

New Zealand Private Equity and Venture Capital Monitor 2018

Full year review



Foreword

We are delighted to bring you the fifteenth full year edition of the New Zealand Private Equity and Venture Capital Monitor.

This full year edition of the New Zealand Private Equity and Venture Capital Monitor consolidates the findings from previous surveys and provides a more detailed review of 2017 including commentary on the industry from the New Zealand Private Equity & Venture Capital Association's (NZVCA) Chair.

Total investment activity in 2017 was \$876 million falling short of the \$1 billion mark exceeded in 2016, largely due to less large buy out activity. The last time investment activity exceeded \$1 billion in consecutive years was 2006 and 2007.

Private equity investment excluding venture capital reached \$658.7m, compared with the \$1,106.4m in 2016.

The venture and early stage total investment of \$217.3m was notable for one larger investment by domestic and international venture firms in Rocket Labs.

International investment in technology companies has continued to extend the access to capital for young companies growing from New Zealand. The 2017 venture & early-stage market activity included a significant increase in the presence of international investors.

The commitment to growing New Zealand's businesses has been clear in responses to the Monitor, with the plans for respondents' investee companies focussing on growth in exports and new markets, product development, recruitment and R&D.

Fund-raising activity took a pause with New Zealand funds deploying capital raised in the previous two years.

There were no Initial Public Offerings sponsored by New Zealand fund managers in 2017. The outlook for 2018 looks better as portfolio companies assess options for new capital raising.

Private capital is a significant contributor to the New Zealand capital market eco-system. Private equity and venture capital fund managers provide more than capital, they are partners for growth companies. NZVCA promotes the growth story with targeted communications that feature business owners' experience working with private equity managers.

Colin McKinnon
Executive Director, NZVCA

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Executive summary

The year to 31 December 2017 was characterised by a continued high level of overall activity of \$989.6m, down on the 2016 high of \$1,557.0m but significantly above the average of \$815.0m since the first survey in 2003.

Mid-market investment activity was twice the 10-year average at \$333.7m, driven by an increase in both volume and average value of deals. This is the first time mid-market investment activity has exceeded \$300m, with the focus of activity being core New Zealand growth businesses. Mid-market divestment activity with disclosed deal values has decreased to \$62.4m.

Meanwhile, 2017 was a record year for venture capital (VC) activity. Investments have increased to \$217.3m with higher levels of foreign capital, and divestments also increasing to \$51.2m.

Buy-out activity has continued, but at a lower level than the 2016 peak, with \$325.0m of investments and nil divestment activity.

Investments

- Total investment value in 2017 was \$876.0m spread across 68 deals.
- The total number of investments with known values increased marginally from 66 to 68.
- Although total average deal value decreased slightly from \$18.2m to \$12.9m, mid-market and VC average deal values have increased from \$9.2m to \$19.6m and \$1.8m to \$4.5m respectively.
- 2017 was a record year for mid-market investment activity, at \$333.7m, an increase from \$100.8m in 2016. This increase was driven by a higher average investment value (2017: \$19.6m, 2016: \$9.2m) over a wider range of transactions (2017:17, 2016: 11).
- Total VC investment increased from \$92.3m to \$217.3m, across a similar number of deals (2017: 48, 2016: 50), with the Rocket Lab capital raise being the standout transaction.

Divestments

- Total divestment value of 2017 decreased to \$113.6m from \$358.3m in 2016.
- Divestment activity in 2017 was driven predominantly by mid-market PE divestments by New Zealand domiciled funds.

