Looking to the future

ZESPRI® ORGANIC Kiwifruit

NOVEMBER 2009
3-Year Outlook
At a glance

The organic kiwifruit category fills a valuable premium niche in the ZESPRI portfolio but has a significant challenge ahead to manage supply increases and optimise performance with constrained market growth opportunities.

ZESPRI® GREEN ORGANIC Kiwifruit volumes supplied are projected to significantly increase to between 3.9 million and 4.0 million trays in 2010 and 4.3 million trays by 2012, while ZESPRI® GOLD ORGANIC Kiwifruit is projected to increase to between 0.75 million and 0.85 million trays by 2012. At the same time, the impact of the economic recession is expected to continue to be felt in major markets including Europe and North America into 2010.

ZESPRI's key response to the increasing supply of organics is to focus sharply on extending organic distribution to maximise retail reach.

2010 to 2012 Trends

Productivity and Costs

<table>
<thead>
<tr>
<th>Productivity and Costs</th>
<th>Trend</th>
</tr>
</thead>
<tbody>
<tr>
<td>On orchard costs</td>
<td>-</td>
</tr>
<tr>
<td>Grower yield</td>
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</tr>
<tr>
<td>Post-harvest costs</td>
<td>-</td>
</tr>
<tr>
<td>Oil cost</td>
<td>-</td>
</tr>
<tr>
<td>Freight</td>
<td>-</td>
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<tr>
<td>Promotional expense</td>
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Supply and Demand

<table>
<thead>
<tr>
<th>Supply and Demand</th>
<th>Impact</th>
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<tbody>
<tr>
<td>Northern hemisphere supply</td>
<td></td>
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<tr>
<td>Southern hemisphere supply</td>
<td>-</td>
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<tr>
<td>New Zealand supply</td>
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</tr>
<tr>
<td>ZESPRI demand</td>
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Financial Impacts

<table>
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<tr>
<th>Financial Impacts</th>
<th>Impact</th>
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<tbody>
<tr>
<td>Foreign exchange impact on returns</td>
<td>-</td>
</tr>
<tr>
<td>Global economic environment</td>
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Market Impacts

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<th>Market Impacts</th>
<th>Impact</th>
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<tr>
<td>Fruit consumption per capita</td>
<td>-</td>
</tr>
<tr>
<td>Kiwifruit category share of fruit bowl</td>
<td>+</td>
</tr>
<tr>
<td>GREEN ORGANIC OGR per hectare</td>
<td>+</td>
</tr>
<tr>
<td>GOLD ORGANIC OGR per hectare</td>
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</tbody>
</table>

*Net Orchard Return (NOR)*

Arrow colour and direction indicates expected future trend.
Red   : negative
Green : positive
Symbol : stable

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Overview

ZESPRI® ORGANIC Kiwifruit plays an important role as a premium niche within the ZESPRI® Kiwifruit product range, offering consumers a natural choice to suit their lifestyle and an alternative to conventional products. Organic growers play a lead role in developing and piloting sustainable production initiatives as they strive to maximise the production of premium ZESPRI® ORGANIC Kiwifruit while protecting the natural environment.

Organic fruit and vegetable sales have been through a difficult 12 months in all major markets as the underlying economic conditions have accelerated a value trend. Premium products, including many organic lines, have been under pressure and in some cases delisted by retailers as consumer spend has reduced and consumers have reprioritised discretionary spending. Regular organic eaters have typically continued to purchase organics with an increased focus on value while some less frequent organic consumers have bought less or moved away from organics. These trends have seen the double digit growth rates for organic products fall significantly and a decline in some markets including the United Kingdom.

In 2009, the strength of the ZESPRI® Brand and unified industry’s ability to deliver premium superior-tasting fruit has provided a strong platform and resilience through difficult market conditions. To drive growth and performance ahead, ZESPRI is implementing a series of strategic initiatives including an enhanced focus on consumer health and consumer-focused promotion to increase the number of regular eaters and repeat purchase rates. The health platform underpinning the brand essence of ‘pure vitality from within’ is a natural fit for ZESPRI® ORGANIC Kiwifruit, offering all the health benefits of ZESPRI® Kiwifruit and delivered from a pure production system free of chemicals and artificial inputs.

The short to medium-term outlook for ZESPRI® GREEN ORGANIC Kiwifruit sees a low rate of demand growth as economies recover from the impacts of the recession. A real challenge for the ZESPRI® ORGANIC Kiwifruit category will be to manage supply increases in line with the limited opportunities for market growth. ZESPRI® GREEN ORGANIC Kiwifruit supply is projected to increase steadily to 4.3 million trays by 2012, up from 2.9 million in 2008. Supply growth is driven by an additional 66 producing hectares currently in conversion to organics, and a projected increase in average yields that will continue to underpin supply growth beyond 2012.

