingly, Grant Samuel has determined the market value of SFF Co-Op's Gross Assets by reference to its assessment of the market value of SFF as set out in Grant Samuel's Independent Report dated September 2015.**

**In Grant Samuel's opinion the aggregate market value of the Gross Assets transferred from SFF Co-Op to its subsidiary companies falls within the range of \$200 million to \$215 million. This value range equates to less than 50% of Grant Samuel's assessment of the market value of the Gross Assets of SFF Co-Op immediately prior to undertaking the Corporate Restructure. Accordingly, Grant Samuel has concluded that the Corporate Restructure was not a Major Transaction.**

This letter should be read in conjunction with Grant Samuel's Independent Report dated September 2015.

Yours faithfully,

*Grant Samuel + Associates*



LEVEL 31  
VERO CENTRE  
48 SHORTLAND STREET AUCKLAND  
PO BOX 4306 AUCKLAND  
T: +64 9 912 7777 / F: +64 9 912 7788  
www.grantsamuel.co.nz

11 July 2016

The Directors  
Silver Fern Farms Limited  
283 Princes St  
**Dunedin**

Dear Directors,

### **Proposed Transaction with Shanghai Maling Aquarius Co. Ltd**

#### **1. Introduction**

Grant Samuel & Associates Limited (**Grant Samuel**) prepared an independent report for the shareholders of Silver Fern Farms Limited (**SFF Co-Op**) in relation to a proposed transaction involving a NZ\$261.4 million equity investment by Shanghai Maling Aquarius Co. Ltd (**Shanghai Maling**) into SFF Co-Op's operating business Silver Fern Farms Beef Limited (**SFF**) (the **Proposed Transaction**) in September 2015. SFF Co-Op shareholders met on 16 October 2015 and by a majority of 82% approved an ordinary resolution for SFF Co-Op to proceed with the Proposed Transaction.

#### **2. Scope of Work**

SFF Co-Op shareholders are meeting on 12 August 2016 to vote on a special resolution requisitioned by a number of shareholders. Essentially, the resolution deals with the same subject matter as was the subject of the resolution proposed by the Board of SFF Co-Op at the shareholder meeting in October 2015. In this letter Grant Samuel has been asked to review its opinion that the Proposed Transaction is fair and reasonable to the shareholders of SFF Co-Op in the light of the following new information (the **New Information**):

- Audited financial statements for the year ended 30 September 2015; and
- Q2 forecast for the year ending 30 September 2016 prepared for the SFF Co-Op directors by management in April 2016.

Grant Samuel was not asked to prepare a new independent report. The report dated September 2015 is based on economic, market and other conditions at the date of that report. The scope of work undertaken by Grant Samuel in preparing this letter has been limited to a review of the New Information only.

The New Information provided has been evaluated through analysis, enquiry, and review for the purposes of reconsidering whether the Proposed Transaction is fair and reasonable. An important part of the information used in forming an opinion of the kind expressed in the earlier report and this letter are the opinions and judgment of the management of the relevant enterprise. However, it must be recognised that such information is not always capable of external verification or validation.

The New Information provided to Grant Samuel included actual audited historical financial information which was not available to Grant Samuel or shareholders before the 16 October 2015 meeting and financial projections of future

revenues, expenditures, profits and cash flows of SFF Co-Op prepared by the management of SFF Co-Op in April 2016. Grant Samuel has used and relied upon the New Information for the purpose of its analysis. Grant Samuel has assumed that the financial projections were prepared accurately, fairly and honestly based on information available to management at the time and within the practical constraints and limitations of such projections. It is assumed that the projections do not reflect any material bias, either positive or negative. Grant Samuel has no reason to believe otherwise.

However, Grant Samuel in no way guarantees or otherwise warrants the achievability of the projections of future profits and cash flows for SFF Co-Op. Projections are inherently uncertain. Projections are predictions of future events that cannot be assured and are necessarily based on assumptions, many of which are beyond the control of management. The actual future results may be significantly more or less favourable.

### **3. The Proposed Transaction is Fair and Reasonable**

**Having considered the New Information Grant Samuel reaffirms that the terms and conditions of the Proposed Transaction are fair and reasonable to the shareholders of SFF Co-Op. In Grant Samuel's opinion SFF Co-Op remains undercapitalised and a financial restructuring is critical to its future.**

This letter should be read in conjunction with Grant Samuel's Independent Report dated September 2015.

Yours faithfully

*Grant Samuel + Associates*



# 5

## SECTION *FIVE*

BOARD'S RESPONSE TO ALLEGATIONS  
MADE IN THE STATEMENT PROVIDED BY  
MESSRS SHRIMPTON AND GALLAGHER



# SECTION FIVE

## BOARD'S RESPONSE TO ALLEGATIONS MADE IN THE STATEMENT PROVIDED BY MESSRS SHRIMPTON AND GALLAGHER

Messrs Shrimpton and Gallagher have provided a detailed Statement for publication with this Notice of Meeting. In this Section the Board addresses the main allegations made in that Statement. Following that, the Board has addressed each of the allegations made in the "Summary" to the Statement.

The full Statement provided by Messrs Shrimpton and Gallagher is set out in the Appendix to this Notice of Meeting.

### FIRST AND SECOND MAIN ALLEGATIONS: SHAREHOLDERS WERE MISLED AS TO THE FINANCIAL POSITION OF SILVER FERN FARMS, AND AS TO THE LIKELIHOOD OF RECEIVERSHIP IF THE SHANGHAI MALING TRANSACTION DID NOT PROCEED

We address these allegations together. Your Board's view is that they are entirely unfounded.

The Statement provided by Messrs Shrimpton and Gallagher asserts that the financial information presented to shareholders was so materially different from the actual position of the Silver Fern Farms group that it calls into question the legitimacy of the October 2015 shareholder vote.

This allegation is wrong. This same complaint was made to, and rejected by, the Financial Markets Authority, as shown by the Financial Markets Authority's announcement dated 25 May 2016 where it made the following statements:

*"Complainants alleged that the SFF [Notice of Meeting and Shareholder] Information Pack misrepresented the financial position of SFF by showing a more negative position than was the case. It was alleged that the purpose of this negative misrepresentation was to encourage shareholders to vote in favour of the Transaction with Shanghai Maling.*

*The FMA engaged with the directors and senior management of SFF to verify whether relevant information in the [Notice of Meeting and Shareholder] Information Pack could be substantiated. We are satisfied that we have been provided with sufficient evidence to substantiate the relevant information. **We do not have any reason to believe the [Notice of Meeting and Shareholder] Information Pack was misleading or deceptive.**" (Emphasis added)*

*"We note that the Information Pack was finalised on 23 September 2015 and contained forecast financial information for the financial year-end 30 September 2015. These forecasts included a forecast debt of between \$140 million and \$160 million. The actual year-end results, released on 9 November 2015, showed that debt on 30 September was \$121 million. The actual profit and revenue figures were also better than in the Information Pack."*

*"Although the debt position on 30 September 2015 was lower than forecast, SFF's debt is highly variable and can change significantly from day to day. Due to the seasonal nature of SFF's business, the level of debt also changes significantly depending on the time of year. Given the variability of SFF's debt and the position taken by SFF's existing banking syndicate, we accept the SFF Board's view that **the differences between the forecasts in the [Notice of Meeting and Shareholder] Information Pack and the actual results in the annual report were not material to the shareholders' resolution on the Transaction.**" (Emphasis added)*

A full copy of the Financial Markets Authority's announcement can be found on the Unlisted market platform for Silver Fern Farms Limited at [www.unlisted.co.nz](http://www.unlisted.co.nz).

The previous Notice of Meeting was finalised and printed before the Co-operative's financial year end of 30 September 2015 and, therefore, included forecast information reflecting what the Board expected the financial performance and financial position of the Co-operative would be at 30 September 2015. The audited financial results were not approved by the Board until 9 November 2015 (following completion of the audit).

It was not possible for the Co-operative to delay holding the previous Special Meeting until its audited financial statements had been prepared. This was because:

- the Silver Fern Farms group's bank facilities expired on 31 October 2015 and it was a condition to the provision of the new facility for the 2015/16 season that both Shanghai Maling's and the Co-operative's shareholders had approved the Shanghai Maling transaction.
- under the agreements with Shanghai Maling, the Co-operative was contractually bound to hold its Special Meeting "as soon as practicable and in any event prior to 31 October 2015".

As the Financial Markets Authority has independently determined, the financial information provided in the previous Notice of Meeting was not misleading or deceptive. Further, your Board does not consider that the differences between the forecast financial information provided and our audited results for the financial year ended 30 September 2015 were material, having regard to their amounts, their “point in time” nature and the material swings in the debt requirements of Silver Fern Farms’ business across the season. This is addressed fully in the Chairman’s letter and further information is also included in Sections Two and Four.

As to the uncertainty of financial support from the Co-operative’s lenders, independent expert, Grant Samuel has reviewed the Co-operative’s audited financial results for the financial year ended 30 September 2015 and a trading update for the current financial year. In Section Four, Grant Samuel has reaffirmed its views that the transaction is fair and reasonable to shareholders, and that a financial restructuring remains critical to the Co-operative’s future.

As a result of the Co-operative’s disappointing financial performance this year (see Section Two), the Co-operative has not met a number of the financial covenants under the facility agreement. The lenders have, to date, not sought to exercise rights in relation to the areas of non-compliance and have continued to support the Co-operative. We appreciate their support. However we are under no illusion that if the partnership proposal with Shanghai Maling was not progressing to implementation, we would be having very different conversations with our lenders. Even if we had their continued support in the face of a failed transaction (support which we believe cannot be relied upon, illustrated by the statements made by the Co-operative’s lenders set out in the Chairman’s letter), we think it would be at an even higher cost, greater financial constraints and very likely require asset and business restructure, disposal and or heavily discounted recapitalisation.

This is in stark contrast to the financial certainty and business opportunity provided by the Shanghai Maling investment.

The Board’s view is that there is no substance to the first and second allegations and it is supported by:

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- the Financial Markets Authority, which has had access to the Co-operative’s confidential information, management and Board in coming to its conclusions; and
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- 
- independent expert, Grant Samuel, which has had access to the Co-operative’s confidential information and its lenders in coming to its conclusions.
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### THIRD MAIN ALLEGATION:

#### **THE TRANSACTION IS A MAJOR TRANSACTION UNDER THE COMPANIES ACT AND REQUIRED APPROVAL BY SPECIAL RESOLUTION**

A core assertion made in the Statement provided by Messrs Shrimpton and Gallagher is that the Co-operative has undertaken a “Major Transaction” as defined in the Companies Act without complying with the applicable legal requirements.

Your Board’s view is that this allegation is entirely unfounded.

In this context, a Major Transaction under the Companies Act means:

*“The disposition of, or an agreement to dispose of, whether contingent or not, assets the value of which is more than half of the value of the company’s assets before the disposition.”*

Under the Companies Act, a Major Transaction must be approved by shareholders by way of a special resolution (75% of the votes of shareholders entitled to vote and voting on the resolution, including a majority of the votes of ‘Current Suppliers’ entitled to vote and voting on the resolution).

**The Statement provided by Messrs Shrimpton and Gallagher does not provide any legal, financial or other analysis to support their assertions that the transaction was a Major Transaction.**

In contrast, the Board explicitly took professional valuation advice from PricewaterhouseCoopers and carefully considered whether the Shanghai Maling transaction (and all its related elements, including the restructure) constituted a Major Transaction for the Co-operative. The Board was, and remains, satisfied that the transaction with Shanghai Maling does not constitute a Major Transaction. If the advice had been that it was a Major Transaction, then the Board would have sought a special resolution.

The key aspects of the Board’s analysis were:

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- The legislation, as mirrored in the Co-operative’s constitution, requires that the Major Transaction test is applied on a company specific basis, not by aggregating distinct transactions across different companies in a group.
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- The test is applied on the basis of the 'gross market value' of the assets of the relevant company (i.e. not historic cost, book value or some other notion of value).

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- The Board obtained external professional valuation advice from PricewaterhouseCoopers regarding the gross market value of the assets of the Co-operative and the gross market value of the assets of the Co-operative proposed to be transferred under the restructure.

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- PricewaterhouseCoopers assessed the gross market value of the assets of the Co-operative by reference to the values demonstrated by Shanghai Maling's subscription price. This price resulted from the Co-operative's extensive capital raising process and the Board considered that this was an appropriate, and the best, indicator of market value at that time.

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- PricewaterhouseCoopers determined that the restructure involved the transfer of assets with a gross market value of less than half of the gross market value of the Co-operative's total assets. This outcome was not a surprise to the Board because the shares in Silver Fern Farms Beef Limited were not being transferred as part of the restructure. Silver Fern Farms Beef Limited holds the beef business which is the group's most profitable and valuable business, and the advice to the Board has been that it is worth more than the balance of the group collectively.

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As a result of this analysis, the Board's considered view was, and is, that the restructure to facilitate the Shanghai Maling transaction was not a Major Transaction for the Co-operative.

Grant Samuel has independently assessed the matter and has also concluded that the restructure did not constitute a Major Transaction. Grant Samuel's conclusions are included in its letter in Section Four.