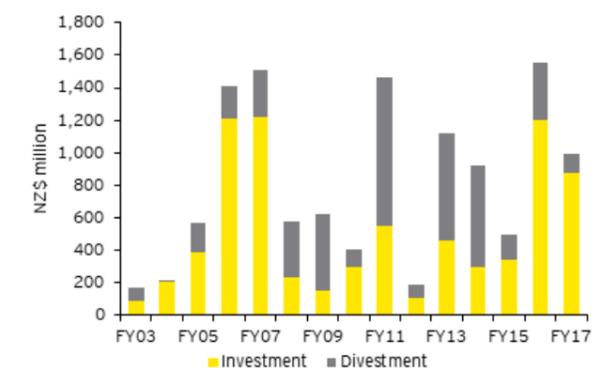


Brad Wheeler
Partner, Transaction Advisory Services
EY



Colin McKinnon
Executive Director
NZVCA

Overall activity summary 2003 to 2017

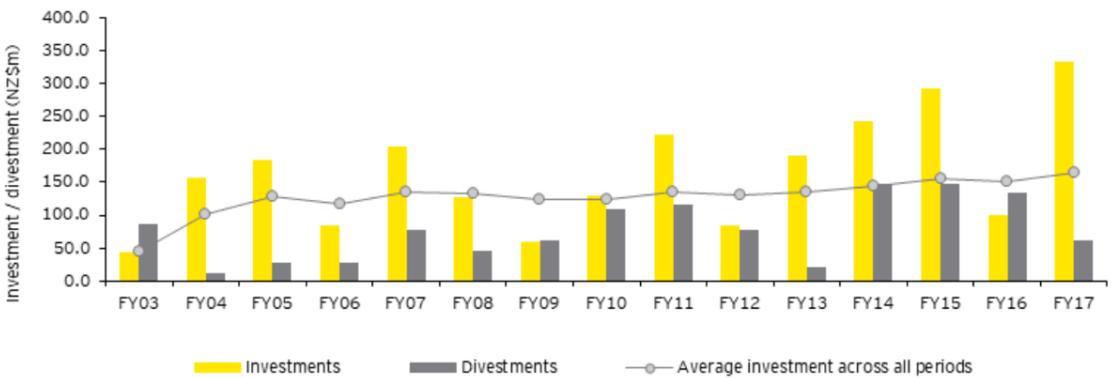


“It was great to see the investment into the mid-market dominated by New Zealand’s fund managers in 2017.”

Matthew Riley, NZVCA Chair

Mid-market private equity

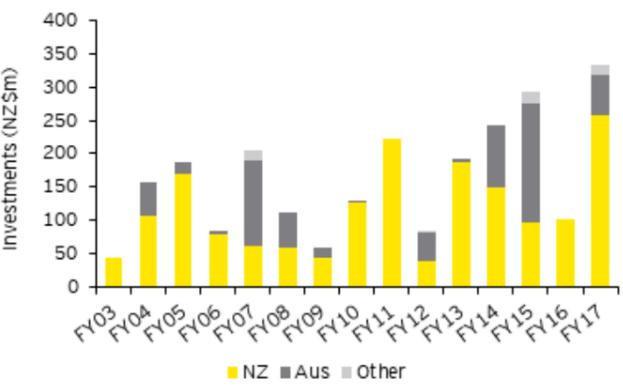
Mid-market private equity investment/divestment summary 2003 to 2017



Mid-market investment

- ▶ The level of mid-market investment from deals with disclosed values increased to a record \$333.7m from \$100.8m in 2016 and over twice the 10-year average of \$161.3m.
- ▶ The average investment value increased markedly from \$9.2m in 2016 to \$19.6m in 2017.
- ▶ Mid-market deals exclude any transactions where the target has an enterprise value over \$150m, as these are categorised as buy-out transactions for the purposes of this report.

Mid-market investments - domicile



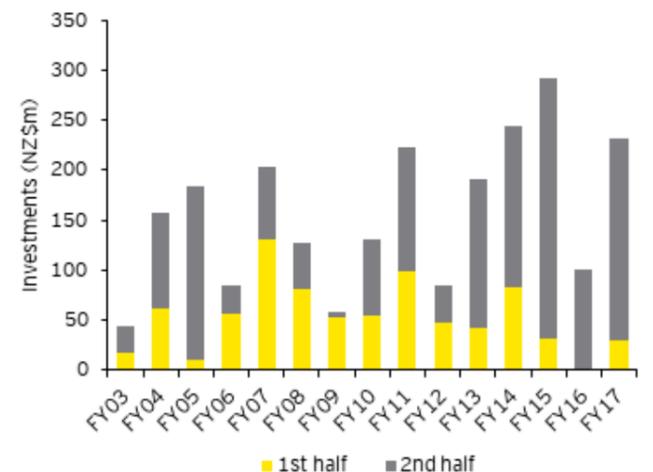
Mid-market investment

- ▶ Mid-market investment activity lifted well above the 10-year average in 2017, driven by record levels of investments by New Zealand domiciled funds including investments by Direct Capital, Waterman Capital, Pioneer Capital, Pencarrow Private Equity, Maui Capital and Oriens Capital.
- ▶ There was also a continuation of investment activity from Australian-domiciled funds, including Adamantem Capital acquiring a majority stake in Heritage Lifecare.

