

February 2019 Update

Pencarrow Newsletter

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Pencarrow completes three platform investments for newly raised Fund V

Since our last newsletter update in November 2017, Pencarrow has had a busy year in 2018, having raised Fund V in April 2018 at its hard cap of \$250 million after around two months of fund raising and then having undertaken three platform investments. In this newsletter we will discuss each of the new Fund V investments (The Collective, Sequent and Avanti Finance) and provide an update on each of our other continuing funds, Fund IV and the Bridge Fund.

With the raising of Fund V, Pencarrow now manages just over \$450 million of aggregate committed capital across three funds with virtually all of the aggregate committed capital of the older two funds, Fund IV (\$124 million) and the Bridge Fund (\$80 million) deployed. In total with the three new investments in Fund V, Pencarrow has a portfolio of nine investments across three funds with one of those investments (The Collective) spanning two funds.

Fund V Raised in April 2018

Pencarrow was pleased to be able to raise Fund V, by far its largest fund to date with \$250 million of committed capital, in a very short two month timeframe and at the hard cap. We were particularly pleased with the support received from a broad range of New Zealand investors including government funds, superannuation funds, iwi, charitable trusts and foundations, family offices and high net worth individuals. In addition there were a small number of overseas investors who participated.

Three New Investments

Following Fund V's successful raising, Pencarrow immediately got to work finding and executing new opportunities.

The first investment for Fund V, executed immediately after the raising of the fund, was a 40% investment in

The Collective (split approximately 27.5% in Fund V and 12.5% in the Bridge Fund). The Collective (also known as Epicurean Dairy) is a leading New Zealand manufacturer of premium yoghurts and other dairy products through the grocery channel. It has operations in New Zealand, Australia and the United Kingdom.

The second investment for Fund V was the purchase of a 10% stake in a prior Fund IV portfolio company, Sequent, alongside its new majority owner Accel-KKR, a leading global mid-market investor in technology companies. Sequent is a world leader in geological modelling software for the mining industry and is expanding into additional verticals including energy, environment and civil engineering. Sequent sought a larger financial sponsor partner in order to continue its impressive growth both organically and through acquisition. Shortly after the new investment from Accel-KKR, Sequent acquired one of the world's leaders in geophysics software, Toronto-based Geosoft. Further additional bolt-on acquisitions are currently being assessed.

The third and most recent investment for Fund V has just been completed and is a minority investment in Avanti Finance, one of New Zealand's leading non-bank lending institutions. Fund V provided expansion capital which will be used to support the acquisition of a significant auto-lending receivables book as well as other growth initiatives. Avanti was established in 1989 and provides a range of consumer loan products. It has grown rapidly in the last five years and achieved

Personnel Changes and New Office

Since our last newsletter there have been a number of personnel changes at Pencarrow, mainly to enlarge the investment team to seven as we take advantage of a significant pipeline of opportunities for Fund V. Geoff Romijn joined us as Investment Manager from the corporate finance team of Deloitte and Alex Perry joined as Analyst from PricewaterhouseCoopers. In addition Lloyd Percival joined as Finance Manager taking over from Leah Anderson.

In addition to the new staff, Pencarrow has, as of the beginning of 2019, opened an Auckland office which will initially be staffed by Jonathan Goldstone and Hazel Martin who have relocated from Wellington. The additional location will enable us to broaden our geographic coverage as we seek out new opportunities for Fund V.

About Pencarrow

Pencarrow was formed in 1993 and is New Zealand's longest established private equity manager.

In December 2012 we closed our fourth fund, the Pencarrow IV Investment Fund, with committed capital of \$123.7 million. In November 2016 Pencarrow closed an extension of that fund at the hard cap of \$80 million. The commitments in Fund IV and the Bridge Fund were fully deployed across ten investments, seven of which remain in the portfolio. In 2018 Pencarrow raised Fund V which closed after a period of two months at its hard cap of \$250 million. So far, Fund V has made three investments and will seek to undertake a further 5-7 investments.

The investment team is made up of seven executives with a range of complementary skills and experience.

More information on Pencarrow and the team can be found at www.pencarrowpe.co.nz.