Shanghai Maling's \$261 million investment in return for new shares equal to a 50% shareholding in Silver Fern Farms Beef Limited is not a transaction that involves the Co-operative disposing of any assets. It is not a Major Transaction for the Co-operative.

Nonetheless, despite the Board concluding that there was no Companies Act, constitutional or other statutory requirement, it elected to seek shareholder approval:

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- in the interests of good governance and having regard to the principles of our Co-operative;

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- out of respect for our shareholders; and

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- in acknowledgement of the fact that many of our suppliers are also shareholders of the Co-operative – without their support the transaction could not be an ongoing success.

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The voting threshold was set by the Board at the customary ordinary resolution level (50.01% of the votes of shareholders entitled to vote and voting on the resolution).

The Requisitioners now propose that substantively the same resolution that was proposed as an ordinary resolution (50.01% majority requirement) in October 2015 and passed by 82.22% of the votes cast, be put again - but this time as a special resolution (75.01% majority requirement).

**The Co-operative does not accept that this is a valid approach. The Board is firmly of the view that the transaction has already been properly authorised by the Board and approved by shareholders at the October 2015 Special Meeting.**

The leadership of the political party NZ First Party, made a complaint to the Registrar of Companies that the directors of your Co-operative were in breach of their duties to act in good faith and in the best interests of the Co-operative, including on the basis of his allegations that:

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- the directors deliberately structured the Shanghai Maling transaction so as to avoid the Major Transaction provision of the Companies Act; and

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- the directors failed to obtain a proper shareholder approval, under the Major Transaction provision of the Companies Act.

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The Co-operative supplied the Registrar of Companies with detailed information regarding the Co-operative's considerations in respect of the Major Transaction provision of the Companies Act, and the Registrar of Companies concluded that the allegations of breach of duty were unfounded, stating:

*"the Registrar has not identified any evidence of a breach of s 138A of the Companies Act 1993 (relating to criminal breach of directors duties). This investigation is now complete..."*

#### FOURTH MAIN ALLEGATION:

##### **THE RESTRUCTURE UNDERTAKEN BY THE CO-OPERATIVE INVOLVED A CHANGE IN THE 'ESSENTIAL NATURE' OF SILVER FERN FARMS' BUSINESS AND REQUIRED SHAREHOLDER APPROVAL BY SPECIAL RESOLUTION**

This allegation is wrong.

There is no legal requirement, including under the Companies Act or the Co-operative's constitution, for a change in the essential nature of Silver Fern Farms' business to be approved by the Co-operative's shareholders.

The NZX Main Board listing rules do include such a test, however the Co-operative is not listed on the NZX Main Board – and so the NZX Main Board listing rules do not apply to it. Even if it were listed on the NZX Main Board, the applicable listing rule requires shareholder approval by way of an ordinary resolution (which was achieved at the Special Meeting in October 2015).

The Board recognised the significance of the transaction for the Co-operative and shareholders and, as outlined in the previous paragraphs, sought and obtained shareholder approval even though that was not legally required.

#### FIFTH MAIN ALLEGATION:

##### **THE RESTRUCTURE UNDERTAKEN BY THE CO-OPERATIVE WAS CONSTRUCTED SO AS TO AVOID THE MAJOR TRANSACTION PROVISIONS OF THE COMPANIES ACT**

The Statement provided by Messrs Shrimpton and Gallagher asserts that the Board has undertaken “*an opaque, complex and incompletely described set of steps*” to divide Silver Fern Farms' businesses across various subsidiaries for the purpose of avoiding the application of the Major Transaction provisions of the Companies Act.

This allegation is entirely unfounded, and as noted above, the Registrar of Companies has rejected a complaint against the directors based on this allegation.

**The restructure referred to is neither opaque nor complex and was in fact described in detail in the previous Notice of Meeting.<sup>14</sup> The restructure was required under the agreements entered into with Shanghai Maling as a condition of Shanghai Maling's investment. It was not developed for the purpose of circumventing the Major Transaction provisions of the Companies Act.**

The need for the restructure resulted from the investment requirements of Shanghai Maling. A key term of the Shanghai Maling transaction, which strongly suited the Co-operative, was that rather than taking a 50% shareholding in the Co-operative itself, Shanghai Maling would invest at a level below the Co-operative. This was favoured by the Board as it enabled the Co-operative to remain in existence with its constitution, voting rights, director appointment process, Board composition requirements and other existing farmer control features uncompromised. It was considered that this would better facilitate a true joint venture structure between two equal shareholders with shared governance arrangements.

The alternative, of Shanghai Maling holding a 50% shareholding in the Co-operative itself, would have led to a fundamentally different, more complex and challenging set of governance and operating requirements, forever changing the dynamics of the Co-operative and principles of farmer control.

The purpose of the restructure was to ensure that the joint venture entity (Silver Fern Farms Beef Limited) in which the Co-operative and Shanghai Maling would hold a 50:50 interest following Shanghai Maling's investment, would hold all of the assets required for it to operate Silver Fern Farms' business. Without this restructure, the features described in the preceding paragraph would not have been available – and Silver Fern Farms Beef Limited would not hold the sheepmeat business, head office functions and other assets which were at that time held by the Co-operative, and which are essential to the operation of Silver Fern Farms' business.

Silver Fern Farms was, at the time of this restructure, already the owner of the beef and venison businesses through separate wholly owned subsidiaries.

The Board firmly denies the allegations that it in any way misled shareholders in respect of the restructure required to give effect to the Shanghai Maling transaction, or that it has completed the restructure in such a way so as to circumvent the Major Transaction provisions of the Companies Act.

<sup>14</sup>. Pages 22-25 and 47-50 of the previous Notice of Meeting.

## THE BOARD'S COMMENTARY ON THE "SUMMARY" FROM THE STATEMENT PROVIDED BY MESSRS SHRIMPTON AND GALLAGHER

The table on the following pages repeats the "Summary" from the Statement provided by Messrs Shrimpton and Gallagher (green), and provides the Board's responses to the various points (black).

- > *"The Special Resolution was requisitioned by more than 5% of shareholders because of concerns each of those had about the Proposed Transaction and how it has been pursued by the Company and its advisors. It has been expressed that numerous aspects of this do not appear to sit well with the traditional co-operative values, including that of transparency."*

**The Board's Response:**

Your Board is entirely satisfied that it has pursued the Shanghai Maling transaction properly, transparently, legally and in accordance with appropriate governance practices.

- > *"An attempt to raise these concerns before with the Company was unsuccessful."*

**The Board's Response:**

This is incorrect. Mr Shrimpton addressed the Annual General Meeting of shareholders on 16 December 2015 with some of his concerns.

Messrs Shrimpton and Gallagher and their advisors have been invited to meet the Board, management and their advisors, but having accepted this they subsequently cancelled the meeting that had been arranged without reason.

The Board continued to make itself available on the same basis to discuss these matters, but Messrs Shrimpton and Gallagher chose not avail themselves of this opportunity. On 23 May 2016 and subsequently, Messrs Shrimpton and Gallagher have indicated a preparedness to meet, but "without lawyers present". Given that the issues raised are of a legal character, the Board considered such a meeting would not be constructive.

- > *"Many of the Requisitionists actually voted in favour of the ordinary resolution put to shareholders about the Proposed Transaction on 16 October 2015 (the October Vote).*

*But subsequent developments and analysis have convinced those shareholders that requisitioned the Special Resolution that the Proposed Transaction was not properly approved then, and how it has been pursued by the Company overall has led those that requisitioned the Special Resolution to conclude that it is not in shareholders' best interests and should not be approved now.*

*The first of those concerns arises because the Companies Act and SFF's own Constitution strongly protect shareholders' interests by preventing the Company from entering into a major transaction without the approval of a special resolution, which has not been sought until now."*

**The Board's Response:**

Refer earlier in this Section Five for the Board's response to this allegation.

Although Messrs Shrimpton and Gallagher have stated this to be the conclusions of all of the Requisitioners, Messrs Shrimpton and Gallagher have not established to the Board's satisfaction that they are authorised to make any statements on behalf of all of the Requisitioners. The Appendix lists the names of 31 of the 80 Requisitioners, and only that number have advised the Co-operative that they endorse the Statement.

The Board continues to consider that the transaction is in the best interests of the Co-operative and its shareholders. It is satisfied that it has acted at all times in accordance with the Companies Act and the Co-operative's constitution.



- > *“The Companies Act and our Constitution define a major transaction as including disposal of more than half the Company’s assets. The Proposed Transaction itself would require the transfer of 100% of SFF’s existing business into the SFF JV, clearly qualifying it as a major transaction.”*

**The Board’s Response:**

Refer earlier in this Section Five for the Board’s response to this allegation. Shareholders are also encouraged to read Grant Samuel’s letter in Section Four.

The Board was, and remains, satisfied that the transaction with Shanghai Maling does not constitute a Major Transaction.

The restructure **did not** involve the transfer of 100% of the Co-operative’s existing business.

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- > *“The Company expects to spend some \$7m of shareholders’ funds, including on a complex and opaque restructuring which has involved the formation of 5 or more, new subsidiaries after the Proposed Transaction was announced to shareholders (the **Restructuring**). We believe that this Restructuring seemingly served no clear purpose other than, it would appear, to avoid the substance of the sale of SFF’s entire business being considered as a major transaction.”*

**The Board’s Response:**

Refer earlier in this Section Five for the Board’s response to this allegation.

The restructure, including the incorporation of various subsidiaries of Silver Fern Farms Beef Limited, was described in detail (including the provision of structure diagrams naming the subsidiaries) in the previous Notice of Meeting.<sup>15</sup> That restructure has been completed.

Silver Fern Farms Management Trustee Limited was incorporated as part of the restructure as a trustee company for the protection of the employment entitlements of the 200 or more head office employees of the Co-operative before they accepted employment with Silver Fern Farms Management Limited. This was required to protect the interests of the affected employees recognising that Silver Fern Farms Management Limited has very few assets of its own to provide security of entitlements to those individuals.

Messrs Shrimpton and Gallagher have made statements in the media asserting that the structure of the Silver Fern Farms group and in particular the composition of the boards of those subsidiaries is in some way unorthodox. The Board firmly disagrees.

In fact the practice of having subsidiaries and having fewer directors on the boards of those subsidiaries than on the board of the parent is common place. By example, ANZCO, another significant meat processor, has (based on its Annual Report for the period to 31 December 2015) more than 20 wholly owned subsidiaries, the majority of which have a board comprising only two directors.

Transaction costs in a complex capital raising process and transaction for a business of this scale are always high, but the costs have been spent across a large number of items, and the costs of the restructure are a relatively minor part of the overall costs for this transaction. The largest element of these costs is investment banking fees referable to the running of the capital raising process and the securing of the approximately \$261 million investment.

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<sup>15</sup>. Pages 18, 42, 43 and 44 of the previous Notice of Meeting.

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- *“In addition, we consider that the Proposed Transaction would also result in the Company effectively becoming an investment entity rather than a co-operative company in substance. Such a change also requires shareholders’ approval by way of a special resolution which has also not been the case so far.”*

**The Board’s Response:**

This is incorrect.

The Shanghai Maling transaction will have no impact on the Co-operative’s status as a co-operative company. Farmer shareholder suppliers will continue to supply their livestock to the Co-operative, holders of ordinary and rebate shares will retain their shares and the farmer control enshrined in the Co-operative’s constitution will remain uncompromised.

The Statement asserts that shareholder approval is required due to some notion of fundamental or essential change in the business. No such legal test is applicable to the Silver Fern Farms group.

The Board appreciated the significance of the Shanghai Maling transaction, and voluntarily put it before shareholders for approval.

It is the Board’s firm view that the assertion that shareholder approval is or was required in any form in respect of the Shanghai Maling transaction has no legal foundation.

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- *“In other words, we believe that the Company has seemingly deployed extensive legal advice (at shareholders’ expense) not, it would appear, to protect or act in shareholders’ best interests (as it claims), but seemingly to go around those very shareholders’ rights which are otherwise protected under the major transaction and change in the essential nature of business provisions.”*

**The Board’s Response:**

The Board refutes these allegations in the strongest terms.

The Board understands its fiduciary and statutory duties and is satisfied that it has acted at all times in accordance with those duties, the Companies Act and the Co-operative’s constitution.

The Registrar of Companies has investigated this matter and has not identified any evidence that directors have acted in anything other than accordance with their duties.

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- *“Furthermore, even though the Company has tried to claim regularly that it has complied with “all relevant laws, regulations and the Company’s constitution”, by seemingly having attempted to avoid the proper method of approving the Proposed Transaction, the Company appears to have either ignored, or acted contrary to its own best practice corporate governance standards. These are also aimed ultimately at protecting shareholders’ interests.”*

**The Board’s Response:**

It is the Board’s firm view that the assertion that shareholder approval is or was required in any form in respect of the Shanghai Maling transaction has no legal foundation.

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- > *“Second, key information presented to shareholders about the Company’s financial performance and position was so materially different from the actual 2015 financial results announced just 24 days after the October Vote as to call its legitimacy further into question.”*

**The Board’s Response:**

Refer earlier in this Section Five for the Board’s response to this allegation. Shareholders are also encouraged to read Section Two.

