



Commentary for Appendix 4C

- *Dairy processing sales growing steadily with good prospects.*
- *CDC customer and product diversification continues.*
- *Vertical supply chain integration milk logistics in place.*
- *Dairy farms achieve budgeted milk production and lower feed costs.*
- *Drainage and water retention benefits evident in wet farming environment.*

Farm Operations

Overview

The strategic planning and reporting components of farm management has improved materially under the experienced hands on approach of Operations Manager, Graeme Willis who commenced the role in June 2016 after several years in a similar role with another corporate dairy farming group and a lifetime in the Victorian dairy industry managing and owning family farms.

The individual farms have live-on farm managers who have advanced their own management and farming skills now focus their management efforts largely on the day-to-day operations for each farm, with particular emphasis on the health and welfare of the livestock and ensuring that all cows maintain premium production condition throughout the whole year. Graeme undertakes and co-ordinates the reporting, budgeting, feeding plans, herd management, pasture plans, capital investment budgeting and planning in conjunction with the Farm Managers before reporting back to the directors.

Their combined efforts and clear management direction, together with the above average growth rates for October and November has been reflected in solid milk production resulting from very healthy and well managed herd. Management is anticipating a successfully planned autumn “peak” that will see strong milk production from fresh cows to benefit milk supply through 2018.

The extensive capex spent on the farm pastures, drainage, laneways, water storage and irrigation as well as machinery, has transformed AHF’s properties, which are regarded as among the most resistant in their regions for extreme seasons. This will be measured by and reflected in each farm maximizing production and ultimately in the values of the farms.

Weather and Seasons

This winter and spring seasons in the South West Victoria regions where the AHF farms are located have experienced almost 150% of their average seasonal rainfall. For farms not properly drained for fast run-off, this level of consistent rainfall in relatively condensed periods, would typically have meant a material decline in production, animal health and a significant damage to pasture.

All the AHF properties have enjoyed an enormous benefit from the extensive and well-planned drainage work



ABOVE: Drumborg V-Drains 2hours and 24hours after rainfall

undertaken in the previous dry summer, which was 90%, completed just before the wet season arrived. Although soils were wet, surface water drained off quickly during winter and spring reducing pasture damage from being sodden and from livestock movement. Laneways were relatively free from mud during the worst of the season – and the cows were happy with that.



ABOVE: Drumborg V-Drains before and after refurbishment

Some of the photographs in this commentary show the really major difference that the drainage works achieved by eliminating the weeks of water-logging of paddocks that previously killed off new grass and prevented access to cows for grazing or vehicles for harvesting.

The outlook for seasonal rain in 2017 predicted by BOM is to be lower than average for February to April. South West Victoria's local farmers hope to see the "Autumn Break" (the first significant rainfall event of the winter growing season) by Anzac Day 25 April.

Between end of January and the first grass grown after the Autumn Break – late May, there is usually no grass available for livestock on farms that do not have irrigation or suitable surplus feed in the form of silage and hay. Typically, for those farms milking to maintain a flat milk supply, a significant amount of feed is required to be purchased and transported to the farms from the main cropping regions in Northern Victoria and South Australia.

One of the main risks in terms of fodder costs is that the Autumn Break is late and the necessary rain does not arrive in sufficient quantities to enable grass germination and deliver sufficient growth before the onset of winter cold. The high on farm quantities of silage this year, significantly mitigate that risk.

Irrigation installed during last summer is in full operation at Drumborg Farm, watering a fully renovated 30 hectares of pasture under pivot. Grazing of this pasture will be available from early February 2017.

Fodder and Feed Costs

The harvesting of grass this spring season has resulted in available silage of 1.3 tonnes per cow, which significantly exceeds silage harvesting in an average year. However the quality at 70% is not as high as desired because the grass growth was so rapid and continuous that the livestock could not consume it quickly enough to maintain grass heights at the most nutritious shorter levels until it could be harvested. With 1.3 tonnes per cow in stock, silage supply will be able to be carried over to the next season.



