

Annual Report 2005-2006



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Annual Report 2005-2006

The Directors are pleased to present the Annual Report of Livestock Improvement Corporation Limited for the year ended 31 May 2006.

For and on behalf of the Directors



STUART BAY / CHAIRMAN / 17 August 2006



MURRAY JAGGER / DIRECTOR / 17 August 2006

MISSION

*Leading the world with genetics
and knowledge to create wealth
for pastoral dairy farmers.*

VISION

*Leadership in pastoral livestock
solutions.*

Core values

- **Integrity**
- **Customer Focus**
- **Innovation**
- **Teamwork**

Strategic objectives

By 2006:

- **Innovation** – increase profit to \$10 million before biotechnology
- **Performance** – return on capital of 10% after tax
- **Customer focus** – achieve Silver Business Excellence Award

Company structure

Operational Divisions

- Genetics
- Information
- International

Support Groups

- Corporate Services
- Innovation/Research and Development
- Sales
- Secretariat
- Strategic Development

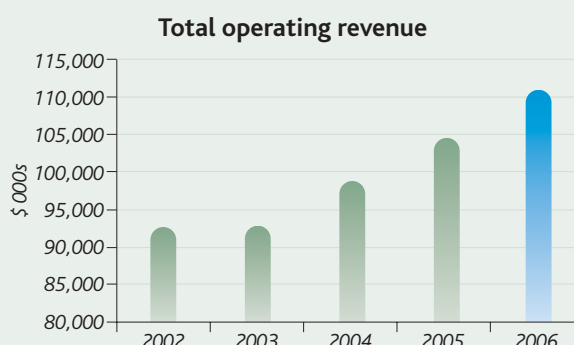
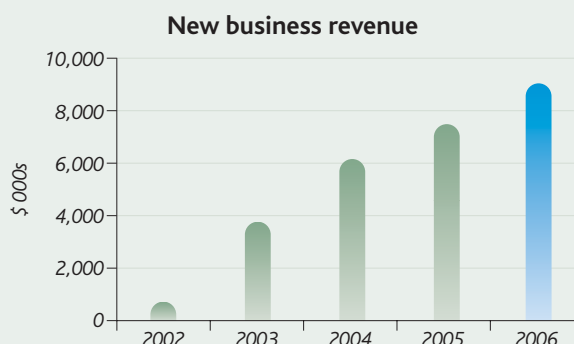
Subsidiaries

- Livestock Improvement (New Zealand) Corporation Limited
 - Livestock Improvement Pty Limited, Australia
 - Livestock Improvement (UK) Limited
- New Zealand Genetics (IRL) Limited
- Animal Breeding Services Limited
- LIC Deer Limited trading as Deer Improvement

Highlights

- Revenue \$110.5 million
- Net profit (after tax but before biotechnology) \$10.9 million, up 25% over previous year
- Total dividend of 24.5 cents per Investment Share, up 23.7% over previous year
- Achieved all three Strategic Plan objectives – Profit, ROCE and Silver Business Excellence Award
- Dividend Reinvestment Plan introduced
- Mark Dewdney appointed CEO on the resignation of Stuart Gordon
- New traceability business – Trace Solutions – launched
- DNA Punch launched
- Establishment of Australian farm automation business with purchase of assets of On-Farm Electronics
- World first – Once-a-Day Progeny Test Scheme established
- Collaborative biotechnology grant
- Record levels of industry sponsorship
- Record levels of inseminations in New Zealand
- KiwiCross™ launched as PREMIER SIREs option
- MINDA preferred herd recording system for more than 90% of New Zealand dairy farmers
- More than 9 million herd test samples analysed
- Limited launch of simplified herd testing system, EZ Link
- Average herd testing turnaround 3 days
- Record International semen sales
- Purchase of balance of New Zealand Genetics (Ireland) Limited
- Gene discovery advances with new research grant from Technology New Zealand
- NZ Test Day Model set to replace animal model for animal evaluation in February 2007
- Record levels of reproductive solutions delivered by Animal Breeding Services
- Growth of 67% in Deer Improvement commercial AI service

Performance



Livestock Improvement is a **dairy farmer owned co-operative** providing a comprehensive range of herd improvement services to the dairy industry. Its subsidiaries deliver breeding solutions for a range of animal species, including bovine, deer, sheep, pigs, goats, both domestically and internationally.



STUART BAY / CHAIRMAN

Chairman's Report

Financial result

Revenue for the 2005/2006 year was \$110.5 million. The net profit (after tax but before biotechnology) was \$10.9 million. The net profit after tax and biotechnology was \$7.6 million, an increase of 43% over the previous year. This contrasts with Livestock Improvement's net profit (after tax and biotechnology) of \$5.3 million in 2004/2005.

Dividend

The total dividend of 24.5 cents per Investment Share represents an increase of 23.7% over the 2004/05 dividend of 19.8 cents per Investment Share.

Shareholders received a final dividend of 15.5 cents per Investment Share at the end of July topping up an interim dividend of 9 cents paid in February.

A dividend of 8.5 cents per Co-operative Control Share was also paid at the end of July.

Dividend Reinvestment Plan

Consultation was held with shareholders regarding the introduction of a Dividend Reinvestment Plan to provide shareholders with options on dividend utilisation – either direct payment in cash or applied to the purchase of more Investment Shares.

The recommendation, to implement the Dividend Reinvestment Plan, was overwhelmingly endorsed at a Special Shareholder Meeting in April 2006. Approvals to implement were also received from the NZ Stock Exchange and the Minister of Agriculture together with the necessary exemptions from the Securities Commission.

A formal invitation to participate was mailed to shareholders in May and, by mid-July, 2,360 shareholders with 7.2 million Investment Shares had elected to participate. Applications can be made anytime but will only commence with the next declared dividend payment.

The Dividend Reinvestment Plan benefits all shareholders because of the increase in share trading liquidity. The Board therefore resolved to cover the administration, brokerage and incidental interest costs of providing the Plan and the new entrant purchasing requirements.

Disclosure of Financial Assistance is set out on page 59 of this report.

Full details of the Dividend Reinvestment Plan are contained on page 61 of this Report.

Shareholding

The Share Register received and processed more than 4,000 calls during the season as farmers variously entered or exited the industry, altered their farming entities or traded shares both on and off the NZ Alternative Stock Exchange. To date nearly 1,000 trades have occurred at an average price of \$1.38 which is slightly above valuations conducted at the time of listing in April 2004.

Governance

At the 2005 Annual Meeting, shareholders approved changes in the Constitution to reduce the size of the Livestock Improvement Board and National Council.

With effect from 1 June 2006, the Livestock Improvement Board comprises seven regionally elected Farmer Directors (formerly nine) and three Independent Directors. The National Council comprises 21 Ward Elected members (formerly 29 and 5 Dairy Company representatives).

Change of Chief Executive

Stuart Gordon, who had been Chief Executive of Livestock Improvement for eight years, retired in February 2006 to devote his energies to personal business interests.

Stuart took the helm of this organisation at a critical time in its evolution, as momentum built for the restructuring of the dairy industry. He successfully oversaw the company's change in focus and culture from industry good to commercial, forging a strong Management Team and a high performance culture focused on innovation and growth.

While an international search was undertaken for his replacement, experienced industry executive, Graeme Milne, was appointed Acting Chief Executive. In due course the Board was delighted to appoint Mark Dewdney, whose career has focused on the New Zealand dairy industry both in New Zealand and internationally. He was a member of Livestock Improvement's Senior Management Team in the late 1990s and, for the last few years, was Regional Managing Director of Fonterra Ingredients Asia, based in Japan.

Mark assumed the role in May 2006 and his skills as a business leader combined with his empathy and understanding of the integrated value chain, from farm to market, has already been instrumental in helping define the company's strategies for the next period of growth.

In summary

The company has undergone significant change in the past few years. We've restructured, listed and the business focus has widened opening significant opportunities for the future. We are now in a position to expand in New Zealand and internationally while retaining a core focus on delivering real products, services and value to our owners, the New Zealand dairy farmer.

My thanks go to the Board, past and present Chief Executives, Senior Management and all staff for the individual and team contributions which have generated such a strong performance.

In particular, appreciation is recorded to long serving directors Ron Jackways and John Bicknell who have made a large contribution to Livestock Improvement. They retired on 31 May having dedicated over 40 years between them to governance at a Regional and National level.



STUART BAY / CHAIRMAN



Premier Sires – then, now and always

"Twenty five years ago we started off milking 120 Jerseys. We used Premier Sires then, and still do now with 330 cows.

"It is so simple to use Premier Sires, convenient, especially with DataMATE which prevents inbreeding.

"The team concept is easy and no hassle. You don't have to worry about selecting bulls for different traits because it's already done. We've always wanted the best bulls to improve the herd and feel Premier Sires had them. The proof of this is that we've now got a bull in the KiwiCross™ Forward Pack team – Legendaire by Hugo. And we've still got Legendaire's grandmother in the herd.

"I'd never change."

WAYNE MUDFORD

- Wayne and Brenda Mudford, Te Waotu, Waikato
- 106 effective hectares
- 330 Crossbred cows
- Herd average 370 kgMS per cow, 1125 kgMS per hectare on grass
- Herd BW 137, highest cow BW 219
- 8% empty rate



MARK DEWDNEY / CHIEF EXECUTIVE

Chief Executive's Report

I am very happy to be back with Livestock Improvement.

When I last worked here (from 1997 to 1999) I thought Livestock Improvement was a good business. The empathy staff had for customers was strong; there was a common vision but, probably due to the industry good drivers which applied at the time, this occasionally erred into 'we know best' what farmers want. I felt that perception blinkered the business from what customers really wanted and the potential value and growth we could add to their business, and ours.

I've been away from Livestock Improvement for seven years during which time deregulation took place launching the company into a commercial environment.

There is now a greater clarity of purpose and connectedness with customers than ever before. This business is responsive to the wide variety and scope of farming businesses today and on a daily basis we are developing innovative tools and services which demonstrably add value on farm.

I am delighted to report to shareholders on a year of strong performance and growth.

Strategic plan

Five years ago Livestock Improvement set targeted objectives to increase profit by \$10 million, to achieve return on capital employed (ROCE) of 10% and achieve a Silver Business Excellence Award.

We have delivered on all three:

- **Profit**

The company's net profit (after tax but before biotechnology) of \$10.9 million is a record.

- **Return on Capital Employed**, before tax and biotechnology, of 11.3%.

- **Silver Business Excellence Award**

In December 2005 the company achieved what no other agricultural company in Australasia has ever done – Silver status under the most rigorous evaluation criteria for business processes in the world, the Baldrige Business Excellence criteria.

Judges' comments are worth repeating; they speak of a company with 'very strong and visible leadership and staff who are passionate about the company' and 'of excellence built into processes and strategy around a core product which is possibly the best in the world'.

Winning Silver is a huge achievement on an international scale, let alone nationally. It confirms our business processes, strategy and customer focus are on a par with the best companies in the world.

New business and innovations

- **Trace Solutions**

In June 2005 the Board approved a business plan to extend animal recording services into the beef, sheep, and deer sectors. In doing so, the Board supported a Management Team assessment that the skills, knowledge and infrastructure in our world-leading dairy animal management systems could be further developed to provide similar services in other animal farming sectors.

A major pan-industry traceability initiative in New Zealand will require mandatory individual animal recording in future. This means many more animals will need to be recorded onto a central database to ensure that animals can be traced throughout their lifetime, and that information on them and their ownership is available to support any future Biosecurity response.

The new business unit, Trace Solutions, has developed a product aimed at fostering animal tracking amongst a sector of the rural community vital to New Zealand's biosecurity – lifestyle farmers. The TRACKA website provides a simple, user-pays interface for farmers to register and tag their animals.

New products, modelled on the highly successful MINDA dairy software system, will be launched in the 2006/2007 year.

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- **DNA Punch**

Collaboratively developed by GeneMark and Zee Tags, the DNA Punch was launched to the market in March 2006 and has generated a high degree of interest from farmers wanting the highly reliable parentage verification which only DNA analysis can provide.

- **Farm Automation**

Farmers, particularly those with larger herds or labour issues, are continuing to appreciate the value that Protrack farm automation units provide to their operations. The company extended its reach in this area with the purchase of the assets of On-Farm Electronics Pty Ltd in Australia, and is providing sales and support to an expanding customer base in that country.

- **EZ Link**

A new system, designed to take the hassle out of herd testing, was launched to a limited group of 200 farmers in the Waikato and Canterbury during the Spring of 2005.

EZ Link combines the existing milk meter system with barcoded flasks and a hand-held electronic device which has a keypad and infra-red scanner.

The system will progressively be an option for farmers from the start of the 2006 dairy season.

- **World first – Once-a-Day (OAD) Progeny Test Scheme**

The company's scientists incorporated the performance data from over 300 Once-a-Day (OAD) herds to develop a new ranking index especially for OAD.

The index will be used to identify elite OAD young sires based on ancestry. The top 40 will be made available on frozen semen for use in commercial OAD herds as well as being progeny tested in the normal manner in Livestock Improvement's Sire Proving Scheme herds.

Collaborative partnerships

The company received a \$1.16 million grant from Technology New Zealand for a two year research project on genomic selection. This project involves various partners in Europe, as well as in the USA and will consolidate Livestock Improvement's expertise at the foremost edge of genomic research for livestock breeding.

Industry sponsorship

Livestock Improvement is proud to support its farmer clients and industry through numerous quality sponsorship programmes. Events such as Sharemilker of the Year, Dairy Excellence Awards and the Ballance Farm Environment Awards help encourage best practice, transfer knowledge, and build future leaders. These are critical factors in ensuring we have a strong vibrant industry that attracts quality staff and succeeds into the future.

We are also involved in sponsoring numerous other programmes such as SIDE, Dairy 3, Large Herds Conference, AGITO, Breed Society Conferences and research programmes designed to add value to farmers and the industry through sharing information, developing new products and bringing people together.

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Strategies for the future

Management and Directors are in the process of preparing a Strategic Plan for the next five year phase of growth. Significant opportunities exist for Livestock Improvement to expand its activities in New Zealand and internationally. High focus will remain on our core business activities, but we will further expand our investments in the areas of full farm productivity improvement systems, farm automation, diagnostics, multi-species reproductive technologies and animal traceability.

Staff appreciation

The 2005/06 results are a direct testament to the expertise and focus of staff throughout the organisation. Our culture is evolving to be much more focused, faster paced and innovative. In the future we will deal with a much larger and more diverse customer base and targets will be stretched further than ever before.

I am confident that we have the team we need at Livestock Improvement to continue to deliver successful results in the future.



MARK DEWDNEY / CHIEF EXECUTIVE

Genetics Division

Genetic gain in dairy cattle adds \$35 million per annum to the net profit of dairy farms by improving the efficiency of conversion of feed into milksolids.

Livestock Improvement's Genetics Division is the engine room for this vital productivity increase, and is responsible for breeding more than three quarters of the national dairy herd.

The genetic improvement process involves scanning millions of animals on the database for outstanding sires and dams to produce the next generation of dairy cows. Sophisticated software developed by our R&D team is used to individualise these pairings to ensure genetic outcomes are optimised. Contract artificial insemination (AI) matings, embryo transfer, and DNA parentage testing are some of the technologies employed to deliver the most promising young bull calves to our Newstead bull farm.

As yearlings, 300 of these young bulls contribute enough semen to generate 80 heifer calves each, spread over 400 Sire Proving Scheme herds nationwide. It is the performance of these offspring in the commercial environment, in comparison with their herd mates, that provides the 'proof' of a sire's genetic merit as measured by a long list of individual traits.