The Board does not consider that the financial information provided in the previous Notice of Meeting was in any way misleading. The Board’s view has been vindicated by the Financial Market Authority.

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- > *“The statement issued on 24 May 2016 by the Financial Markets Authority (the FMA) in this regard referred only to very select aspects and failed to address why shareholders were not provided with more accurate information before the October Vote was held.”*

**The Board’s Response:**

This Statement is incorrect.

The Financial Markets Authority has investigated this complaint and has determined that it does *“not have any reason to believe the Information Pack was misleading or deceptive”* and further that it accepted the Board’s position that *“the differences between the forecasts in the Information Pack and the actual results in the annual report were not material to the shareholders’ resolution on the Transaction.”*

Shareholders are also encouraged to read the letter from Grant Samuel in Section Four.

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➤ *“Also the circular Shanghai Maling issued to its own shareholders contained more material provided by SFF’s management than seems to have been shared with SFF’s own shareholders, including forecast net operating profits after tax for 2017 of \$60m and \$73m for 2018.*

*This seemingly led to significantly different valuations, part of which appears to be attributable to activities and performances forecast for those periods not detailed for SFF’s shareholders.”*

**The Board’s Response:**

The Board notes that the Financial Markets Authority has publicly stated in its response to these assertions that it has reviewed the information provided by Shanghai Maling to its shareholders and maintains its view that the information provided to shareholders by Silver Fern Farms in the previous Notice of Meeting was not misleading.<sup>16</sup>

The Financial Markets Authority has also stated in its response to questions from TV3 and other media outlets that had the Co-operative included projections for the 2017 and 2018 financial years in its previous Notice of Meeting this would have been misleading because of how uncertain those forecasts would have been.<sup>17</sup>

As shown by the actual, unaudited, half year financial performance for this financial year against budget included in Section Two, industry factors outside of the Co-operative’s control (including market prices, climate, exchange rates and stock volumes) mean that medium and long term forecasting is inherently unreliable. As Grant Samuel noted in its independent report which accompanied the previous Notice of Meeting,<sup>18</sup> this is why the Board only considers and approves forecasts one year ahead at any time.

The projections referred to by Messrs Shrimpton and Gallagher were in fact created by Shanghai Maling based on a financial model provided by the Co-operative’s adviser to Shanghai Maling on 31 July 2015 during the course of its due diligence review of the business (at least six weeks before the agreements with Shanghai Maling were signed). The financial model was neither reviewed nor approved by the Board, nor endorsed for any particular use or release, and was expressly disclaimed in this way.

It is important to emphasise that the financial model was provided, not the forecasts and valuation which Shanghai Maling and its advisers then generated (based on their own assumptions) and published in the information circulated to Shanghai Maling’s shareholders.

Unlike the Board approved budget for 2015/16 which was included with the Notice of Meeting and provided to Grant Samuel for the purposes of its independent report, the financial model provided management workings for the purpose of assisting a bidder to develop its own models and forecasts in assessing its potential investment in Silver Fern Farms.

As stated by the Financial Markets Authority,<sup>19</sup> the two sets of information provided by each of Shanghai Maling and the Co-operative to their respective shareholders were based on fundamentally different assumptions, were prepared for fundamentally different purposes and related to fundamentally different circumstances.

The information provided by the Co-operative to its shareholders describes the situation where the Shanghai Maling transaction does not go ahead, in which case the financial position of the Co-operative was uncertain.

The information provided by Shanghai Maling to its shareholders assumed the opposite, that the transaction does go ahead, in which case the resulting benefits of the cash investment of approximately \$261 million would be able to be realised.

<sup>16.</sup> The NZ Farmers Weekly, Neal Wallace “Misinformation claim rejected” 6 June 2016.

<sup>17.</sup> TV3, Story, 2 June 2016.

<sup>18.</sup> Page 27 of Appendix Three of the previous Notice of Meeting.

<sup>19.</sup> The NZ Farmers Weekly, Neal Wallace “Misinformation claim rejected” 6 June 2016.



- *“Third, shareholders’ approval for the October Vote was induced based on various representations including the effective threat that the Company would be put into receivership if the Proposed Transaction was not passed, even though this does not appear to have been justified, based on the 2015 actual financial results. Others have described this as an ultimatum.*

*But viewed in its historical context, SFF then, and likely now, appears to be relatively healthy, bankable and able to refinance, if required, without the need to sell a 50% controlling interest.”*

**The Board’s Response:**

Refer earlier in this Section Five for the Board’s response to this allegation.

The Board refutes this allegation. There was no certainty of ongoing lender support if shareholders had voted down the proposed investment by Shanghai Maling, and those same lenders had in writing stated that the syndicate would not refinance the Co-operative without a material capital transaction.

Further information regarding Silver Fern Farms’ actual, unaudited, half year financial performance for this financial year is included in Section Two. Shareholders are also encouraged to read the letter from Grant Samuel in Section Four.

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- *“Fourth, the notice to shareholders dated 28 September 2015 (the 2015 Notice), which would have been very carefully drafted, failed to state unequivocally that the Proposed Transaction was in the best interests of the Company, bringing into question whether this was actually the case.”*

**The Board’s Response:**

This is incorrect.

The previous Notice of Meeting included the following statements:

*“Your Board has thoroughly considered the alternatives to address the capital structure of the business, including raising equity from existing shareholders, and is unanimously of the view that Shanghai Maling’s proposal is the best option for Silver Fern Farms. It represents an unrivalled game changing opportunity for the Co-operative.”*

*“The Board unanimously agrees that the proposed partnership with Shanghai Maling is compelling. The partnership will provide the Co-operative and the Co-operative’s shareholders and suppliers with the opportunity to secure a viable and sustainable future.*

*The Board unanimously recommends Shanghai Maling’s partnership proposal to you and urges you to vote in favour...”*

By way of these (and other) statements, shareholders could not have been in any doubt that the Board considered the Shanghai Maling transaction to be in the best interests of the Co-operative and its shareholders.

That has been the Board’s consistent view at all relevant times preceding and at the October 2015 Special Meeting. In the period since October 2015, the Board has only become more convinced of the merits of the transaction.

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- *“Fifth, no risk assessment has been presented to shareholders of the Proposed Transaction or Shanghai Maling. This is despite possible risks including future, potential capital calls by SFF JV being passed onto farmer shareholders, loss of the benefits of the Company’s current markets being diversified, dependency on increased sales into China, as well as food safety issues from there possibly damaging the Company’s brand.”*

**The Board’s Response:**

This statement is incorrect.

The Board engaged independent expert Grant Samuel to prepare an independent report which accompanied the previous Notice of Meeting and in which Grant Samuel specifically assessed *“the benefits, disadvantages and risks”*<sup>20</sup> of the Shanghai Maling transaction. In its independent report Grant Samuel concluded that in its opinion the terms and conditions of the Shanghai Maling transaction were fair and reasonable to shareholders. Shareholders are also encouraged to read the updated view of Grant Samuel set out in Section Four.

Further, the Board considers that any perceived risks are either addressed by the governance arrangements that have been agreed between the Co-operative and Shanghai Maling<sup>21</sup> or are existing risks of the business that are not materially impacted by the Shanghai Maling transaction. To reiterate what was made clear in the previous Notice of Meeting, there is no commitment to sell product to China and there is no commitment to sell product to Shanghai Maling or any of its related parties under this transaction.

- *“On these bases, the ordinary resolution vote held on 16 October 2015 did not and could not properly authorise the Proposed Transaction.*

*Taking all the above factors into account, we believe that it is extremely difficult to see how the Proposed Transaction has been pursued either in shareholders’ best interests, or in accord with traditional co-operative values.*

*Given these strong concerns surrounding the Proposed Transaction, this special meeting has been requisitioned to consider and vote on the Special Resolution so that the Proposed Transaction might be properly approved, or not if shareholders see fit to reject it.”*

**The Board’s Response:**

The Board is firmly of the view that the Shanghai Maling transaction was approved by shareholders in compliance with all relevant laws, regulations and the Co-operative’s constitution.

20. Page 9 of Appendix 3 of the previous Notice of Meeting.

21. Pages 22-25 and 47-50 of the previous Notice of Meeting.



- *“If the Special Resolution is not passed, then it would be difficult from legal and other perspectives for the Company’s Board to claim proper authority to continue to pursue the Proposed Transaction and it should not proceed.”*

**The Board’s Response:**

The Board is firmly of the view that it already has full authority to complete the Shanghai Maling transaction.

All of the conditions to the transaction have been satisfied, other than OIO approval. Once OIO approval is obtained, the Board intends to complete the transaction as the Board considers the Co-operative is contractually bound to do.

It is the Board’s view that the Co-operative will be exposed to significant legal liability if, being bound to do so, it fails to complete the Shanghai Maling transaction.

The Board is obligated to call this Special Meeting under the Companies Act, but is unanimous in stating that this Special Meeting is of no benefit to the Co-operative or its shareholders, cannot be binding on us, and cannot undo the previous approval and the binding contracts we have.

- *“Should that happen, shareholders would retain our current 100% interest in the Company’s ownership, future profits and dividends when the Company has budgeted a record net profit of \$46m for this year, and for year-end net debt to fall to just \$89m or less at 30 September 2016.”*

**The Board’s Response:**

The Co-operative expects its results for the financial year ending 30 September 2016 to be materially below those for 2015 and those budgeted. The Co-operative’s net profit before tax is expected to be approximately breakeven and year end net debt is expected to remain at a very similar level to that at the end of the 2015 financial year.

The Board considers that it is important for shareholders to continue to be aware that until the Co-operative’s capital structure is addressed, it will not be in a position to deliver sustainable returns to our shareholders. Further information regarding the status of Silver Fern Farms’ bank facilities as a result of this year’s disappointing trading is set out earlier in this Section Five.

Shareholders are also encouraged to read Sections Two and Four.

- *“Following what we believe could be viewed as an improperly induced approval of the ordinary resolution, the Company’s banks (the Banks) renewed their facilities for the current season. The previous, effective threat of receivership now no longer stands and the Company should likely have ample time to refinance its debt and replace any Banks that might want to exit its current syndicate.”*

**The Board’s Response:**

Refer earlier in this Section Five for the Board’s response to this allegation.

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- *“Retaining full ownership would also provide flexibility to sell a smaller stake at a better valuation, resulting in shareholders surrendering less equity than by having to sell a 50% controlling interest under the effective threat of receivership.”*

**The Board’s Response:**

The Board has thoroughly considered the alternatives to address the Co-operative’s capital structure. The Board continues to believe that the partnership with Shanghai Maling remains the best option for the Co-operative.

The Board notes that the capital raising process was a thorough one, run by a global investment bank, was widely publicised and one that took over eight months to reach a final offer capable of acceptance.

No party (New Zealand or offshore) made a final offer of a smaller stake, or at a better valuation, despite the opportunity to do so.

Messrs Shrimpton and Gallagher have provided no evidence to support their “better valuation” assertion.

- *“Further, the recently announced opening of the Chinese market to chilled meat products from New Zealand provides the real “game-changer”. This could substantially increase margins in that market and eliminate any need to sell a controlling 50% interest in our Company to Shanghai Maling.”*

**The Board’s Response:**

The Co-operative considers that the opening of China for New Zealand chilled meat products does provide a good medium term opportunity for the New Zealand red meat industry and our business. However, this will take time to come into effect (there are no protocols agreed between the two countries) and to become material (given the supply chain constraints that exist in China).

A number of New Zealand export meat processing plants (including some of ours) do not yet even have approval to export frozen meat and offals to China, some 10 years after red meat exports to China began in earnest.

As noted by special trade envoy Mike Petersen:

*“I just get a feeling this is going to take a lot longer...what has to happen before there is meat on the water is there has to be all the processes that the Ministry for Primary Industries and their counterpart in China will have to go through, agreeing the protocols and making sure that we get plant inspections and that we have plants registered for chilled product into China.”<sup>22</sup>*

The Board believes that the partnership with Shanghai Maling will mean that Silver Fern Farms’ business will be best placed to take advantage of this opportunity as and when it arises. Shanghai Maling has an extensive wholesale and retail network. Shanghai Maling has one of the few existing chilled distribution chains (currently used for its pork products).

Following completion, the Co-operative and Shanghai Maling want to develop the “Silver Fern Farms” brand into the premium red meat brand in China. The Co-operative considers that the ability to sell chilled product into the China market only increases the value of the opportunity that is offered by the Shanghai Maling transaction.

22. Farmers Weekly, Nigel Sterling “China chilled meat trade not close” (<https://farmersweekly.co.nz/topic/markets-and-data/exports/china-chilled-meat-trade-not-close>).



- *“Given SFF’s position and the favourable outlook expressed by management in November 2015, it is difficult to see how shareholders’ best interests are likely to be better served other than by voting down the Proposed Transaction and retaining 100% ownership of our Company.”*

**The Board’s Response:**

Refer earlier in this Section Five for the Board’s response to this allegation.

Shareholders are also encouraged to read Sections One, Two and Four.

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- *“The Special Resolution vote represents the last opportunity that shareholders have of retaining the Company in its current co-operative state and ownership. A vote for the Special Resolution will lead to an irreversible change, including loss of control of our co-operative.”*

**The Board’s Response:**

It is the Board’s firm view that the assertion that the outcome of Special Resolution proposed by Messrs Shrimpton and Gallagher will influence the outcome of the transaction has no foundation.