ABOVE LEFT: Cropping the silage, and ABOVE RIGHT: Anaerobic storage for silage

Purchased feed

The higher than average rains have also resulted in significant extra production of Lucerne, Lupins, Canola as well as cereal and protein hays throughout Victoria and South Australia, which has kept downward pressure on prices. Management has moved to lock in fixed prices on much of the needs for the summer and autumn period. Examples are:

- Cereal hay costs down 50%.since July 16 peak.
- Protein hays such as Lucerne are down 20%.
- Wheat grain price down 40% - locked in until June with low risk of any short-term rise.
- Lupins down 30% locked in for Autumn usage.
- Canola locked in at low of \$380. Price has risen since on US soy price increase.
- Very large stocks of lower quality hay in market will hold that end of the market down for some time.

Notwithstanding the attractive prices and supply volumes, there is always a seasonal risk and prices usually increase at Autumn and Spring milking peaks.

Feeding Regimes

Each farm has a different feeding regime suited to the farms and for efficiency comparisons:

- Drumborg Farm – focus is on predominantly grass feeding production with supplement protein.
- Brucknell North – feeding high lupins for protein. Feeding higher Lupin level to reduce Lucerne hay requirement as comparison with Ecklin South.
- Brucknell South – feeding Lucerne hay for protein plus silage.
- Ecklin Farms – feeding Lucerne and Vetch hay for protein plus silage



Above: Wet silage stacks



ABOVE: Ecklin South – Holstein herd in paddock

Value of 13-13.5 megajoules per kg of dry matter. It is generally a cheaper form of protein feed than Lucerne hay. Lupins are of the legume or pea family and an ideal feedstuff for both sheep and cattle. It is completely safe to feed, it is rich in both protein, and energy has a crude protein value of about 30% and a metabolizable energy.

Milk Collection and Segregation – Irrefutable Traceability

Milk collection for the AHF farms and supply to Fonterra ceased on 31 December 2016 with a very seamless and trouble free transition to Australian Consolidated Milk Pty Ltd (ACM), which made the first milk collection for all AHF farms around dawn on the first day of 2017. This was achieved with helpful cooperation from Fonterra management. All milk pickups transitioned without incident as result of good planning and prior orientation between tanker drivers and farm managers.

ACM is an Australian owned company that collects milk from their farmer suppliers and delivers directly to end-user customers in the domestic and export markets. ACM has been a key supplier to Camperdown Dairy from the day CDC commenced operations in 2010.

The arrangement with ACM allows for a high degree of flexibility for AHF and CDC to enable the use of milk produced on AHF farms to be used in the processing and manufacture of milk products by CDC. In particular, the agreement with ACM enables the segregation of milk from one farm from the milk from other farms.

Specialty Milk Types

Now that Brucknell North Farm is producing Jersey milk and the Drumborg Farm is targeted for another segregation type, CDC is able to bottle or package premium branded Jersey milk and milk products, which have been segregated in transport and processing to provide a clear and direct line to the farms, the cows that produce the milk and the individual Farm Managers. This particular opportunity can be expanded to include Organic Milk and other organic milk products. These premium products can be branded as CDC products or specific retailer brand product.

Jersey Milk is considered to have a higher degree of milk stretching capacity and is highly regarded in making high quality coffee drinks – both hot ones and cold ones.

Milk processed and packaged for domestic and export by CDC can be produced from farms in respect of which we can provide a transparent and irrefutable traceability to the farms and cows and farm managers who produced the milk.

All of these attributes are differentiating factors, which demand a price premium that discerning consumers are willing to pay.

These initiatives capitalise on the small enough / big enough flexibility that CDC has and large processors mostly do not.