The progeny test process takes several years and costs \$30,000 for each of the 300 bulls tested, and this \$9 million annual investment results in the identification of the truly elite PREMIER SIREs. Only about 15 bulls are retained for the PREMIER SIREs team with the rest (approximately 95% of the total) sent to slaughter. This means that each proven sire costs approximately half a million dollars, but clearly its value far exceeds this figure.

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The highly concentrated spring mating season places enormous demands on our ability to deliver more than 3 million inseminations via a daily service to 10,000 locations all over the country. What makes this possible is a combination of exclusive semen technology, highly specialised software to predict daily demand on individual properties, and a team of 1,000 artificial breeding (AB) Technicians who form part of the finely tuned nationwide distribution network needed to ensure that product processed in our Hamilton laboratory is used within three days of manufacture.

Each Technician carries a DataMATE hand-held computer that stores animal records so inbreeding can be avoided, as can matings of animals whose ancestry indicates the potential presence of a lethal recessive gene known as CVM. This level of mating management, provided along with useful herd data such as submission rates and non-return rates, is provided at no extra charge and represents a level of sophistication not seen anywhere else in the world.

The combination of the technologies and systems outlined above has been developed over decades and provides a service that is fully competitive against the best genetics in the world. The proof of this claim is evident in the extraordinary results achieved during the past year:

- Service volume set a new record during the year with inseminations up 3.0% to exceed 3.2 million.
- Simultaneous market share gains were achieved by PREMIER SIREs and Alpha Nominated, resulting in a net increase of 2.9%, taking overall market share into the high 70s.
- The new sire breed KiwiCross™ was launched as a PREMIER SIREs option and immediately accounted for 14% of all inseminations.
- A progeny test programme aimed at breeding specialist Once-a-Day cows was launched and 12,000 inseminations were carried out.
- Demand for the CustoMate Plus service enjoyed rapid growth among breeders eager to optimise individual sire/dam combinations.
- The Short Gestation Length breeding option, the only one of its kind in the world, continued to increase in volume and was assisted by the launch of a fresh semen service to enable future volume growth.




Sire Proving to get tomorrow's genetics today

"We've been Sire Proving farmers for 25 years; we're the first to see the changes. It wasn't long ago that you'd be out there in spring having to assist 10% of cows to calve because the calves were so big, but we'd only assist five or six per season now and we're still getting good calves.

"I first got into Sire Proving because it was cheap; we were young and didn't have any money. But we've stayed with it because we're one step ahead of everyone else in terms of the latest and best genetics. We get to milk daughters of top bulls, like Dauntless, three to four years before anyone else.

"The quality of the herd is good. They have to fit the system. The best cows are doing around 500 kgMS and the top cow (which is a contract mating cow) has a BW of 234. And two of our heifers were photographed for the current *Livestock Improvement Alpha Catalogue*. I cull ruthlessly from the bottom PWs of the herd and bringing around 140 heifers in each year, but it's getting tougher to find ones to go. We'll stay with the Sire Proving Scheme as long as the quality keeps going up."

DAVE KOWALEWSKI

- 
- Dave and Sue Kowalewski, Midhurst, Taranaki
 - 250 hectares
 - 600 cows
 - 1000 kgMS per hectare
 - Highest BW in herd 234
 - SPS Farmers of the Year 2005

Information Division

The Information Division provides products and services that allow dairy farmers to get information on their cows and herds, so they can make profitable farming decisions. Along with Genetics, Information is one of the two major customer interface Divisions within Livestock Improvement.

MINDA

MINDA – the herd recording service used by 90% of New Zealand dairy farmers to maintain records of animal identification, pedigree, milk production performance and other on-farm events – is at the heart of Livestock Improvement’s information products.

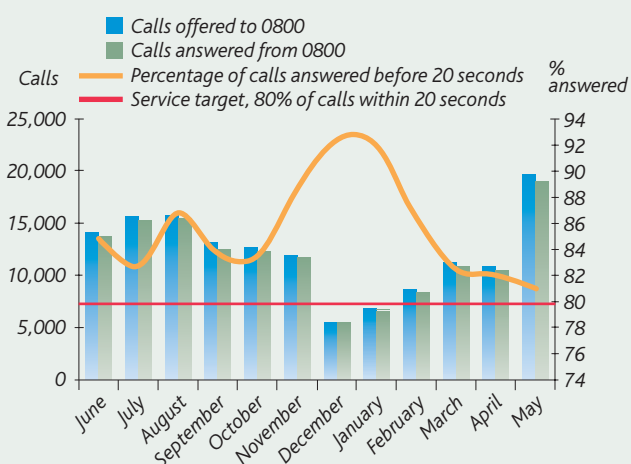
The use of computers and MINDA software for herd recording has grown substantially in recent years. In the 2005/06 season 70% of herds and 76% of cows were recorded electronically. MINDA software is regularly updated, and the development of a new release of MINDA software (for spring 2006) was a major area of activity.

MINDA continues to ensure that dairy farmers have access to the best information for making selection and management

decisions, by providing Breeding Worth (BW), Production Worth (PW) and Lactation Worth (LW) indices for cows.

A key feature of the MINDA service is the backup support available from the MINDA contact centre (0800 2 MINDA). The service target is to answer 80% of calls within 20 seconds. This was consistently achieved during the season, making the contact centre a benchmark for phone based customer service.

Phone calls presented to the MINDA 0800 number for the 2005/2006 season



Herd Testing

Livestock Improvement’s origins lie in herd testing – the process of collecting milk samples from individual cows and analysing them to determine their milk volume, fat, and protein production. These form a vital input to MINDA, being used for the calculation of Breeding Worth, Production Worth and Lactation Worth as well as the estimated production of an animal during a season.

Herd testing also delivers individual cow Somatic Cell Count (SCC) information to farmers, which is vital for managing milk quality and mastitis on the farm.

The 2005/06 season saw 9.1 million samples analysed from 8,500 herds. This was similar to the



DNA analysis – to be sure

"We've DNA profiled all our cows because we wanted to improve ancestry which hasn't been up to scratch.

"Now all we have to do is take a sample from our in-calf heifers each year and the DNA Punch has made this a lot easier. We used it for the first time on 420 heifers and it was so simple.

"When we're calving it's so busy; now we don't have to worry about pairing calves to mothers in the paddock; we simply bring them in and tag them. Less stress and more accuracy.

"It's reduced the number of times we have to check calving cows; we only check them for animal health now not rushing out to put tags in their ears as we used to. That's all a thing of the past.

"It helps keep staff motivated and reduces stress and the chance of making mistakes."

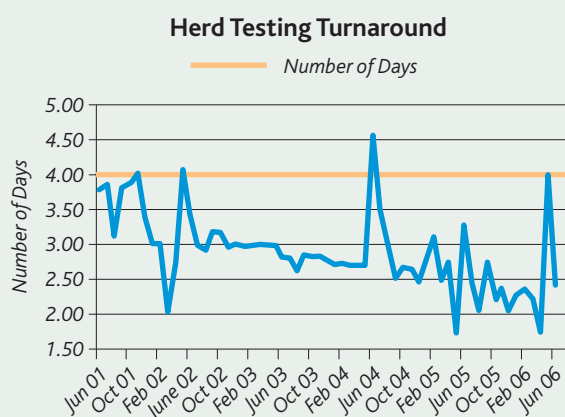
HENRIE AND JACK SCHERES



- Henrie, Jack and Peter Scheres, Lichfield, Waikato
- 4 dairy farms and 1 drystock farm
- Total of 1560 Premier Sires Holstein-Friesian cows
- Average 490 kgMS per cow and improving

previous season, although the volume of samples processed was assisted by good grass growing conditions across many of New Zealand's major dairying districts.

Simplifying herd testing has been a key focus and, after a commercial trial in the 2004/05 season, the EZ Link service was offered to a total of 200 farmers – 120 in the Waikato and 80 in Canterbury. Using a handheld device with a barcode reader, and barcoded sample flasks, EZ Link allows users to reduce the time involved in testing, while at the same time performing error checking during the milking. It was well received, and is being rolled out across the country on a larger scale in 2006/07.



Diagnostics

The diagnostics function within Livestock Improvement processes samples submitted for DNA and ELISA testing. The major areas of work for the Diagnostics business include animal parentage testing using DNA, and running the dairy industry EBL (Enzootic Bovine Leucosis) control scheme.

There has been considerable year-on-year growth in DNA testing, with more than 60,000 samples submitted by dairy farmers in the 2006/07 season. More than 100 dairy herds are now using DNA testing exclusively as a means of determining calf parentage, no longer attempting to match calves to cows during the calving period.

The ease of DNA testing was boosted substantially by the launch of the DNA Punch in autumn 2006 – a device for collecting a small tissue biopsy from animal ears developed collaboratively by Zee Tags and Livestock Improvement.

Livestock Improvement continues to manage the EBL control scheme on contract to Dairy InSight, and during the year was able to cement the position of the New Zealand dairy industry by meeting OIE (Office International des Epizooties, or the World Organisation for Animal Health) standards for freedom from the disease. Ongoing monitoring will continue in coming years.

Diagnostics carried out trials into the provision of a milk based Selenium test in the autumn and spring of 2005. Unfortunately the results were not sufficiently robust to proceed with a commercial launch of the service, but there was heartening interest from farmers into a novel test that sought to utilise milk samples already collected for herd testing.

The Diagnostics laboratories are certified to provide health testing for animals being exported from New Zealand. The substantial live-cattle trade with China in 2004/05 was not sustained in the 2005/06 season, which resulted in a loss of business for Diagnostics.

Protrack

Farm automation – the use of electronic identification devices for cows and various items of hardware and software in the farm dairy – is a growing area of interest for medium and large herd farmers, and for Livestock Improvement.

An increasing number of farmers are utilising Protrack systems for a range of tasks, from simplification of recording, to scheduling of routine farm events and automation of tasks such as drafting, making Protrack a logical extension of the traditional recording practices embodied in MINDA.

The existing Vantage system, incorporating full in-dairy identification and integration with a range of peripheral devices, achieved greater sales than in past years. Significant investment in software development has resulted in a series of software upgrades for users which deliver improved functionality based on customer feedback.

The new scaled-down Vector system delivers an automated drafting solution integrated with an in-dairy management system. At a lower price point, the Vector system offers a less expensive means of capturing some of the benefits of farm automation. It was launched during the 2005/06 season and has achieved excellent early levels of uptake in the market.

The field of farm automation is growing significantly, and Livestock Improvement expects to continue to participate actively in this field, delivering solutions that not only simplify the collection of data on the farm, but also provide real added value options that allow farmers to capture the benefits of the information available to them.

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FarmWise

Formed in the early 1990s, FarmWise is a user pays consultancy service that helps dairy farmers make profitable farm management decisions. Twenty one consultants were employed during the 2005/06 season, offering services in all regions of New Zealand.

A key function of the FarmWise team, beyond the provision of advice to individual farmers, is to contribute to the ongoing development of products and services at Livestock Improvement. FarmWise Consultants also assist industry initiatives such as the National Mastitis Advisory Committee.

The FarmWise influence extends beyond New Zealand, with Consultants linked to FarmWise working alongside our United Kingdom subsidiary, and short term visits taking place in South Africa and Australia in support of wider Livestock Improvement activities in those countries.

International Division

The International Division is involved in the marketing, sales and distribution of semen to more than 15 overseas markets. Livestock Improvement has subsidiaries in Australia, Ireland and the United Kingdom and provides semen sales in other markets via local partners.

The 2005/2006 year saw record sales and revenue achieved.

Australia

The 'Future First' progeny-testing programme in Australia has continued to expand and the first intake of young sires will get Australian proofs in early 2007.

The Australian market seems to be gaining in confidence after the drought. Livestock Improvement sales have recovered and grown beyond pre-drought levels.

A Farm Automation business has been established and initial sales results are promising.



United Kingdom

The United Kingdom business has had a profitable year despite the limitation to growth imposed by the inability to import new bulls due to IBR rules. Management focus on achieving sales growth will continue.

Ireland

In late 2005, Livestock Improvement purchased Peter Daly's 50% share of the Joint Venture, New Zealand Genetics (Ireland) Ltd, making it a fully owned subsidiary. The agreement included the ongoing involvement of Peter Daly in the business, however, he was tragically killed in a road accident in early 2006. The impact of this and the ongoing European Union restriction on importing proven bulls resulted in a disappointing year for sales in Ireland.

South Africa

Another solid year in South Africa where our partners, Genimex, are doing an excellent job representing our product and have achieved record volumes.



Top EBI herd mix of the best of New Zealand and British genetics

"Winning the EBI is a vindication of a breeding policy formulated 10 years ago.

"Cows were becoming too extreme; they'd produce gallons and gallons at peak but needed extreme amounts of supplements and suffered energy deficits. Fertility was a problem along with associated health problems. We wanted to avoid that.

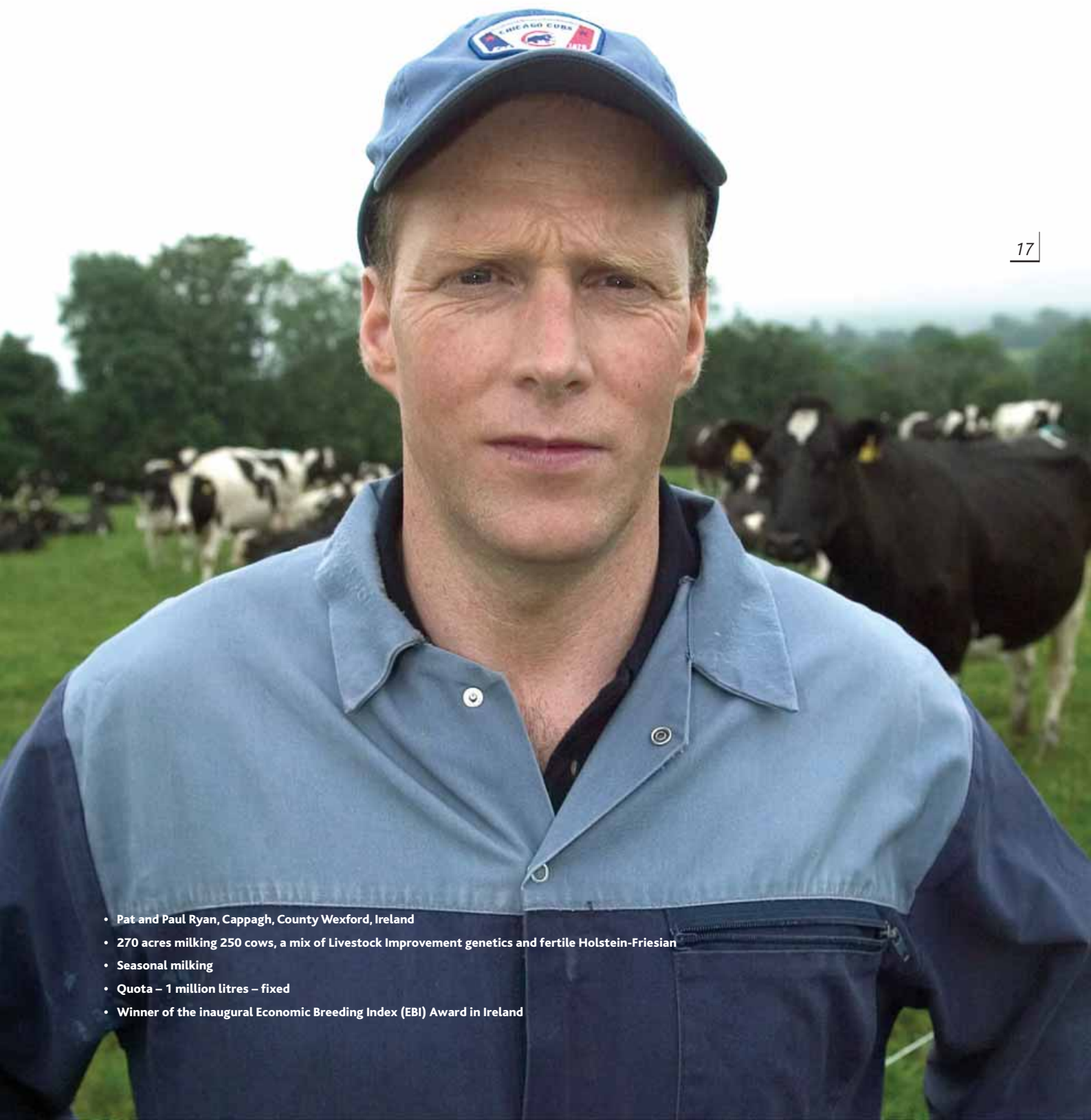
"We set our sights on an easy care cow which wouldn't need much minding; a 'middle of the road' cow which'd be fertile and capable of maintaining herself without high amounts of maintenance.

