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Institutional Investment in Private Companies

**INFINZ Conference
25 September 2008**



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Focus is on Private Equity – not VC



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1. NZ Private Equity Landscape



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NZ Private Equity

- 6 NZ based, institutional investment grade, PE fund managers
- 18 Australian PE funds have invested in NZ companies
- Australian institutional investors have increased NZ allocations in Australian PE funds from 10% to 40%
- In 2006 30%, and in 2007 20%, of Australian PE capital invested in New Zealand (Source: AVCJ)
- So due diligence on the NZ PE market has been done many times before



NZ Private Equity



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NZ Industry Size

	2006	2007
Committed Capital	\$2.0bn	\$1.8bn
PE Deals Done	\$1.1bn / 35 deals	\$1.1bn / 25deals

Sources: Direct Capital, NZVCA

240 PE deals since 1995 – 100+ MBO's



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Why is NZ Private Equity Growing?

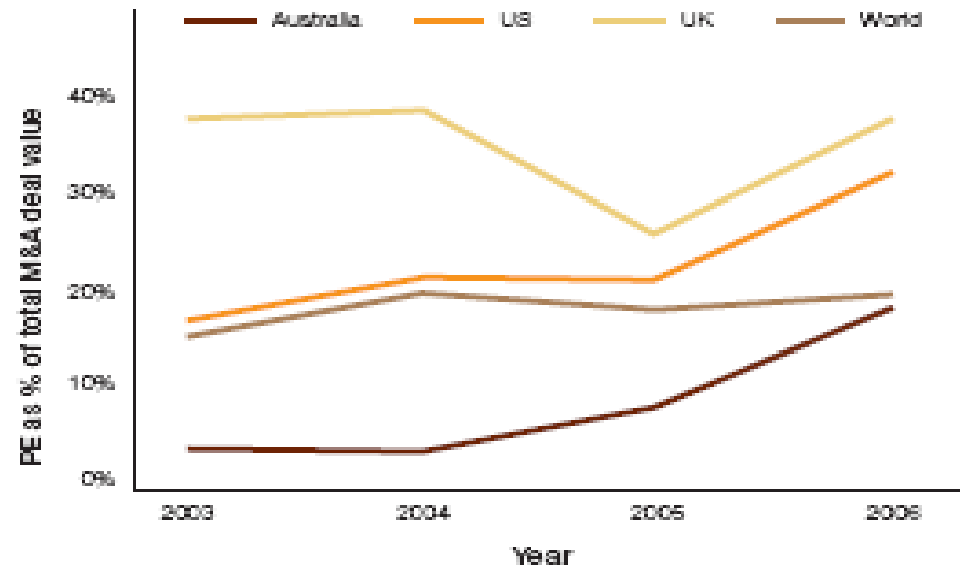
- Huge number of private companies
- Age 55 – 65 ownership
- Not enough trade buyers → PE Capital
- Vendors have done well - MetroGlass, EziBuy, Express etc
- Managers push the concept
- PE funds have made large \$ for investors
- Companies under PE ownership do well
- Large profit generation for advisory community & banks



Market Maturing . . . but still room for growth

- PE activity in NZ as % of M&A is low (M&A as % of GDP also low)
- 6% compared with 21% in AU/US and 30-50% in the UK
- PE will play an increasing role in NZ M&A

Value of private equity transactions as a proportion of total M&A transactions.
Source: Dealogic 2006



Deloitte Top 200

	Listed	Unlisted	% Unlisted
TOP 10	3	7	70%
TOP 50	17	33	66%
TOP 100	31	69	69%
TOP 200	40	160	80%

200th company revenue = \$120m

Source: Management Magazine Dec. 2007

Only 10-15% of NZ GDP generated by NZX companies



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Existing Institutional Investors in NZ PE

- ACC
- NZ Super Fund
- NZ Funds Management
- 1358 Investments (Rotorua Energy Community Trust)
- Development West Coast
- DLJ Funds (Credit Suisse) (US)
- Alliance Bernstein
- Central Lakes Trust
- Industry Funds Management (Aus)
- Quay Partners (Aus)
- Thinking About Tomorrow (Forsyth Barr)
- AMP (Capital Investors and Life NZ)
- ING (and ING Private Equity Access) (Aus)
- Canterbury Community Trust
- Anglican Church Pension Board
- K1W1
- Macquarie (Aus)



Why Are Some New Zealand Institutions Not Investing In Private Equity?