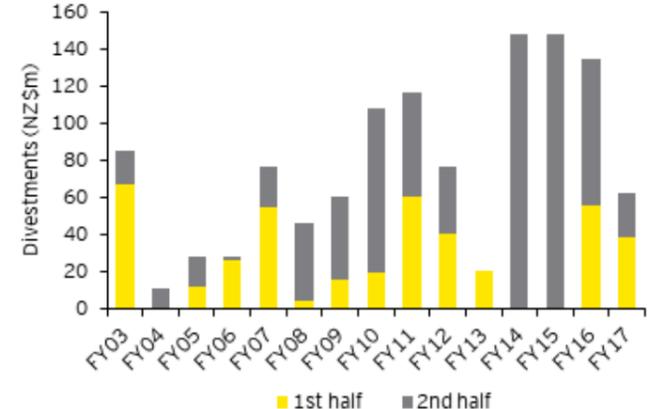
Mid market divestment

- ▶ Mid-market divestment activity showed a decline, albeit partly due to some deal values being undisclosed.
- ▶ Divestment activity was primarily driven by New Zealand domiciled funds.

Mid-market investments – half year split



Mid-market divestments – half year split





Venture and early stage capital

Venture capital investment/divestment summary 2003 to 2017

Overview

Since 2009 our survey results for venture capital activity have been supplemented by deal information from the Startup Investment NZ publication. This has led to broader data capture, and the inclusion of early stage investment activity within the VC segment. Early stage investment includes activity of fund managers, angel networks and individuals. We have included only activity of fund managers (who employ a General Partner / Limited Partner structure) in our dataset.

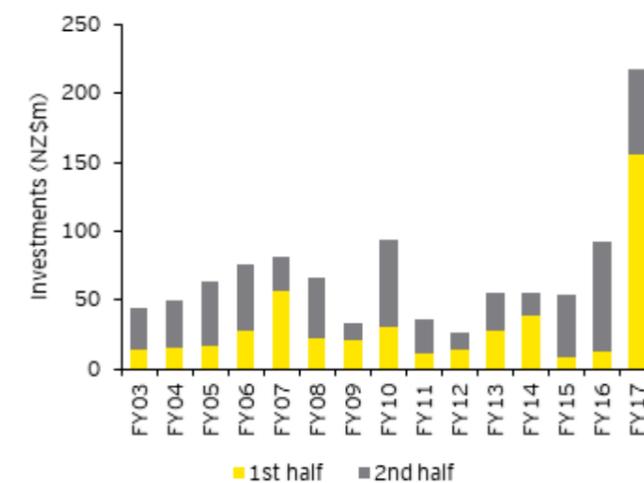
Fund managers or General Partners manage capital provided by investors. Fund managers have investment programmes to attract investor's capital prior to deploying the capital. Their activity is distinct from angel networks that help individuals to invest their own capital usually on a deal by deal basis.

The size of early stage funds varies from large venture capital funds (greater than \$50m funds under management) to small and micro VC (\$2m-10m funds under management). The stage of investment describes the path from seed/early stage to expansion.

Venture and early stage investment

- ▶ Total investment value of disclosed VC activity in NZ was \$217.3m across 48 deals in 2017 (compared to \$92.3m across 50 deals in 2016). This represents a notable increase in the value of VC activity.
- ▶ Headline deals included additional funds raised by technology company 8i and by Rocket Lab, an aerospace technology company.