"We had some experience with New Zealand bulls, like Athol Famous Prefect and Nicholas Storm and could see that their influence, and that of more modern bulls like Hugo, had pushed up strength with better chest and rump widths and good protein percentages. That experience encouraged us to use more.

"It's all about growing grass and utilising that grass well. But overall it's about breeding the right type of cow and doing the right things with her."

PAT RYAN

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- Pat and Paul Ryan, Cappagh, County Wexford, Ireland
- 270 acres milking 250 cows, a mix of Livestock Improvement genetics and fertile Holstein-Friesian
- Seasonal milking
- Quota – 1 million litres – fixed
- Winner of the inaugural Economic Breeding Index (EBI) Award in Ireland

Innovation Group

The Innovation Group's objectives are the development of new and improved products and services for New Zealand dairy and deer farmers.

Scientific Research

Research in the 2005/2006 year covered the following main areas of interest:

Gene discovery programme

Livestock Improvement's major gene discovery programme targets the identification of Quantitative Trait Loci (QTL) which control animal productivity traits through a number of projects including the Friesian-Jersey Crossbred Trial. One of the focal points of the programme in 2005/06 was the measurement of the production variation that exists between cows on once-a-day milking regimes.

Since the initiation of the International bovine genome project to map the entire bovine genome, scientists have speculated about how much genetic information could be used to predict the expression of certain traits. Livestock Improvement is currently evaluating new methods of calculating breeding values using large volumes of genomic data because, in the future, this data is expected to form the basis of breeding schemes and accelerate genetic gain.

Highlights for the year include:

- **Genemil**

The University of Liege completed a statistical software package that allows us to understand the inheritance patterns of genes across large populations and refine location of genes of interest on the genome. This tool will help speed the gene discovery process.

- **Crossbred trial**

A highlight of the Friesian-Jersey Crossbred trial was the measurement of the production variation that exists between cows on once-a-day milking regimes. A group of cows were milked once daily for the entire season. Preliminary analysis confirms that significant variation exists in this crossbred herd for milk production on a once-a-day regime and there are individual animals that perform better compared to a twice-a-day regime. A larger group of crossbred trial cows will be tested this season. The challenge will then be to identify the genetic factors that modulate this variation and use this for future selection of breeding elite stock for once-a-day farmers.

- **Transcriptome Mapping**

The Transcriptome mapping project team has successfully measured energy balance data (milk, volume and composition, live-weight, condition score, progesterone concentration). All the data collected will be analysed and linked to give a better understanding of the relationship between the energy balance and the genetic makeup of the cows, allowing for better breeding decisions.



Protrack's unreal

"I started off in dairying 11 years ago with 100 cows at Culverden, and got into conversions because you can set them up the way you want. The current 828 conversion used to be two sheep farms. We took over at Christmas with the aim of resowing and refencing the whole place, building 10 houses, two 80 bail rotary sheds, one acre of calf sheds and seven centre-pivots covering 745 hectares for the start of the 2006 season.

"I've got a Protrack Vantage system in the shed at home and it's b..... wonderful, unreal, so it was a no-brainer to have it in both sheds here. It saves us labour. With groups of cows at mating or for vet checks etc you just programme it once and tell it when to whip that group out and it's just done.

"We can get 100 calves a day; having all the cows DNA profiled means we don't have to mother-up. Cow numbers are entered as cows calve and all we have to do is brass tag the calves and record them for that day, and then GeneMark matches calf to cow. Same thing at mating. We can get 200 cows to put up per day, their numbers are entered and Protrack automatically drafts them out in three weeks without us having to give it another thought.

"I didn't realise how much we'd use it. When we bought it we thought it would be good for drafting and feeding but we're doing much more than we ever thought.

"It's made me redundant – I used to be the spare part who'd be there for jobs like drafting, but now I'm not needed."

DAVID DRAKE

- David and Jo Drake, Orari and Geraldine, Canterbury
- Two equity partnerships –
 - 401 hectares farm milking 1600 crossbred cows at Orari, Canterbury.
 - 828 hectare conversion milking 3200 crossbred cows at Geraldine



- **Genomic selection**

A new research project is being undertaken under the Technology New Zealand Genomic Selection grant. The research aims to develop an alternative breeding technology that exploits the genetic variation which exists across the entire genome to make better selection decisions in the breeding scheme.

Quantitative Genetics

Livestock Improvement's quantitative genetics programme supports New Zealand Animal Evaluation Limited by developing breeding values for new traits for potential incorporation into the National Breeding Objective.

- **NZ Test Day Model (NZTDM)**

For more than 15 years a statistical model, referred to as the 'animal model,' has been used to estimate lactation yields from herd tests conducted by clients. A more sophisticated method for assessing animal evaluations has been in use overseas, and adapting and extending that science specifically for New Zealand has been a focus of the Livestock Improvement R&D team. Timed for launch in February 2007, the NZ Test Day Model will analyse test day records instead of accumulated lactation records generating more accurate information from a similar number of performance records.

NZ Test Day Model will influence genetic evaluation of animals and herd testing.

- **Genetic evaluations** – NZ Test Day Model will generate accurate Breeding Values and Production Values for dairy cows, and Breeding Values for dairy sires.
- **Herd testing** – NZ Test Day Model will, from the start of the 2007 season, allow more flexible herd test systems to be implemented in New Zealand and more reliable records for lactation persistency.

Reproduction

Livestock Improvement has a strong commitment to semen and female reproduction research. In the semen area, research is focused on finding better and more efficient ways to package and deliver semen into cows. The objective is to maximise bull utilisation and therefore genetic gain, while maintaining or improving semen fertility.

Animal Health and Welfare

Livestock Improvement plays an active role in many initiatives to improve the general health of the New Zealand dairy herd. One of the most important is:

- **Enzootic Bovine Leucosis (EBL)** – faster and cheaper screening

Following extensive testing Livestock Improvement is now able to replace the pooled milk EBL screening test with a single ELISA test which has resulted in significant efficiency gains and cost savings while improving overall surveillance.

Subsidiaries

Animal Breeding Services Limited

Activities

- Multiple Ovulation Embryo Transfer (MOET)
- Trans Vaginal Recovery and In Vitro Production (TVR/IVP)
- Custom Semen Collection and Freezing
- Artificial Insemination
- Genetic sales of Embryos

Trans Vaginal Recovery and In Vitro Reproduction (TVR/IVP)

Based on the successful development of the TVR/IVP platform over the previous year, the number of commercial TVR sessions increased to over 1,100 sessions for the year. The increase in demand for this service is based on our ability to undertake two to three sessions per week for each cow and our ability to undertake this service on early pregnancy cows and heifers. In addition, some 20% of cows do not respond to conventional MOET activities and therefore the provision of TVR/IVP services enables clients to undertake reproductive technologies on a larger pool of donors than previously possible.

Over the season, Animal Breeding Services achieved a transferable embryo per TVR session of 1.7. This exceeds the international benchmark of 1.0 embryo per session.

Around 7,300 sheep embryos were produced in New Zealand for domestic and international implantation. The international embryos are destined for implantation in Chile, Argentina, Uruguay, Brazil, Paraguay and the United Kingdom.

From the implantations carried out the previous year pregnancy rates, averaging well in excess of 60%, have been achieved with one client achieving a pregnancy rate of 81%.

Sheep reproductive technologies

New Zealand sheep genetics are proving popular on the international market. This is not only because of New Zealand's relative disease free status but also because of the advances made in genetic selection over the last few years. International sheep breeders are now beginning to place more emphasis on low-input maternal lines. These are the genetics that have been bred in New Zealand over recent decades.

The provision of sheep reproductive technologies in Australia has grown by over 30%. The majority of this growth is the result of a major shift in the Australian sheep industry away from wool production to meat production and the requirement for larger numbers of meat rams.

Porcine reproductive technologies

The pig semen collection facility produced over 43,000 tubes of semen which represents a 23% increase over last year's production and follows on from increases of 28% the year before. The piggery is now at maximum production capacity with 32 boars on site.

Deer Improvement

Livestock Improvement's dairy cattle genetics business is one of the largest and most sophisticated in the world. In 2004, a new initiative was launched to leverage the organisation's capabilities into the deer market.

The deer industry was attractive because of its critical mass and the potential for genetics to add value in the venison segment which is the main income earner for deer farmers, but which had been largely ignored by conventional breeders in their quest for improved antler production. Another key factor encouraging investment in this sector was the recent development of conventional cervical artificial insemination (AI) procedures as used in cattle, whereas earlier efforts in deer involved surgical AI under sedation.

Deer Improvement has just completed its third mating season and continues to break new ground.

- Despite unfavourable trading conditions due to the low venison schedule, demand for the commercial AI service grew by 67%, making Deer Improvement the market leader in venison genetics.
- The production of the first across-herd Breeding Values by the industry database included six Deer Improvement sires in the top 20, more than any other breeder.
- AI conception rates averaged 74%, up from 71% last year and 67% in year one.
- A 400 hectare farm was purchased near Balfour in Southland and has been developed as a base for the elite nucleus herd of breeding hinds which will form the heart of the genetic improvement programme. Biosecurity is a key objective in this establishment process that includes double boundary fencing and the creation of two separate blocks, one for quarantine of introduced animals, and the main 'isolation block' where only semen or embryos will be introduced.
- The embryo transfer programme designed to rapidly increase the number of elite breeding hinds in the nucleus herd achieved outstanding results with 100% success rate in semen collection from spiker stags, nearly 7 embryos per yearling hind, and a hold-rate of 90%.



Herd testing's never going to be fun, but at least it's manageable

"We put 1450 cows through a 70 bail rotary so herd testing was pretty hectic. There'd be trays and pottles everywhere, around the sides. It wasn't easy.

"EZ Link saw an end to that. It meant we had one person less in the shed and a lot less storage space needed for trays.

"Now we just have one stack.

"We used to have two Herd Test Assists too, and now only have one.

"The EZ Link computer worked well – just needs to keep up with the speed of the platform as per cow volume goes down, and the platform speeds up, in the second half of the season.

"Herd testing's never going to be fun but this handheld makes it manageable with so many cows."

ANDREW PECK

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- Andrew and Fiona Peck, Ashburton
- 390 hectares
- 1450 cows
- 380 kgMS per cow

National Council Report

As Chairman of the National Council of Livestock Improvement, it again gives me pleasure to present the Council's report for the 2005/06 year.

National Council Activities

This year has seen major changes in the composition of the National Council. Following the report from the Governance and Representation Review Committee, consultation with the National Council and subsequent vote at the 2005 Annual Meeting, the size of the Council was reduced and is now made up of 21 Councillors and no Dairy Company representatives.

This number will provide shareholders with representation and allow a more streamlined group to carry out the activities required.

Communication with shareholders continues to be an important issue and the Council has been looking at ways to improve this. It is a two way process and shareholder input is needed, especially now that Liaison Groups no longer exist.

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The Council has continued to ask pertinent and probative questions of the Board and management regarding the performance and direction of the business. Areas of focus have tended to be those which, at present, are not contributing positively to the balance sheet. The Biotechnology expenditure and results achieved are also being scrutinised.

In the 2005/06 year the National Council began to develop its own strategic view for Livestock Improvement to compare with the Board's. This will continue and reach a conclusion in the 2006/07 year.

Council Perspective on Board and Business Performance

The achievement of the five year strategic objectives of a \$10 million profit after tax and before biotechnology, ROCE of 10% and Silver Business Excellence Award is a wonderful result.

This year's result of a \$10.9 million profit and a dividend of 24.5 cents per Investment Share is a very good result by Board and Management. The Council sees the present situation, in regards to reserves and overall balance sheet performance, as a very good spring board into the future and we look forward to monitoring and being involved in this process.

The Dividend Reinvestment Plan, introduced this year, is a very good vehicle for shareholders to increase their investment shareholding and the Council is encouraged to see a significant number of shareholders taking advantage of this Plan to acquire more Investment Shares.



Front row (L-R): **PETER LE HERON, BRIAN ASPIN, WAYNE BERRY, JEANETTE QUIN, HAMISH ANDERSON / CHAIRMAN**

2nd row (L-R): **JENNY MORRISON, JOHN SCRIMGEOUR, ROBERT SLACK**

3rd row (L-R): **MURRAY KING, GORDON GLENTWORTH, CHRISTINE FINNIGAN, RON MONK, PETER FORD**

Back row (L-R): **LLOYD McCALLUM, KEN POLGLASE, DON BLUMHARDT, ALISTAIR WHITE, IAN STOREY**

Absent: **GARY STOKES, JOHN VAN POLANEN**

Summary

The National Council welcomes, and looks forward to working with, new Chief Executive, Mark Dewdney.

The three work groups of the Council, which cover Governance, Representation and Strategic, will continue to focus on these areas for the benefit of shareholders.

As a Council, we will continue to work for shareholders to enable Livestock Improvement to continue to be a world leader in its field and provide shareholders with products and services on farm in New Zealand at fair value, and which allow farming businesses to prosper.

The National Council is an important vehicle for representing shareholder interests and I urge shareholders to become involved with either the National Council or the Board if they feel they are able to add value to either group.

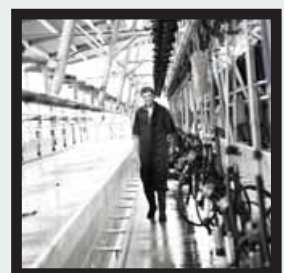
National Council representatives are located across New Zealand and I encourage shareholders to contact them at any time to discuss anything which will advantage your Co-operative.

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I know I speak for all members of the National Council when I say it has been an honour and a pleasure representing shareholders in 2005/06.



HAMISH ANDERSON / CHAIRMAN, NATIONAL COUNCIL




Management decisions easier

"We use MINDApro and CustoMate *Plus* on both herds. Having two farms, MINDApro allows me to build my own customised reports to compare cows between herds and the information is always up to date. The herds have good Breeding Worth (BW) and it's difficult to continue to make gains through BW so I use 100% Nominated CustoMate *Plus* for additional traits. My udder Breeding Values were average so I was looking to make improvement. By focusing on udders and capacity as well as BW I hope to have longer lasting, high producing cows. This means my culling in the future will be more on production and less on unsuitably uddered cows.

"Customate *Plus* matches each of my cows to the right bull to correct her weak trait. If her traits are too poor, Customate *Plus* gives me the information to decide to not keep replacements from her at all. It enables me to use a team of bulls that meet my trait requirements and still match or better Premier Sires' BW statistics. In time, I hope to have a more consistent line of high BW cattle."

