DIRECT CAPITAL

DIRECTIONS

NEWSLETTER OF DIRECT CAPITAL LIMITED **JULY 2010**

$325 MILLION AND LOOKING TO INVEST

DIRECT CAPITAL IV RAISES A RECORD $325 MILLION FOR INVESTMENT IN PRIVATE COMPANIES

Investing in private companies is what Direct Capital was established to do back in 1994. With the experience of having invested in more than 35 companies, our belief in partnering with business owners and managers to continue creating growth and value is stronger than ever.

Why is it so compelling?

Put simply, it works. Our investment is usually associated with change in the business we invest in. Whether it's an owner thinking about selling to their management team, or an owner thinking about growing their business, acquiring a competitor or establishing their business across the Tasman, new capital helps them achieve a quantum leap forward.

There is no better investment than investing alongside the owners and managers of a well-run private company. They know their own business, industry, risks and opportunities better than anyone. They know where the right investment will make the biggest difference.

Our investment is partnership based with a shared goal and desire to continue growing the business. We act the same whether we are a 20% shareholder or an 80% shareholder. Our investment relationship becomes a long-standing one and it's no coincidence that many of the owners we've invested with have also become good friends.

Direct Capital has a track record of success investing with great companies. Some of them are household names like Ryman Healthcare, EziBuy, Max Fashions, New Zealand King Salmon, Rodd & Gunn, and Fishpond. Well-known or not, what all our companies have in common are competitive market positions, owners and managers thinking strategically, and the desire to continue growing the business and creating value.

Having completed its fund raising in December 2009, Direct Capital IV will continue the investment approach the firm has successfully followed for sixteen years, investing between $10 million and $60 million into successful private companies, alongside owners and managers.

BACKING THE EXPANSION OF BAYLEYS

DIRECT CAPITAL'S INVESTMENT IN BAYLEY CORPORATION WILL FUND GROWTH IN ITS REAL ESTATE SERVICES

In June 2010 Direct Capital completed the second investment from its Direct Capital IV fund, into well-known real estate services provider, Bayley Corporation Limited.

Like Direct Capital, Bayleys has viewed the recession as a time to be bold, a time to continue the growth of its successful agency businesses, but to also extend its services into complementary areas such as property management, valuation services and funds management.

The key to taking these opportunities is of course, capital. Coming off the back of a record earnings year, Bayleys had the financial base to grow without taking on a financial partner. But with the desire to achieve growth more quickly, taking on a partner made good strategic sense.

For Direct Capital the investment was a culmination of discussions which first took place with Bayleys chairman and shareholder, John Bayley, more than 10 years ago.

From its beginnings in 1973 the Bayley family has built the industry's market leader. Professionally managed and with a long history of profitable growth achieved through its national franchise partners and agency owned network of more than a thousand agents, it's little wonder the company enjoys the top market share in the commercial and industrial sectors and a large business in residential, rural and lifestyle sectors.

Taking on a partner, particularly in a long-established, family-owned business is a big decision to make. It becomes a catalyst for change, an investment in growing the business and taking it to the next stage. The decision is seldom just a financial one: the relationship is for the long term and the trust and confidence required makes the 'people' decision the most important element. With the investment 10 years in the making, Bayleys and Direct Capital are confident that we've got it right.

INSIDE

OTHER RECENT INVESTMENTS

BIG FISH, LITTLE FISH
ALL IN ONE BIG POND!

BOOKS, TOYS AND GAMES DRIVING THE CONTINUED GROWTH OF AUSTRALASIA'S LARGEST ONLINE RETAILER

In October 2009 when Direct Capital announced that it had purchased a minority shareholding in online retailer, Fishpond, the stats were impressive - a range of more 2.2 million book titles and 200,000 CDs and DVDs available to purchase online.

By June of 2010, just 8 months later, the numbers were even larger - over 3.3 million book titles, 310,000 CDs and DVDs, and the addition of new product categories like games (over 2,500 video games, consoles, and accessories), toys (with popular titles like Lego, National Geographic, and Nerf), and an electronic category offering a range of over 1,000 popular consumer electronic gadgets.