Venture and early stage investment summary

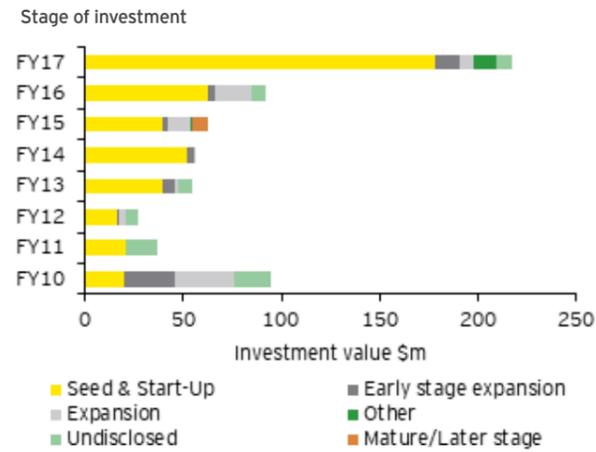


2017 saw a significant increase in VC investment activity driven by continued activity in the technology sector

Stage of investment

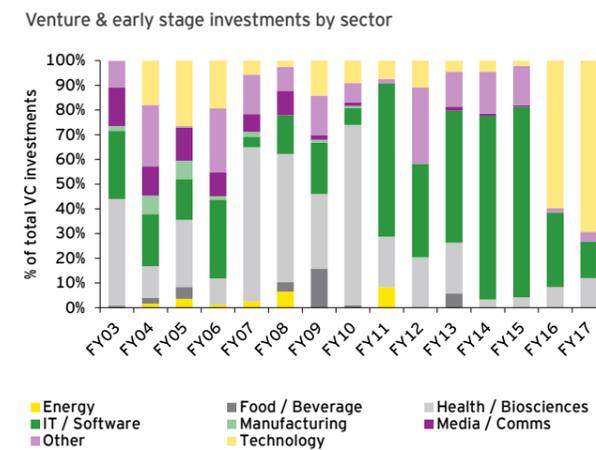
This chart shows the stages of investment of VC activity in NZ.

Seed and start up investment has increased significantly in 2017 alongside expansion investment, while mature/late stage investment has not continued from previous years.



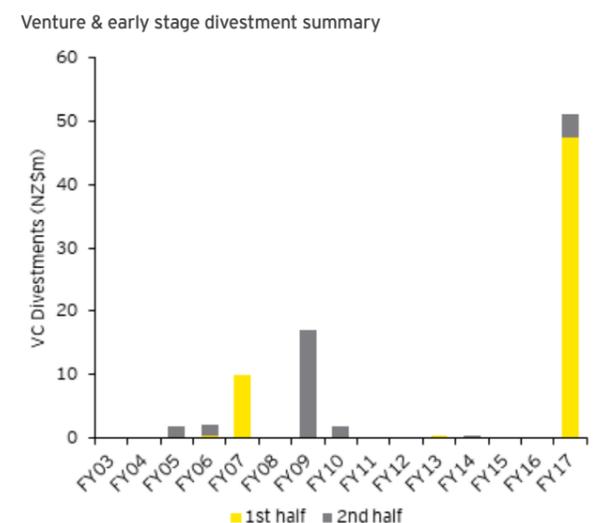
Venture & early stage capital - sector review

- Technology is the dominant sector for VC activity, while IT / software presence has reduced.
- Other sectors obtaining VC funding in the year included food / beverage and health / biosciences.



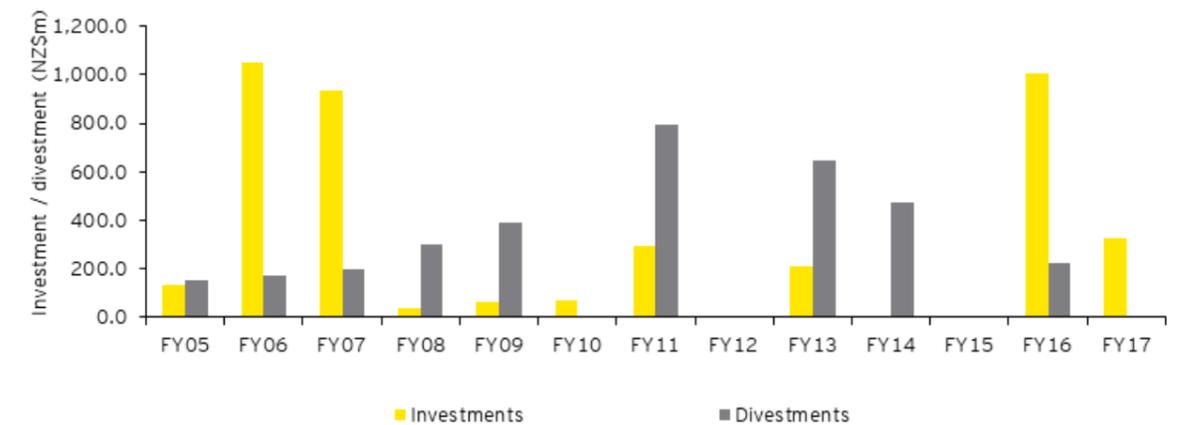
Venture & early stage capital - divestment