In order to maximise sales of the increased crop, ZESPRI will sharpen its focus and resource to drive ZESPRI® ORGANIC Kiwifruit category performance to optimise opportunities in primary and secondary markets while supporting our entry and growth in developing markets. In the current economic climate it is important to work closely and support our existing distribution partners and retail customers as these strong long-term relationships underpin the ZESPRI business. In addition, ZESPRI is focused on achieving growth over the next three years in our secondary markets of Italy, France, and the United States, through continued distribution gains and recruiting consumers into kiwifruit.

Emerging opportunities in new and developing markets such as China and South East Asia are expected to provide growth opportunities for ZESPRI® GREEN and GOLD ORGANIC Kiwifruit.

Direct competition from Chilean organic growers is expected to increase and we are already seeing an increased presence of competing organic kiwifruit, particularly in Europe and the United Kingdom.

New cultivars are expected to provide niche opportunities for ZESPRI® ORGANIC Kiwifruit growers with several organic growers involved in the trials to understand how the new cultivars perform in an organic production system.
Priority Category Issues and Strategic Focus Overview

ZESPRI has identified a number of key issues facing the GREEN and GOLD ORGANIC category, and a number of strategic focus areas to address these issues and, in particular, increase GREEN ORGANIC growers’ profitability.

Priority Category Issues

1. Managing ZESPRI® GREEN ORGANIC Kiwifruit supply in line with limited demand growth
   - The projected supply increase of ZESPRI® GREEN ORGANIC Kiwifruit through orchard conversions and yield increases, at a time when we have limited growth opportunities in developed markets, is expected to place pressure on organic returns as incremental volumes are sold in developing markets and later in the season. Growth rates in organic demand are expected to pick up as economies recover from the economic recession, however, the timing of this is unknown.

2. Pressure on premiums through an underlying value trend, magnified by the global economic crisis
   - The organic customer base continues to be polarised between retailer/distributors who want to position themselves as offering premium niche products and an increasing trend in the current economic environment of customers determined to drive the price of organics down to a more affordable everyday level for consumers.

3. Determining the opportunities for new cultivars produced organically
   - ZESPRI expects new ZESPRI cultivars to offer opportunities to both organic growers and organic customers in the future. Organic orchards are included in new cultivar trials to understand how they perform in an organic production system.

4. The ZESPRI® ORGANIC Kiwifruit point of difference is reducing, relative to the ZESPRI conventional offering
   - Conventional growers are finding it an easier leap to “go organic”, while the markets have relatively few tangible points of difference over and above the ZESPRI® Brand platform to justify price premiums to customers.

Strategic Focus Overview

Marketing and Market Development
- Proactively supporting key distributors and retailers to raise the profile of organics (refer to page 3)
- Strengthening the health platform (refer to page 3)
- Growing secondary and emerging markets
- A strong focus on organic distribution
- Strategic development of in-market resource and focus on organic distribution
- Increased focus on consumer marketing
- Sustainability from soil to spoon
- Further development of the Taste ZESPRI® programme
- Ongoing focus on our 12-month supply programme, ensuring New Zealand growers are supported by securing year-round shelf space
- Support of collaborative marketing programmes that positively assist market development

Supply Chain
- Ongoing focus on driving down manageable costs throughout the supply chain (refer to page 3)
- Overcoming South Korea market access constraints

Innovation
- Investment in new cultivars (refer to page 3)
- Develop compostable packaging and fruit labels
- Orchard productivity
Strategic Focus
Snapshots of key areas

Proactively supporting key distributors and retailers to raise the profile of organics

ZESPRI has had recent success at growing organic demand in Japan through supporting key distributors and maintaining strong direct relationships with key retail customers. This includes bringing key customers to New Zealand to understand more about our production systems, our growers, and the purity of our natural environment. Continuing to build and leverage these relationships is a priority in Japan, and the approach will be evaluated and applied in other key markets.