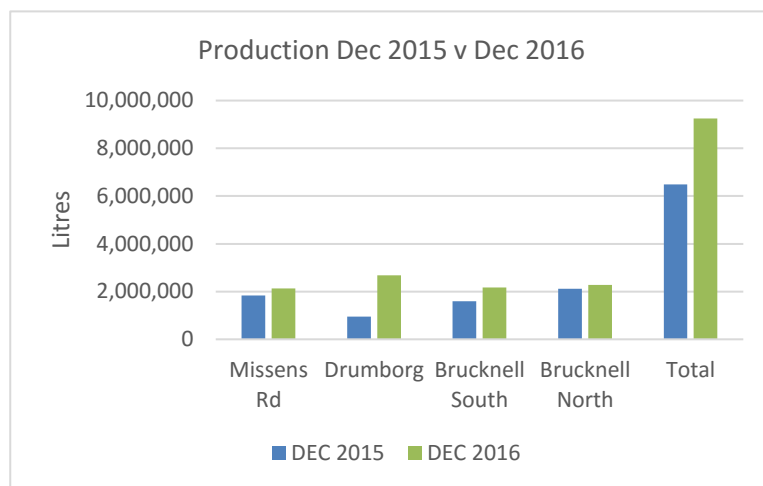
ABOVE (LEFT & RIGHT): Brucknell North Jersey herd has settled in well

Milk Production

The combined production of the dairy farms have achieved strong milk volume production of 9.25 million litres during the six months to 31 December 2016 with 5.04 million litres in Q2. This volume reflects the lower milk volumes from the Jersey herd on Brucknell North although milk solids productions are in line with expectations as the Jersey cows produce lower milk volumes with higher milk solids per litre than Holsteins. (See above under Livestock).

This result is slightly above YTD budget and is in line with the budgeted production of 16.1million litres for the full 2017 financial year

Farm	DEC 2015	DEC 2016	Variance
Missens Rd	1,833,646	2,129,066	295,420
Drumborg	946,809	2,676,774	1,729,965
Brucknell South	1,594,484	2,168,730	574,246
Brucknell North	2,113,890	2,278,846	164,956
Total	6,488,829	9,253,416	2,764,587



Milk Pricing

Milk price changes reflect very quickly in the markets of dairy cows and dairy farms. When milk prices decline, many farmers move quickly to reduce herd sizes, which leads to larger than usual numbers of good quality cows being offered for sale.

Cow prices can also decline quickly and often provide opportunities for buyers who are looking to change or expand herds. The reverse also applies and currently with the expectation of higher milk prices, farmers are expanding their herds and cow prices are on the increase. AHF has managed to gather a herd of premium Jersey cows at attractive prices in the last year and a half after milk prices declined in 2015 and farmers reduced herd sizes. At the same time, we have also upgraded the Holstein herds.

National production of milk has declined to close to its lowest level as farmers reduced herd size in reaction to the lower milk price. This has occurred internationally as the hubris associated with milk exports to China was deflated and Chinese regulations changed to make it virtually impossible for fresh milk from around the world to enter China.

Export of live dairy heifers declined as China buying eased and it was a good time in the 18 months to rebuild herds of high quality cows.

Milk prices are now on the way up again with reliable market commentators including the CBA suggesting opening prices of \$6.10 to \$6.20 per kilo of milk solids, compared with \$5.10 currently and \$5.60 before the Murray Goulburn rethink of April 2016.

Livestock

Livestock on all farms are in excellent condition and the Autumn calving season is expected to be very successful with herd testing indicating a closely timed calving period.

Drumborg and Ecklin South farms primarily join their herds to concentrate the calving period to the Autumn, when milk production is lowest and feed cost are highest. On the Brucknell farms a split calving system is adopted so that part of the herd is timed to calve in Autumn and some in Spring, which allows cows that don't become pregnant for the Autumn calving can be swapped to the spring calving. It also assists to flatten the total milk production over the combined farms.

As Drumborg has a new irrigation system operational and is a strong pasture producer, it is the logical farm for grass only milk production. Investigations are in train to determine if the current water supply has sufficient capacity to duplicate the existing pivot irrigation equipment to double the total area under irrigation.



ABOVE: Jersey Herd



ABOVE: Mixed Herd



ABOVE: Drumborg Irrigation System

Brucknell North Farm is in the final stages of conversion to a Pure Jersey Herd. The Jersey cow at around 450kg is a smaller animal than the Holstein cow at about 700kg and as a result eats less and has a lower milk production volume. However, the Jersey cow's milk has a higher milk solids (4.75% fat, 3.95% protein) component than the larger Holstein cows (3.7% fat, 3.1% protein).