It is little surprise then that Fishpond, launched in January 2004 by Daniel Robertson, has been able to achieve compound revenue growth in excess of 100% per annum to become Australasia's largest online retailer. That it's also been profitable every year just adds to the impressive track record this company is achieving.

Today, the company operates from a distribution centre in Auckland, employs more than 50 staff and services both the Australian and New Zealand markets from its fishpond.co.nz and fishpond.com.au websites.

Daniel has built a great team and infrastructure around him: people that have built fast-growing businesses previously; specialist marketers in new online categories; a powerful search engine, sophisticated recommendations and pricing algorithms; and robotics that sort and pack several thousand orders a day.

The internet now comprises specialist online retailers who focus every element of their business model around technology. Fishpond is a great example of this and its month on month, year on year growth is telling evidence of its success.

TRANS-TASMAN SUCCESS

DIRECT CAPITAL CONTINUES A WELL-ESTABLISHED INVESTMENT THEME - INVESTING IN BUSINESSES WITH TRANS-TASMAN OPERATIONS

In January 2010 Direct Capital completed a $24 million investment in Transaction Services Limited, Australasia's largest third party recurring payment processing company.

Operating under the brands Debitsuccess and FFA Paysmart, Transaction Services manages the payment processing function for clients in a wide range of industries that includes health and fitness facilities, sports clubs, property management companies, maintenance providers, home service providers, and insurance companies.

Many customers want the flexibility of paying for services by direct debit, but it's a costly overhead for clubs and businesses to offer. Transaction Services has the technology, infrastructure and systems to provide this service to clients in a cost-effective way, and has been doing so since 1994. Today, the company annually processes more than 13 million transactions on behalf of more than 2,000 clients, from their 500,000 customers in New Zealand and Australia.

Although it began life in New Zealand, Transaction Services now generates more than 75% of its revenue from Australia.

This is an important feature for Direct Capital and one we value highly. Across the Direct Capital III portfolio of companies, more than 50% of revenues are generated outside New Zealand. Having exposure to more than one economy, especially through a major recession, has been one of the key reasons that the value of our investments has continued to grow.

THE TIME TO BE BOLD

CHALLENGING ECONOMIC CONDITIONS OFFER BUSINESS OWNERS AN OPPORTUNITY TO MAKE A QUANTUM LEAP FORWARD

When we launched Direct Capital IV in February 2009, the financial markets had imploded and the 'global financial crisis' had commenced. More than a few eyebrows were raised questioning whether this was the best time to be raising capital and making investments. But when would there be a better time?

We think business owners face the same question and the same dilemma. It's easy to wait for better times, or wait until there is perfect knowledge to make a perfect decision. But of course, life isn't like that and opportunities pass by that can in hindsight end up looking like the best decisions never made.

In the good times, market share is hard to gain because every competitor is doing well. Or it's expensive to acquire because prices get leveraged up. It's during the tougher times that astute business owners look ahead, see the opportunities, and act on them.

This is the theme we've been sharing with our company owner partners and it's no coincidence that since the beginning of the recession, we've completed ten investments, many of which have been bolt-on acquisitions made by the companies we've invested in.

Having a strong equity base really counts in these times and Direct Capital is a natural partner for private company owners wanting to grow their businesses and seize the opportunities a recession provides.

ALL ABOARD WITH GO BUS

WITH A BIG SHIFT TO PUBLIC TRANSPORT, THE 'DRIVERS' WERE RIGHT FOR DIRECT CAPITAL'S INVESTMENT IN GO BUS.

Transport is a significant sector in the economy and public transport is benefiting from local and central government initiatives to encourage people out of their cars and on to buses.

Go Bus traces its roots back more than 30 years and is the amalgamation of several family bus operations that today has become the largest operator north of Wellington and south of Auckland. It provides urban, charter and school bus services through a fleet of more than 620 vehicles serviced from 20 depots.

