Pohutukawa AGM

Tuesday 15th May held at AMB AMRO Craigs' office

Thank you for coming to the annual meeting for Pohutukawa Private Equity, which is part of Direct Capital's private equity fund, DCP III. As you know, Pohutukawa is $53m of a $118.5m private equity programme.

Today, I want to talk to you about three things,

1. the companies we have invested in to date
2. the initiatives we have under way at the moment to invest in new companies
3. the investment climate we are operating in;

and I will give you my views on the private equity industry as a whole.

I will deal with our investments to date in order of investment. We have given some detail in the annual report for the December 31 year. I will expand on that, explain why we invested in the company and discuss trading to date as well.

I will also talk about our most recent investment Paper Coaters, which is not covered in the annual report as it was only settled on the 2nd May.

In the annual report, there is a table for each company and that sets out Pohutukawa's investment in each company. I need to remind you again that Pohutukawa is one component of Direct Capital's private equity fund with the other being DCP III, which is made up of our other institutional investors, such as the New Zealand Super Fund.
So the investment and the percentage held by Direct Capital in each company is larger. For each million dollars Direct Capital invests, $447,000 is contributed by Pohutukawa and $553,000 by DCPIII.

1. COMPANIES WE HAVE INVESTED IN TO DATE:

1. Max Fashions – 64.3%

We invested in Max because of its incredibly strong brand in the women's fashion industry.

Max continues to trade very strongly. For this autumn season Max launched its new advertising campaign 'Woman's Republic of New Zealand'; you may have seen the billboards and magazine advertisements. Certainly Max's customers have been taking notice because for the first quarter of this year sales are up over 20% on the prior year and 10%+ over budget which is an outstanding start to the year.

Last year finished above Direct Capital's base case expectations at the time of our investment and represented a pleasing result.

The recent appointments of Mike Beagley and Sandy Burgham as Managing Director and Director respectively were very positive events for the company. Last year new stores were opened in Queen St, Sylvia Park, Queenstown, Te Rapa and Papamoa, further enhancing Max's strategic position as the leading woman's apparel chain in NZ for the 18-40 year old bracket.

While the current impressive levels of growth are unsustainable, particularly if the economy begins to slow, we continue to believe the outlook for Max is very bright.

2. Express Logistics – 46.2%

Since the Annual Report Express has completed the acquisition of Victory International, a Sydney based international forwarding business. Victory also has branches in Melbourne, Brisbane and the rapidly expanding region of the Gold Coast. Victory will strengthen the service offering for sea freight from Asia and the United States.

Victory was founded by James Sparke and Frank Dugdale who have accepted Express shares as part of the merger of the two Australian businesses. This will ensure the on going contribution of the two founders.

This is a critical expansion for Express and will create a combined business in Australia of $50m. This is another example of the success Direct Capital has had with assisting portfolio companies to expand in Australia. It continues to be a great market for us.

In addition Express will open an office in Los Angeles this month. This is initially to serve our existing apparel customers who both ship directly from China to the United States in addition to shipments from Australia and New Zealand.

Trading remains strong and 13% ahead of the same time last year.

3. NZ Pharmaceuticals – 46.5%

NZP has continued to perform strongly with profit up another 20% this year, despite the high NZD, and EBIT is on track to get close to $20 million.

NZP has also made substantial progress in its focus on broadening its product portfolio, with around 10 separate product lines expected to generate turnover in the millions this year.

A significant event for the company was the opening of its new Glycotherapeutics factory in February. This is the largest capital project in the company's history (involving $10m expenditure) and was funded as part of the Pohutukawa investment process. Worldwide demand for glycotherapeutic products has been estimated as growing by approximately 20% per annum. NZP's expertise in extracting and refining biochemicals has established a firm footing in this niche sector, with glycotherapeutic revenues this year expected to be around $8 million, and the company see significant growth potential for this part of its business.

Finally, NZP has made very good progress towards its planned public listing, which the company is targeting for early 2008. We remain very optimistic about the prospects for this investment.

Gluck – 51.5% (of IFL) IFL holds 20% of Gluck, so DC – 10.3% of Gluck

The investment in Gluck was an example of leveraging off our knowledge and experience in a certain industry sector. Gluck is an Australian based business again and highlights our focus on the Aussie market for investment activity. Our offering to the current Gluck shareholders was compelling.

As Gluck and Express operate in the same industry we have been able to co operate in a number of areas to the mutual benefit of both organizations.

Gluck has expertise in the area of W&D and believe this is a critical offering to customers as they increasingly outsource central warehousing. They are currently building this business from a clean start 12 months ago in Sydney, Melbourne and Auckland. This will take some time to fully reach its potential but Direct Capital supports this important strategic initiative and is in line with global peers.