IAN STOREY

- 
- Ian and Pamela Storey, Ohinewai, Waikato
 - Owner: 75 hectares milking 240 crossbred cows
 - Sharemilker: 90 hectares milking 280 crossbred cows

Governance Report

Role of Board of Directors

The Board is responsible for the direction and control of Livestock Improvement's activities. It is committed to the guiding values of the company – integrity, respect, continuous improvement and service to shareholders. Legislation and the Constitution establish the Board's responsibilities and include provisions for how the Co-operative will operate.

Responsibilities

The Board is responsible for setting the strategic direction and approving significant expenditures, policy determination and stewardship of the Co-operative's assets. The Board and the security holders shall not, except with the written consent of the Minister, exercise any of their rights, directions and powers under or alter the Constitution so as to cause or permit the Company to cease to be a Co-operative supplying goods and services to shareholders, and operating the core database for the benefit of a large number of shareholders who continue to be representative of New Zealand dairy farmers (including shareholders) and who are entitled to elect the majority of the Directors on a regional or other basis.

Co-operative Principles

The Constitution records the following Principles:

- The Company will remain a Co-operative Company;
- The Company is controlled by Co-operative Control Shareholders who have voting rights in proportion to their use of the Company's qualifying products and services;
- Core products and services are made available to all shareholders at fair commercial prices;
- Products and services which benefit shareholders, and which otherwise might not be made available, are developed and made available to shareholders, provided that the Company receives a commercial return; and
- Shareholders co-operate with the Company and each other including the sharing of information to promote their common interests.

Pricing of Products and Services

In setting prices to be paid for products and services Livestock Improvement should seek to create wealth for the Company and its Shareholders, and accordingly should supply goods and services at commercial prices reflecting market conditions, taking into account the Company's co-operative principles and key strategic objectives set by the Board and approved by the National Council.

Principal Activities

The Board has a responsibility to ensure the principal activities of the Company are the co-operative activities of supplying goods and services to its shareholders with particular reference to:

- The measurement and evaluation of growth, yield of milk or milk constituent and feed conversion efficiency of livestock, and any other factor relevant to decisions on breeding and management of livestock;
- The development and commercial application of artificial breeding or livestock;
- Improvement of livestock and of farm management practices through products based on genetics, biotechnology, information and advice.

Board Composition

Until 31 May 2006 the Constitution prescribed nine Elected Directors representing the regions and up to three Independent Directors.

As from 1 June 2006 the Constitution was amended to reflect the Governance and Representation review recommendations (approved by Shareholders at the Annual Meeting in October 2005). The number of Elected Directors became seven, representing 4 Regions and up to three Independent Directors. All elected Directors now hold office for four years.

Transitional Provisions

In accordance with the Transitional Provisions of the Constitution, Messrs J E Bicknell and R D Jackways retired on 31 May 2006. The nine existing regions became four regions on 1 June 2006 represented by:

- Northern M E Jagger
- Midland S B Bay
 E G Coats
- Central Election held for two Directors
- Southern K D Straight
 A J Reid

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Election

Each Elected Director holds office as a Director for a period of four years. A retiring Director is eligible for re-election as a Director of the Company.

The Directors representing previous farmer regions six (P J Lynskey) and region seven (B R Guy) retired by rotation in 2006 and being eligible stood for re-election in the new combined Central region. Mr G B Maughan also stood for election in this region. Elected Directors from 1 June 2006 were:

- Central B R Guy
 P J Lynskey

Committees

• Audit, Finance and Risk Committee

This is a sub-committee of the Board comprising five Directors and is chaired by an Independent Director, Mr G Fraser. It is constituted to monitor the veracity of the financial data produced by the Co-operative and its Subsidiaries and ensures controls are in place to minimise the opportunities for fraud or material error in the accounts.

The Audit, Finance and Risk Committee meets at least five times a year with the external Auditors and Executive.

– Internal Audit

The Audit, Finance and Risk Committee engaged PricewaterhouseCoopers as internal auditors to audit Finance and Risk critical systems and procedures for the third year of the programme.

• Remuneration and Executive Appointment Committee

This is also a sub-committee of the Board comprising three Directors and is chaired by Independent Director, Mr P Lough.

The committee is constituted to approve appointments and terms of remuneration for Senior Executives of the Company, principally the Chief Executive and those reporting to him. It also considers and, if appropriate, approves any wage and salary percentage adjustments for the Co-operative's employees.

- **Biotechnology Governance Committee**

Chaired by Mr B Guy the committee's role is to consider the opportunities available and the risks associated with investment in biotechnology research and development. The Committee reports to the Board.

- **Information Systems Governance Committee**

This committee considers and makes recommendations to the Board for approval of the strategic plan for the IT and communication technologies which align with the company's overall strategic requirements. The Committee is chaired by Mr E Coats.

- **Governance and Representation Committee**

The function of this committee is to review the structure of governance (Board) and representation (National Council) to ensure an efficient and effective structure is in place while maintaining shareholder and stakeholder communications and interaction. Chaired by Mr M Jagger this committee, including some National Councillors, recommended the changes to the size and region/ward structures approved by shareholders at the October 2005 Annual Meeting and implemented on 1 June 2006.

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Meetings

The Board met nine times in 2005/06 plus Directors called a Special Shareholders Meeting on 5 April 2006 to consider and approve the Dividend Reinvestment Plan.

Insider Trading

All Directors of the Co-operative are familiar with and have formally acknowledged acceptance of an 'Insider Trading Code' that controls any dealings in securities by Directors. The provisions of the code are substantially in accordance with the 'Insider Trading (Approved Procedure for Company Officers) Notice' issued under the Securities Amendment Act 1988.

Shareholding

- **Co-operative Control Shares**

An Elected Director shall hold the minimum Co-operative Control Share holding requirement.

Investment Shares

An Elected Director shall hold the minimum Investment Share holding requirement, which shall be twice the number of Co-operative Control Shares held. A description of Livestock Improvement's dual share structure and the Divident Reinvestment Plan is contained on pages 60-61 of this Report.

Interests Register

A Directors' Interest Register is maintained and Directors interest in transactions during the financial year are outlined on page 54 of this Report.



Cheap, no hassle way to manage stock movement

"We own a lifestyle block and run 40 dairy grazers and now have 6 of our own stock. We have an old dairy cow which up till now has calved every year and also always takes another calf. So over the course of a couple of years we now get a freezer beast and have an animal to sell each year.

"It got to the point where I was ready to sell an animal and I was thinking about my tag requirements. It was about the same time I stumbled across the TRACKA website.

"I've given all our stock basic names and ordered the tags required to enable us to trade. The site is well laid out and easy to follow. And certainly caters for any traceability requirements that will become important now and in the future.

"With the ever increasing number of lifestylers and their stock this certainly seems to provide a cheap, no hassle answer to meeting those requirements."

MICHAEL BAILEY



Livestock Improvement Board 2005/2006

Farmer Directors

- **Stuart Bruce Bay**, Chairman. *B.AgSc (Hons) Massey. Certificate in Company Direction*
Dairy farmer/Director
 - 370 ha milking 1400 Jersey and KiwiCross cows at Manawaru in the Eastern Waikato
 - Livestock Improvement Director 1989; Deputy Chairman in 1996 and Chairman in 2004Current Directorships include:
 - Baylea Farms Ltd
 - Farming Trusts
- **Peter John Lynskey** (known as John)
Dairy Farmer
 - 255 and 90 ha milking 1160 Friesian, Jersey and Crossbred cows at Oeo in South Taranaki
 - Director of Livestock Improvement since 1993Current Directorships include:
 - New Zealand Animal Evaluation Limited
 - Maolla Land Company
- **Murray Ernest Jagger**, *Dip.Ag Massey, Kellogg Rural Leadership (2002)*
Dairy farmer
 - 160 ha milking 450 Jersey cows at Whangarei
 - Director of Livestock Improvement since 2000Current Directorships include:
 - Manaia View Farms Ltd
 - LIC Deer Limited
- **Bryan Robert Guy**, *Kellogg Rural Leadership (1990), Executive Development Programme for Primary Producers (Queensland)*
Dairy farmer
 - 370 ha milking 650 Friesian cows at Feilding
 - Director of Livestock Improvement since 1994Current Directorships include:
 - Byreburn Ltd (family farming business)
- **Edward George Coats**, *Kellogg Rural Leadership (1994)*
Dairy farmer
 - 333 ha milking 479 Crossbred cows at Okoroire in the Waikato
 - Director of Livestock Improvement since 1996Current Directorships include:
 - Family farming company
 - Dairy InSight
 - New Zealand Animal Evaluation Limited
- **Alvin John Reid**, *Dip.Ag (Massey)*
Dairy farmer
 - 575 ha across four farms milking 2600 Crossbred cows at Temuka
 - Director of Livestock Improvement since 1998Current Directorships include:
 - AJ & JG Reid Ltd
 - Reid Partnership Ltd
 - Ohape Milkers Ltd
 - Riverholme Agriculture Ltd
 - Accord Dairies Ltd
 - Conical Hill Dairy Ltd (including 5 fully owned subsidiary companies)
 - Dexcel Ltd and Dexcel Holdings Ltd



L-R: JOHN LYNSKEY, RON JACKWAYS, JAY WALDVOGEL, GRAHAM FRASER, ALVIN REID, STUART BAY / CHAIRMAN,
KEVIN STRAIGHT, JOHN BICKNELL, MURRAY JAGGER, BRYAN GUY, PHIL LOUGH, TED COATS

- Kakahu Irrigation Ltd
- South Canterbury Farmers Irrigation Society
- WA Systems (2003) Ltd & WA Systems Ltd
- Hi Tech Foods Ltd

- **Kevin Dennis Straight**

Dairy farmer

- 250 ha milking 740 crossbred cows and 230 ha drystock at Canvastown, Marlborough
- Director of Livestock Improvement since June 2004

- **Ronald Douglas Jackways**

Farmer/Director

- 20 ha lifestyle block in Hamilton and 439 ha milking 1600 Friesian and Crossbred cows at Rakaia in the South Island
- Director of Livestock Improvement since 1986 (retired 2006)

- **John Eric Bicknell**, *Kellogg Rural Leadership (2001)*

Dairy farmer

- 60 ha milking 190 Friesian/KiwiCross™ cows at Galatea
- Director of Livestock Improvement since 1998 (retired 2006)

Independent Directors

- **Graham Alexander Fraser**, *B.Com*

Rotorua

- Former dairy farmer and Chairman of New Zealand Dairy Board, Graham has held a number of Chairmanship positions including Glencoal Energy Ltd, Anchor Superannuation, Anchor Investments, New Zealand Dairy Research Institute and the Audit Committee of the New Zealand Dairy Board

Current Directorships include:

- Skellerup Holdings Limited
- LIC Deer Limited
- AgResearch

- **Philip (Phil) Vernon Lough**

Nelson

- Phil Lough is a former Deputy CEO of the New Zealand Dairy Board and CEO of the Sealord Group, a leading global seafood business. He now operates as a professional Director

Current Directorships include:

- New Zealand Trade and Enterprise
- Port Nelson
- Tatua Co-operative Dairy Company
- Methven Group

- **Jay Scott Waldvogel**

Wisconsin, USA

- More than 20 years experience in the global dairy industry
- Held senior roles in finance, marketing, sales, operations, logistics, business development and general management while working for dairy co-operatives in the United States of America, Europe and New Zealand
- Held a number of senior positions, including Chief Operating Officer, with Fonterra in New Zealand
- Currently a strategic consultant, professional director and cattle farmer/breeder

Statement of Financial Performance

for the year ended 31 May 2006

	Note	Consolidated		Parent	
		2006 \$'000	2005 \$'000	2006 \$'000	2005 \$'000
Total operating revenue	1	110,471	104,041	102,086	96,571
Total operating expenses	2	(99,589)	(95,319)	(88,255)	(86,200)
Operating surplus before biotechnology research and income tax		10,882	8,722	13,831	10,371
Biotechnology research		(3,310)	(3,426)	(3,310)	(3,426)
Operating surplus before income tax		7,572	5,296	10,521	6,945
Income Tax	3	–	–	–	–
Net surplus for the year		7,572	5,296	10,521	6,945
Net surplus comprises					
Parent interest		7,572	5,211	10,521	6,945
Minority interest		–	85	–	–

Statement of Movements in Equity

for the year ended 31 May 2006

	Consolidated		Parent	
	2006 \$'000	2005 \$'000	2006 \$'000	2005 \$'000
Total recognised revenues and expenses				
Net surplus for the year:				
parent interest	7,572	5,211	10,521	6,945
minority interest	–	85	–	–
Translation difference	(46)	15	–	–
	7,526	5,311	10,521	6,945
Contributions from owners				
Shares issued	688	457	688	457
	688	457	688	457
Distributions to owners				
Dividends:				
parent interest	(6,361)	(7,465)	(6,361)	(7,465)
Repurchase of shares	(390)	(423)	(390)	(423)
Share purchase from minority shareholders	–	(410)	–	–
	(6,751)	(8,298)	(6,751)	(7,888)
Movements in equity for the period	1,463	(2,530)	4,458	(486)
Equity at beginning of year	95,234	97,764	97,229	97,715
Comprising:				
parent interest	95,234	97,439	97,229	97,715
minority interest	–	325	–	–
Equity at end of year	96,697	95,234	101,687	97,229
Comprising:				
parent interest	96,697	95,234	101,687	97,229
minority interest	–	–	–	–

Statement of Financial Position

as at 31 May 2006

Note	Consolidated		Parent	
	2006 \$'000	2005 \$'000	2006 \$'000	2005 \$'000
Current Assets				
Cash balances	19,206	25,115	18,819	24,310
Intra-group receivables	–	–	8,796	5,156
Trade receivables	14,454	12,532	9,023	7,849
Inventories	4 6,625	5,595	4,006	4,580
Other current assets	1,009	945	988	853
	41,294	44,187	41,632	42,748
Non-current Assets				
Investments	5 56	213	6,634	2,450
Bulls and database	22,500	22,500	22,500	22,500
Fixed assets	6 49,562	43,754	43,575	42,947
Goodwill	7 1,265	381	–	–
Development costs	8 1,431	183	1,416	171
Intragroup loans	–	–	3,591	968
Loans	36	84	36	84
	74,850	67,115	77,752	69,120
Total Assets	116,144	111,302	119,384	111,868
Current Liabilities				
Intra-group payables	–	–	206	204
Trade payables	11,553	8,374	10,154	7,233
Provisions	9 3,380	3,309	3,176	3,086
Prepaid receivables	238	425	238	425
	15,171	12,108	13,774	10,948
Non-current Liabilities				
Provisions	9 4,258	3,960	3,923	3,691
Other non-current liabilities	18	–	–	–
	4,276	3,960	3,923	3,691
Total Liabilities	19,447	16,068	17,697	14,639
Net Assets	96,697	95,234	101,687	97,229
Equity	10 96,697	95,234	101,687	97,229

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STUART BAY / DIRECTOR / 12 July 2006



MURRAY JAGGER / DIRECTOR / 12 July 2006

Statement of Cash Flows

for the year ended 31 May 2006

	Note	Consolidated		Parent	
		2006 \$'000	2005 \$'000	2006 \$'000	2005 \$'000
Net cash from/(used in) operating activities					
Cash provided from:					
Receipts from customers		106,175	100,900	95,511	93,637
Interest income received		1,755	1,418	1,969	1,481
		107,930	102,318	97,480	95,118
Cash applied to:					
Payments to suppliers and employees		(90,670)	(86,651)	(80,243)	(79,015)
Interest expense paid		(28)	(37)	(24)	(11)
Income tax paid		–	–	–	–
		(90,698)	(86,688)	(80,267)	(79,026)
	11	17,232	15,630	17,213	16,092
Net cash from/(used in) investing activities					
Cash provided from:					
Proceeds from sale of other non-current assets		865	457	677	457
		865	457	677	457
Cash applied to:					
Acquisition of associate/shares/advances to subsidiaries		(1,847)	(396)	(6,758)	(1,091)
Acquisition of non-current assets		(16,096)	(5,254)	(10,560)	(4,881)
		(17,943)	(5,650)	(17,318)	(5,972)
		(17,078)	(5,193)	(16,641)	(5,515)
Net cash from/(used in) financing activities					
Cash provided from:					
Shares paid up		688	457	688	457
		688	457	688	457
Cash applied to:					
Repurchase of shares		(390)	(423)	(390)	(423)
Dividends paid to shareholders of the Group		(6,361)	(7,465)	(6,361)	(7,465)
		(6,751)	(7,888)	(6,751)	(7,888)
		(6,063)	(7,431)	(6,063)	(7,431)
Net increase (decrease) in cash balances		(5,909)	3,006	(5,491)	3,146
Cash balances at beginning of year		25,115	22,109	24,310	21,164
Cash balances at end of year		19,206	25,115	18,819	24,310

Statement of Accounting Policies

for the year ended 31 May 2006

(a) Basis of Preparation

Livestock Improvement Corporation Limited (the Parent) is a company domiciled in New Zealand, registered under the Companies Act 1993 and the Co-operative Companies Act 1993 and listed on the Alternative Board of the New Zealand Stock Exchange Limited. The Parent is an issuer for the purpose of the Financial Reporting Act 1993 and its financial statements comply with that Act. The reporting currency used in the preparation of these financial statements is New Zealand dollars.