The transaction has been approved in accordance with all relevant laws, regulations and the Co-operative’s constitution.

The Board will not consider the Co-operative bound by the result of the resolution proposed by the Requisitioners whether it is passed or not.

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- *“If you share any of the concerns expressed here about the Proposed Transaction, or have any doubts that it is not in our best interests as shareholders, or if you simply believe that more benefits and flexibility are retained with our Company continuing to operate as a co-operative, then we strongly recommend that you vote against the Special Resolution.”*

**The Board’s Response:**

**YOUR BOARD UNANIMOUSLY SUPPORTS THE SHANGHAI MALING TRANSACTION.**

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## CONCLUDING COMMENTS

The Statement includes a wide range of other allegations, which the Board does not accept and is not going to respond to. The Board believes that the commentary in this Section Five more than adequately addresses, and rejects, the allegations made in the Statement.

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# APPENDIX

## FULL STATEMENT BY MESSRS SHRIMPTON AND GALLAGHER

Shareholders should note that this Statement is well beyond the 1,000 word limit the Co-operative is required to publish under the Companies Act. The Board agreed to publish the full Statement on the understanding it was authorised by all of the Requisitioners. It transpired that this could not be established – however, despite this, the Board has honoured its agreement to allow this Statement to be published in its full form.

The names of a further 31 shareholders that support the Statement provided by Messrs Shrimpton and Gallagher are included at the end of the Statement.

## STATEMENT IN OPPOSITION TO THE SPECIAL RESOLUTION

The special resolution (the **Special Resolution**) has been requisitioned by some 80 Silver Fern Farms Limited (**SFF**, or the **Company**) shareholders (the **Requisitionists**). Mr John Shrimpton of Lake Coleridge in Canterbury and Mr Blair Gallagher of Surrey Hills in Canterbury have provided the following statement in opposition to the Special Resolution:

This Statement sets out in detail:

- the reasons why the Requisition has been raised to call the special meeting to consider and vote on the Special Resolution;
- the strong concerns about the proposal under which SFF's *entire* business would be transferred into a joint venture (the **SFF JV**) in which Shanghai Maling would hold a controlling 50% interest, and the Company would effectively become an investment entity rather than a co-operative company in substance (the **Proposed Transaction**); and
- despite having put forward the resolution, why you are urged as fellow shareholders to **vote AGAINST the Special Resolution**. To be completely clear, we are recommending that shareholders should NOT vote in favour of the Special Resolution that has been proposed.

We ask that you please carefully read the summary below, as well the detail that follows, as this presents a very different perspective from that put before shareholders by the Company to date.

### Summary

- The Special Resolution was requisitioned by more than 5% of shareholders because of concerns each of those had about the Proposed Transaction and how it has been pursued by the Company and its advisors. It has been expressed that numerous aspects of this do not appear to sit well with the traditional co-operative values, including that of transparency.
- An attempt to raise these concerns before with the Company was unsuccessful.
- Many of the Requisitionists actually voted in favour of the ordinary resolution put to shareholders about the Proposed Transaction on 16 October 2015 (the **October Vote**).
- But subsequent developments and analysis have convinced those shareholders that requisitioned the Special Resolution that the Proposed Transaction was not properly approved then, and how it has been pursued by the Company overall has led those that requisitioned the Special Resolution to conclude that **it is not in shareholders' best interests and should not be approved now.**
- The first of those concerns arises because the Companies Act and SFF's own Constitution strongly protect shareholders' interests by preventing the Company from entering into a major transaction without the approval of a special resolution, which has not been sought until now.
- The Companies Act and our Constitution define a major transaction as including disposal of more than half the Company's assets. The Proposed Transaction itself would require the transfer of 100% of SFF's existing business into the SFF JV, clearly qualifying it as a major transaction.
- The Company expects to spend some \$7m of shareholders' funds, including on a complex and opaque restructuring which has involved the formation of 5 or more, new subsidiaries *after* the Proposed Transaction was announced to shareholders (the **Restructuring**). We believe that this Restructuring seemingly served no clear purpose other than, it would appear, to avoid the *substance* of the sale of SFF's *entire* business being considered as a major transaction.
- In addition, we consider that **the Proposed Transaction would also result in the Company effectively becoming an investment entity rather than a co-operative company in substance. Such a change also requires shareholders' approval by way of a special resolution** which has also not been the case so far.
- In other words, we believe that **the Company has seemingly deployed extensive legal advice (at shareholders' expense) not, it would appear, to protect or act in shareholders' best interests (as it claims), but seemingly to go around those very shareholders' rights which are otherwise protected under the major transaction and change in the essential nature of business provisions.**
- Furthermore, even though the Company has tried to claim regularly that it has complied with "*all relevant laws, regulations and the Company's constitution*", by seemingly having attempted to avoid the proper method of approving the Proposed Transaction, the Company appears to have either ignored, or acted contrary to its own best practice corporate governance standards. These are also aimed ultimately at protecting shareholders' interests.
- Second, key information presented to shareholders about the Company's financial performance and position was so materially different from the actual 2015 financial results announced just 24 days after the October Vote as to call its legitimacy further into question.
- The statement issued on 24 May 2016 by the Financial Markets Authority (the **FMA**) in this regard referred only to very select aspects and failed to address why shareholders were not provided with more accurate information before the October Vote was held.



- Also the circular Shanghai Maling issued to its own shareholders contained more material provided by SFF's management than seems to have been shared with SFF's own shareholders, including forecast net operating profits after tax for 2017 of \$60m and \$73m for 2018.
- This seemingly led to significantly different valuations, part of which appears to be attributable to activities and performances forecast for those periods not detailed for SFF's shareholders.
- Third, shareholders' approval for the October Vote was induced based on various representations including the effective threat that the Company would be put into receivership if the Proposed Transaction was not passed, even though this does not appear to have been justified, based on the 2015 actual financial results. Others have described this as an ultimatum.
- But viewed in its historical context, SFF then, and likely now, appears to be relatively healthy, bankable and able to refinance, if required, without the need to sell a 50% controlling interest.
- Fourth, the notice to shareholders dated 28 September 2015 (the **2015 Notice**), which would have been very carefully drafted, failed to state unequivocally that the Proposed Transaction was in the best interests of the Company, bringing into question whether this was actually the case.
- Fifth, no risk assessment has been presented to shareholders of the Proposed Transaction or Shanghai Maling. This is despite possible risks including future, potential capital calls by SFF JV being passed onto farmer shareholders, loss of the benefits of the Company's current markets being diversified, dependency on increased sales into China, as well as food safety issues from there possibly damaging the Company's brand.
- On these bases, the ordinary resolution vote held on 16 October 2015 did not and could not properly authorise the Proposed Transaction.
- Taking all the above factors into account, we believe that it is extremely difficult to see how the Proposed Transaction has been pursued either in shareholders' best interests, or in accord with traditional co-operative values.
- Given these strong concerns surrounding the Proposed Transaction, this special meeting has been requisitioned to consider and vote on the Special Resolution so that the Proposed Transaction might be properly approved, or not if shareholders see fit to reject it.
- **If the Special Resolution is *not passed*, then it would be difficult from legal and other perspectives for the Company's Board to claim proper authority to continue to pursue the Proposed Transaction and it should not proceed.**
- Should that happen, shareholders would retain our current 100% interest in the Company's ownership, future profits and dividends when the Company has budgeted a record net profit of \$46m for this year, and for year-end net debt to fall to just \$89m or less at 30 September 2016.
- Following what we believe could be viewed as an improperly induced approval of the ordinary resolution, the Company's banks (the **Banks**) renewed their facilities for the current season. The previous, effective threat of receivership now no longer stands and the Company should likely have ample time to refinance its debt and replace any Banks that might want to exit its current syndicate.
- Retaining full ownership would also provide flexibility to sell a smaller stake at a better valuation, resulting in shareholders surrendering less equity than by having to sell a 50% controlling interest under the effective threat of receivership.
- Further, the recently announced opening of the Chinese market to chilled meat products from New Zealand provides the real "*game-changer*". This could substantially increase margins in that market and eliminate any need to sell a controlling 50% interest in our Company to Shanghai Maling.
- Given SFF's position and the favourable outlook expressed by management in November 2015, it is difficult to see how shareholders' best interests are likely to be better served other than by voting down the Proposed Transaction and retaining 100% ownership of our Company.
- The Special Resolution vote represents the last opportunity that shareholders have of retaining the Company in its current co-operative state and ownership. A vote for the Special Resolution will lead to an irreversible change, including loss of control of our co-operative.
- If you share any of the concerns expressed here about the Proposed Transaction, or have any doubts that it is **not** in our best interests as shareholders, or if you simply believe that more benefits and flexibility are retained with our Company continuing to operate as a co-operative, then **we strongly recommend that you vote AGAINST the Special Resolution.**

## Why The Special Meeting Has Been Requisitioned

The Requisitionists are a group of SFF shareholders representing more than 5% of the Company's shares who became sufficiently concerned at the nature of the Proposed Transaction and how it has been pursued by the Company to have requisitioned the Special Resolution.

The Requisitionists comprise small through to large shareholders in the Company from around the country, with a considerable number having been supplier shareholders dedicated to the Company for decades. The Requisitionists include a former chairman of the Company, a former vice-chairman, former farmer directors and a former member of the Securities Commission, as well as others with significant commercial, investment and Asian experience.

Many of the Requisitionists actually voted in favour of the Proposed Transaction in October 2015. But subsequent developments and analysis were sufficient to convince those that requisitioned the Special Resolution that the Proposed Transaction has not been properly approved to date and that the manner in which it has been pursued by the Company strongly suggests that **it is not in shareholders' best interests**.

To be completely clear, as far as we are aware, all the Requisitionists care deeply about our Company. We believe in its strategy (at least until the Proposed Transaction was announced), and we believe that the Company has a bright future under its current ownership, not least for the flexibility that would be retained, which is discussed below.

Equally, we do not believe that the Company was a candidate for receivership as was represented before the October Vote, and we certainly do not believe there is any need to sell the Company's entire business into a joint venture in which control would be lost, nor that it would be in the best interests of shareholders to do so.

We believe that whether to proceed with the Proposed Transaction or not will likely be the most significant decision in the Company's long history. As such, it is critical that shareholders make the right decision for our long term futures as shareholders and suppliers, as well as for those that will come after us.

Further, the Requisition has certainly not been raised with any intention of "disrupting" the business of the Company. Neither has it been raised on the basis of trying to "split hairs" on process. On the contrary, the seriousness of a number of the Requisitionists is evidenced by the hundreds of hours of effort that have already been dedicated to arrive at the current position. The Special Resolution has been put forward because we, and many of the Requisitionists, genuinely have very serious concerns about how the Proposed Transaction has been put to shareholders and its potentially detrimental impact on us.

In sum, we strongly believe that the Proposed Transaction has not been properly approved to date, and that it would not be in shareholders' best interests to proceed with it now.

Our concerns are set out in detail in the following pages. We would urge you to consider them carefully and to join us to **vote AGAINST the Special Resolution**.

## How This Position Arose

Before moving to those concerns, we believe that it is important for shareholders to reflect on why the supposed need for the Proposed Transaction arose in the first place.

Clearly, SFF's year-end net debt of \$388 million (**m**) as at 30 September 2013 was not sustainable. However, as a result of tremendous efforts not least from the Board, management and employees, the Company achieved a significant reduction in year-end net debt of \$99m in 2014. Greater levels of reduction in year-end net debt had only occurred twice previously since 2000.

In its annual report for that year dated 23 December 2014, the Company informed shareholders that:

*"We are focused on reducing debt under our own steam – through further improvements in working capital... and operating profitably. As previously announced we want to potentially accelerate this reduction through introducing new capital... The Board of Directors has a strong desire to maintain the co-operative status and farmer control...*

*The directors consider the completion of a capital transaction, or transactions, to achieve a more sustainable capital base and materially reduce its bank borrowings is likely, but not certain... Should the group substantially achieve its 2015 budgeted financial performance and budgeted cash flows, or conclude a capital transaction, the directors expect that satisfactory banking facilities will be negotiated to take effect at the expiry of the facilities in October 2015 or earlier." (Emphasis added; pages 6 and 49.)*

The purpose of the *potential* capital-raising exercise then was to enable the Banks to "*materially reduce*" their exposure to the Company further. The objective does not appear to have been to allow the Banks to exit of their risk completely, though. The result for shareholders, though, was to surrender a measure of ownership in the business (and have our equity interest reduced) in order to fund that debt reduction. Effectively, this brought the interests of the Banks into direct opposition with ours as shareholders.

It could be that the Banks may not have considered whether shareholders retained, as examples, an 80%, 50% or even 20% interest in the Company, provided the debt was reduced in accordance with what the Banks required.

Subsequently, something appears to have changed in the stance of the Banks from what shareholders were told in December 2014 when the Company stated the objective to be to “*materially reduce its bank borrowings*”.

When the Proposed Transaction was announced on 15 September 2015, just two weeks before the end of the Company’s financial year, it is likely that a very substantial portion of the total debt reduction for the year may already have been made to the Banks, or was likely visible in some way to them. It was later confirmed that year-end net debt had been reduced by \$168m for the 2015 financial year.