- Divestment activity in 2017 was led by NZVIF, TMT Ventures and K1W1's divestment of Amphenol Phitek Limited.
- Divestment activity presented in this report excludes a number of deals where values were not disclosed (e.g. the divestment of PowerbyProxi to Apple).



Buy-out private equity

Buy-out private equity investment/divestment summary 2005 to 2017



Overview

- Buy-out deals are defined as those transactions with an enterprise value over \$150m. The observed deal value trends from 2005 to date are a result of a small number of high value transactions in this segment. 2017 saw continued buy-out investment activity with three estimated investments in this category, and nil divestment activity.

Buy-out investment

- Three estimated buy-out investments were completed in 2017, reflecting activity by Australian and global funds:
 - Navis Capital Partners acquired a 75% stake in Mainland Poultry, New Zealand's largest egg producer.
 - Australian private equity firm, Mercury Capital, received OIO approval to acquire half of Nirvana Health, New Zealand's largest independent primary health care group.
 - Privately owned transport and shipping company, Strait Shipping Limited was acquired by Australian based CHAMP Private Equity.



Case studies

Investment in new pain therapy

The Medical Research Commercialisation Fund (MRCF) invested NZ\$8 million in March 2017 in Series A funding for KEA Therapeutics, an early stage pharmaceutical company which is developing a new drug for the relief of severe pain.

KEA Therapeutics is a spin-out of the Auckland Cancer Society Research Centre and University of Auckland Faculty of Medical and Health Sciences. It will use the investment from the MRCF, including co-investment and support from University of Auckland Inventors Fund to advance the clinical development of a new pain drug.

KEA Therapeutics expects to commercialise their substitute for strong opioids in a range of clinical scenarios from pre-hospital to post-surgical pain relief and sedation. Kea Therapeutics will enter an already large and growing addressable market, driven by an aging population, chronic disease and increased hospital admissions.

Therapeutics has a highly-experienced management team and Board, including Dr Tom McCarthy. Dr McCarthy is former President and CEO of Spinifex Pharmaceuticals, who led the MRCF-funded pain treatment company through to its sale to global pharmaceutical company Novartis for US\$725 million in 2015.

The MRCF is Australia and New Zealand's largest life science investment fund, with AU\$500 million under management and is managed by venture capital firm Brandon Capital Partners. The MRCF is a unique collaboration between major Australian superannuation funds, the Australian and New Zealand governments, Australian state governments and more than 50 leading medical research institutes and research hospitals. The MRCF supports the development and commercialisation of early-stage biomedical discoveries originating from member research organisations, providing both capital and expertise to guide the successful development of new therapies.

Auckland UniServices, the managers of the University of Auckland Inventors Fund, partners with the best minds in academia and business to apply intelligent thinking to ideas that have the potential to change the world.

Borne to be global

Apple bought Kiwi tech company PowerbyProxi in October 2017.

The company was set up by university student Fady Mishriki who studied wireless power systems through his Bachelor of Engineering. PowerbyProxi was borne out of the world renowned wireless power research centre at The University of Auckland.

Fady Mishriki sought to commercialise this research and entered the Spark (now Velocity) entrepreneurship challenge in 2003, finishing as runner up and securing initial investment to develop the technology, leading to incorporation of PowerbyProxi in 2007.

In 2009, the company received its initial angel and venture capital backing led by Movac (with co-investor Evander) and in subsequent years secured funding from Ice Angels and technology giants like Samsung and TE Connectivity.

PowerbyProxi used magnetic induction and resonance for its wireless power technology and has developed a broad set of applications for consumer and industrial sectors. These include battery recharging solutions, wind turbines, industrial applications and process automation.