Financial statements for the Parent and consolidated financial statements are presented. The consolidated financial statements comprise the Parent, its subsidiaries and interests in associates.

The financial statements comprise statements of the following: significant accounting policies; financial performance; movements in equity; financial position; cash flows; as well as the notes to these statements. The financial statements have been prepared in accordance with generally accepted accounting practice in New Zealand. Where no financial reporting standard exists in New Zealand in relation to a particular issue, the accounting policies and disclosures adopted have been determined with regard to other forms of authoritative support.

(b) General Accounting Policies

The general accounting policies for the measurement and reporting of earnings and financial position on an historical cost basis have been followed in the preparation of these accounts, except that livestock inventories (other than the breeding bulls) are stated at valuation. The financial statements have been prepared based on the going concern concept.

(c) Particular Accounting Policies

The following particular accounting policies which materially affect the measurement of earnings and financial position have been applied.

(i) Foreign Currencies

Transactions involving foreign currencies are translated at rates of exchange ruling at the date of the transaction. Monetary amounts outstanding at balance date are converted using the year-end rate. All exchange differences are taken to the Statement of Financial Performance. Short-term transactions covered by forward exchange contracts are translated at the exchange rates specified in those contracts.

Translation of the financial statements of independent foreign operations

The assets and liabilities of the Group's and associate's overseas operations, being independent foreign operations, are translated at the exchange rates ruling at balance date. The revenues and expenses of these entities are translated at rates approximating the exchange rates ruling at the dates of the transactions. Exchange differences arising on the translation of independent foreign operations are recognised directly in the foreign currency translation reserve.

(ii) Fixed Assets and Depreciation

All owned items of property, plant and equipment are initially recorded at cost, and, except for land, depreciated. Initial cost includes the purchase consideration, or fair value in the case of donated assets, and those costs directly attributable to bringing the asset to the location and condition necessary for its intended use. Costs cease to be capitalised when substantially all the activities necessary to bring an asset to the location and condition for its intended use are complete. All feasibility costs are expensed as incurred. The useful economic lives of depreciating assets have been assessed as:

Buildings	40 years
Plant and Equipment	5 years
Vehicles	5 years
Office Equipment	5 years
Field-based Laptop Computers	3 years
Other Personal Computers	4 years
Other Computer Equipment	5 years
Computer Software	4 years

Leased assets

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Assets acquired by way of finance lease are stated initially at an amount equal to the present value of the future minimum lease payments, and are depreciated as described above.

(iii) Bulls and Database

These assets are comprised of the pool of Breeding Bulls and the Parent's database and are included at the cost attributed to the assets when acquired.

Breeding Bulls

The pool of Breeding Bulls was acquired in May 1988 and it is the Parent's policy to maintain this pool. The composition of the pool constantly changes with the average bull having a productive breeding life of three years. All costs incurred in maintaining the pool including the costs of replacement bulls are expensed as they are incurred.

Accordingly, on the basis that the pool will be maintained, there is no defined economic life of this asset. Thus it is not considered appropriate to amortise the cost of this asset unless there is a permanent impairment in its value.

Livestock Improvement database

In May 1988, the Parent acquired the Livestock Improvement database as part of its acquisition of the net assets and operations of the then Livestock Improvement Division of the New Zealand Dairy Board and the six Livestock Improvement Associations. Under the Dairy Industry Restructuring Act 2001, the core database, covering some 40 fields of animal data, was defined. While the Livestock Improvement database includes these defined fields, no value is attributed, specifically, to the core database.

All costs of maintaining and enhancing the Livestock Improvement database are expensed when incurred as a period cost. Accordingly there is no defined economic life of this asset. Thus it is not considered appropriate to amortise the cost of this asset unless there is a permanent impairment in its value.

(iv) Inventories

Inventories are valued at the lower of cost or their net realisable value on a first in first out basis. The cost of frozen semen includes the direct cost of production.

Livestock inventories, other than breeding bulls, are revalued annually to market rates.

(v) Accounts Receivable

Accounts Receivable are stated at estimated net realisable value.

(vi) Taxation

Income tax expense is recognised on the operating surplus before taxation adjusted for permanent differences between taxable and accounting income. Deferred tax is calculated using the comprehensive basis under the liability method. This method involves recognising the tax effect of all timing differences between accounting and taxable income as a deferred tax asset or liability in the Statement of Financial Position. The future tax benefit or provision for deferred tax is stated at the income tax rates prevailing at balance date.

Future tax benefits are not recognised unless realisation of the asset is virtually certain.

Future tax benefits and provisions for deferred tax are not offset if they arise in different tax jurisdictions.

Any income tax effect of movements in reserves is recognised directly against the related reserve and allocated to deferred or current tax.

(vii) Basis of Preparing Consolidated Financial Statements**Subsidiaries**

Subsidiaries are those entities controlled, directly or indirectly, by the Parent. The financial statements of subsidiaries are included in the consolidated financial statements using the purchase method of consolidation.

Associates

Associates are entities in which the Group has significant influence, but not control, over the operating and financial policies. The Group's share of the net surplus/net deficit of associates is recognised as a component of operating revenue/expense in the Statement of Financial Performance, after adjusting for the amortisation of goodwill arising on acquisition. Dividends received from associates are credited to the carrying amount of the investment in associates. The unamortised balance of goodwill arising on acquisition is included in the carrying amount of the associate.

Partnerships

Partnerships are those relationships that the Group has with other persons whereby the partners carry on a business in common with a view to profit. Where the Group has a controlling interest in a partnership it is accounted for in the consolidated financial statements as a subsidiary. Where the Group has significant influence over the operating and financial policies of the partnership it is accounted for in the consolidated financial statements as an associate.

Joint Ventures

Joint ventures are joint arrangements with other parties in which the Parent has several liability in respect of costs and liabilities, and shares in any resulting output. The Parent's share of the assets, liabilities, revenues and expenses of joint ventures are incorporated into the Parent and consolidated financial statements on a line-by-line basis using the proportionate method.

Goodwill Arising on Acquisition

Goodwill arising on the acquisition of a subsidiary or associate represents the excess of the purchase consideration over the fair value of the identifiable net assets acquired. Goodwill is amortised to the Statement of Financial Performance on a straight-line basis over the period during which benefits are expected to be derived – a period not exceeding five years.

Transactions Eliminated on Consolidation

The effects of intragroup transactions are eliminated in preparing the consolidated financial statements.

(viii) Derivative Financial Instruments

The Group uses derivative financial instruments within predetermined policies and limits in order to reduce its exposure to fluctuations in foreign currency exchange rates and interest rates.

Derivative financial instruments that are designated as hedges of specific items or economic exposures are recognised on the same basis as the underlying hedged items. Where a hedge of an anticipated purchase or sale transaction is undertaken the exchange difference on the hedging transaction up to the date of the purchase or sale transaction, and any costs associated with the hedge transaction to that date, are deferred and included in the measurement of the purchase or sale transaction.

Derivative financial instruments that do not constitute hedges are stated at market value and any resultant gain or loss is recognised in the Statement of Financial Performance.

Where a derivative financial instrument, which is a hedge of an anticipated transaction, is terminated early but the anticipated transaction is still expected to occur, the deferred gain or loss that arose prior to termination continues to be deferred and is recognised as part of the transaction when it occurs. If the transaction is no longer expected to occur, the deferred gain or loss is recognised in the Statement of Financial Performance immediately. The Group does not engage in speculative transactions or hold derivative financial instruments for trading purposes.

(ix) Research and Development Expenditure

Research is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding. Development expenditure is expenditure on the application of research findings or other knowledge to a plan or design for the production of new or substantially improved products or services.

All research expenditure, including biotechnology research, is expensed in the Statement of Financial Performance as incurred.

Development expenditure is recognised as an asset when it can be demonstrated that the commercial production of the product or service will commence. Development expenditure recognised as an asset is stated at cost and amortised on a straight-line basis over five years, being the period of expected benefits. Amortisation begins at the time that commercial production commences. All other development expenditure is recognised in the Statement of Financial Performance as incurred.

(x) Operating Leases

Payments made under operating leases are recognised in the Statement of Financial Performance on a basis representative of the pattern of benefits expected to be derived from the leased asset. Lease incentives received are recognised as an integral part of the total lease payments made.

(xi) Cash and Cash Equivalents

For the purpose of the Statement of Cash Flows, cash comprises cash balances (net of bank overdrafts) and demand deposits. Cash excludes bank bills that are not used as part of the Group's day-to-day cash management.

(xii) Changes in Accounting Policies

Uniform accounting policies have been applied throughout the Group on a consistent basis with those of the previous year.

(xiii) Comparative Information

Certain comparative information has been reclassified in order to provide a more consistent basis for comparison.

Notes to the Financial Statements

for the year ended 31 May 2006

1. Operating Revenue

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Operating revenue comprises:				
Related-party sales revenue	–	–	1,613	1,134
External sales revenue	108,530	102,423	98,646	93,756
Interest income	1,573	1,618	1,788	1,681
Net foreign exchange gain	342	–	39	–
Gain on disposal of fixed assets	26	–	–	–
Total Operating Revenue	110,471	104,041	102,086	96,571

Biotechnology research is net of contract revenues received of \$1.9 million (2005 \$1.4 million).

The unrealised gain arising from the revaluation of livestock is \$0.833 million for the Group, nil for the Parent (2005: \$0.222 million Group; \$0.181 million Parent).

2. Operating Expenses

Note	Consolidated		Parent	
	2006 \$'000	2005 \$'000	2006 \$'000	2005 \$'000
Operating expenses include:				
Interest expense	28	37	24	11
Equity accounted losses of associates	23	7	–	–
Depreciation of fixed assets:				
Buildings	563	528	533	526
Plant and Equipment	3,201	3,149	2,960	2,988
Furniture and Fittings	128	211	125	142
Vehicles	1,377	1,379	1,250	1,318
Computers and Software	4,430	4,378	4,397	4,360
Amortisation of development costs	71	53	71	53
Amortisation of goodwill	321	164	–	–
Impairment of goodwill	571	–	–	–
Amounts incurred and expensed for research – excluding biotechnology research	3,047	3,203	1,784	2,291
Doubtful debts:				
Written off	177	149	47	57
Increase/(decrease) in provision	217	–	–	–
Increase/(decrease) in provisions:				
Employee Entitlements	105	74	83	(12)
Employee Retirement Allowances (Refer Note 9)	51	21	51	21
Operating lease expenses	816	842	508	541
Net foreign exchange loss	–	205	–	38
Loss on disposal of fixed assets	–	559	10	559
Employee remuneration:				
Fees to Directors	485	432	475	432
Fees to National Councillors	84	92	84	92
Staff Salaries and Wages	44,298	42,138	40,654	39,229
Auditors' remuneration:				
KPMG – audit services	80	50	80	50
– other services	94	87	94	87
Clifford Fry & Co – audit services	8	8	–	–
FDC & Associates – audit services	7	–	–	–
Donations	–	–	–	–

This analysis involves disclosure items as required by accounting standards and does not represent a comprehensive listing of all expenses.

3. Taxation

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
(a) Income Tax Expense				
Operating surplus from income tax	7,572	5,296	10,521	6,945
Permanent differences:				
Deductions arising from change in tax status	(1,520)	(1,959)	(1,520)	(1,959)
Other	1,933	534	1,199	152
Tax losses from prior years	(12,318)	(5,939)	(11,965)	(5,842)
Timing differences not recognised	2,340	739	1,765	704
Tax loss not recognised	1,993	1,329	0	–
	(7,572)	(5,296)	(10,521)	(6,945)
Taxable income	–	–	–	–
Tax expense @ 33%	–	–	–	–
Income tax over provided in prior year	–	–	–	–
Total income tax expense:				
Current taxation	–	–	–	–
Deferred taxation	–	–	–	–
(b) Imputation Credits				
Balance at beginning of year			–	–
Income tax paid			–	–
Balance at end of year			–	–
The imputation credits are available to shareholders of the parent:				
Through the parent	–	–		
Through the subsidiaries	98	172		
(c) Tax Losses				
Unrecognised tax losses available for offset against future assessable income:				
	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Tax losses	11,902	22,226	7,276	19,241
Tax saving thereon	3,928	7,335	2,401	6,349

A future tax saving will also arise over approximately three years from the ability to depreciate certain fixed assets from a higher cost or book value for tax purposes than applies for accounting purposes. The associated contingent tax benefit has reduced the current year's tax by \$0.501 million (2005: \$0.646 million) and the balance, which has not been recognised in the financial statements, is \$1.539 million (2005: \$2.04 million).

The ability to utilise these tax losses depends on the generation of sufficient assessable income in the respective tax jurisdictions.

(d) Deferred Tax

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Deferred tax asset				
(liability) not recognised	506	(265)	251	(332)

Outstanding timing differences arising in respect of the current and prior periods are not recognised due to the existence of tax losses in excess of the net deferred tax liability.

4. Inventories

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Semen	1,271	1,536	1,375	1,442
Livestock	2,784	1,264	445	872
Equipment	2,258	2,346	2,186	2,266
Other	312	449	–	–
	6,625	5,595	4,006	4,580

Only that semen projected to be sold in the next financial year has been valued at cost and included in the accounts on the assumption that it is fully useable. All other semen stock has been included at nil realisable value.

5. Investments

	Note	Consolidated		Parent	
		2006 \$'000	2005 \$'000	2006 \$'000	2005 \$'000
Non-current investments					
Shares in listed companies		3	3	3	3
Shares in unlisted companies		53	47	53	47
Investments in subsidiaries		—	—	6,578	2,400
Investment in associates		—	163	—	—
		56	213	6,634	2,450

The market value of shares in listed companies at balance date is \$ 0.002 million (2005: \$0.003 million).

(a) Carrying amount of associates

	<i>Consolidated</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Carrying amount at beginning of year	163	170
Full acquisition of associate	(140)	–
Share of total recognised revenues and expenses	(23)	(7)
Equity accounted value of investment	–	163

(b) Included within the above carrying value is goodwill relating to investment in associate

	<i>Consolidated</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Goodwill arising on acquisition of associate	271	271
Accumulated amortisation	(271)	(253)
Net carrying amount	–	18

(c) Results of associates

Equity accounted earnings comprise:		
Share of surplus (loss) before income tax	(5)	47
Income tax	–	–
Share of net surplus (loss)	(5)	47
Amortisation of goodwill	(18)	(54)
Total recognised revenues and expenses	(23)	(7)

The Group has equity accounted the unaudited result of New Zealand Genetics (IRL) Limited for the seven months prior to full acquisition.