This was the second highest reduction of year-end net debt achieved by the Company since 2000. Again, it is testament to the substantial efforts of the Board, management and employees, as well as support from suppliers, that the year-end net debt had been reduced at that point by a total of \$267m over just two financial years. This was a remarkable achievement.

→ **Had the Company already met or exceeded any debt reduction target set by the Banks in late 2014 by the time the Proposed Transaction was announced, or was likely to do so?**

As the Banks had probably been made aware before the Company’s announcement in mid-September 2015, the scale of investment from the Proposed Transaction opened the prospect for the Banks to go beyond “*material*” debt reduction to exit their exposure to the Company completely.

The prospect of having all their debt repaid may have appealed to those Banks, if any, whose SFF exposure had previously been referred for particular attention internally within such Banks, such as to a work-out committee. Typically, the objective of such bodies is to ensure loan recovery for a bank as fully, swiftly and painlessly (for the bank) as possible, as this can impact their profitability.

The possible shift in stance by the Banks to being able to completely exit their risk is a potentially important context to understand why the 2015 Notice provided to shareholders two weeks later on 28 September 2015 appears to have contained an effective threat that the Banks’ funding may not be renewed, and that the Company would potentially be put into receivership if the Proposed Transaction was not approved. As more than one commentator has put it subsequently, in effect, an ultimatum had been delivered to shareholders.

Shareholders should also be reminded that the main intention of the capital-raising was *not* to identify a definitive partner for the Chinese market. With the Company’s focus on capital-raising, any such collateral “benefits” claimed subsequently for the Proposed Transaction would effectively be by-products of the method by which the Banks would reduce their exposure, or exit it completely.

In short, it appears to us that the paramount interests that were to be served best by the Proposed Transaction were those of the Banks, and in our view those impacted most detrimentally were those of shareholders.

The key difference in this stakeholder equation is that the Banks appear to have been able to enforce their interests through an effective threat being laid out of them not renewing the Company’s banking facilities for this season and, potentially, of putting SFF into receivership or liquidation if the Proposed Transaction was not approved by shareholders.

→ **Given the scale of debt reduction already in hand or visible, was the threat of not renewing banking facilities actually justified when it was made in late September 2015?**

## **The Special Resolution**

As referred to elsewhere in this Notice, the special meeting has been requisitioned to consider and vote on the following Special Resolution:

**“Resolution:** as a Special Resolution:

*That the shareholders of Silver Fern Farms Limited (the **Company**) hereby approve the proposed partnership of the Company with Shanghai Maling and the restructure described in the Notice of Meeting and Shareholder Information Pack dated 28 September 2015 by way of this special resolution of shareholders.”*

It is our clear view that the Proposed Transaction requires proper approval and that this appears not have been the case to date. The reasons for this view are detailed below.

Accordingly, the special meeting has been requisitioned to consider and vote on the above Special Resolution so that the Proposed Transaction might be properly approved, or not.

**If the Special Resolution is *not passed*, then it would be difficult from legal and other perspectives for the Company’s Board to claim proper authority to continue to pursue the Proposed Transaction and it should not proceed.**

**Should that happen, shareholders would retain our current 100% interest in the Company's ownership, future profits and dividends at a time when the Company has budgeted a record net profit of \$46m for this year, and for year-end net debt to fall to just \$89m at 30 September 2016.**

This should also allow for an orderly refinancing of the Company's reduced debt and to replace any Bank or Banks that might want to exit the current banking syndicate.

And as the Company's CEO stated on 9 November 2015 in the 2015 results announcement:

*"We achieved our goal of a material and sustainable improvement in profitability... More importantly, we see significant scope for continued improvement across all three species."*

Viewed in its historical context, SFF then, and likely now, appears to be relatively healthy, bankable and able to refinance, if required, without the need to sell a 50% controlling interest. Achieving its budget could even enable a dividend to be paid before the end of 2016 and for shareholders to receive larger dividends in future than if a 50% non-controlling interest were retained under the Proposed Transaction.

Accordingly, given SFF's position and its own favourable outlook, it is difficult to see how shareholders' best interests are likely to be better served other than by retaining 100% ownership and by preserving an important range of options for the future.

If you share any of the concerns expressed here about the Proposed Transaction, or have any doubts that it is **not** in our best interests as shareholders, or if you simply believe that more benefits and flexibility are retained with our Company continuing to operate as a co-operative, then **we strongly recommend that you vote AGAINST the Special Resolution.**

The balance of this Statement sets out the detailed reasons for seeking your support for this course of action.

## **The Independent Report on the Proposed Transaction**

The Board engaged Grant Samuel & Associates Limited (**Grant Samuel**) to prepare an independent report in relation to the Proposed Transaction (the **GS Report**). The GS Report formed an important part of the 2015 Notice and a copy dated 23 September 2015 was appended to the 2015 Notice.

The GS Report contained important qualifications as how it should be considered by shareholders. This Statement offers no opinion as to the process followed by Grant Samuel, nor the opinions expressed by them. This Statement had sought to include a small number of quotations from the GS Report, but unfortunately, Grant Samuel declined a polite and reasonable request to do so.

## **1. The Proposed Transaction Requires Approval by Special Resolution**

### **1.1. More subsidiaries than species**

SFF's news release dated 1 May 2016 stated that:

*"The only substantive step remaining [in the Company's restructuring] once conditions are satisfied is Shanghai Maling's investment in new shares to be issued by the Company's subsidiary."*

The phrase "*the Company's subsidiary*" is misleading, though, as it suggests there is only one subsidiary. In fact, numerous SFF subsidiaries existed as of 1 May 2016, of which five alone were registered *after* the Proposed Transaction was announced on 15 September 2015. (Curiously, the 2015 Notice referred (at page 44) only to four subsidiaries being required.)

As such, it is not clear if "*the Company's subsidiary*" means Silver Fern Farms Beef Limited, or Silver Fern Farms Sheepmeat Limited, or even Silver Fern Farms Venison Limited. It could also mean Silver Fern Farms Joint Ventures Limited, or Silver Fern Farms Holdings Limited. Or it could even be Silver Fern Farms Management Limited.

It could also possibly mean Silver Fern Farms Management Trustee Limited, although that, for some reason yet to be explained to shareholders, is owned by the Company's CEO and finance director, not the Company itself.

- **Why have so many new subsidiaries been formed beyond those that are species-specific?**
- **What specific role does Silver Fern Farms Management Trustee Limited have in the Proposed Transaction, especially given that it is not owned by the Company?**
- **Why is the Company's chairman the sole director of a number of these subsidiaries?**

So with this expansion of subsidiaries, the shuffling of their ownership as part of the Restructuring, and even suppliers' kill-sheets now no longer issued by Silver Fern Farms Limited, it is not even clear what the Company means when it refers to "the Company", let alone what "the Company's subsidiary" might be.

- **Why did the Proposed Transaction need to rely on such complex Restructuring?**
- **Precisely what role have all those other subsidiaries played in the Restructuring?**
- **And why has the Company not sought to explain this fully to shareholders before?**

As with so much to do with the Proposed Transaction, SFF's shareholders have been kept in the dark.

## 1.2. Proper process for a Major Transaction has not been followed

Whether to proceed with the Proposed Transaction or not is likely to be the most important decision that shareholders will take in the Company's history. Shareholders sell control of the Company only once, and it is our clear view that we should not have been put in this position.

As such, it is critical that shareholders be informed fully, treated fairly and afforded absolute transparency, as co-operative values would require. But it is difficult to see how this has been the case to date.

What is completely clear, though, is the Companies Act. In section 129, it states:

*"A company must not enter into a major transaction unless the transaction is... approved by special resolution". It defines a major transaction as including, "the disposition of, or an agreement to dispose of... assets of the company the value of which is more than half the value of the company's assets before the disposition".*

On any objective view, the substance of the Restructuring intended to facilitate the Proposed Transaction appeared (from the limited information provided to shareholders to date) to constitute a major transaction under the Companies Act.

According to the GS Report, Shanghai Maling valued 100% of the equity of what were referred to in the GS Report as the existing three operating businesses (the meaning of which was not made clear) at \$311.4m (page 6).

That detail effectively confirmed that the major transaction value criterion was met. Equally clearly, SFF's Constitution states that:

*"Major Transaction" has the meaning set out in Section 129(2) of the [Companies] Act [and under clause 17 of the Constitution] ... The Company must not enter into a major transaction unless the transaction is... approved by a Special Resolution of Shareholders."*

For SFF shareholders to pass a special resolution, clause 9.3 of the Constitution states as follows:

*"Shareholder Resolutions: To be passed, a resolution of Shareholders... must be approved by: ...(b) in the case of a Special Resolution: (i) 75 percent of the votes of all Shares carrying voting rights and voting on that resolution..."*

Despite this, and without detailed justification, the Company has maintained that the ordinary resolution put before shareholders at the October Vote could approve the Proposed Transaction and that:

*"The investment by Shanghai Maling was approved by Silver Fern Farms Limited's shareholders in compliance with all relevant laws, regulations and the Company's constitution."*

But the Company's contention is simply not supported by the plain language of the Companies Act or the Constitution.

Both of those clearly point to the conclusion that the Proposed Transaction could only be properly approved if a special resolution is passed and that has not been the case to date. The Special Resolution has been requisitioned so that shareholders might consider and properly approve the Proposed Transaction, or not if we now chose that.

The Company has also consistently stated that it has had "extensive external professional advice" on how the Proposed Transaction has been pursued, although that is somewhat self-evident from the \$7m of shareholders' funds that the Company said it expects to spend on the Proposed Transaction in total.

Shareholders should consider here an unrelated counter-argument: presumably banks that have paid tens of billions of dollars in fines and settlements to regulators globally in recent years would have each similarly received extensive legal advice in support of the very activities that were later found by regulators to have been illegal, or to have infringed regulations.

Notwithstanding the presence of legal opinions to the Company, those opinions might simply be wrong. In any event, it is likely that those opinions would have acknowledged that the Proposed Transaction could be challenged, as is now the case, on the basis that it constituted a Major Transaction, or that the Company would effectively become an investment entity rather than a co-operative company in substance.

### 1.3. The Restructuring

Clearly, the biggest obstacle to selling the Company's entire business was the need under the Companies Act and the Constitution for it to be approved by a special resolution.

But with five or more subsidiaries formed even after it was announced, the Proposed Transaction appears to have been structured as an opaque, complex and incompletely described set of steps in which SFF's entire business was broken up into subsidiaries, with their ownership then being transferred between what the 2015 Notice states as "*Head Office Subsidiary*", "*General JV Subsidiary*" and "*Non-Trading Holdco*", as examples (page 44). Notably, the purpose and role of those subsidiaries was and has not been made clear to shareholders.

As such, the Restructuring goes beyond any preparation previously required for the possible sale of one or more species-specific parts of the Company. This appears to have been of more relevance to the situation in 2014, rather than after the Proposed Transaction was announced to shareholders. Any counter-argument from the Company then with reference to a species-subsidiary sale should be discounted readily.

We believe that the critical point which has yet to be addressed by the Company is that the complexity of the Restructuring has seemingly served no clear purpose other than, it would appear, to avoid the sale of SFF's entire business being considered as a Major Transaction.

The Company may attempt to argue that the Major Transaction provisions apply only to a company, not a group of companies into which SFF's entire business has been broken up. It may also argue that the threshold for a Major Transaction was not reached.

But any such argument should be viewed as a clever evasion, likely put up to attempt to justify how the Company's business could be dispersed into smaller units and then arranged for sale in such a way as to seemingly avoid the requirement for proper approval to be sought from shareholders by way of a special resolution.

As the Company's Board, Banks and advisors would have been aware, though, both the Companies Act and the Constitution are intended to provide strong tests to protect *shareholders* against a significant change of our Company's asset base, or a change in the essential nature of its business, without a special resolution approving either such change.

- **Why have the key provisions intended for shareholders' protection and benefit apparently been circumvented?**
- **If shareholders lost the benefit of those protections, then who gained from their apparent circumvention?**
- **Why has the Board failed to take fully into account shareholders' interests as protected under the Constitution?**

**The critical point, we believe, is that the Company appears to have seemingly deployed its extensive legal advice (at shareholders' expense) not to protect or act in shareholders' best interests (as it claims), but seemingly to go around those very shareholders' rights which were otherwise protected by the Major Transaction and change in the essential nature of business provisions.**

As such it is extremely difficult to understand how the Company can claim its actions to be in shareholders' best interests when the opposite seems more likely.

Indeed, shareholders should weigh very carefully any statement from the Company that this entire exercise or the Proposed Transaction has been in "*the best interests of shareholders*" in light of this.

- **How have shareholders' best interests been served by the Company *not* regarding the Proposed Transaction as a Major Transaction, or a change in the essential nature of its business?**
- **How much of the \$7m has been spent by the Company in apparently circumventing such shareholders' protections?**

A further, related disadvantage of the Restructuring is that it also allowed SFF to avoid other Companies Act provisions protecting minority shareholders. These include a requirement that a company must buy the shares of any shareholders who have unsuccessfully opposed a Major Transaction at a "*fair and reasonable*" price.