Our current funds continue our long established focus on MBOs, expansion capital and replacement capital investments in businesses with enterprise values typically in the range of \$20 million to \$150 million that have strong management teams, attractive positions in their markets, potential to deliver regular dividend income and the opportunity to create significant value.



Pencarrow Lighthouse

Portfolio Investments



BrewGroup is an iconic New Zealand business well positioned for future growth

icebreaker

Icebreaker is a leading designer and marketer of outdoor apparel



Seequent is a global leader in the development of visual data science software and collaborative technologies

Pencarrow currently has three investment funds with nine current portfolio investments. Fund IV concluded its investment period in September 2016 with six portfolio investments which has since been reduced following the successful sales of Icebreaker, BrewGroup and Seequent.

The Bridge Fund concluded its investment period in May 2018 following investment into The Collective. The Bridge Fund currently has a full complement of four investments, including one shared with Fund V. Fund V was raised in April 2018 and to date has deployed close to one third of its committed capital of \$250 million into three investments. Each of the investments in Fund IV, Bridge Fund and Fund V is described in more detail below.

BrewGroup (previously named Bell Tea & Coffee Company)

BrewGroup was the first realisation from Fund IV, having been acquired by Jacobs Douwe Egberts (JDE) in November 2016, representing a very successful outcome for investors.

Icebreaker

Icebreaker was sold to VF Corporation in April 2018 producing another very successful outcome for Fund IV investors.

Seequent

In July 2014, Fund IV made a significant minority investment in Seequent, providing mainly expansion capital to become the largest single shareholder. Seequent is a leading global provider of 3D geological modelling software for mining and exploration geologists. The flagship product is Leapfrog, which uses sophisticated mathematical functions to rapidly analyse scattered data for surface interpolation, enabling the creation of 3D images of ore bodies much more quickly and efficiently than other software.

Seequent has a global client base spanning over 50 countries and encompassing over 400 mining and exploration companies, including most of the majors. The business has strong recurring licence revenue and has performed strongly despite the significant downturn in the mining sector.

Pencarrow's investment was made to assist the company to enhance its product suite and provide capital for complementary acquisitions. During Fund IV's ownership Seequent increased its revenues over 100% and renewal rates to in excess of 90%. Further the company undertook a number of successful bolt-on acquisitions and expanded its offering further along the mining chain and into other industry verticals such as civil engineering and environmental science.

BeGroup

BeGroup provides affordable and modern retirement villages with an emphasis on helping residents enjoy life to the fullest extent possible

SOLARCITY

solarcity plans to revolutionise the way energy is delivered by giving customers a cleaner, more affordable alternative to their monthly utility bill

In 2018 Seequent sought further expansion capital from US-based equity investor Accel-KKR, a leading global mid-market investor in technology companies. As a result of this transaction Fund IV sold its shareholding in Seequent with Fund V reinvesting alongside Accel-KKR, taking a ~10% shareholding in the company.

The transaction was a very successful outcome for Fund IV investors with Seequent having experienced robust organic growth in revenue of over 30% CAGR during Fund IV's ownership.

Shortly after completing that capital raise Seequent acquired a key, complementary Canadian-based geosciences business, Geosoft. Geosoft is a global leader in geophysics software that will complement Seequent's suite of geoscience software. Other acquisitions are intended as part of the investment thesis.

BeGroup

In May 2014, Fund IV acquired a platform asset, The Falls Estate retirement village, located in Whangarei as the foundation for a larger opportunity in the rapidly growing retirement village and aged care industry. A holding company, BeGroup, was formed to acquire this seed asset and it aimed to develop a network of modern retirement villages providing a full range of care ranging from independent living to hospital level care.

Guy Eady, a highly respected and experienced retirement industry executive, was recruited to lead the rollout and subsequently hired a CFO and development manager. BeGroup has made strong progress against its ambition of achieving a portfolio of aged care sites at various stages of development with three sites now in the portfolio. The first site acquired by BeGroup was The Falls in Whangarei where occupancy was increased early on to 100% and extended to include a further 27 units which are now at full occupancy.

The second site at Rawhiti in one of Auckland's wealthiest suburbs was acquired in May 2015. Construction on the site has been completed and the development, comprising 27 independent living units and 68 care beds, is fully staffed and management is in the process of selling down this stock which is progressing well.