(d) Acquisition of Associate

On 1 January 2006 Livestock Improvement (New Zealand) Corporation Ltd acquired the remaining 50% of the shares of New Zealand Genetics (IRL) Ltd, a company selling bovine semen in Ireland. The contribution of New Zealand Genetics (IRL) Ltd to the consolidated net surplus for the period 1 January 2006 to 31 May 2006 was \$113,142.

The acquisition was accounted for using the purchase method with the resulting goodwill being amortised in accordance with the Group's policy.

The acquisition had the following effect on the consolidated financial position at acquisition.

	2006 \$'000
Current Assets	
Receivables	55
Other current assets	12
	67
Non Current Assets	
Fixed Assets	81
	81
Current Liabilities	
Other current liabilities	6
	6
Net Assets	142
Net assets acquired	71
Cash paid	1,847
Goodwill arising on acquisition	1,776

6. Fixed Assets

	Consolidated		Parent	
	2006 \$'000	2005 \$'000	2006 \$'000	2005 \$'000
Land				
At cost	12,178	6,534	8,786	6,534
Buildings				
At cost	21,773	20,509	21,014	20,509
Accumulated depreciation	(5,528)	(4,985)	(5,512)	(4,985)
	16,245	15,524	15,502	15,524
Plant and Equipment				
At cost	27,688	25,607	26,536	24,936
Accumulated depreciation	(21,308)	(18,335)	(20,779)	(17,965)
	6,380	7,272	5,757	6,971
Furniture and Fittings				
At cost	2,054	1,970	1,949	1,929
Accumulated depreciation	(1,813)	(1,699)	(1,767)	(1,666)
	241	271	182	263
Vehicles				
At cost	10,480	9,642	9,260	9,088
Accumulated depreciation	(6,707)	(6,265)	(6,364)	(6,088)
	3,773	3,377	2,896	3,000
Computers and Software				
At cost	27,912	24,155	27,500	23,930
Accumulated depreciation	(17,167)	(13,379)	(17,048)	(13,275)
	10,745	10,776	10,452	10,655
Total net carrying amount	49,562	43,754	43,575	42,947

In June 2006 land and buildings were independently valued at \$46.7 million.

7. Goodwill

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Balance at beginning of year	381	545	–	–
Arising on acquisition	1,776	–	–	–
Amortised	(321)	(164)	–	–
Impaired	(571)	–	–	–
Balance at end of year	1,265	381		

8. Development Costs

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Balance at beginning of year	183	233	171	224
Costs capitalised	1,319	3	1,316	–
Amortisation	(71)	(53)	(71)	(53)
Balance at end of year	1,431	183	1,416	171

Development costs arise principally from the Group's activities in developing software for the business.

9. Provisions

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	<i>Note</i>	<i>Consolidated</i>		<i>Parent</i>	
		<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Current					
Employee Entitlements	9(a)	2,172	2,062	1,968	1,881
Sire Proving Rebates	9(b)	1,208	1,247	1,208	1,205
Dividends	9(c)	–	–	–	–
		3,380	3,309	3,176	3,086
Non Current					
Employee Entitlements	9(a)	1,146	1,099	1,146	1,099
Sire Proving Rebates	9(b)	3,112	2,861	2,777	2,592
		4,258	3,960	3,923	3,691

A dividend was declared post balance date and therefore does not reflect in year end accounts.

(a) Provision for Employee Entitlements

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Balance at beginning of year	3,161	3,066	2,980	2,971
Additional provision made	2,856	3,167	2,630	2,957
Amount utilised	(2,699)	(3,072)	(2,496)	(2,948)
Balance at end of year	3,318	3,161	3,114	2,980
Current	2,172	2,062	1,968	1,881
Non-current	1,146	1,099	1,146	1,099

The provision for employee entitlements relates to employee benefits such as accrued annual leave and retirement allowances. The provision for retirement allowances is affected by the estimate of eligibility for the allowance (the employee must continue in employment until eligible for National Superannuation). The retirement allowance portion extends out over the next 30 years.

(b) Provision for Sire Proving Rebates

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Balance at beginning of year	4,108	3,474	3,797	3,474
Additional provision made	1,695	2,026	1,671	1,715
Amount utilised	(1,483)	(1,392)	(1,483)	(1,392)
Balance at end of year	4,320	4,108	3,985	3,797
Current	1,208	1,247	1,208	1,205
Non-current	3,112	2,861	2,777	2,592

The provision for sire proving rebates relates to the cost of herd testing daughters resulting from sire proving inseminations. The provision is affected by a number of estimates including the expected number of heifer calves born and raised, and the herd testing options used. The non-current portion is payable within three years.

(c) Provision for Dividends

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Balance at beginning of year	–	–	–	–
Additional provision made	6,361	7,465	6,361	7,465
Amount utilised	(6,361)	(7,465)	(6,361)	(7,465)
Balance at end of year	–	–	–	–
Current	–	–	–	–
Non-current	–	–	–	–

The Directors declared a final dividend in relation to the current year on 12 July 2006 (\$4.876 million). The final plus interim dividend represented 70% of the operating surplus before biotechnology research. However, since the declaration was made after balance date, no provision has been made in this year's accounts. Provisions were made during the year for the 2005 final dividend (\$3.704 million) and the 2006 interim dividend (\$2.657 million). However, these dividends were paid in July 2005 and February 2006, and the provision cleared.

10. Capital

The Parent had 3,278,255 Co-operative Control shares on issue at balance date. The shares have a nominal value of \$1 each. All shares confer identical rights, privileges, limitations and conditions on the holders of the shares. Co-operative Control Shares must be redeemed when a Shareholder has ceased to be, or no longer has the capacity to be, a user of the Parent's products and services. Redemptions can occur either on application for voluntary surrender by the Shareholder or by the Parent pursuant to the Constitution.

The Parent also had 29,528,590 Investment Shares on issue. These do not confer voting rights, but are tradable between Co-operative Control shareholders on the Alternative Board of the New Zealand Exchange Limited (NZAX). Investment Shares were created by a sub-division of existing Co-operative Shares into 1 Co-operative Control and 10 Investment Shares, in April 2004. The Constitution prescribes the minimum and maximum shareholding limits for Investment Shares and the requirement that all Shareholders must sell their total holding of Investment Shares within two years of ceasing to be a Co-operative Control Shareholder.

Earnings per Share

Earnings per Investment Share, after allowing for Co-operative Share dividends, equated 24.7 cents (2005: 17.1 cents).

11. Net Cash Flow from/(used in) Operating Activities

The following is a reconciliation between the surplus after income tax shown in the Statement of Financial Performance and the net cash flow from/(used in) operating activities.

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Net surplus for the year	7,572	5,296	10,521	6,945
Items classified as investing/financing activities				
(Gain)/loss on sale of other non-current assets	(26)	559	10	559
Non-cash items				
Depreciation	9,770	9,698	9,336	9,387
Equity accounted losses	5	7	–	–
Goodwill amortised	892	164	–	–
Movement in working capital				
(Increase)/decrease in inventories	(1,030)	(627)	574	(517)
Decrease/(increase) in other receivables	(1,986)	(1,875)	(4,949)	(1,564)
(Decrease)/increase in other payables	2,035	2,408	1,721	1,282
Net cash from/(used in) operating activities	17,232	15,630	17,213	16,092

12. Foreign Currency Translation Reserve

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	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Balance at beginning of year	32	17	–	–
Difference arising on translation of independent foreign operations	(46)	15	–	–
Balance at end of year	(14)	32	–	–

13. Operating Lease Commitments

The Group has the following future operating lease commitments:

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Non-cancellable operating lease rentals are payable as follows:				
Not later than one year	834	677	418	438
Later than one year but not later than two years	586	456	341	365
Later than two years but not later than five years	856	927	809	896
Later than five years	432	626	432	626
	2,708	2,686	2,000	2,325

14. Financial Instruments

Exposure to currency, interest rate and credit risk arises in the normal course of the Group's business. Derivative financial instruments are used as a means of reducing exposure to fluctuations in foreign exchange rates and interest rates. While these financial instruments are subject to the risk of market rates changing subsequent to acquisition, such changes would generally be offset by opposite effects on the items being hedged.

(a) Foreign Currency Risk

Foreign currency risk is the risk that the value of the Group's assets and liabilities will fluctuate due to changes in foreign exchange rates. The Group is exposed to currency risk as a result of transactions that are denominated in a currency other than the respective Parent's functional currency. Such transactions, which would typically expose the Group to foreign currency risk include exported sales, imported purchases, purchases of certain plant and machinery and offshore investments, which include subsidiaries and associates. The currencies, giving rise to currency risk, in which the Group primarily deals are Great British Pounds, United States Dollars, Australian Dollars and Euros.

The Group's policy is to hedge 90% of all existing net foreign currency exposures more than three months out. The Group hedges its net exposures by using forward exchange contracts. At balance date the Group had the following unhedged currency exposure arising on foreign currency monetary assets that fall due within the next 12 months.

	<i>Consolidated</i>		<i>Parent</i>	
	<i>2006 \$'000</i>	<i>2005 \$'000</i>	<i>2006 \$'000</i>	<i>2005 \$'000</i>
Trade Debtors				
US Dollars (USD)	1,056	345	–	–
Australian Dollars (AUD)	93	–	–	–
Cash Balances				
US Dollars (USD)	159	126	85	126
Great British Pounds (GBP)	21	11	21	11
Australian Dollars (AUD)	8	380	8	–
Euros (EUR)	178	–	178	–

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(b) Interest Rate Risk

Interest rate risk is the risk that the value of the Group's assets and liabilities will fluctuate due to changes in market interest rates. The Group is exposed to interest rate risk primarily through its cash balances and advances.

(c) Credit Risk

Credit risk is the risk that the counterparty to a transaction with the Group will fail to discharge its obligations, causing the Group to incur a financial loss. The Group is exposed to credit risk through the normal trade credit cycle, advances to third parties and through the use of derivative financial instruments. No collateral is required in respect of financial assets. Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. Reputable financial institutions are used for investing and cash handling purposes. A sum of \$11.2 million is deposited with Westpac (2005 \$10.9 million) and a further \$5 million with Kiwibank (2005 \$10 million) and \$3 million with ASB (2005 \$3 million). At balance date there were no other significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying value of each financial asset in the Statement of Financial Position. The maximum exposure to credit risk arising from amounts receivable under forward exchange contracts is nil (2005: \$0.503 million) and for amounts payable under forward exchange contracts is \$1.367 million (2005: \$0.893 million).

(d) Fair Values

The fair values of the Group's financial instruments do not differ significantly from their carrying values shown in the Statement of Financial Position.

15. Contingent Liabilities

In the normal course of business, Livestock Improvement is subject to claims against it. All claims are contested and defended. No provision has been made in these financial statements, as directors do not expect that outcomes from current claims against the Company will have a material adverse affect on the Group's financial position.

16. Group Investments

The Group has the following significant subsidiaries:

Name	Country of Incorporation	Class of Share	Voting Interest Held		Balance Date	Principal Activity
			2006 %	2005 %		
Subsidiaries						
Livestock Improvement (New Zealand) Corporation Ltd	NZ	Ordinary	100	100	31 May	Semen Sales
Livestock Improvement (UK) Ltd	UK	Ordinary	100	100	31 May	Semen Sales
Livestock Improvement Pty Ltd	Australia	Ordinary	100	100	31 May	Semen Sales
LIC Bovine Ltd	NZ	Ordinary	100	100	31 May	Research – non-trading
Animal Breeding Services Ltd	NZ	Ordinary	100	100	31 May	Reproductive Technologies
LIC Deer Ltd	NZ	Ordinary	100	100	31 May	Deer Artificial Breeding
New Zealand Genetics (IRL) Ltd	Ireland	Ordinary	100	50	31 May	Semen Sales

17 Segmental Information

The Parent and Group predominantly provides goods and services to the New Zealand pastoral farming sector.

Any operations conducted outside of New Zealand, only facilitate export sales from domestic operations and are therefore not deemed to be separate geographical segments.

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18. Capital Commitments

No capital commitments exist at balance date.

19. Related Party Transactions

(a) Identity of related parties with whom material transactions have occurred

Note 16 identifies all entities in which the Group has an interest. All of these entities along with the elected Directors are related parties of the Parent.

(b) Types of related party transaction

The Parent enters into transactions with its subsidiaries in the ordinary course of business as follows:

- Treasury; and
- Sales and services.

All Directors, excluding Messrs Lough, Fraser and Waldvogel, are customers of the Parent and purchase products and services for their farming activities on an ongoing and arms length basis.

20. Events after Balance Date

On 12 July 2006 the Directors declared a final dividend, which along with the interim dividend, represented 70% of the operating surplus before net expenditure on biotechnology research (refer note 9). The Record Date for dividend payment is 28 July and payment (on both Co-operative Control and Investment Shares) will be made on 31 July 2006.

21. Adoption of International Financial Reporting Standards

In December 2002 the New Zealand Accounting Standards Review Board announced that New Zealand International Financial Reporting Standards ("NZ IFRS") will apply to all New Zealand reporting entities for the periods commencing on or after 1 January 2007. Entities have the option to adopt NZ IFRS for periods beginning on or after 1 January 2005.

Livestock Improvement Corporation Limited intends to implement NZ IFRS in its annual financial statements for the year ending 31 May 2008.

Transition Management

Livestock Improvement Corporation Limited has started a project to:

- assess the key differences in accounting policies under NZ IFRS and current accounting policies;
- determine the impacts on the financial statements from transition; and
- determine and implement processes to deal with any related business impact

Change in accounting policies on transition to NZ IFRS

Significant differences identified by Livestock Improvement are outlined below. It should not be regarded as a complete list of changes in accounting policies that will result from the transition to NZ IFRS, as some decisions have not yet been finalised where choices of accounting policies are available.

Livestock Improvement has not yet completed an exercise to quantify the effects of the differences in accounting policies discussed below, and is therefore currently unable to reliably quantify impacts on the financial statements, which will arise from transitioning to NZ IFRS. It is possible that the actual impact of adopting NZ IFRS may vary from the information presented below, and the variation may be material.

Livestock Improvement intends to provide further information, including quantifying the impacts of transitioning to NZ IFRS, in the Group's annual financial statements for the year ending 31 May 2007.

(a) Bulls and Database

Currently Livestock Improvement's bull team and database are recognised at the cost attributed to these assets when acquired. No defined economic life is assigned, and they are not amortised.

Under NZ IFRS, agricultural assets are required to be recognised at fair value, which, for the bull team (since there is no ready market) will involve an assessment of its revenue earning capacity. Changes in fair value will be taken to the income statement. It is proposed to treat the database as a finite-life intangible asset, amortised over its assigned life.

(b) Semen Inventories

Currently Livestock Improvement values frozen semen stocks, projected to be sold in the subsequent financial year, at cost, being the direct cost of production. Under NZ IFRS, the cost of harvested agricultural assets is deemed to be its fair value at the date of harvest.

(c) Co-operative Shares

Currently Livestock Improvement's co-operative shareholding is treated as part of its equity (capital). Under NZ IFRS, 'puttable instruments' which give the holder redemption rights, must be classified as a financial liability.

(d) Long Service Leave

Livestock Improvement permanent employees become entitled to special additional holidays after 15, 25 and 35 years of unbroken service. Currently, long service leave is recognised when the conditions for its granting have been met. Under NZ IFRS, it must be accrued on an actuarial basis and a new provision created.