The investment had many attractive features for Direct Capital - predictable revenues from multi-year contracts with councils and the Ministry of Education, positive demand-side factors and, in an industry where scale counts, a real opportunity to grow the business both organically and through acquisition.

The investment was a typical succession investment for Direct Capital. Owners rarely want to sell and retire in one go, as the business has been too big a part of their life for them. Nor do they necessarily want to go through a trade-sale process where they open their books to competitors. Often they simply want to reduce their personal exposure, take some cash off the table and introduce a financial partner to help the next generation of management acquire the business, and put in place a succession plan to suit their own timetable.

Having reduced his investment in the business, former majority owner Marcus Gerbich, remains a director, working closely with Direct Capital on new initiatives. We've also been delighted with the success which Calum Haslop has achieved since taking over as managing director, ably supported by chairman Dallas Fisher. Calum has a strong industry background and past success as a business owner himself, while Dallas is a well known figure, particularly in the Waikato, through his very successful management and ownership of the NDA Group.

Since Direct Capital's investment, the company has won a number of new contracts that have grown the business into the country's third largest operator.

A HEALTHY INVESTMENT

EXPOSURE TO THE HIGH-GROWTH FOOD SECTOR IS A FEATURE OF DIRECT CAPITAL'S INVESTMENT IN NEW ZEALAND KING SALMON

While New Zealand is renowned for its food production it's a difficult sector for investors to access. Direct Capital was delighted with the opportunity to invest in one of the country's leading food groups, New Zealand King Salmon.

Direct Capital's investment in the company provides exposure to the global protein market and to a company offering a sustainable food source for which domestic and export demand continues to grow as consumers switch to the significant health benefits of salmon, a rich source of Omega-3.

NZKS is the country's largest salmon supplier servicing both the domestic and export markets. With a fully integrated operation, NZKS farms its fish from brood stock through to full maturity. It manages all production from harvesting to the processing of a wide variety of products including whole fish through to filleted, smoked and "ready to eat" servings. More importantly, the company owns the well-known brands through which its products are distributed - Seasmoke, Regal and Southern Ocean.

With hatcheries, farms and processing facilities located around the South Island's Marlborough region, New Zealand King Salmon enjoys a global reputation for quality and is one of the leaders in New Zealand's growing aquaculture sector.

With the company and shareholders thinking about a future IPO, it was important to get a local partner who was able to add value ahead of a listing but also continue supporting the company afterwards. Direct Capital is well-recognised by institutional investors as a good partner for companies targeting a listing.

Direct Capital is also a firm believer in the value of independent directors. We were delighted with the appointment of well-known director, Tom Sturgess, as chairman, joined by directors John Ryder and Paul Steere. Paul very successfully led NZKS for 15 years and wanted to retain his interest in the company and its continued success. The company is very fortunate to have attracted directors of this calibre.

With Paul's transition to the board, the company has been joined by new chief executive, Grant Rosewarne, an Australian with a highly successful international career in consumer goods. Grant's most recent position was with Sara Lee Corporation where he ultimately achieved the position of Chairman of the UK and Ireland.

DIRECT CAPITAL

DELIVERING LONG TERM VALUE

SUCCESSFUL REALISATIONS ILLUSTRATE THE VALUE CREATED BY PRIVATE COMPANY INVESTMENT

As a long term investor, Direct Capital's investment approach is to back good people in good industries and encourage management to be ready to act on opportunities as they arise. With this approach, we believe long term value accrues naturally. It often surprises people that Direct Capital's investment processes never focus on future liquidity. This is quite different to other models offshore where exit strategies are often developed prior to investment.

Our approach is simple; it takes a lot of effort to find the right investment where there is a great combination of good industry, good business, and great partnership with owners and managers. So why think about exiting from a business that we know and understand, and which continues to be successful?

When it does happen, it's probably because our owner partners have chosen to make changes in their personal lives, step away from running the business, spend more time with family, or take on new challenges.

And while we're sad that our investments in the following great businesses have come to an end, we're proud of our involvement, thankful for the friendships we've made and really pleased to see the financial success our partners have achieved.

