

# Change needs new mindset

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Trading among farmers (TAF) will drive the mindset of Fonterra's governors, managers and farmers away from cooperative principles towards being a farmer-owned business – a distinctly different structure from what it is today, according to cooperative specialist Onno van Bekkum.

Netherlands-based van Bekkum, one of the keynote speakers at the International Cooperatives Conference, is also the author of a report for the Fonterra Farmers Protecting Our Co-op group.

While he agrees that the fair value share system, whereby farmers take their full value in the cooperative with them when they leave, is a “millstone around Fonterra's neck” he doesn't believe TAF is the way to solve it.

The structure brings to the fore conflicting organisational principles integrating into a single system both the cooperative and stock market models. The increased status of the investment model would push return on investment to top of mind in management and governance thinking, he said.

While it now looks like TAF will proceed, being able to recognise these behaviours and control or make calls against them would be important to the continuing protection of the co-op, he said.



Onno van Bekkum – doesn't believe TAF is the solution.

**'The market behaviour of external investors will influence the pace at which New Zealand dairy farmers can grow their farms and supplies to Fonterra ...'**

No structure is ever set in concrete and Fonterra's chair Sir Henry van der Heyden has said if TAF doesn't deliver as expected the cooperative can unwind it within two years. So looking out for signs of the problems foreshadowed in van Bekkum's report will be important over the next two years.

In his report van Bekkum warns that TAF could encourage a shift in management focus too far in favour of driving profits. “Beware of executive

incentive payments being linked to the share price,” he said.

Language and attitudes could change so that milk is seen as cost factor rather than a source of farmers' and the country's wealth creation.

He also suggested looking out for increasing tensions between cooperative members who will have a greater diversity in investment profiles. Some will have a maximum of dry shares, others will only have wet shares, some will have fund units and there will be many who will have a mix of each.

Governors will be working for masters with a much greater range of needs than ever before.

Van Bekkum believes the structure will induce a higher share price that will ultimately incentivise members to sell the economic rights of their shares and disincentivise milk growth and new entrants to the cooperative.

The market behaviour of external investors will influence the pace at which New Zealand dairy farmers can grow their farms and supplies to Fonterra. He points out that people aren't born cooperative, and opportunists who don't have the long

term, inter-generational view of being a cooperative member aren't protected against in TAF.

Instead the structure encourages free-riding behaviours that Fonterra has labelled flexibility, he warned.

Van Bekkum had never seen a cooperative that actively encouraged its members to sell their shares as they were being encouraged to do with the Fonterra shareholders fund (FSF).

Up to \$500m worth of shares would be linked to the fund which was half the amount the board was worried about protecting against with redemption risk. Van Bekkum warned farmers to be wary if the regulations and restrictions designed to protect them within TAF begin to be blamed for stagnation of the fund as the next step could be to convince them the restrictions need to be relaxed.

“That would be the slippery slope then towards loss of ownership.”

The fact one third of Fonterra's milk solids voted against the proposal would have Fonterra's governors' eyes wide open and trust now had to be put in them to also be on the lookout for unwanted outcomes of TAF.

# Tension drives success

Bob Edlin  
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Two Fonterra directors, Nicola Shadbolt and John Wilson, acknowledged the importance of a healthy tension and robust debate within the co-op when addressing the conference on the role of cooperatives and mutuals in economy and society in Wellington in June.

Shadbolt said Fonterra shareholders had an intense desire to discuss ownership and control, “and that's what keeps cooperatives alive”.

Wilson likened cooperative membership to being part of a big family, “with all the foibles of a typical reality TV show family”. He had just been engaged in the rounds of farmer meetings before the vote on trading among farmers (TAF). He described these as a “a magnificent engagement and discussion of the key issues within our cooperative”.



Nicola Shadbolt – long term view of world.



John Wilson – like a reality TV show.

**'We must listen to what our shareholders say and make sure our farmers have every chance to understand the issues before us at any time.'**

the issues before us at any time.

“That's what we call healthy tension.”

It led to real consensus and to ensuring the company could move forward cooperatively. Diversity must be celebrated, not squelched.

“Passion” was a key element of cooperative membership, too, Wilson said. He and his brother are the third generation of a dairy-farming family.

“And we have benefited greatly over the years by being both suppliers and owners of our cooperative,” he said.

It hadn't been easy and there had been major challenges. But “a co-op model for us as dairy farmers is the only possible solution ... it just makes sense at every level”.

Shadbolt said Fonterra had a long-term view of the world. It was structured to discourage short-term opportunism, and it was a social construct. It was rare in any business for managers to be told they must pay the most they possibly can for inputs and make a profit.

“It creates a wonderful tension and drives a fantastic efficiency,” she said. “So we have the long term, we have efficiency drivers and we have this sort of egalitarian construct within that business model.”

Shadbolt said one of her students at Massey University had examined the differences between cooperative and corporate businesses. The big point of difference was mutuality – “the co-op is about the collective good, the mutual benefit”.

Social cohesion and balancing the interests of different factions had its challenges, she said.

This – and loyalty – were “a critical difference”.

Referring to the TAF debate, Shadbolt said farmers had a keen desire to discuss ownership and control, “and that's what keeps cooperatives alive – it keeps them very vibrant”.

How else could they re-invent the cooperative, without a debate about what the reinvention should look like?

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