The third site at Half Moon Bay in eastern Auckland has received resource consent for the construction of 200 villas and 80 care beds and earthworks to prepare the site have been completed.

solarcity

In June 2014, Fund IV provided expansion capital in two instalments to solarcity, New Zealand's leading solar power company, resulting in it becoming the largest shareholder with a 37% stake. The expansion capital was primarily to assist solarcity to roll out a new rooftop solar offering, SolarZero, to residential customers. SolarZero is a solar-as-a-service offering requiring no upfront payment by the household with payments made monthly alongside the retail electricity bill over a 20-year contract period. The company is creating an attractive 20-year receivables book of residential installations and has a target of 15,000 residences within 5 years. Early progress has been strong and solarcity has significantly exceeded its targets.

There are strong economic and industry drivers for growth in distributed solar installations in New Zealand, as the cost of solar generated electricity is now below the generation cost from the grid without subsidies.

solarcity works closely with Panasonic, a world leader in battery technology that supports solar systems. Through this relationship solarcity offers solar systems with batteries as the standard default option and aims to provide 100% of a customer's electricity bill at a low cost.

solarcity is currently pursuing a number of strategic initiatives with the most recent success being to create in effect the world's largest virtual power plant connecting batteries provided by solarcity to Transpower's national grid. The virtual power plant creates a generation and storage network that can support the national grid when it is unable to cope with demand or there is a fault.



Umbrellar is the leading domestic domain name and SME-focused cloud hosting company in New Zealand

Umbrellar

In September 2014, Fund IV partnered with the management team of Umbrellar to acquire the business from its founder. Simultaneously, Umbrellar acquired Webdrive, another domain name and web hosting business, and Arrenway, a small underutilised data centre. Both acquisitions offer significant cost synergies with Umbrellar and an early part of the investment thesis was to execute and realise these synergies.

The combination of these three businesses represented the first part of a consolidation strategy in the domain names and web hosting industry in New Zealand. In September 2015, Umbrellar undertook further consolidation of the industry via the acquisition of Freeparking.

Umbrellar is now New Zealand's leading domestic domain name company and is leading the market in the promotion and delivery of cloud services, specifically Microsoft Azure and Azure Stack. Umbrellar offers a unique solution for businesses that enables data to be hosted domestically whilst retaining all the benefits of the public cloud. Umbrellar continues to pursue cost saving initiatives across the business whilst growing top line revenue. This has resulted in a significant improvement in maintainable earnings of the business and puts the company on a strong footing as it heads into 2019.



MMC is the leading NZ outsourced fund and investment administration service provider

MMC

In November 2016, the Bridge Fund acquired a 50% stake in MMC, a leading New Zealand outsourced fund and investment administration business with over \$25 billion of client funds under administration. MMC is well positioned for strong growth by increasing economies of scale through organic growth, capturing a significant part of the funds management value chain and introducing adjacent services to new and existing clients.

MMC has a history of strong revenue growth and is forecast to increase revenue through a number of strategic growth initiatives which include:

- Securing additional clients in the core fund accounting and unit pricing service primarily those in a rapidly growing Kiwisaver market;
- Providing additional services to both existing and new clients;
- Transitioning further in-house providers to an outsource arrangement driven by an increasingly complex administrative and compliance burden.

MMC's intuitive and easy-to-use web interface is a key differentiator in the fund administration market. MMC has performed in line with expectations since the Bridge Fund's investment driven primarily by the growth of funds under administration to in excess of \$30 billion.

Mix

Mix is a leading New Zealand branded producer of natural personal care products.

In March 2017, the Bridge Fund acquired a 50% stake in Mix, a leading New Zealand personal care products business, alongside the founders. Mix is strongly positioned in the pharmacy and grocery channel in both New Zealand and Australia with a diverse portfolio of brands using natural ingredients covering the facial skincare, hand & body skincare, haircare and men's grooming categories. The main skin and haircare brand is Essano. Future growth is expected to come from further expansion of its sales base in New Zealand, Australia and Asia, including South East Asia and China.

Mix's product portfolio is positioned in the "natural" segment, a high growth area as consumers steer away from products considered unsustainable, unethical or to contain harmful ingredients. Its brands also have a mid-market price point, positioning it at the top end of the mass market.





Netlogix is an innovative New Zealand based freight logistics provider.