Jersey milk is favoured as a specialty milk by many baristas for making higher quality coffee with greater consistency of "frothing" after pasteurisation for which a higher price is achieved. Preliminary "stretch testing" of the Brucknell Jersey milk has been undertaken with a view to producing a Jersey brand milk product especially for this coffee *aficionado* market.

Capital Works

The new Pivot irrigation system at Drumborg is now operational with further investigation now being undertaken to confirm if an additional pivot irrigator can be supported by the aquifer on the farm.

In summer 2016, an "experimental" three-phase power converter (to convert two phase power to three phase) was installed at Drumborg, where only two-phase power is provided from the Powercor electricity grid.



ABOVE: 3-Phase Inverter installed on Drumborg farm.

This investment of \$60,000 compared with a \$330,000 grid conversion and a two year wait, has paid off handsomely in the first year by enabling the existing farm infrastructure such as cooling plant and stock water pumps to accommodate a 100% increase in milk production and allowing farm operation to continue during many planned and unplanned power outages common in the area.

Brucknell Farms North and South – Finalisation of drainage work and lane repairs as the farms dry out again this summer.



ABOVE: Brucknell North New Effluent Ponds (before and after)

Dairy processing (CDC) sales growing and achieving budget forecasts

CDC sales YTD2016 have significantly increase from the YTD 2015 comparative (prior to acquisition by AHF) and while fresh milk is the largest sales item, the CDC product range has expanded and sales of yoghurts, butter and cream are gaining momentum are retailing arrangements are secured.

Total sales reached 92.7% of budgeted sales for the half year to December 2016, resulting primarily from later than expected commencement of ranging with retailers.



ABOVE: CDC Range of products currently on the market

On-going negotiation with retailers for expanded and new product ranging continues positively.

CDC has seen continued support for the Farmers Own branded milks through Woolworths stores and strong support for the Camperdown branded milk particularly in regional stores. However, in certain socio-economic demographical regions nationally, there has been a noticeable shift back to the major retailers' \$1.00 per litre branded milk in Q2, as the initial public support has waned.

Since the enforcement by Chinese authorities of strict milk cell counts throughout the whole of the shelf life for fresh milk exports to China earlier in 2016, CDC like almost every other Australian milk company, suspended fresh milk sales for that market to mitigate risk.

AHF is working cooperatively with its Chinese industry partner (as announced on 7 November 2016) to develop a solution which is aimed at resuming exports once the very stringent shelf life regulatory requirements can be safely achieved through technology adaptations. The technology, which requires additional plant, is available currently to achieve this. It has been noted that fresh milk sales for export have been a very small percentage contributor to sales in the past.

Ends.

Further Details

For additional company information or media enquiry matters please contact:

Peter Skene

Group CEO/ Director

Australian Dairy Farms Limited

Mob: +61 4 1859 2330

Email: peterskene@adfl.com.au

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AHF makes ASX market releases at times directors believe it would be helpful or necessary for investors and as required by the Listing Rules. For further information regarding our shareholder communications policy, please refer to our website: www.adfl.com.au

About Australian Dairy Farms Group

Australian Dairy Farms Group (AHF) was Australia's first ASX listed dairy farmer. Its initial focus was on aggregating high quality dairy farms in Victoria, initially in the South Western region with particular emphasis initially, on the famous Dairy Golden Triangle region of South West Victoria between Warrnambool and Colac south of the Princes Highway to the coast around Port Campbell.

In April 2016 the Group completed the acquisition of Camperdown Dairy Company Pty Ltd - ACN 140 640 606 (CDC) – see announcement on <http://www.adfl.com.au/announcements>.

CDC is a wholly owned subsidiary of AHF. The Group is now a vertically integrated milk producer, processor and product distributor in Australia and for export.

Australian Dairy Farms Group is listed as a stapled security comprising one fully paid share in **Australian Dairy Farms Limited (the Company)** and one fully paid unit in **Australian Dairy Farms Trust (the Trust)**. Within the structure, the Company is the operator and manager of the dairy farm properties, which are leased from the Trust as the registered owner.

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