- Not yet researched the market
- Advised not to
- Insufficient resources to implement NZ PE allocation
- Investors going direct to PE funds – guard your pitch!



Quotes From Frank Russell

“Any dramatic fall-back in investor demand in Private Equity is unlikely. According to the 2007-2008 Russell Investments Survey, institutions generally forecast that their strategic allocations to Private Equity will continue to increase through 2009”

“Institutional investors have high expectations for Private Equity and are forecasting double digit returns for the next two years”

“Private Equity managers in the top two quartiles outperform public equities by a significant margin”

**Owns a PE business with NZ\$25bn
under management**



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Quotes From Mercer

“Recommend making additional allocations to Private Equity or initial allocations to infrastructure and timber”

“Pension Funds are generally still very slow to put money to work in alternatives..... with only 4.9% allocated to Private Equity in the U.K.”





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2. Investor Returns



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PE Generates Superior Investor Returns...

Aggregated performance data from NZ and Aust PE managers

NZ Horizon IRR to 30/6/07	3 year	5 Year	
NZ PE (Net IRR, pooled)	24.8%	22.1%	
NZX 50 (Gross)	16.9%	16.7%	
Australian Returns IRR	3 year	5 Year	10 Year
Australia (Private Equity)	33.5%	17.7%	14.9%
S&P/ASX3000 (Accumulation)	23.9%	12.3%	12.8%

Source: NZVIF and AVCAL

NZVCA / EY Monitor data suggests similar performance

- Reported mid market PE IRRs ranging between 40% and 80% (2003-07)



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. . . And Works for Companies

- PE backed companies grow faster
- Increase EBIT faster
- Have higher working capital efficiencies
- Have higher capex





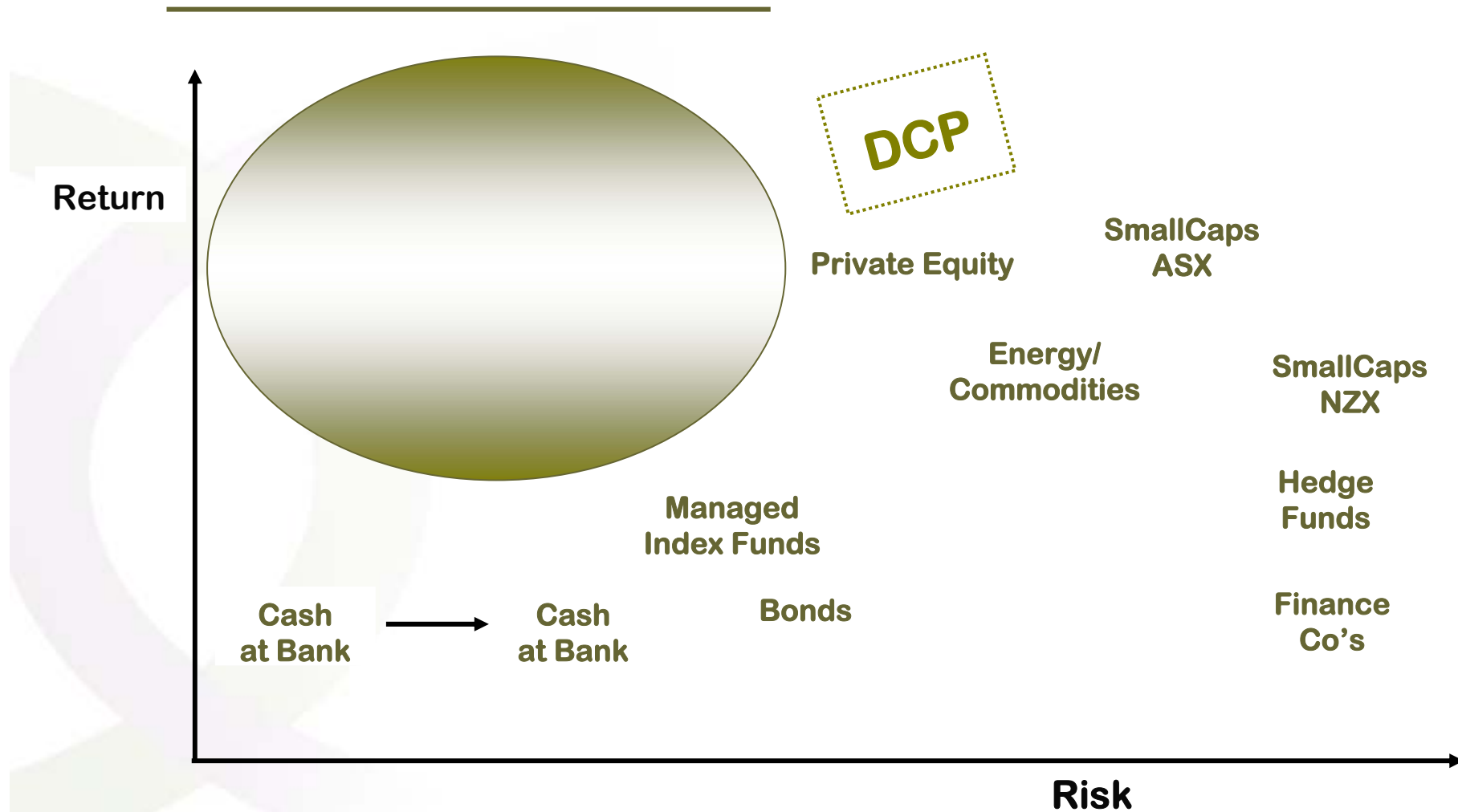
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3. Risk / Return