(e) ACC Self-Insurance

Livestock Improvement is a member of the ACC Partnership Programme, under which it assumes part of the liability to an employee for rehabilitation and/or compensation. Currently, this liability is not recognised. Under NZ IFRS, an outstanding claims liability will need to be calculated and recognised.

(f) Goodwill

Currently goodwill is amortised on a straight-line basis over the period during which the benefits are expected to be received, up to 5 years. Under NZ IFRS, goodwill is no longer amortised, but is instead tested for impairment. Goodwill will be allocated to the cash-generating unit (CGU) to which it relates and tested for impairment annually. Impairment losses will be recognised in the income statement.

(g) Deferred Taxation

On transition to NZ IFRS deferred tax is provided using the balance sheet approach rather than the income statement approach currently applied. The balance sheet approach provides for all temporary differences between the carrying amount of assets and liabilities for accounting and tax purposes. Deferred tax will be recognised in the income statement except to the extent that it relates to items recognised directly in equity or as part of a business combination. Currently, future tax benefits are not recognised unless realisation of the asset is virtually certain. Under NZ IFRS, a deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

(h) Financial Instruments

Accounting for financial instruments under NZ IFRS involves some major changes from our current policies. All derivative contracts will be carried at fair value on Livestock Improvement's balance sheet.

If a derivative contract qualifies for cash flow hedge accounting, the effective portion of the fair value movement will be taken to a reserve within equity. All other changes in fair value are recognised immediately in the income statement.

(i) Investments in Shares

Investments in shares held for trading are classified as current assets and are stated at fair value, with any resultant gain or loss recognised in the income statement. Investments in shares that are not held for trading are classified as available-for-sale and are stated at fair value, with any resultant gain or loss being recognised directly in equity.

Other impacts on transition to NZ IFRS

NZ IFRS 1 also allows a number of exemptions to assist in the transition to reporting under NZ IFRS. The explanatory comments below include details of the NZIFRS 1 exemptions Livestock Improvement intends to adopt.

(a) Foreign Currency Translation Reserve

Livestock Improvement intends to deem the cumulative translation differences for all foreign operations to be zero as at 1 June 2006 and thus eliminate the foreign currency translation reserve.

(b) Property

Livestock Improvement intends to deem the fair value of items of property as their cost as at 1 June 2006. It is not proposed to revalue these assets on an ongoing basis.



Audit report

To the shareholders of Livestock Improvement Corporation Limited

We have audited the financial statements on pages 35 to 52. The financial statements provide information about the past financial performance and financial position of the company and group as at 31 May 2006. This information is stated in accordance with the accounting policies set out on pages 38 to 40.

Directors' responsibilities

The Directors are responsible for the preparation of financial statements which give a true and fair view of the financial position of the company and group as at 31 May 2006 and the results of their operations and cash flows for the year ended on that date.

Auditor's responsibilities

It is our responsibility to express an independent opinion on the financial statements presented by the Directors and report our opinion to you.

Basis of opinion

An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. It also includes assessing:

- the significant estimates and judgments made by the Directors in the preparation of the financial statements;
- whether the accounting policies are appropriate to the company's and group's circumstances, consistently applied and adequately disclosed.

We conducted our audit in accordance with New Zealand Auditing Standards. We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to obtain reasonable assurance that the financial statements are free from material misstatements, whether caused by fraud or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. Our firm has also provided other services to the company and certain of its subsidiaries in relation to taxation and general accounting services. Partners and employees of our firm may also deal with the company and group on normal terms within the ordinary course of trading activities of the business of the company and group. These matters have not impaired our independence as auditors of the company and group. The firm has no other relationship with, or interest in, the company or any of its subsidiaries.

Unqualified opinion

We have obtained all the information and explanations we have required.

In our opinion:

- proper accounting records have been kept by the company as far as appears from our examination of those records;
- the financial statements on pages 35 to 52:
 - comply with New Zealand generally accepted accounting practice;
 - give a true and fair view of the financial position of the company and group as at 31 May 2006 and the results of their operations and cash flows for the year ended on that date.

Our audit was completed on 12 July 2006 and our unqualified opinion is expressed as at that date.

Hamilton

Statutory Information

for the year ended 31 May 2006

Activities

The Parent is primarily involved in the development, production and marketing of artificial breeding and herd testing services to the New Zealand dairy industry, the control and maintenance of the Livestock Improvement Database, and the execution of research relating to dairy herd improvement.

The activities of subsidiaries are described in the Directors and Chief Executive's reports.

Directors and Remuneration

Directors of the Parent received the following remuneration:

	Fees \$000
S B Bay	80
J E Bicknell	35
E G Coats	35
B R Guy	35
R D Jackways	35
M E Jagger	35
P J Lynskey	35
A J Reid	35
K D Straight	35
G A Fraser	40
P V Lough	40
J S Waldvogel	35
	475
Directors of LIC Deer Limited were paid the following fees:	
G A Fraser	5
A F Porter	5
	10
Group Total	485

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Entries Recorded or to be Recorded in the Interests Register

(a) Directors' Interests

The following entries were recorded in the Interest Register of the Company and its subsidiaries during the year:

S Bay: Declared that he sold one bull calf to the Company in the 2005/06 season for \$2,500.

S Bay: Declared that he was a participant in the Company's Contract Mating Scheme, which could potentially lead to the sale of one bull calf to the Company in the 2006/07 season for \$2,500.

J Bicknell: Declared that he sold one bull calf to the Company in the 2005/06 season for \$2,500.

J Bicknell: Declared that he was a participant in the Company's Contract Mating Scheme and one Donor Lease Scheme, which could potentially lead to the sale of two bull calves to the Company in the 2006/07 season for \$5,000, and also the sale of a donor in the 2006/07 season for \$1,500.

E Coats: Affirmed that he is a Director of New Zealand Animal Evaluation Limited, Dairy InSight Incorporated, and a member of the Animal Identification and Traceability Governance Group and will therefore be interested in all transactions between this company and Livestock Improvement Corporation and/or its subsidiaries.

M Dewdney: Declared that he was a participant in the Company's Contract Mating Scheme, which could potentially lead to the sale of two bull calves to the Company in the 2006/07 season for \$5,000.

G Fraser: Affirmed that he has been and remains a Director of:

Skellerup Holdings Ltd – Director since May 2002

AgResearch Limited – Director since December 2003

LIC Deer Limited

and will therefore be interested in all transactions between these companies and Livestock Improvement Corporation and/or its subsidiaries.

B Guy: Declared that he sold one bull calf to the Company in the 2005/06 season for \$2,500.

B Guy: Declared that he was a participant in the Company's Contract Mating Scheme, which could potentially lead to the sale of three bull calves to the Company in the 2006/07 season for \$7,500.

M Jagger: Declared that he is a Director of LIC Deer Limited and will therefore be interested in all transactions between this company and Livestock Improvement Corporation and/or its subsidiaries.

P Lough: Affirmed that he has been and remains a Director of:

Tatua Co-operative Dairy Co Ltd – Director since November 2002

Chairman of New Zealand Trade & Enterprise since July 2003

Dairy Equity Limited since June 2006

and will therefore be interested in all transactions between these companies and Livestock Improvement Corporation and/or its subsidiaries.

P J Lynskey: Affirmed that he is a Director of New Zealand Animal Evaluation Limited and will therefore be interested in all transactions between this company and Livestock Improvement Corporation and/or its subsidiaries.

A Reid: Reaffirmed earlier disclosures that he has been, and remains, a Director of:

Dexcel Holdings Limited – Director since March 2001

Dexcel Limited – Director since March 2001

W A Systems Limited

and will therefore be interested in all transactions between these companies and Livestock Improvement Corporation and/or its subsidiaries.

K Straight: Declared that he was a participant in the Company's Contract Mating Scheme, which could potentially lead to the sale of one bull calf to the Company in the 2006/07 season for \$2,500.

All Elected Directors of the Company – are customers and Shareholders of Livestock Improvement Corporation Limited and purchase Products and Services for their farming activities on an ongoing basis.

(b) Share Dealings of Directors

The Directors other than the independent directors (either in their own names and/or in the name(s) of their dairy farming entities) as qualifying users of Livestock Improvement Corporation's products and services are holders of the following shares:

	2006		2005	
	<i>Co-operative Control Shares</i>	<i>Investment Shares</i>	<i>Co-operative Control Shares</i>	<i>Investment Shares</i>
S B Bay	1,751	30,000	1,559	30,000
J E Bicknell	585	6,000	449	6,000
E G Coats	587	4,970	586	4,970
B R Guy	1,135	10,050	1,081	10,050
R D Jackways	1,593	14,130	1,508	14,130
M E Jagger	719	14,820	538	14,820
P J Lynskey	2,448	32,600	1,329	32,600
A J Reid	3,256	64,420	3,189	64,420
K D Straight	816	7,040	747	7,040

Directors did not purchase Investment Shares during the financial year.

(c) Loans to Directors of the Parent and its Subsidiaries

There have been no loans to Directors during the year.

(d) Directors' Indemnity and Insurance

The Parent has issued a Deed of Indemnity and insured all its Directors and Officers against liabilities to other parties (except the Parent or a related party) that may arise from their positions as Directors of the Parent and its Subsidiaries. The indemnity and insurance does not cover liabilities arising from criminal actions.

(e) Use of Company's Information

There were no notices from Directors of the Company requesting to use Company Information received in their capacity as Directors which would not otherwise have been available to them.

Executive Employees' Remuneration

During the year the following numbers of employees received total remuneration, including benefits, of at least \$100,000:

100,000 – 109,999	10
110,000 – 119,999	10
120,000 – 129,999	8
130,000 – 139,999	4
140,000 – 149,999	2
150,000 – 159,999	4
160,000 – 169,999	1
180,000 – 189,999	3
190,000 – 199,999	2
200,000 – 209,999	1
210,000 – 219,999	1
580,000 – 589,999	1

Co-operative Company Resolution

Pursuant to section 10 of the Co-operative Companies Act 1996, the following resolution was passed unanimously at a meeting of the Directors of the Company held on 12 July 2006.

That it be recorded

- Livestock Improvement Corporation Limited ("Company") was registered as a co-operative company under the provisions of the Co-operative Companies Act 1996 ("Act") on 1 March 2002.
- In the opinion of the Board of Directors, the Company has been a co-operative company from that date to the end of the accounting year ended 31 May 2006.
- The grounds for this opinion are:
 1. The principal activity of the Company involves supplying artificial breeding, herd testing, herd recording and other services to transacting shareholders (as that term is defined in section 4 of the Act). Accordingly, the principal activity of the Company is, and is stated in the Constitution of the Company as being, a co-operative activity (as that term is defined in section 3 of the Act); and
 2. Not less than 60% of the voting rights attached to shares in the Company are held by transacting shareholders.

Shareholder Information as at 28 July 2006

Twenty Largest Shareholders of Quoted Securities

	<i>Investment Shares held</i>
South Hilton Ltd	43,070
Christopher John Stark, Allan James Hubbard (Ealing Partnership)	40,800
Rakaia Island Dairies Ltd	40,580
Peter John Lynskey, Carole Joyce Lynskey & Other(s)	32,600
Stuart Bruce Bay, Doris Beth Bay	30,000
Koromatua Holdings Ltd	29,280
Christopher John Stark, Allan James Hubbard (Maronan Partnership)	26,550
Allan James Hubbard, Allan Pye & Other(s)	26,160
Clarksfield Holdings 1996 Ltd	25,380
Lichfield Lands Inc	24,930
Waratah Farms Ltd	23,850
D B Douglas Ltd	23,580
Dairy Heaven Ltd	23,100
Malcolm John Piggott, Rosalie Freda Piggott	23,000
John S Wilson, Brian Gallichan & Other(s)	22,930
David Philip Jensen, Lesley Kaye Jensen, Philip Peter Jensen	22,710
Timothy Pearce Watson, Wendy Jane Watson	22,200
Kennedy Farms Ltd	21,960
Shane Robert Carroll, Nicola Mary Shadbolt & Other(s)	21,930
Douglas Maxwell Lovelace Bull, Teresa Zita Bull	21,750
	546,360

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Size of Shareholding

<i>Holdings</i>	<i>Shareholders</i>	<i>Investment Shares Held</i>	<i>% of Total</i>
1-1,000	2,252	1,347,714	4.5
1,001-2,000	3,381	5,124,911	17.4
2,001-3,000	2,621	6,450,099	21.8
3,001-4,000	1,410	4,871,930	16.5
4,001-5,000	692	3,092,800	10.5
5,001-10,000	916	5,993,686	20.3
Over 10,000	180	2,647,450	9.0
Total	11,452	29,528,590	100.0

Credit Rating Status

The Co-operative currently does not have a credit rating status.

Substantial Security Holders

No persons are substantial security holders of the Company as referred to in Section 26 of the Securities Act 1988.

Donations

The Company made no donations during the year ended 31 May 2006.

Non Standard Listing

Livestock Improvement Corporation Limited has been classified as a Non Standard NZAX Issuer by the NZX, pursuant to NZAX Listing Rule A3.3.3, by reason of it being a co-operative company having a unique constitution which includes provisions having the following effect:

- the acquiring of Investment Shares is restricted to New Zealand dairy farmers who hold Co-operative Control Shares and who purchase qualifying products and services from Livestock Improvement Corporation Limited; and
- holders of Investment Shares have no voting rights (except on matters affecting the rights of Investment Shareholders).

Waivers and Approvals granted by New Zealand Exchange Limited (NZX) in the process of the approval of the Constitution of Livestock Improvement Corporation Limited

Waivers and approvals were granted in respect of the following NZAX Listing Rules:

1. Rule A1.1.2 to allow the definition of "Renounceable" to refer to a Right or offer that is transferable to any other person who is entitled to hold the Securities to which the Right or offer relates.
2. Rule 7.6.4 in Appendix 1 to allow clause 3.6.6(c) of the Constitution to permit financial assistance to be given to an Approved Holding Entity.
3. Rule A4.2.1 is not applicable in the case of LIC, given its status as a Non Standard NZAX Issuer and as such LIC is not required to comply with the restrictions of that rule and clause 20 of the Constitution which provides for a more extensive lien on Securities is allowed.
4. Rule B2.1.2 to allow for the following aspects of the Company's corporate governance structure:
 - (a) Directors to be nominated by Co-operative Control Shareholders by region;
 - (b) certain qualifications to be required of Directors;
 - (c) the nomination procedure for Directors.
5. Rule B2.1.3 to allow for the filling of casual vacancies by the Board where the position becomes vacant less than 8 months before the date on which that Director is due to retire by way of rotation.
6. Rule B2.1.6 to allow for the rotation of Elected Directors as set out in clause 1(f) of schedule 3 of the Constitution whereby one-third are due to retire on the 1st day of June in each year and a rotation schedule is provided for in paragraph 1(g) of schedule 3.
7. Rule A4.6.5 allows an NZAX Issuer to include restrictions on the issue, acquisition or transfer of Equity Securities in its constitution, subject to the prior approval of NZX. NZX approved restrictions in the Constitution as follows:
 - (a) Clause 3.2.2 restricts the issue of Voting Securities with the aim of ensuring that LIC remains a co-operative company controlled by its Co-operative Control Shareholders (whose control is directly proportionate to the amount of products and services purchased by each such shareholder).
 - (b) Clause 3.2.3 restricts the issue and transfer of Securities so that they are only held by Users (or by other persons in certain specified circumstances). Again, this aims to protect the fundamental nature of a co-operative company.
 - (c) Clauses 10.1(b) and (d) place restrictions on the persons who may hold Investment Shares (so that such shares are only held by a Co-operative Control Shareholder, an Approved Holding Entity or the Company itself, or by other persons in certain specified circumstances).
 - (d) Clauses 10.2 to 10.7 (inclusive) and clause 13.5 relate to the acquisition and disposition of Investment Shares and, in particular, provide for the regulation of the minimum and maximum holding requirements for Investment Shares. Such provisions are intended to regulate the identity and interests of the shareholders, as is common for a co-operative company.
 - (e) Clause 24 lists matters, which require the consent of the Minister for Agriculture and Fisheries (or other relevant Minister). This provision is required by the Dairy Industry Restructuring Act 2001 and must therefore take precedence over all other provisions in the constitution and the Listing Rules.
8. The NZX has approved differences in text between certain Listing Rules and the provisions of the Constitution as follows:
 - (a) Clause 3.5.1(a) reflects Appendix 1 Rule 7.3.1(a). However that Rule only requires approval to be given by the classes of Quoted Equity Securities. As the Investment Shares are the only class of shares proposed to be quoted, clause 3.5.1(a) requires the approval of each class of Equity Securities, regardless of whether or not they are quoted.
 - (b) The rules in Appendix 1 Rule 7.3.3(b), Appendix 1 Rule 7.6.3(a) and Rule A4.3.2(b)(i) (which all relate to issues of securities before 1995) have not been included in the Constitution because, as a matter of fact, these provisions do not apply to the Company.
 - (c) Where the Listing Rules contain provisions which only apply to the issue of securities to, or holding of securities by, employees of the NZAX Issuer (e.g. Appendix 1 Rules 7.3.2(a), 7.3.6, and 7.6.5(b)), these provisions have not been replicated in the Constitution as employees of the Company are not permitted to own shares in the Company and, to the extent Directors are categorised as employees, it is not proposed that an issue of securities ever be made to Directors as a separate class.
 - (d) Where the Listing Rules refer to Minimum Holdings, these provisions have not been replicated in the Constitution as the minimum and maximum holding requirements in respect of the Co-operative Control Shares and the Investment Shares (and the issue or surrender of shares to meet those requirements) are expressly set out elsewhere in the Constitution. This means that the Rules in Appendix 1 Rule 7.3.4(e), Appendix 1 Rule 7.3.8(c), Appendix 1 Rule 7.6.2 (which is otherwise dealt with in clause 3.6.3) and Appendix 1 Rule 7.6.3 (which is otherwise dealt with in clause 3.6.4(b)) are not included in the Constitution.
 - (e) Clause 21 reflects Appendix 1 Rule 9.1. However, the definition of the "Average Market Capitalisation" has been amended to take account of the fact that it is only the Investment Shares which will have a market capitalisation value and that therefore the nominal value of the Co-operative Control Shares will be added to such value.
 - (f) Paragraph 6.1 of Schedule 1 reflects Rule A5.1.7; however it applies to notices of meetings of shareholders rather than to Quoted Security holders.

Disclosure of Financial Assistance as required under the Companies Act 1993

1. **Dividend Reinvestment Plan:** Livestock Improvement has provided financial assistance to those shareholders who elect to participate in the Dividend Reinvestment Plan ("Dividend Plan") by agreeing to pay to the Guardian Trust Company of New Zealand Limited ("Guardian Trust") as the Approved Holding Entity the services and administration fees and brokerage and commission costs incurred for the purposes of the Dividend Plan. ABN AMRO Craigs Limited ("ABN AMRO") has been appointed as the Broker to purchase the Investment Shares on the NZAX market for the purposes of the Dividend Plan, and the moneys paid by Livestock Improvement to Guardian Trust as Approved Holding Entity will include the administration fee, brokerage and commission costs of ABN AMRO. Livestock Improvement is required to make disclosures to all shareholders in respect of this financial assistance. The exact amount of the costs depends upon the extent to which shareholders participate in the Dividend Plan. However the total amount of costs in the next twelve months is estimated to be in the region of \$45,000.

In relation to the financial assistance provided for the Dividend Plan, the Livestock Improvement Board resolved on 5 May 2006 that Livestock Improvement should provide the financial assistance referred to above ("Dividend Plan Financial Assistance"), and that the giving of the Dividend Plan Financial Assistance is in the best interest of Livestock Improvement and is of benefit to shareholders not receiving that financial assistance; and that the terms and conditions under which the Dividend Plan Financial Assistance is given are fair and reasonable to Livestock Improvement and to the shareholders not receiving that financial assistance. The grounds for the Board's conclusions are:

- (a) the Dividend Plan Financial Assistance enables Livestock Improvement to provide shareholders with an efficient means of acquiring additional Investment Shares in Livestock Improvement without incurring transaction costs which they would otherwise incur;
- (b) the Dividend Plan Financial Assistance is available to all eligible shareholders, giving equal opportunity to participate in the benefits of the Dividend Plan;
- (c) shareholders who do not participate will not be diluted or otherwise disadvantaged as no new shares are being issued under the Dividend Plan;
- (d) the additional Investment Shares will be purchased by ABN AMRO at the NZAX market price and participating shareholders will pay the average NZAX market price paid by ABN AMRO on market for those Shares;
- (e) the Dividend Plan will enhance the liquidity in the market for the Investment Shares, providing a more liquid market for both participating and non-participating shareholders wishing to sell those Shares;
- (f) the Dividend Plan enables Livestock Improvement to offer Shareholders a mechanism to reinvest dividends in Investment Shares without resulting in unnecessary new capital being raised through the issue of new shares; and
- (g) the amount of financial assistance is minimal in comparison to the benefits arising out of the Dividend Plan for shareholders and Livestock Improvement.

2. **Minimum Investment Shareholding Requirement:** Guardian Trust has also been appointed by the Livestock Improvement Board as the Approved Holding Entity to acquire Investment Shares on behalf of or in order to sell Investment Shares to Co-operative Control Shareholders to enable them to meet their obligations in respect of the Minimum Investment Shareholding Requirement ("Minimum Investment Plan"). ABN AMRO has also been appointed by Guardian Trust as the Broker for the purposes of the Minimum Investment Plan. It is desirable that, as far as practicable, ABN AMRO should purchase Investment Shares for the Dividend Plan and the Minimum Investment Plan as a single pool on the same terms and conditions and accordingly Livestock Improvement proposes to pay costs, brokerage and commission in respect of the Minimum Investment Plan on the same basis as for the Dividend Plan. The exact amount of these costs will depend upon the number of transactions which are made. However the total amount of costs in the next twelve months is estimated as being in the region of \$20,000.

The Livestock Improvement Board resolved on 5 May 2006 that Livestock Improvement should pay the annual services fee of Guardian Trust and all fees, brokerage costs and commission incurred by Guardian Trust for the purposes of the Minimum Investment Plan ("Minimum Investment Plan Financial Assistance"); and that the giving of the Minimum Investment Plan Financial Assistance is in the best interest of Livestock Improvement and is of benefit to shareholders not receiving that financial assistance; and that the terms and conditions under which the Minimum Investment Plan Financial Assistance is given are fair and reasonable to Livestock Improvement and to the shareholders not receiving that financial assistance. The grounds for the Board's conclusions are that:

- (a) it is in the interest of Livestock Improvement and of all shareholders that Livestock Improvement acquire new shareholders and the Minimum Investment Plan Financial Assistance assists in achieving this as follows:
 - the Minimum Investment Plan Financial Assistance encourages dairy farmers to become members of Livestock Improvement by providing them with an efficient means of acquiring the Minimum Investment Shareholding Requirement without incurring transaction costs which they would otherwise incur;
 - the Investment Shares purchased by ABN AMRO for the purposes of the Minimum Investment Plan will be purchased at the NZAX market price and the shareholders for whom the Investment Shares are purchased will pay the average NZAX market price paid by ABN AMRO on market for the Shares;
- (b) shareholders who have met their obligations in respect of the Minimum Investment Shareholding Requirement will not be diluted or otherwise disadvantaged as no new shares are being issued;
- (c) the amount of financial assistance is minimal in comparison to the benefits arising out of the Minimum Investment Plan; and
- (d) it is efficient and cost effective for ABN AMRO to purchase Investment Shares for the Dividend Plan and the Minimum Investment Plan as a single pool on the same terms and conditions, and accordingly it is desirable for Livestock Improvement to pay costs, brokerage and commission in respect of the Minimum Investment Plan on the same basis as it is obliged to do in respect of the Dividend Plan.

APPENDIX I

Livestock Improvement's Share Structure

Livestock Improvement's dual share structure comprises Investment Shares and Co-operative Control Shares.

In general terms, Investment Shares confer the assets of the Co-operative, the right to receive profit distributions and can be traded on the NZAX by Co-operative Control Shareholders at market determined prices, but have no voting rights (except as described below).

In contrast, Co-operative Control Shares have voting rights, may receive a priority dividend akin to a first mortgage interest rate and a priority payment on liquidation, and can only be surrendered to the Co-operative at the nominal issue price of \$1.00 per share.

More specifically, the features of both classes of share are as follows:

Co-operative control shares

- Are issued pursuant to the Co-operative Companies Act 1996 and have a nominal value of \$1.00 per share.
- Have a voting entitlement of one vote per share except in the case of the election of National Councillors where the voting entitlement is one vote per Shareholder in the relevant Ward.
- Can only, and must, be held by dairy farmers who have a Livestock Improvement Debtor's Code and purchase at least \$500 of qualifying products and services from the Co-operative per season, and earn income from the supply of milk to a licensed milk processor in New Zealand.
- Must be held to the value of 4% of the value of the previous season's purchases from the Co-operative of qualifying products and services.
- Are not tradable but can be transferred in certain circumstances with the prior written approval of the Livestock Improvement Board.
- Are issued by the Co-operative and are subject to surrender at the request of the Board or of a Shareholder in accordance with co-operative principles.
- Receive a dividend (if any is declared by the Board) in priority to dividends on the Investment Shares up to a maximum amount equal to the first mortgage lending rate of the Co-operative's principal bankers in respect of secured loans made to dairy farmers.
- Rank ahead of Investment Shares in the event of a liquidation with the payment being limited to repayment of the nominal value of the Co-operative Control Shares less any amount unpaid on those shares.
- Have no right to participate in the profits or assets of the Co-operative except for priority dividend payments and payment on liquidation.

Investment Shares

- Do not have a nominal value.
- Are entitled to dividends and to the profits and assets of the Co-operative subject to the priority rights of the Co-operative Control Shares.
- Have no voting rights (except where any resolution will affect the rights of Investment Shareholders).
- Can only be held by Co-operative Control Shareholders, the Co-operative, or the Approved Holding Entity or its broker on behalf of new Shareholders or for the purpose of the Dividend Reinvestment Plan.
- Must be held by Co-operative Control Shareholders who must hold between 2 and 30 Investment Shares for each Co-operative Control Share held.
- Are listed and quoted on the NZAX and can be traded at market determined prices.
- Entitle a holder to receive reports and financial statements and attend meetings of Shareholders.
- Must be sold within two years once a Shareholder ceases to be a Co-operative Control Shareholder.

APPENDIX II

Description of Dividend Reinvestment Plan

1. Introduction

In May 2006, the Board of Directors of Livestock Improvement Corporation Limited approved the adoption of the Livestock Improvement Corporation Limited Dividend Reinvestment Plan ("Plan").

The Plan enables shareholders to reinvest the net cash dividends after tax ("Net Proceeds") payable on all of their shares in Livestock Improvement Corporation Limited by acquiring further Investment Shares.

These Plan Shares will not be new Investment Shares issued by Livestock Improvement Corporation Limited, but will be existing Investment Shares purchased on behalf of Participants through market transactions on the NZAX Market. Livestock Improvement Corporation Limited has appointed The New Zealand Guardian Trust Company Limited ("Guardian Trust") to administer the Plan, and that company has appointed ABN AMRO Craigs Limited ("ABN AMRO") as the Broker to acquire the Plan Shares on behalf of Participants.

The main terms and conditions of the Plan are now summarised.

2. Participation

- (a) Participation in the Plan is optional and open to all shareholders except:
 - those who exceed the 30:1 ratio of Investment Shares to Co-operative Shares;
 - shareholders who are required to sell their Investment Shares and no longer trade with Livestock Improvement Corporation Limited;
 - Directors of Livestock Improvement Corporation Limited and their associated persons;
 - shareholders whose shares are subject to a sale notice issued by Livestock Improvement Corporation Limited in exercise of its lien; and
 - shareholders who have not acquired the minimum number of Investment Shares required to be held by them – their dividends will be applied to acquire that minimum number and when the minimum number has been acquired, the dividends may be used for participation in the Plan.
- (b) To participate in the Plan, a shareholder must complete the application form which accompanies the Offer Document. A copy of this document can be obtained from the Company Secretary of Livestock Improvement Corporation Limited, email: shares@lic.co.nz.
- (c) An application will continue to be effective for all subsequent dividends paid until terminated or amended.

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3. Operation of the Plan

- (a) By participating in the Plan, each Participant directs Livestock Improvement Corporation Limited to pay to Guardian Trust the Net Proceeds of every cash dividend payable or credited on all the Shares registered in the Participant's name.
- (b) Guardian Trust shall instruct ABN AMRO to acquire existing Investment Shares by on market transactions through the NZAX Market.
- (c) The purchase price to Participants of the Investment Shares acquired shall be set by Guardian Trust and shall be the volume weighted average price paid to ABN AMRO for the Investment Shares. Where this would result in a Participant being entitled to less than a whole Share, part Shares will be rounded up or down in an equitable manner so as to enable all of the Plan Shares to be allocated.
- (d) In respect of each dividend paid by Livestock Improvement Corporation Limited, ABN AMRO will endeavour to use all of the Net Proceeds of that dividend to purchase Investment Shares, and Guardian Trust will then transfer to Participants the Investment Shares purchased using those Net Proceeds. This must be completed at least one month before the record date for the next dividend.
- (e) If, for any reason, a Participant does not receive all or any of the Plan Shares to which the Participant is entitled, then Livestock Improvement Corporation Limited will pay to or credit the Participant with the amount of the Net Proceeds of the dividend payable or credited on the Participant's Shares that the Participant did not receive in Plan Shares if that amount is \$2.00 or more. Amounts less than \$2.00 will be forfeited to Livestock Improvement Corporation Limited to meet expenses of operating the Plan.
- (f) Interest on moneys held by Guardian Trust or ABN AMRO in the course of administering the Plan shall be paid to Livestock Improvement Corporation Limited to meet expenses of operating the Plan.
- (g) Any dividends paid on Plan Shares prior to transfer to a Participant will be held on behalf of and paid or credited to that Participant.

4. Statements to Participants

- (a) Livestock Improvement Corporation Limited will send to each Participant, on each dividend payment date, a statement detailing:
 - the number of Shares held by the Participant;
 - the Net Proceeds of the cash dividend to be reinvested in Investment Shares;
 - the amount of any taxation deduction made;
 - advice as to the amount of any imputation or other taxation credits; and
 - such other matters required by law with respect to dividends and/or reinvestment.

- (b) Within 5 Business Days after each transfer of Investment Shares to Participants under paragraph 3(d) above, Livestock Improvement Corporation Limited will send to each Participant a statement detailing:
- the Net Proceeds of the cash dividend reinvested;
 - the number of Plan Shares the Participant has acquired;
 - the average price of the Plan Shares acquired by the Participant; and
 - the amount (if any) paid or credited to the Participant pursuant to paragraph 3(e) above.

5. No Costs to Participants

No brokerage or commission costs will be payable by Participants subject to clause 3(e) above.

6. Termination of Participation by Participant

A Participant may at any time, by giving written notice to Livestock Improvement Corporation Limited terminate participation in the Plan.

7. Modification, Suspension and Termination by Livestock Improvement

Notice of any modification, suspension or termination of the Plan by Livestock Improvement Corporation Limited will be given to all Participants.



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