ZESPRI recognises that the organic category is a speciality product right along the supply chain. In 2007, ZESPRI appointed a new organic distributor in the United States to ensure appropriate specialist focus and support on organic customers. ZESPRI's General Manager Asia has tasked each of his country marketing managers to work in partnership with ZESPRI's ORGANIC Category Manager to take a special interest and identify new ZESPRI® GREEN ORGANIC Kiwifruit distribution opportunities. In Europe, ZESPRI's General Manager Europe is to engage a research agency to conduct a distribution audit on ZESPRI® ORGANIC Kiwifruit in the first half of 2010 and update our knowledge on the changes the recession has driven. The regional Market Managers will then work with the ORGANIC Category Manager to identify and pursue growth opportunities.

Strengthening the health platform

ZESPRI® GREEN and GREEN ORGANIC Kiwifruit has a strong health association with consumers and there is significant potential to build on this platform. Some initial research into the health attributes of kiwifruit presents exciting opportunities for ZESPRI® GREEN Kiwifruit. The first phase of research to help support our ‘digestive aid’ platform has demonstrated that eating ZESPRI® GREEN Kiwifruit as part of a meal may improve the digestion of protein – improving overall digestion. In addition, Vitamin C from ZESPRI® GREEN and GOLD Kiwifruit has been shown to have 10 times the uptake and delivery by the tissues than that of a supplement. This research is in the early stages, but is very exciting for use in immunity and natural protection in the future.

We are now focused on developing motivating consumer messages that are substantiated by the new and significant scientific research that we have invested in. ZESPRI® ORGANIC Kiwifruit is a natural fit with the ZESPRI health platform giving consumers the choice of benefiting from all of the health benefits of ZESPRI® Kiwifruit, delivered from a pure organic production system.

Ongoing focus on driving down manageable costs throughout the supply chain

Focusing on supply and operational planning processes

Land, labour and shipping costs mean New Zealand is a relatively high cost producer. Of course these are offset by some of the best growing conditions globally and the decision by New Zealand growers to market the produce as a premium offering through their brand ZESPRI.

While this strategy is primarily focused on maximising market returns, cost management remains a component of maximising grower returns. Three of our industry’s biggest controllable costs are onshore fruit loss, condition checking and repacking. If these costs could be entirely eliminated, then Fruit and Service Payments for GREEN ORGANIC growers would be 4.8 percent higher, and Fruit and Service Payments for GOLD ORGANIC growers would be 4.3 percent higher. ZESPRI is working closely with post-harvest operators to target these costs through developing the industry’s sales and operational planning processes to support optimal inventory management and minimal order iterations.

Investment in new cultivars

New cultivars are an exciting area for the industry as we position ourselves for future growth

With four cultivars in grower block trials (the final stage before commercialisation), attention is now being directed towards identifying a licensing process that will enable growers to take up the opportunity that new cultivars present.

The block trial cultivars are about extending the sales window for ZESPRI® GOLD Kiwifruit and taking to market an earlier, sweeter, more-consistent-tasting green. All four of these new cultivars represent a real opportunity for ZESPRI® GREEN and GOLD ORGANIC Kiwifruit growers. While further research is needed to understand the opportunities and the risks of each variety, they do have the potential to increase returns by stimulating consumers, the category and ultimately our brand.

ZESPRI expects new cultivars to offer new opportunities to both organic growers and organic customers in the future. Organic orchards are included in new cultivar trials to understand how they perform in an organic production system and at least one of the varieties is showing signs that they could be suited to organic production with naturally larger fruit size and yield.
Single Point of Entry  
– Adding Future Value for Growers

The Single Point of Entry into markets creates significant value for the kiwifruit industry. It means that New Zealand kiwifruit growers are not competing with each other, undercutting quality and supply and driving down pricing to the level of the weakest seller. Kiwifruit growers have chosen this integrated structure in order to maximise their returns from the market.

The Single Point of Entry supports significant investment in the brand and in promotional activity, which in turn drives consumer demand and retail distribution. It allows a managed approach to market allocation and phasing of supply, avoiding flooding profitable markets with oversupply as so often happens with fruit trading. Quality standards are maintained through the season and reinforce the ZESPRI® Brand promise to consumers.

Most importantly, a combination of our scale and the Single Point of Entry provides a tremendous platform for future wealth creation. Not only can we invest heavily in a breeding programme (in expectation of future returns) to create the cultivars of the future, but when we do develop outstanding new products we have the scale, brand and market position to commercialise them effectively as we have done with ZESPRI® GOLD. Plant Variety Rights without the Single Point of Entry will not optimise value because returns from premium cultivars will be quickly undermined by ‘me-too’ varieties and weak selling.

In tough market conditions such as we are experiencing in 2009, growers can see first-hand, in comparison to other industries, how the Single Point of Entry provides an effective buffer against turbulent price movements and value destruction.