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Risk / Return



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Similar NZX Risk Profiles (Market Cap)

Abano	\$110m	Pumpkin Patch	\$230m
Allied Workforce	\$15m	Scott Technology	\$35m
EBOS	\$200m	Skellerup	\$120m
Comvita	\$50m	Steel & Tube	\$280m
Delegats	\$220m	Turners & Growers	\$190m
Hallensteins	\$165m	Wakefield	\$125m
Methven	\$100m		

But in private companies - full due diligence available, no insider trading regulations, have a shareholders' agreement, weekly (or better) disclosure, directorship.



Volatility

- Small cap = high volatility

ASX

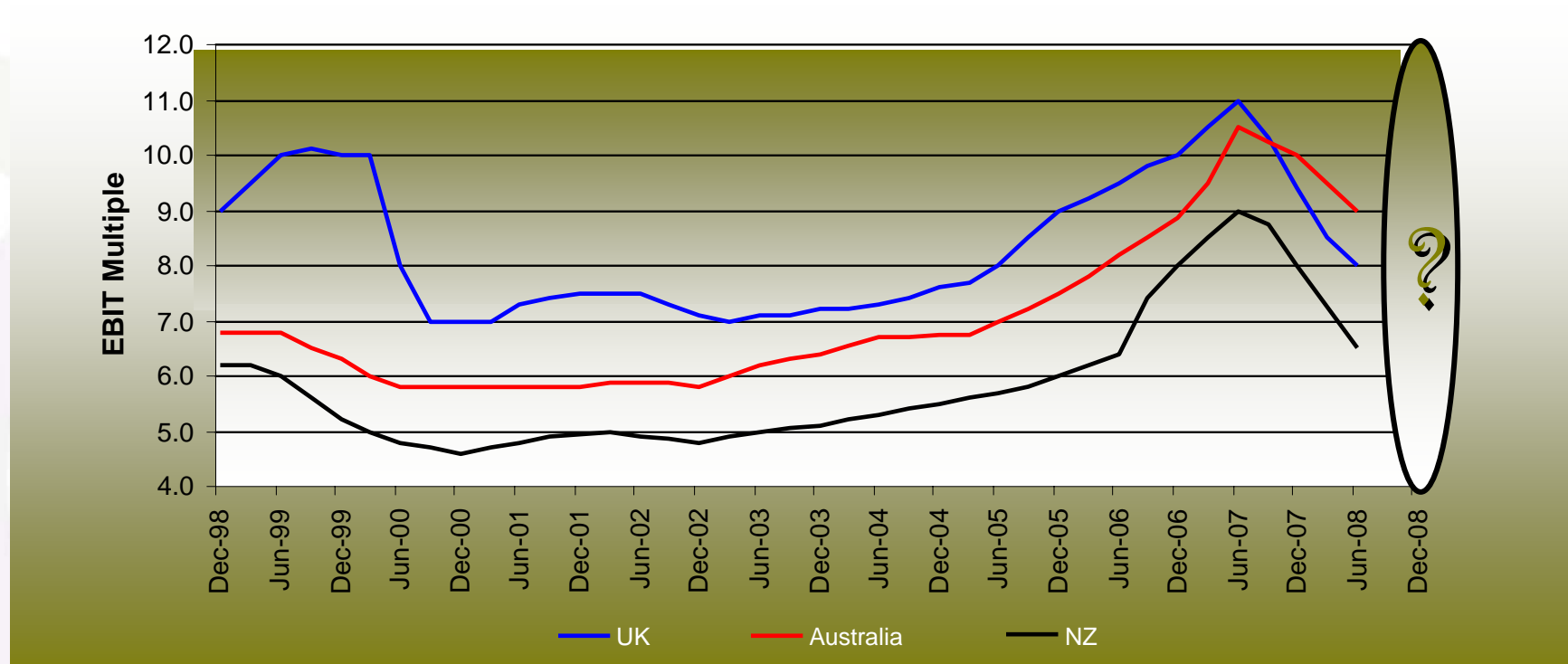
600 companies with market cap under \$200m (June 2008)