EXPRESS LOGISTICS

Express Logistics was one of Direct Capital's early investments from its Direct Capital III fund, completed in 2005.

The investment was a typical succession buy-out supporting the existing management team to acquire the business from the owners, Brendon Thomas and Graeme Mann.

The transport and logistics sector has been a key investment focus for Direct Capital and we worked closely with Express to complete a number of acquisitions in New Zealand and Australia in order to build sufficient scale with which to achieve a share market listing. By 2009 Express had become the 3rd largest airfreight handler in New Zealand and 14th largest in Australia.

And, as happens when management are successful in building a great business, it becomes an attractive opportunity for other industry players. In October 2009 ASX-listed Toll Holdings made an approach to the company with an offer that our management partners were keen to accept, producing a great outcome for all.

MAX FASHIONS

In 2005 Direct Capital completed a succession buyout with David Wright, the founder and owner of Max Fashions, one of New Zealand's leading retail chains for women's apparel. David retained a shareholding in the business and continued as chairman, handing over day to day operations to fellow shareholders, Venecia Martin and Leanne Jones.

Max continued to enjoy great success in the market, growing its retail chain to 39 stores and well-advanced in its plans to enter the Australian market.

In late 2007 several approaches were made to the company. While Direct Capital was happy to continue its shareholding, it became clear that only a 100% sale of the business would be possible and a successful sale was completed in December 2007.

INNOVAIR

In August 2007, Direct Capital acquired a minority shareholding in Innovair, the company behind the RoboCan pest control product. With its unique 'advanced micro-mist' technology and use of natural repellants, Robocan had quickly cornered a large share of the New Zealand pest control market off the large multi-nationals.

Direct Capital completed an initial investment and had agreed with the company further investment to fund its international expansion – the beginnings of a long investment relationship.

But, in the same way that Direct Capital had been greatly attracted to Innovair, so too was one of its multi-national competitors - keen to acquire the company and secure its global potential.

In June 2008 the majority of shareholders voted to accept what turned out to be an excellent offer for the company and as a minority shareholder Direct Capital chose not to stand in the way. It was disappointing for Direct Capital not to see the company reach its full potential under the current shareholding but nonetheless it has been a great financial outcome.

COMPANY UPDATES

NEW ZEALAND PHARMACEUTICALS

Direct Capital invested in NZP in 2005 and the company continues to be a great example of what New Zealand does well – being a world leader in a niche, global manufacturing market. NZP turns animal by-products into something useful (our technical term for glycosaminoglycans, protein hydrolysates, amino acids and complex carbohydrates) - component products used by the global pharmaceutical industry.

In September 2009 the company acquired UK based Dextra Laboratories. Dextra is an internationally highly regarded carbohydrate chemistry company, the area into which NZP has been looking to grow its capability in recent years. Dextra gives NZP a greatly increased capability in the carbohydrate space, as well as a northern hemisphere physical and marketing presence. The acquisition enhances the product range and capabilities of NZP by offering customers a full package of drug development and production services to reduce time to market for new products. NZP is a continuing success story and one you'll hear more of in the future.

STRATEX

Next time you tear open a sugar sachet and notice the waxy sheen protecting the sugar from moisture, think of Stratex. This is just one of the many applications produced in the company's specialist manufacturing operations that laminate paper, polymer and foil materials to provide protective packaging for customers.

In May 2007 Direct Capital backed management in a succession buyout of the company that was then known as Paper Coaters. It's a transition that has gone well, with the renamed Stratex continuing to grow its business in both New Zealand and Australian markets.

Stratex has also sought out other growth opportunities, expanding its Australian operations through the acquisition of a Melbourne based film extrusion business. The acquisition provides Stratex the ability to 'do to plastic what Stratex does to paper' by laminating polymer on to film based material. The acquisition has extended Stratex's product range, particularly in food packaging where product protection is critical. With manufacturing operations in both New Zealand and Australia, Stratex is well placed to meet customer demands throughout the region.