To the best of our knowledge, none of the Requisitionists have expressed interest in having their shares bought back by the Company.

But if correctly treated as a Major Transaction, a potential buy-out liability would then have competed for some of the monies due to be raised from the Proposed Transaction. This may have been a concern for those of the Banks focussed on full repayment of their debt and a complete exit of their risk. This is actually an extremely serious point for shareholders to consider.

#### **1.4. Conversion of the co-operative into an investment company**

As indicated above, a further concern with the Proposed Transaction is that the Company would effectively become an investment company and so would no longer be a co-operative in substance. The conversion from an in-substance co-operative to an investment company would also require approval by way of a special resolution because we believe that would constitute a fundamental change in the essential nature of the business, quite apart from being a Major Transaction. Again, the ordinary resolution passed in the October Vote would not have been sufficient to approve this aspect of the Proposed Transaction.

#### **1.5. Announcement of the October Vote**

When the Company announced the result of the October Vote on the ordinary resolution, it stated that shareholders “*strongly support*” the Proposed Transaction and that “*a strong majority (82.22%) of votes had been cast in favour of [it]*”.

However, this appeared to be ambiguous or misleading as 82% referred only to the percentage of votes in support out of the total of votes cast, **not the total of shares eligible to vote**.

Although the Company has not made clear what the total number of shares eligible to vote was then, it appears to have been some 100.1m.

So with 55.2m shares voted in favour, only 55%, or a bare majority of total shares eligible to vote, were in favour of the ordinary resolution under which the Company claims the Proposed Transaction could be authorised.

The law requires the procedure for a special resolution to be followed and this will only be the case with the Special Resolution that shareholders are now being asked to consider and vote on.

#### **1.6. Supposed Board approval**

Shareholders have also been told consistently by the Company that the Proposed Transaction could simply have been approved by a Board resolution. But if there really was confidence in such a far-fetched proposition as a Major Transaction or the change in the essential nature of the co-operative being approved on the sole authority of the Board, then it is difficult to understand why the Company even sought shareholders’ approval by way of an ordinary resolution in the first place.

To answer a minor point, whilst the Company has criticised the Requisition as “*not an effective use of the Company’s management and financial resources*”, it did not apply this itself when calling for the October Vote, if the Proposed Transaction could have actually been approved by the Board, as it has claimed was possible.

More to the point, a great deal of shareholders’ own time and money could have been saved if approval by way of a special resolution vote had simply been sought in the first place. Specifically, less shareholders’ funds than the estimated \$7m would have been spent if the raft of new subsidiaries had not been required.

#### **1.7. Corporate governance best practice**

Even though the Company has tried to claim that it has complied with “*all relevant laws, regulations and the Company’s constitution*”, by seemingly having attempted to avoid what we consider is the proper method of approving the Proposed Transaction, the Company appears to have either ignored, or acted in breach of, its own best practice corporate governance standards.

In the Company’s 2015 annual report published after the October Vote, SFF re-stated for shareholders’ benefit that:

*“Silver Fern Farms’ governance policies are reviewed to ensure they are consistent with best practice”* (page 22).

But applying corporate governance best practice would, in our view, require the Company to have sought approval for the Proposed Transaction using the highest test, not the lowest or most expedient. That now means properly approving the Proposed Transaction, or not, by passing the Special Resolution, not trying to suggest that an ordinary resolution, or even Board approval, would suffice.

By even putting forward such suggestions, the Company has rendered its own corporate governance best practice as meaningless.

As with the protections afforded by the Major Transaction and change in the essential nature of business provisions, shareholders should be reminded that corporate governance best practice is intended for our benefit and protection of our interests.

If the Company seriously intends to adhere to best practice, then it must either do so, or abandon reference to its use altogether. Merely decorating corporate communications to shareholders with empty statements serves no purpose, in our opinion, other than to mislead shareholders.

- **If the Company applies corporate governance best practice, then why did it not provide a special resolution vote in the first place?**

## 1.8. Further governance implications

The first page of the 2015 Notice emphasised “*shared governance principles*” between the Company and Shanghai Maling.

Aside from the obvious concerns this should raise for shareholders in light of the sections above, it is notable that Shanghai Maling’s own shareholders apparently approved the Proposed Transaction with a special resolution vote of their own, although this was denied to SFF shareholders until the Requisition was raised. This is indicated in the 2015 Notice (at page 32) which stated that:

*“The partnership proposal is a material transaction for Shanghai Maling which requires the approval of a two thirds majority of the shareholders of Shanghai Maling able to vote and voting on the transaction.”*

- **What message would the Company send to Shanghai Maling about its “*governance principles*” if the Major Transaction and change in the essential nature of business provisions have been circumvented and the Proposed Transaction had not been properly approved with a special resolution passed?**

Lastly on governance, the 2015 Notice also stated that the SFF JV “*shall operate to standards of governance conventional for leading companies listed on the New Zealand NZX Main Board*”.

But the NZX Listing Rules (the **Listing Rules**) expressly forbid precisely the use of a series of linked or related transactions that the Restructuring itself appears to rely upon, without proper approval by a special resolution (as would apply with the Company).

In its section on “*Transaction with Related Parties and Major Transactions*” and its rule on “*Disposal or Acquisition of Assets*”, rule 9.1.1 of those Listing Rules states:

*“An ... Issuer shall not ... enter into any transaction or series of linked or related transactions to acquire... or... dispose of ... assets of the Issuer...”*

*(a) which would change the essential nature of the business of the Issuer; or*

*(b) in respect of which the gross value is in excess of 50% of the [value] of the Issuer;*

*except with the prior approval of ... a special resolution if that Issuer must obtain approval of the transaction or transactions by a special resolution under section 129 of the Companies Act 1993.” (Emphasis added.)*

In other words, if the Listing Rules were applied to SFF today, which should be the case through the application of corporate governance best practice, then because the Proposed Transaction relies on the Restructuring, in our opinion it could only be properly approved by the Special Resolution being passed.

Shares of SFF are not listed on the New Zealand NZX Main Board, though, and the Company is not subject to its Listing Rules. But the Company has stated expressly that the SFF JV, if formed, would later adhere to standards that would effectively forbid the use of the Restructuring. Moreover, the Company does seek to apply corporate governance best practice which would mean adopting the Listing Rules in any event.

It therefore seems hypocritical, to say the least, to undertake the Restructuring in order to get the entire business out of the shareholders’ hands in the first place, before then renouncing precisely that behaviour in future. Of course, it would then be too late to benefit shareholders as the Restructuring would already have been completed. The irony is unlikely to have been lost on those who drafted the 2015 Notice.

- **Why did the Board simply not seek to have the Proposed Transaction approved by a special resolution in the first place?**
- **Was pressure applied to the Board by the Company’s Banks to avoid seeking proper approval by way of a special resolution?**



## 2. Materially Different Financial Information

### 2.1 Forecasts compared to actual results

Key information presented to shareholders in the GS Report was so materially different from the Company's actual financial performance and position announced on 9 November 2015, just 24 days *after* the October Vote, as to call the legitimacy of the October Vote further into question.

Specifically, the GS Report referred to *the Company's own forecast* of a net profit after tax which was barely half the actual result achieved just one week after the date of the GS Report, which was 23 September 2015.

Also, *the Company's own forecast* of its year-end net debt was almost a fifth higher than the reality, whilst that for net cashflow from operations was nearly 40% lower than the *record* level actually achieved, as shown in the following table:

NZ\$ million Year end 30 September 2015	GS Report	Actual	Difference	
	2015F	2015A	Amount	%
Net debt	(148.0)	(120.9)	27.1	-18%
Net profit after tax	13.4	24.9	11.5	86%
Net cash flows from operations	111.1	152.3	41.2	37%

The statement issued on 24 May 2016 by the FMA focussed narrowly on aspects of the Company's year-end net debt, but notably failed to address why there was a material difference in the Company's net profits. The Company's own media release the next day stated that *"its position on these matters has been vindicated"*, but no clear explanation on the material difference in net profits has been offered, and fundamental questions such as the following have been left unanswered.

- **How could a company with the resources and sophistication of SFF not have known - or at least had a better understanding – of its results before the October Vote?**
- **If it did have a better understanding of its results than the forecasts provided in the 2015 Notice, then why did it not inform shareholders before the October Vote?**

### 2.2 Significance of the 2015 Notice date

As a further detail, it is also significant that the 2015 Notice was dated 28 September 2015, just two days before the Company's financial year-end.

By not issuing the 2015 Notice even on, for example, 1 October 2015 (which would not likely have been achievable in practice), it appears that the Company avoided a requirement to include its audited financial information to 30 September 2015, and so was able to rely instead on its own forecasts, which were later shown to be materially different from reality after the October Vote.

The Company may claim that, having announced the Proposed Transaction on 15 September 2015, it then sought to provide shareholders with information as soon as possible after.

But even this would not explain why the Company appears to have failed to properly inform its shareholders of its true financial performance and position **both before and even when it held the October Vote** to the extent that they were known to the Company.

### 2.3 Continuous disclosure regime

Even though the Company is not currently subject to the Listing Rules, its application of corporate governance best practice would mean that it should have applied a continuous disclosure regime and so should have disclosed any information as to its updated financial performance and position when known, including ahead of the October Vote, if that were the case.

Further, the FMA statement of 24 May 2016 failed to address that if the Company applied best practice then this should have offered protections such as continuous disclosure. The FMA statement did point out that shares traded on the Unlisted market lacked certain protections, but that is not relevant if the Company actually supported corporate governance best practice as its own statements have sought to imply.

## 2.4 More detailed information provided to Shanghai Maling than to SFF's shareholders

On 24 October 2015, Shanghai Maling issued a 548-page circular to its own shareholders and the Shanghai Stock Exchange on the Proposed Transaction (the **Circular**). From a translation, it seems the Circular benefitted from far more material provided by the Company's management than appears to have been shared with SFF's own shareholders. This seems very unusual. The Circular itself can be downloaded using the following URL:  
[http://www.sse.com.cn/disclosure/listedinfo/announcement/c/2015-10-24/600073\\_20151024\\_1.pdf](http://www.sse.com.cn/disclosure/listedinfo/announcement/c/2015-10-24/600073_20151024_1.pdf).

Key parts of the translation can be downloaded from the website <http://www.sffresolution.com>.

The 2015 Notice and GS Report only included the Company's forecast for 2015 and budget for 2016, but the Circular included the "forecast model for fiscal years the 2017 and 2018 provided by SFF management". That forecast the Company's net operating profit after tax for 2017 as \$60m and \$73m for 2018, which would be record levels of profitability.

Those forecasts also appear contrary to claims the Company was an effective candidate for receivership. The following table is a translation of the full table provided in the Circular (at pdf page 482); all units are NZ\$ millions.

SFF	FY15A (9 months)	FY15F (3 months)	FY16B	FY17F	FY18F	Future Value
EBITDA of group	102.9	-25.6	95.9	108.3	131	131
Minus: Depreciation		7.1	25	25	25	25
EBIT of group		-32.7	71	83.3	106	106
Minus: Income tax			19.9	23.3	29.7	29.7
Net operating profit after tax		-32.7	51.1	60	76.3	76.3
Plus: Depreciation		7.1	25	25	25	25
Minus: Capital expenditures		5.1	15	15	15	25
Minus: Capital expenditures (optimized by South Island Factory)				11.1		
Plus: Capital sales (optimized by South Island Factory)				22.7		
Enterprise free cash flow		-30.7	61.1	58.9	109	76.3
Sustainable growth rate						2%
Weighted avg. cost of capital	10.30%					
Future value						973
Enterprise free cash flow		-30	54.2	47.5	80	714
Net present value	865.8					
EBITDA after FY15 is normalized and adjusted	84.14					

An SFF spokesman stated on 3 June 2016 that:

*"the financial data was provided to Shanghai Maling last July as part of due diligence to show the impact of various scenarios and the board stated in writing that "these were not company forecasts for those years".*

Further, the GS Report (on its page 27) expressly stated that SFF's management only forecast one year out. It also cited reasons why SFF's management recognised the challenges of creating a reliable forecast due to the industry factors beyond its control (e.g. market prices, climate, exchange rates and stock volumes).

In our view, none of those factors seem exceptional or to provide an impossible obstacle preventing SFF from providing some form of forecast for the Company's shareholders, as it did for 2016.

Equally, it is difficult to understand how the subsidiaries of the global accounting firms PriceWaterhouseCoopers and KPMG, which advised Shanghai Maling, were able to construct forecasts to their standards, but the Company and Grant Samuel were not.

## 2.5 The Shanghai Maling and Grant Samuel valuations differed greatly

SFF's lack of forecasts to its own shareholders for 2017 and 2018 appears to have had a significant effect on valuation. Grant Samuel stated it was not able to provide a discounted cash flow analysis as that relies on a detailed forecast of future earnings and cash flows and, as there were no such long-term forecasts from SFF, they said this was not possible.

Grant Samuel's valuation of SFF relied instead on the capitalisation of earnings methodology. As a result, they estimated SFF's full underlying equity value as being in the range of \$283.2m to \$330.7m.