A key factor in Mix's success has been its ability to expedite the commercialisation of new products rapidly in response to market trends. Mix's R&D laboratory and team of technical staff provide it with a platform to engage in new product development, to increase its shelf presence with key retailers and drive sales growth. Since Pencarrow's investment Mix has made good progress towards its investment thesis including the development and execution of new product strategies, expansion into Asia and a strong financial return for the fund. The company is assessing a strong pipeline of bolt on opportunities which will enable the company to rapidly deploy further product lines.

Netlogix

In October 2017 the Bridge Fund acquired a 39.7% shareholding in Netlogix, a world leading technology-enabled freight logistics company. Netlogix has developed technology that reduces a freight customer's transport and logistical costs by optimising the transport expenditure across a network of carriers and routes. This enables consolidation of different freight customers' loads as well as a multimodal solution offering connections to road, rail and shipping options. Pencarrow invested growth capital in the company that enabled further development of its technology, and for the company to hire additional resource to assist with the on-boarding of new customers.

Since Pencarrow's investment Netlogix has completed its network of carriers and cross docking facilities throughout New Zealand and now offers less-than-a-truck-load (LTL) services across road and rail nationwide. In addition, the company has expanded its offering into Australia and achieved a number of milestone customer wins in that market. Recently Netlogix launched a joint venture with a major customer that will see it deploy its technology to optimise national and international shipping volumes. The venture has been brought to market under the name Bearing360 and has received strong support from industry players since its launch in January 2019.



The Collective is a New Zealand headquartered dairy company that manufactures and distributes premium yoghurt and dairy products through the grocery channel.

The Collective

The Bridge Fund and the recently raised Fund V invested in The Collective in May 2018. The Collective is a New Zealand headquartered dairy company that manufactures and distributes premium yoghurt and dairy products through the grocery channel. The Collective has operations in New Zealand, Australia and the UK. Funding provided by Pencarrow was used by the company to acquire shares owned by a UK based joint venture party, to consolidate it to full ownership under The Collective.

Since Pencarrow's investment The Collective has launched a number of new products including Kefir and Skyr yoghurts in the New Zealand and UK markets. In addition the company has launched an Australian operation and is in the final stages of expanding into Europe. The company continues to pursue a strong pipeline of new and innovative products that will be launched in all markets in the coming years. The Collective has a strong senior management team which is lead by co-chairman, Mark Hamilton (previously CEO of Pencarrow investee, Bell Tea and Coffee Company) and Chris Britton (UK based chairman with significant experience working with numerous private equity firms to grow businesses in the FMCG space).

AVANTI | FINANCE

Avanti Finance is a leading New Zealand non-bank lending institution that provides a range of consumer loan products.

Avanti Finance

Fund V invested in Avanti Finance in January 2019. Avanti is a leading New Zealand based non-bank lending institution. The company has been in operation for over 30 years. During that time it has developed a sophisticated credit approval process that allows the company to appropriately price risk for consumers that may not meet traditional bank lending criteria. Pencarrow's investment thesis is based around the company's:

- Track record of growth, the company having grown rapidly over the past five years, achieving a compound annual growth rate (CAGR) on its loan receivables book of ~50% between 2014 and 2018;
- Proven management team led by Mark Mountcastle (CEO) and Glenn Hawkins (founder and chairman);
- Large addressable market with the opportunity to accelerate growth via acquisition.

Following Pencarrow's investment the company acquired a complementary auto loan book which has significantly increased the size of Avanti's loan receivable book.

Outlook

Pencarrow has had a busy and successful 2018 having raised its largest ever fund and completed three new investments as well as the sale of Seequent for a very good return to Fund IV investors. In 2019 Pencarrow will focus on continuing to add value to its current nine investments as well as identifying further portfolio investments for Fund V.

New Zealand is in the enviable position of being one of the most geopolitically stable and robust economies in the world, with GDP growth rates consistently in the range of 2.5% to 3.0%. A recent report by IMF indicated New Zealand had one of the highest developed world growth rates per capita over the past five years. The current very low inflation environment suggests the country may also have some of the lowest interest rates for the longest period in the current monetary cycle.

All of this points to a robust environment for mergers and acquisitions and a strong deal pipeline as we head into 2019.

Our Team

The Pencarrow Team



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