SHEARS & MAC

If you've ever wondered who builds those up-market retail shops such as Gucci, Louis Vuitton, Rodd & Gunn, and the many other retail shops of premium brands, look no further than Shears & Mac, New Zealand's leading name in fit-outs.

Combining modern joinery manufacturing with a high quality installation team ensures that when a high street fashion retailer, airport duty free provider, bank, or other commercial business wants their latest shop or branch to be opened on time, on budget and fitted out to the most exacting quality standard, Shears & Mac is the natural choice.

Direct Capital invested in Camm4 in 2008, partnering with Chris and Julie Stafford-Bush to build a substantial trans-Tasman business. Through the subsequent acquisition of Shears & Mak the ownership base was extended to include Patrick Moyne and the new team has been busy successfully merging the two operations.

With the acquisition completed, the focus now turns to Australia where the company is establishing an operation to support its Australian clients wanting to benefit from Shears & Mac's manufacturing cost advantage and local installation services. There's that Aussie growth story again!

RODD & GUNN

With a retail chain of 64 stores and concessions in malls and high streets including 43 stores across Australia and 21 stores throughout New Zealand, Rodd & Gunn has a long-established brand targeting the premium male customer. The company is a great example of the value in building a trans-Tasman business and being bold in a recession.

The company has continued to benefit from retail strength in Australia and has grown its business significantly through developing concession stores within the Myer department chain and continuing to open new high street stores. It has also introduced a diffusion brand targeting a younger, but still premium, male demographic.

In periods such as this there are great opportunities to increase market share. Rodd & Gunn's consistent strategy and boldness leave it well-positioned to benefit and continue to generate value.

COMPANY DIRECTORS

INVESTING IN THE PRIVATE COMPANIES YOU WORK WITH

New Zealand's private company market is significantly larger than the listed market.

There are over 3,500 companies in New Zealand that have annual revenues of $10 million or more. Direct Capital has identified 850 of these companies that are of a size that we generally invest in - companies with revenues between $30 million and $200 million.

The NZX has just over 160 companies listed on it, about half of which are profitable. Of New Zealand's top 200 companies, only 25% are listed.

Direct Capital has been investing in the private company market for sixteen years and we regularly talk to the business owners that operate in it. But a common way we first meet and talk to business owners is through the community of non-executive directors.

It's a network of directors that works closely with owners, trusted to help with strategic issues such as a change of ownership or raising capital to grow the business or make an acquisition.

We invest in private companies because it's a successful area to invest in and it's interesting and rewarding. We offer non-executive directors the same opportunity, to invest alongside Direct Capital and benefit from the growth our investment helps fund.

We value the skills and experience that non-executive directors bring to companies that we invest in. In fact, we think it's a key feature of our success.

Non-executive directors are very active in the private company market and we encourage them to talk to us about the opportunities they see.

ABOUT US

Direct Capital invests equity into New Zealand and Australian private companies. We have a track record of success investing with great companies and being a catalyst for change. We partner with business owners who are thinking about growing their business or looking at ownership changes.

Since 1994 we have invested in more than 35 such successful, medium-sized Australasian companies. From our current active funds, Direct Capital III and Direct Capital IV, we have completed 14 investments since 2005 into companies that have aggregate annual revenues of $840 million and employ more than 3,000 people.

We invest capital to assist business owners with:

- Funding business expansion
- Funding acquisitions
- Funding a company through to an IPO
- Funding changes of ownership

We are firm believers that being a shareholder in a private company requires strong partnership between the business owner, management and investor. It's a partnership that works irrespective of shareholding percentage. And it is far more than a simple financial transaction. It's about having common goals and a desire to continue creating shareholder value.

We invest in companies that are privately owned, have a profitable track record, a professional management team, and a sustainable competitive advantage.

- We can invest equity of between $10m - $60m
- These companies will generally have annual revenues of $30m - $200m
- We invest in both minority or majority shareholding situations
- We are flexible in the way we invest and work with business owners

If you would like to know more about what we do please give one of our investment team a call, or visit our website at **www.directcapital.co.nz**

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