Gluck has experienced strong top line growth over the last year, but margins to date have not matched this growth as we develop the W & D business.

4. Professional Hearing Services – 42.7%

It is early days for the Professional Hearing Services investment however the transition of the business to the new ownership group has been a smooth one. PHS is a hearing aid retail business, with stores in the Waikato and BOP at present. We think it is a very good business and see a nationwide market opportunity for it.

Pohutukawa has invested alongside other Direct Capital funds plus John Ryder and Howard Bretherton. Both John and Howard are highly experienced businessmen with experience in retail, health and in building large businesses from the ground up. John, Howard and Graeme Dodd who is the General Manager will lead the national expansion of PHS. Already new sites have been identified and we are in discussion with potential acquisitions of hearing businesses in other locations.

5. Paper Coaters – 76.5%

Paper Coaters is Direct Capital's most recent investment. The investment was a succession buy-out in which we acquired the company in a tender process co-investing with management who invested 14% of the equity. Despite pricing competition, we were the preferred acquirer as we had the support of management and are locally based – both important factors for the vendor.

Paper Coaters has one of two specialist manufacturing plants in Australasia that is able to coat plastic and foil on to paper for use in packaging – such as bags, boxes, medical and industrial packaging where moisture control is critical. Food packaging is a particular growth area for the company.

Although the NZ business is relatively mature, Paper Coaters is expanding its business in Australia rapidly and both of these features attracted Direct Capital – a stable earnings base from which to build a large Australasian business. The company achieved revenue of $37m in the last financial year, which we expect to grow, and in addition we anticipate making further complementary acquisitions over time.

BioPacificVentures

You will also recall that Pohutukawa participates in investments made by BioPacificVentures, whose investment mandate is heath through food and agriculture.

We have given you an outline of investments made through BPV in the annual report. It has made 7 investments and has 2 more imminent, which will take it to over 50% committed, and yet it celebrated its second anniversary only a few weeks ago.

Since the annual report was printed, BPV has invested in Novotech, a Sydney based Contract Research Organisation, or CRO. CRO's specialise in performing clinical trials, for drug companies, biotech companies and even food companies. Novotech is Australasia's largest CRO, but was founded only a few years ago. They have aggressive plans for expansion offshore and a very entrepreneurial owner/manager. Our investment is partly strategic, because of the number of clinical trials other BPV companies are doing.

Another investment done since the annual report is Rissington, an agritech company from the Hawkes Bay. Rissington is primarily a sheep genetics company but with an excellent value-adding proposition, which is the supply of custom-bred lamb to large food retail chains. They are negotiating right now to sell a branded lamb product into the UK giant, Marks & Spencer. They also have operations starting up in Latin America.

The next two investments on the cards for BPV are a South Island food technology company and an Auckland based drug development company

It is worth noting too that BPV can invest in food and health businesses together with Pohutukawa and DCPIII, and New Zealand Pharmaceuticals is a very good example of this.

Conclusion

In conclusion, we are very happy with the quality of investments made to date and we are extremely happy with their financial performance. It is a relatively rare occurrence for people in our industry, who, by necessity, invest in a wide range of industries, **when all companies** in a portfolio are performing above their investment budgets. This has, and will continue to be reflected in company valuation uplifts.

When we invested in these companies, we invested a certain amount of Pohutukawa's capital to make the investment. We often committed more than this initial amount to the company, which was designed to cover unforeseen circumstances or underperformance. We have not had to utilise this additional commitment for any of the companies.

2. FUTURE INITIATIVES TO INVEST THE BALANCE OF YOUR CAPITAL.

The mega deals which you have been reading about in the newspapers such as the sale of Telecom's yellow pages, Coles and Qantas in Australia and rumours around some larger NZ listed companies are not deals we are involved in. Our investment mandate is to invest in midmarket private companies in Australia and NZ. We have defined the midmarket as companies with total entity values of $10-150m. This is the size bracket we have historically operated in, and have a strong record in it.

As Jon said, we are planning to make the second Pohutukawa drawdown with the next investment.

Our investment criteria remains unchanged – i.e. companies in Australia and New Zealand with entity values of $10m - $150m. This gives us an extremely wide investment mandate, and we review a large number of opportunities each year.

[When we talk about an entity value of $10m - $150m, we hardly ever buy 100% of a business as we usually invest with management partners, and we utilise bank debt in partnership with our equity. The equity amount we invest in companies is usually substantially smaller than the entity value. For example, if we talk about an entity value of $50m and an investment of 60%, we may only apply about $10m of equity.]

Private Company Networks

Direct Capital has been in the private equity industry since 1994. This means that we know a large number of private companies and their owners in Australia and New Zealand. I have absolutely no hesitation in saying that our private company network in New Zealand is unparalleled.