- 300 of these 50% below highs
- 180 of these 70% below highs

PE invests in exactly the same types of businesses, but without the stock exchange volatility.



Private Company EBIT Multiples



Source: Venture Capital Association Data, Direct Capital Data, and Large company multiples significantly higher

Interest rates: UK 5.00%

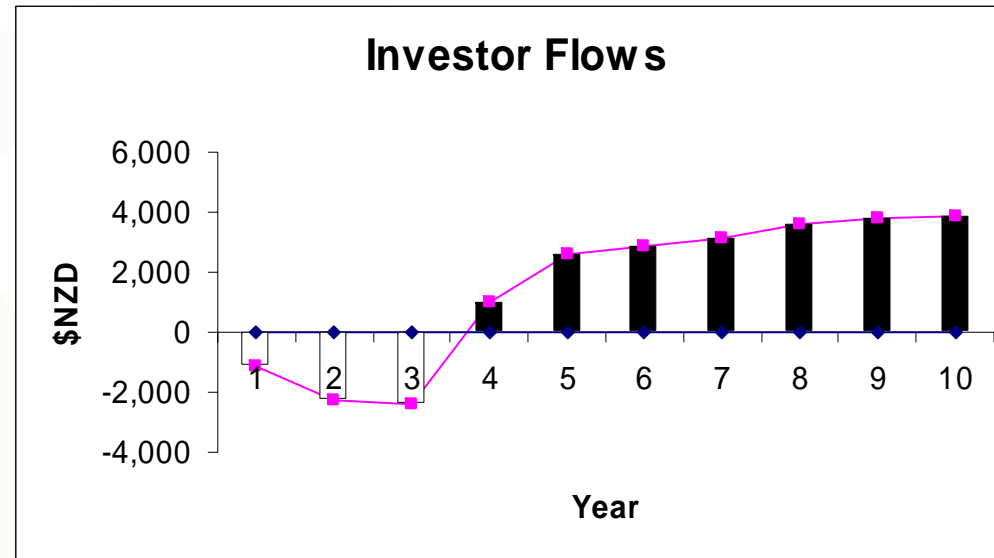
Aus 7.0%

NZ 8.06% as at 8 Sept 2008



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\$10m Commitment to PE Fund



- Private Equity has operated on capital account in NZ since 1993 - all 'big 4' accounting firms and leading lawyers acknowledge capital account status.





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4. Accessing New Zealand Private Equity



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Investors Need to *Start*

- Get advice on market - only qualified advisors are Sydney / Melbourne based
- Returns analysis now factual and comprehensive - 15 year, 10 year, 5 year, 3 year data by fund
- Direct Capital, Pencarrow, AMP, Hauraki, ANZ, Maui all have due diligenced returns data
- Only subjective element is risk for that return

**The key decision for investors in NZ PE is . . .
Manager Selection**



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