In addition to the strategic benefits of the Single Point of Entry to growers as outlined above, the ZESPRI operation is very cost efficient from an overheads perspective. Commission levels are kept low to channel more money back to grower/shareholders.

For the 2010/11 Season, ZESPRI’s net commission calculates to 7.4 percent of total net sales. This is a 31 percent reduction from 10 years ago when the commission was 10.7 percent:

<table>
<thead>
<tr>
<th>Year</th>
<th>Net Sales</th>
<th>Net Return</th>
<th>Total Commission</th>
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<tbody>
<tr>
<td>1999</td>
<td>9 percent</td>
<td>3.6 percent</td>
<td>12.6 percent</td>
</tr>
<tr>
<td>2009</td>
<td>6 percent</td>
<td>6 percent</td>
<td>12 percent</td>
</tr>
<tr>
<td>2010</td>
<td>6 percent</td>
<td>6 percent</td>
<td>12 percent</td>
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Investment in research and development has doubled from $4.8 million 10 years ago to a forecast $9.6 million in the 2009/10 Season. As a proportion of ZESPRI’s corporate net margin, this represents a 31 percent increase.

For the 2010/11 Season, it is estimated that ZESPRI’s margin will be utilised as follows:

- Innovation investment: 0.7 percent
- ZESPRI overheads: 5.8 percent
- Profit before tax attributable to shareholders for NZ supply: 0.9 percent
- ZESPRI’s net margin as a percentage of net sales: Total 7.4 percent
Trends and Statistics

Competitors
- Chile is the predominant direct competitor for ZESPRI® ORGANIC Kiwifruit with the majority of competition coming from conventional kiwifruit or other organic fruits.
- The Chilean organic volume is increasing significantly in line with the Chilean conventional kiwifruit crop. Already there is an increased presence of Chilean organic kiwifruit in Europe and the United Kingdom, competing head-to-head with ZESPRI® Kiwifruit.

Supply and Demand
- ZESPRI® GREEN ORGANIC Kiwifruit supply is projected to increase from 3.5 million trays in 2009/10 to between 3.9 million and 4.0 million in 2010, and approximately 4.3 million trays supplied by 2012/13 (compared with forecast sales of 4.2 million trays in 2012/13). Driving the growth is an additional 66 hectares of ZESPRI® GREEN Kiwifruit currently in conversion to ZESPRI® GREEN ORGANIC Kiwifruit while yield growth is projected to average 3.5 percent per annum.

Foreign Exchange Rates
We are coming out of a favourable cycle for both foreign exchange and oil which has been supporting the underlying performance of ZESPRI® ORGANIC Kiwifruit.

Supply Chain Costs
Total supply chain costs are expected to increase by $0.31 per tray (3.0 percent) from 2009 to 2012.

N.B. All costs are based on the ZESPRI® 3-year plan assumptions from October 2009.
*Arrow colour and direction indicates expected future trend.
Red: negative  Green: positive  Symbol: stable

*Net Orchard Return (NOR)
**Grower Economics**

**Orchard Gate Return (OGR) per Hectare**

- **ZESPRI® GREEN ORGANIC Kiwifruit**
  - On-orchard costs are forecast to increase three percent per annum on average (from $21,500 estimated in 2009/10).
  - Average post-harvest costs are estimated to be $21,600 per hectare this season.

- **ZESPRI® GREEN ORGANIC Kiwifruit average OGR per hectare for 2009 is currently forecast (October 2009) to be $40,521.**

- **ZESPRI® GOLD ORGANIC Kiwifruit**
  - On-orchard costs are forecast to increase three percent per annum on average (from $27,200 estimated in 2009/10).
  - Average post-harvest costs are estimated to be $34,700 per hectare this season.

- **ZESPRI® GOLD ORGANIC Kiwifruit average OGR per hectare for 2009 is currently forecast (October 2009) to be $83,239.**

- We anticipate flat to moderate growth in OGR over the next three years due to increasing volumes, changing the market mix and a challenging foreign exchange position.

**ZESPRI® GREEN ORGANIC Kiwifruit Yield**

- Yield per hectare is increasing and in 2009 is up 11 percent. This is in part due to a drought in the Waikato region in 2008, although yield increases were recorded in most regions.

- 2009 average yield of 6,995 is approximately 1,000 trays (14 percent) below the conventional average. This is a significant improvement from 2008 when average yield of 6,290 was 23 percent below conventional.

- The top 2009 GREEN ORGANIC yield recorded was 11,370 trays per hectare of average size 32.2.