Very few private equity transactions occur in New Zealand without us knowing about it, and usually having an opportunity to make an investment proposal. We have thirteen investment professionals in the firm, which is a large team by New Zealand standards. Each of us works hard to maintain and grow this private company network.

ABN AMRO and ABN AMRO Craigs Partnership.

The Pohutukawa joint venture bought a lot more to Direct Capital's private equity business than just $53m of capital. The deal referrals from ABN AMRO Craigs corporate finance area and its 80 advisors throughout New Zealand is a huge plus that we take advantage of. ABN

AMRO Craigs have had involvement in the investments in New Zealand Pharmaceuticals, Express Logistics and Professional Hearing Services.

We also have a Heads of Agreement with ABN AMRO Capital Partners in Sydney, which includes deal referrals from them in Australia.

Corporate Finance Professionals

Direct Capital maintains links with other deal referral sources such as Corporate Finance professionals in trading banks, chartered accountancy practices and merchant banks.

Conclusion

All of these sources augment Direct Capital's own private company networks and combine to give us a large number of potential investee company contacts.

The issue for us is not the shortage of investment proposals, but rather the shortage of good well priced investment proposals, and this leads me to the third issue I said I would discuss.

3. INVESTMENT CLIMATE

As you know, Pohutukawa has drawn 40% of its capital, is 2 ½ years old, and is drawing the 2^{nd} 40 cents at the time of our next investment. Why have we taken this long to draw the second 40c?

It is interesting to note that Pohutukawa's $20m of capital has been invested in 6 companies with a total entity value of $245.85m. We have been strict with the use of your capital in deals. If we flood individual investments with equity capital, the return on that equity capital decreases.

When we raised Pohutukawa we promised you a diversified investment base with lower levels of volatility and a higher equity return. Our behaviour to date has secured all of these for you.

As you know, 2005 was an active investment year, as we made 3 investments totalling $10m. 2006 was a fantastic year for Pohutukawa portfolio companies, but not one in which we invested heavily. We can assure you that we were not on golf courses. We got very close to making five investments in 2006 and only made 1. The other 4 non-completes were due to the investment climate we are in.

The world is awash with capital. The four deals we did not complete in 2006 were either because we were simply outbid on some and we couldn't make the numbers work on others. Investors who have been with us for some time have seen this before.

We think prices of private companies have increased significantly, but there is an element of over-keenness at present, which we saw in the UK in the early – mid 90's and graphically in the technology markets in the late 90's. This is because the world is awash with investment cash, Australia is at the extreme end of that, and New Zealand is a natural spill-over market for that capital. We see it in the amount of money flowing into our asset class, the capital available in the public equity markets and, most notably, the unprecedented levels of bank debt available to borrowers.

Private Equity funds are borrowing significant amounts at reasonable rates for good private companies. This increased bank participation in our industry is a positive thing for so long as we focus on good quality businesses. If we use this newly available bank debt for average quality businesses at higher prices, then there is some trouble looming. The issue for our industry is to keep that discipline and not pay up for average companies. In our industry a rising tide cannot lift all boats.

Direct Capital uses leverage in our transactions too, and we are happy to take advantage of the increased understanding of private equity by the banks, however we have been through these cycles before and learned from our experience. There is a prudent amount of debt that a company can support without restricting its ability to prosper. Similarly, companies do hit speed bumps and experience turbulence and need the financial flexibility to withstand those shocks. Finally, Bank debt creates additional risk, and investors in Pohutukawa need to be compensated for it.

We are comfortable that we are creating additional returns for you through our use of bank debt. We are also comfortable that the level of bank debt we are utilising is prudent. You will note that New Zealand Pharmaceuticals built its new manufacturing facility post investment by Direct Capital and Express Logistics has expanded geographically in Australia and acquired other businesses.

[We do not believe that there are major problems looming in the private equity industry. There may be individual company failures, but funds are generally behaving professionally. It is interesting to note that funds can in fact suffer a small number of individual company failures and still perform well at the fund level. This is the beauty of our diversified investment approach. In addition, as one UK funds manager told me, "you can only lose a dollar once in your bad investments, but you can make $5 or $6 in your good ones".]

However, investments are being priced to perfection, and risk premiums between public and private markets are beginning to shrink. In this climate, as we always have, we will keep our discipline, pick our investment targets carefully, and remain focused on our strength of being thorough business analysts. This very much means a strong focus on 3-7 year business performance in our existing companies, and our investment targets. If we get that medium term business analysis correct, the financial returns will be significant.

The Direct Capital team thinks it is in that position now, and we hope you share our confidence in our investment approach, style and decisions.

The market commentary portion of this presentation was compiled by Direct Capital and includes its views of the Private Equity market. Sources include its own experiences in the Australasian markets and published material from onshore and offshore bankers and practitioners.