Shanghai Maling valued SFF as at 30 June 2015 using the discounted cash flow method and forecast earnings to 30 September 2018; (see pdf page 480 of the Circular). As a result, it calculated SFF's equity value as being \$595.8m, or some 80% higher than the upper valuation provided to SFF's shareholders by Grant Samuel.

The FMA addressed this subject which they explained as referring to two "different scenarios". The FMA is quoted in the *Farmers' Weekly* as having stated:

*"Maling's information was provided on the basis that the transaction would go ahead, that its capital would be used to pay debt and that the financial position would improve accordingly."*

But both Grant Samuel and Shanghai Maling calculated SFF's net debt for their valuations at some \$278m, with a 3% variance, bringing into question whether a different basis was being used or not.

The translation of the Circular also offered further insight into what drove its valuation:

*"Operational optimization plan proposed by management as shown... drives growth of gross profit and EBITDA mainly in fiscal years 2017 and 2018. Fiscal year 2018 EBITDA especially indicates improvement of NZD 18 million. Performance in fiscal year 2018 is the basis for the calculation of future value in the following DCF [discounted cashflow] model, which has a great influence on the valuation. Materialization of the operational management optimization plan plays an important role in growing enterprise value."*

The Circular then proceeds to detail aspects of plant closures and its financial effects:

*"The South Island plant optimization plan is to close down the Fairton and Waitane plants. Savings from closure of these two plants will produce cash flow of NZD 23 million and lead to growth in EBITDA by NZD 12.40 million in 2018."*

In short, it appears that a large part of the variation between the Shanghai Maling and Grant Samuel valuations could be attributed to activities and performance forecast for 2017 and 2018, although these aspects were not set out for SFF's shareholders.

### **3. The Effective Threat of Receivership Was Not Justified**

#### **3.1 Strong financial performance and position**

As well as materially different information, shareholders' approval of the ordinary resolution was also induced based upon various other representations, including in the 2015 Notice, to the effect that the Company would potentially be put into receivership if the Proposed Transaction was not approved.

Statements were also made that *"the Company is one bad season away from disaster"*.

However, **the Company's actual 2015 year-end financial position and other options apparently available to it, appeared not to support, or no longer supported at the time of the October Vote, any such representations.**

Far from evidencing SFF as a candidate for receivership, **the 2015 actual results showed:**

1. **Total liabilities** were at the **second lowest level since 2002**;
2. **Year-end net debt** was **reduced by \$168m** and had been lower in only **5 out of the previous 15 years**;
3. **Year-end total equity and net assets** were each the **second highest they've ever been**;
4. **The year-end equity ratio** was the **second highest since before 2000**; and
5. The Company also ended the year with **the lowest inventory level seen since before 2000**.

The quality of these results and the Company's financial position were, in our view, inconsistent with the effective threat of receivership put to shareholders.

Despite its obvious successes, the Company's announcement on 9 November 2015 of its 2015 audited results described them, with some understatement, as merely *"positive"*.

This suggested something of a struggle to reconcile the effective threats of receivership made before the October Vote with the strong results actually generated which were only revealed after the October Vote was taken.

#### **3.2 Inconsistent approach**

Further, the severity of the approach apparently taken by SFF's banking syndicate was disproportionate when viewed alongside that adopted towards Alliance Group Limited (**Alliance**), despite two Banks being in both banking syndicates, (each having four banks in total).

Given the considerable focus on the Company's alleged financial position and its debt in particular as the basis for the supposed need for capital-raising, and despite the difference in size of the two co-operatives, notably SFF's 2015 year-end net debt was actually *lower* than Alliance's in absolute terms whilst its equity ratio was *higher*, as shown in the following table:

2015 Financial Metric	SFF	Alliance	Difference SFF / Alliance
Net debt as at 2015 financial year-end (\$m)	(120.9)	(137.8)	-12%
Equity ratio as at 2015 financial year-end	59.4%	57.6%	3%
Revenue (\$m)	2,524.9	1,498.8	68%
Net profit after tax (\$m)	24.9	4.6	438%

But notwithstanding Alliance's inferior financial metrics, its own bank funding was apparently renewed for the 2016 season without particular issue, whereas SFF was seemingly required to hold the October Vote intended to lead to repayment of the Banks' debt under an effective threat of receivership.

Furthermore, Alliance's auditors, KPMG, appeared sufficiently comfortable for Alliance's 2015 annual report to have stated that "*the company's balance sheet remains robust with an equity ratio of 57.6%*". (Emphasis added.)

If a Big Four firm like KPMG seemed comfortable with the view that such an equity ratio was "*robust*", it is questionable as to why SFF, with lower debt and a superior equity ratio, was put under an effective threat of receivership.

- **Why did the Company's Banks treat SFF so differently from Alliance?**
- **Was the effective threat of receivership justified when it was made from 28 September 2015 onwards?**

#### 4. Other Funding Options Available to SFF

It is also notable that two, domestic initiatives, which could each have negated the need for a sale of a controlling 50% interest, appear not to have been pursued in favour of the Proposed Transaction.

The first of these was an equity capital-raising initiative which is understood to have received underwritten commitments of some \$75 million to \$90 million. Second, it is understood that a bank not in the current SFF banking syndicate may also have engaged the Company in discussions as to possible refinancing.

Each initiative would appear to have been credible, but appeared to have been terminated before it was brought to fruition, and ahead of the Proposed Transaction being announced. It is possible, however, that neither alternative may have reduced the Company's debt as much as under the Proposed Transaction.

- **Did the Company's Banks constrain SFF from pursuing other alternatives that may not have led to the sale of the entire business?**
- **Did the Company's Banks prefer SFF to focus on what could repay all their loans as opposed to just part of them?**

#### 5. Current Ownership Retained

##### 5.1 Retaining 100% ownership would be in the best interests of shareholders

If the Special Resolution is not approved, then the Proposed Transaction should not proceed and shareholders would retain our current 100% interest in the Company's ownership, future profits and dividends, rather than having to sell a 50% controlling interest under the Proposed Transaction.

The GS Report referred to the possibility of the Company continuing independently without investment from Shanghai Maling. Indeed, Grant Samuel expressed an opinion that the Company had improved its operating performance and capital structure under the new management such that it would not require additional capital by the end of the financial year ending 30 September 2016, provided the Company achieves its budget (GS Report, page 39).

If shareholders do not approve the Special Resolution and instead retain a 100% interest in SFF, it is notable that **the Company itself has budgeted to make a net profit after tax of \$46m for this year** (GS Report, page 19).

As well as being almost double the \$25m profit achieved for 2015, this budgeted net profit would actually be a record high level, although the GS Report did not highlight that aspect for shareholders.

In addition, the GS Report stated that the Company has budgeted to finish with year-end net debt of \$89m as at 30 September 2016 (page 18). SFF's year-end net debt has only been lower than that just once in the past 15 years, although, again, the GS Report failed to bring this to shareholders' attention.

Further, if this budgeted figure is adjusted to take into account the additional \$27m debt reduction achieved in the 2015 actual results, then net debt could fall to \$62m as at 30 September 2016.

Achieving the budgeted net profit could allow SFF to pay a dividend to ordinary shareholders, or provide greater flexibility as to investment, or both. Indeed, some encouragement as to the Company's capacity to re-invest can be taken from the \$5m investment announced on 9 May 2016 into the Pareora plant, following the planned closure of its Islington site.

To provide some further context, if SFF were able to adopt a dividend pay-out ratio of 65% in relation to this year's budgeted net profit of \$46m, a dividend of 30c per ordinary share would be payable, equivalent to the special dividend possible under the Proposed Transaction.

But the Company may claim that it is no longer in a position where it can meet its previously budgeted net profit of \$46m. Indeed, the Company commented on 13 April 2016 that:

*"based on our performance in the first half of the year, we expect the full year result to be materially below 2015."*

Forecasting is challenging, as was exemplified by the Company's apparent difficulties in producing an accurate forecast of its results just days before its 2015 financial year end. Shareholders should consider the Company's April statement in that light.

The case for remaining under current ownership was further underpinned when the Company announced its 2015 results on 9 November 2015. At that time, the CEO commented that:

*"We achieved our goal of a material and sustainable improvement in profitability... More importantly, we see significant scope for continued improvement across all three species."*

If further *"significant scope for continued improvement"* is possible, then shareholders should carefully consider whether to forego half of the future benefits of what the Company has indicated it might achieve, following years of shareholders' support and forbearance.

Given SFF's position overall and the favourable outlook expressed by management, it is difficult to see how shareholders' best interests are likely to be better served other than by retaining 100% ownership.

## **5.2 The contract with Shanghai Maling is voidable**

As an important side issue here, the Company has claimed that it has a *"binding contract"* with Shanghai Maling in respect of the Proposed Transaction.

But if for any of the range of reasons detailed in this Statement that *"contract"* is deemed to have been entered into, either without proper authority (as we contend, as it has not been approved by way of a special resolution as a Major Transaction or a change in the essential nature of its business), or has been improperly induced (as we contend, by materially different information having been provided to shareholders, or by an effective threat of receivership that we consider was not justified in reality), it would be voidable or void and of no effect.

Furthermore, the claims to have a *"binding contract"* need to be viewed in light of the clarification from the Company's chairman on 6 May 2016 in an article produced by *Farmers Weekly* in which he was quoted as having stated:

*"If the remaining conditions are satisfied and the company does not proceed to complete its side of the bargain, the company will be in breach of contract."* (Emphasis added.)

In other words, the supposed *"contract"* will not even have effect unless *"the remaining conditions are satisfied"*, which is also by no means certain at this time.

## **5.3 Renewed Bank funding allows for a more considered decision**

A key element that further underscores remaining under its present ownership is that the Company's banking facilities are actually in place for the current season.

The previous, effective threat of receivership now no longer stands. The ultimatum, as it was described by others, has dissipated. Indeed, the positions can be considered as somewhat reversed. Following what could be viewed as an improperly induced approval of the ordinary resolution, the Banks renewed their facilities for the current season.

But as a result of the Requisition, shareholders now have the opportunity to consider the Proposed Transaction properly, and without any immediate concern as to the Company being put into receivership.

And if shareholders do decline to approve the Proposed Transaction by voting down the Special Resolution, as is recommended, the Company should likely have ample time to organise an orderly refinancing of its reduced debt and to replace any Banks that might want to exit its current syndicate, if required.

The 2015 Notice states that the Company's current banking facilities are subject to a number of events of review (GS Report at page 33). The Company may claim that the jeopardy of receivership may again be encountered. But that suggestion could be discounted, not least on the basis of all the circumstances in which it was previously deployed.

Also, if the Special Resolution is not approved by shareholders, any Bank that might seek to put the Company into receivership after the forthcoming vote would potentially run a considerable reputational risk if there were no solid, financial grounds to justify that course in reality.

Such a potential outcome would also likely be closely scrutinised, given the questions that arose over the effective threat of receivership that was faced by the Company in October 2015, in contrast with its actual financial position and performance, as was subsequently revealed.

Furthermore, if shareholders can put any credence in the Company's budget for its profitability and year-end net debt for 2016, the basis for potential receivership would be reduced even further. Also, the Company's equity ratio should be on track in the current year to exceed the record high level of 61.5% achieved in 2010.

Finally, the exposure of banks to the red meat sector, including other banks not in the Company's current banking syndicate, would likely incentivise them to assist any refinancing that might be required, rather than risk instability to their own customers and loans that would flow from a protracted process of receivership involving the country's largest meat processor.

In the longer term, should shareholders have concerns as to the Company's debt susceptibility, these could be addressed at the next AGM in some way by shareholders considering and passing an ordinary resolution that the Company cap its year-end net debt, or set a minimum equity ratio, as examples.

#### **5.4 Capital-raising flexibility would be retained**

A further aspect of shareholders deciding to retain full ownership of the Company would be for considerable flexibility for a smaller capital-raising, or setting in a place a more considered approach to the Chinese market, if either were required.

For example, if SFF shareholders really consider that some form of co-operation with Shanghai Maling, or even a similar entity, is still desirable, then the Company would be free to pursue the possible sale of a small stake, or entering into some exclusivity agreement, in order to cement that relationship, whilst still retaining control and full ownership.

The Company may claim that Shanghai Maling might no longer be interested to engage with it if the Proposed Transaction does not proceed, and that might well be the case.

But inevitably there is a second largest meat processor or distributor in China, and a third largest and so on, so this would hardly seem to limit the scope for augmenting the Company's product distribution in the world's largest country, if that is a strategic imperative.

Indeed, rejection of the Proposed Transaction and a more measured approach to limited capital-raising might generate even greater interest from companies keen to replace Shanghai Maling, and offering better terms as a result.

Conversely, as highlighted by the GS Report above, the Company may not need to raise any additional capital at all.

But if an opportunity to raise some capital were sufficiently compelling, then selling a small equity interest on the basis of the budgeted, record net profits for the current year, would likely achieve a more advantageous valuation, which would result in less reduction of shareholders' equity, than selling a 50% controlling interest under the effective threat of receivership, as has been required under the Proposed Transaction.

Shareholders should also be aware that the Banks having their debt repaid and exiting their risk would likely have been far more important to them than whether shareholders were left with a 50% or even 20% equity interest in the resulting business. Arguably, this may not even have been considered in detail by SFF's Banks at all.