**ZESPRI® GOLD ORGANIC Kiwifruit Yield**

- Yield per hectare is increasing as a trend with the 2009 average yield of 8,226 up from 7,054 in 2008. The yield deficit to conventional is 2,562 trays per hectare (-24 percent) in 2009, a significant improvement from 4,304 trays per hectare (-38 percent) in 2008.

- The top 2009 GOLD ORGANIC yield recorded was 12,804 trays per hectare of average size 34.0.
Yield per Hectare and Productive Hectares

- Productive hectares for Zespri® Green Organic Kiwifruit growers are forecast to increase 12 percent to 565 by 2012, with average yields increasing to approximately 7,734 trays per hectare.
- Productive hectares for Zespri® Gold Organic Kiwifruit growers are forecast to increase 68 percent, to 89 by 2012, with approximately 9,880 trays per hectare.

Distribution of Performance Across Orchards

- The chart below shows the makeup of each grower’s payments including Fruit and Service and Incentive payments.
- Fruit and Service Payments per hectare are calculated prior to the deduction of post-harvest and on-orchard costs (excluding pack differential costs).
- The Fruit and Service Payments displayed are those payments that have been generated by the particular grower.
- Actual payments received by individual growers may differ slightly due to the pool rules used by their specific supplier.

Compared to the 2008/09 Season, the ‘average’ Zespri® Green Organic Kiwifruit grower is forecast to receive $4,100 more in Fruit and Service Payments per hectare, or 8 percent.

2009 Fruit and Service Payments per hectare for Zespri® Gold Organic Kiwifruit are forecast to increase by $27,100 on average per hectare. Positive contributions from pricing in Asia, foreign exchange and a reduction in costs, mainly freight, have contributed to a $2.53 per tray increase.
Distribution of Performance Across the Top 20 ZESPRI® GREEN ORGANIC Kiwifruit Orchards

- The average yield for the top 20 orchards of 9,700 trays per hectare is 39 percent above the industry average yield of 6,995 trays per hectare.
- 50 percent of the top 20 growers earned KiwiStart incentives and 85 percent of the top 20 growers earn time payments.

![Graph showing distribution of performance across Top 20 growers.]

Distribution of Net Orchard Return Performance

- The graph below shows the spread of grower numbers throughout the country and their expected Net Orchard Return (NOR) based on the October 2009 Forecast. Note that NOR is the amount growers receive after the average ZESPRI, post-harvest and on-orchard costs are deducted.
- For 2009, the top quartile of ZESPRI® GREEN ORGANIC Kiwifruit growers have generated at least $25,300 per hectare NOR with an average yield of 8,700 trays per hectare.
- The lower quartile of ZESPRI® GREEN ORGANIC Kiwifruit growers accounted for 12 percent of the volume with an average yield of 4,100 trays per hectare. Yield in this quartile ranged from 1,583 to 6,591 trays per hectare with the yield for the orchards with negative NOR averaging 2,964 trays per hectare.

![Graph showing distribution of net orchard return performance.]
ORGANIC Premium Components

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<th>GREEN ORGANIC</th>
<th>GOLD ORGANIC†</th>
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<tr>
<td></td>
<td>OGR Per Tray</td>
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<td>In-market Price Premium</td>
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<td>Market Mix</td>
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<td>Offshore Direct Costs</td>
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<td>Promotion</td>
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<td>Onshore Direct Costs</td>
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<td>Onshore Fruit Loss</td>
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<td>Post-Harvest Costs</td>
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<tr>
<td>Other Income (Class II, NSS)</td>
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<tr>
<td>ORGANIC OGR</td>
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</table>

† The ZESPRI® GOLD ORGANIC kiwifruit premium components are based on the actual earnings and costs. Grower payments will differ as ZESPRI® GOLD ORGANIC Kiwifruit is paid from a combined ZESPRI® GOLD and GOLD ORGANIC Kiwifruit pool and receives a $2 premium (purchase differential) over conventional GOLD, resulting in the GOLD ORGANIC OGR per tray being $9.52.

In-market price premiums form the most significant contribution to both the ZESPRI® GREEN and GOLD ORGANIC Kiwifruit premium. For GOLD, this is strongly supported by favourable market mix driven by niche volumes.

Onshore direct costs are significantly higher for both ZESPRI® GREEN and GOLD ORGANIC Kiwifruit relative to conventional, with the higher organic net revenue and grower return incurring a higher cost of ZESPRI margin per tray.
Key Contact People

If you have further questions please contact a member of the ZESPRI Grower Services Team listed below:

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