## 5.5 The real game-changer

A further, new factor from late April 2016 is that China has apparently agreed to provide access for chilled meat products from New Zealand into its domestic market. This will inevitably take time to be effective. But according to the coverage of this development by *Farmers Weekly* on 25 April 2016, an AgriHQ analyst was quoted as having said that returns for chilled product were 60% higher than for frozen product.

According to the 2015 Notice, SFF exported over \$300m of product to China in 2015. Applying the higher margin indicated above to those SFF exports to China would indicate very substantial gains could be possible for the Company over time. Perhaps taking a conservative view, it suggests annual sales could increase by \$50m or more in due course.

If the Company could make such sales itself, this might even exceed the returns anticipated from the Proposed Transaction in the Chinese market, which would further undermine its attraction.

In the article cited above, the Alliance chairman greeted this news with the comment that *"We'll look back at this in 10 years' time and say that this was a really major breakthrough."* Others have tended to agree. Notably less sanguine, however, was a SFF spokesman who was quoted in the same article as having said: *"it sounded positive"*.

This is undoubtedly a key development that, when operable, will likely reduce or even eliminates the need for ties to one dedicated distributor. Shareholders should consider whether this eliminates many of the benefits described by the Company from selling a 50% controlling stake in the meantime.

Shareholders should also consider here that the Proposed Transaction did not result from a painstaking search by the Company targeted specifically at identifying the definitive partner to assist distribution of the Company's products in China.

Instead, it appears to have been settled upon more because Shanghai Maling was prepared to invest a sum that met the objective, likely set by the Banks, of raising sufficient capital in order to completely repay their debt.

Actually, there appears to have been no dedicated search for a *"game-changing"* strategy for the Chinese or any other market, despite the Company's advocacy of that supposed benefit.

If that were indeed a goal, then shareholders would likely benefit more from the Company launching a specific brief to that end, including detailed analysis assessing the impact of the opening of the Chinese market to chilled products.

Shareholders' interests overall would be best served by treating the raising of capital and improving penetration of the Chinese market as the two very different goals that they are.

## 6. The Best Interests of the Company

Documents such as the 2015 Notice are typically required to state expressly to shareholders that what is proposed *"is in the best interests"* of a company, not least as it is a duty of directors to act in such interests. This might appear as a small detail, but is nevertheless very important.

It was unusual then that where SFF set out its summary of the Proposed Transaction on page 2 of the 2015 Notice, it stated instead that:

*"Your Board... is unanimously of the view that Shanghai Maling's proposal is the best option for Silver Fern Farms."* (Emphasis added.)

The GS Report included a similar statement. At page 40, Grant Samuel expressed the view that the Proposed Transaction was considered the best option available to the Company's directors at the time of its report.

The use of these phrases is concerning for two reasons. First, these statements seem intended to look like what would normally be expected, but, equally important, they actually fell short of the usual requirement.

As the 2015 Notice was the key document for shareholders to consider in a process apparently costing \$7m, it is certain that these phrases would have been subject to considerable legal scrutiny and very careful review. As such, the wording used is unlikely to have been accidental. Accordingly, the motivation for the use of such phrases in the 2015 Notice is somewhat questionable.

However, the 2015 Notice did state that the Proposed Transaction is *"in the best interests of the [C]ompany and its shareholders"*. But its sole appearance is unusually sited where the Company provided its response to the requisitioned, second resolution considered at the October 2015 special meeting, not where the Company is putting its own case forward. This does not appear normal.

Taken together, these short statements appear to have failed to deliver the usual, express clarity that, without qualification, the Proposed Transaction is in the best interests of the Company. Understandably, this leaves open the question as to whether that was unequivocally the case or not.

- **Why didn't the 2015 Notice plainly state at outset that the Proposed Transaction was in the best interests of the Company?**
- **Without such clear statement, then was it the case that the Proposed Transaction was indeed in the best interests of the Company, or not?**

Subsequently, in its news release dated 1 May 2016, the Company did indeed state that:

*"The Board ... reiterates its support for the Shanghai Maling transaction as being in the best interests of the Company and its shareholders".*

But if the Board was as clear on this point before, then it is puzzling why it did not simply state that at outset in the 2015 Notice, without resorting to lesser phrases that left open the possibility that the Proposed Transaction was *not* actually in the best interests of the Company.

Overall, the statement in the 1 May 2016 news release leaves an impression of the Company belatedly scrambling to address its somewhat questionable, previous position. This should only serve to compound shareholders' reasonable concerns.

## **7. Assessing the Beneficiaries of the Proposed Transaction**

The Company's Banks would have been significant beneficiaries of the Proposed Transaction as it was envisaged that, according to the GS Report, the Company's debt would be reduced by over \$200m (GS Report, page 6).

But notwithstanding clarity on sums intended to cover the transaction and even details such as future governance costs, **the 2015 Notice did not specify what sum, or even a range of amounts, would actually be left from the possible \$261m cash investment to develop the business in future**, (which would then be owned by SFF JV), **after repayment of the Banks**.

The 2015 Notice, however, was clear that the Proposed Transaction would raise excess capital, as is evidenced by the \$50m proposed to be returned to shareholders by redeeming the supplier investment shares and paying the special dividend. The 2015 Notice stated on page 19 that:

*"The Board ... considered that if the business were to receive the full \$311 million in cash the resulting capital structure would have been inefficient."*

In other words, the Proposed Transaction would actually have raised too much capital, even after repaying the Banks. The corollary of this is that **shareholders would have surrendered too much equity**.

So with surplus capital being generated, it is open to question as to whether it should have been necessary to pursue the sale of such a large interest in the business under the Proposed Transaction, or if it would have been more appropriate for a smaller stake to be sold.

- **Why did the Company not sell a lower stake and retain control of its business as a co-operative company, rather than allow surplus capital to be raised and control to be lost?**

The sale of a suitably, smaller interest in the Company would also have avoided the issue of the Major Transaction and change in the essential nature of business provisions being encountered and may even have resulted in a less expensive exercise as a result.

The probability, however, is that Shanghai Maling demanded that a controlling interest be sold and the Board felt unable to resist that.

For Shanghai Maling, gaining a controlling 50% interest in the SFF JV would have been significant as achieving this threshold would have enabled it to equity account the SFF JV's results in its own accounts in a way that a smaller shareholding level would not allow. Equity accounting this interest would have been an important benefit which would have enabled Shanghai Maling's own net profits to increase in line with the performance of the SFF JV.

It was also anticipated that if the Proposed Transaction had proceeded, then **Shanghai Maling would have benefited from SFF's performance from 1 October 2015. Coincidentally, this is the start of the period for which the Company is budgeting to make a record net profit.**



At the December 2015 annual general meeting, it was also stated that the SFF JV *not the Company* would benefit from a transfer of accumulated tax credits that have previously accrued solely for the benefit of the Company. The effect of this on the Company does not appear to have been made clear to shareholders to date, but it does not appear likely to operate in the best interests of shareholders.

Taken as a whole, it could be argued that the interests of *shareholders* appear to have been under-weighted relative to other stakeholders when the Proposed Transaction was negotiated.

In short, it could be said that if the Banks' interests came first in the Proposed Transaction, those of Shanghai Maling came second, and those of SFF shareholders, last.

## 8. No Risk Assessment of the Proposed Transaction

One of the most striking features of the 2015 Notice is the complete absence of any assessment of potential risks flowing from either the prospective "*partnership*" with Shanghai Maling, or of the Proposed Transaction itself. Such risk assessments are standard and have featured in previous SFF documents of a similar nature to the Notice.

It is almost impossible that no risk assessment was performed on Shanghai Maling and the Proposed Transaction as part of the Company's due diligence.

But just why any issues flowing from such risk assessment were not summarised for shareholders gives rise to considerable concern, either as to what may have been discovered, or on the basis that it has not been revealed to shareholders for their consideration.

Shareholders should again be reminded that considerable resources were expended on preparing the Notice and that it would have been drafted and reviewed extremely carefully, including as to what would have been appropriate for disclosure to shareholders.

Given the importance to shareholders of making the right decision on the Proposed Transaction, for the Company to just put forward the supposedly, "*game-changing*" benefits without any discussion whatsoever of potential risks, is truly worrying.

Games, of course, do indeed have a habit of changing, often in unexpected ways, and sometimes for the worse. The same can also be said for any business and it is important for shareholders to have been made fully aware of the risks that could flow from approving the Proposed Transaction and the prospective "*partnership*" with Shanghai Maling.

One key area of risk flows from the fact that the 2015 Notice failed to address the scenario where the SFF JV may start from a position of limited working capital, but debt free, as has been indicated would be the case. This opens the possibility that Shanghai Maling may decide later that the SFF JV needs additional capital, as it would fully be entitled to do through its control of the business plan.

Shanghai Maling could reasonably be assumed to be in a better position than the Company to meet any capital calls in the SFF JV. In that case, farmer shareholders would face the prospect of either having such a capital call passed onto ourselves (as SFF would have retained no significant capital), or seeing the Company's interest in SFF JV be reduced, perhaps even severely.

Farmer shareholders could well run this risk for as long as the SFF JV operates. Indeed, this long term, capital call risk to shareholders may even be greater from the Proposed Transaction than from any requirement of the Banks, if the Company remained in its current ownership.

In the absence of any risk assessment of the Proposed Transaction by the Company, the following, further observations are offered for consideration by shareholders:

- i. The proposed "*partnership*" brings together parties with effectively opposite interests: Shanghai Maling, as a distributor of product, would rationally be interested in purchasing such product at the lowest possible price, whilst supplier shareholders would remain interested in receiving the highest value for our output. It is difficult to see how this might be reconciled in favour of shareholders with control already having been lost.
- ii. The risk would also exist of control being exercised such that a substantial flow of products is directed into the Chinese market and away from long-standing customers elsewhere, with the effect that those customers are lost and a dependency on sales to Shanghai Maling is created, or that a beneficial level of sales risk diversification is lost anyway.
- iii. Any further additions to the unfortunate litany of incidents of food contamination that has been a particular feature of the Chinese market might affect the Company's products in such a way as to pose a risk to its future sales into China.
- iv. Should any such risk crystallise, this might well be compounded by the Company's brand suffering collateral damage, perhaps in other international markets.

- v. In any event, it is not clear what effect control by Shanghai Maling would have on SFF's brand and other customers, either internationally or in the domestic market here, especially if other food safety issues did arise in China, even if they were unrelated to the Company's products.
- vi. Although various, positive attributes of Bright Food Group, the main investor in Shanghai Maling, were advanced, shareholders' attention was not drawn to the significant development approximately one month before the Proposed Transaction was announced to shareholders that the chairman of Bright Food Group was jailed for 18 years for embezzlement and bribery.
- vii. Relationships are generally paramount in any commercial undertaking in Asia. But the Company seems to have embarked on negotiating the Proposed Transaction with Shanghai Maling after comparatively little contact, or time spent with, or in-depth knowledge of Shanghai Maling or its principals. In short, the essential foundation of this prospective relationship appears flimsy to say the least.
- viii. The Board apparently has one director only with any experience of doing business in Asia, which brings into question just what level of effective oversight might be achieved, including at the managerial level.

## Conclusion and Recommendation

The Special Resolution vote represents the last opportunity that shareholders have of retaining the Company in its current co-operative state and ownership. A vote for the Special Resolution will lead to an irreversible change, including loss of control of our Company as a co-operative in substance.

If you share any of the concerns expressed here about the Proposed Transaction, or have any doubts that it is **not** in our best interests as shareholders, or if you simply believe that more benefits and flexibility are retained with our Company continuing to operate as a co-operative, then **we strongly recommend that you vote AGAINST the Special Resolution**. To confirm, we are recommending that shareholders do NOT vote in favour of the Special Resolution we have proposed.

Finally, should you have any questions or require any further information, please do not hesitate to contact us on 020 411 44 585 and [sffresolution@gmail.com](mailto:sffresolution@gmail.com), or visit <http://www.sffresolution.com>.

Thank you for your kind attention.

John Shrimpton and Blair Gallagher

Supported by:

Richard White

JL & JM Whiteside

Brent & Ann-Maree Robinson

Mary Hutton, John Hutton, Tom Couper

David and Douglas Turner

Tim Coop

Hamish and Jodie Johnson

JR & EM Hart

Robert Schikker

Hayden McIntyre

Sally McIntyre

Graham and Kay Kirke

Roger Lundie

David Botting

Lester Appleton

Derrick Millton, Jane Millton, Ben Millton and William Millton

R & S Smith

Josephine Jan Clucas and Craig Norman Clucas

Holmes Byars

Allan Richardson

Neil H Shallard

Lindsay Alderton

James Guild

John Cochrane

WS & LA Murray

Hugh and Kathie Gardyne

Grant and Karen Bradfield

David & Robyn Shaw

David John Andrew

Hugh Benjamin Richards

Richard J Somerville





**NOTICE** *OF MEETING*

**FOR INFORMATION CONTACT:**

The Returning Officer  
Silver Fern Farms Limited  
Silver Fern Farms Shareholder Meeting  
PO Box 3138  
Christchurch 8140

**Tel.** 0508 666 886

**Fax.** 03 377 1474

[www.silverfernfarms.com](http://www.silverfernfarms.com)