PowerbyProxi became a leading example of commercialising university IP. With a licensing agreement with The University of Auckland (UoA), the company went on to further develop and expand the potential applications for wireless power. In the process, PowerbyProxi built the largest and most valuable IP portfolio in the industry (over 350 patents). PowerbyProxi and UoA have developed a strong relationship together both recognising the benefits from aligning an industry leader close to a world leading research facility.

Movac is currently investing Movac Fund 4 through Series A and beyond investments into companies that have proven a product market, have a team in place to grow their business, and the potential to scale to over NZ\$100m in revenue.

PE funds grab a slice of Rockit Apples

Pioneer Capital and Oriens Capital teamed up in March 2017 to acquire a majority shareholding in Rockit Global Limited, which has the exclusive global license to grow and market the Rockit™ apple. Rockit™ is transforming both the snack food market and the fruit market worldwide with its unique size, flavour, novel tube packaging and healthy snack brand positioning.

Rockit™ apples were initially planted in orchards in Hawke's Bay and the business has expanded by licensing growers worldwide - this enables Rockit Global to meet rapidly increasing demand with Rockit™ apples available all year round. With thousands of trees reaching maturity in the next few years, revenue and profitability is expected to increase significantly.

Rockit Global earns revenue from royalties, marketing and IP levies as well as commissions charged to growers in NZ and overseas. In New Zealand, Rockit Global provides packing and distribution services to New Zealand growers, as well as management services to a number of orchards.

Rockit™ apples are prewashed, small in size (1.5 x the size of a golf ball) with a sweet flavour, thin skin, a distinctive bright red blush, small core, long shelf life and a crisp crunch. Its red skin with yellow/golden fruit colour is highly desirable in Asian markets.

Rockit Global was also a success story for members of Enterprise Angels who invested in the business in 2011 when the founder first sought to raise capital. Subsequently, the company attracted investment from private equity investors - something that few start-ups ever manage.

Rockit was the first investment by Oriens Capital, a recently established private company investor focused on mid-market businesses situated in regional New Zealand with enterprise values between NZ\$10 million to NZ\$50 million.

It was also the first investment in Pioneer Capital's NZ\$260 million third fund. Pioneer Capital is an investor in New Zealand businesses that are focused on growth in large international markets.

“Access to capital and expertise accelerates growth of NZ businesses.”

Matthew Riley, NZVCA Chair

Opinion – NZVCA Chair

Matthew Riley
Chair, NZVCA



The strong 2016 fund-raising year was expected to precede a period of strong investment activity. The total investment in 2017 of nearly \$900 million into accelerating the growth of New Zealand companies is indicative of a strong and healthy private capital market.

When we combine that growth capital with the financial and strategic expertise introduced by specialist private equity managers, the outcome is invariably better businesses that achieve their objectives more quickly. This has the ability to create an enduring legacy of accelerated growth and efficiency in a domestic economy that has struggled to make any meaningful gains in productivity for some time.

The continued strength of the New Zealand market has attracted international investment alongside New Zealand investors and managers, confirming the presence of good quality companies and management teams. International fund managers were as numerous as local fund managers investing in New Zealand in 2017 although this was predominantly in the early-stage venture space.

The EY New Zealand Private Equity and Venture Capital Monitor measures the level of professional investment activity in New Zealand's private markets. Given the relative importance of private markets in this country when compared to most of its peers, this is an important piece of research and our thanks go to EY for producing it.

The solid contribution of venture, mid-market and top-end total activity demonstrated a balance across the entire market not previously witnessed. It is particularly pleasing to see the increase in early-stage venture activity, including both investments and divestments.

Capital invested

The investment activity of domestic mid-market fund managers in 2017 was unprecedented. The highest level of total mid-market investment was led by the highest level of recorded investment by local managers. This investment performance in a competitive market illustrates the increasing maturity of this space, with a number of managers now deploying their third or fourth fund and having successfully navigated a range of different economic cycles.

In the early-stage venture market we have long acknowledged a gap in the market for Series A/B funds managed by teams with the particular skillset to execute in this challenging environment. The active participation of international funds in investment rounds in 2017 is positive for both domestic investors and entrepreneurs but does not remove the need to promote more local fund managers.

Outlook

The short-term optimism of survey participants has reduced since last year and remains subdued further out due to continuing expectations of global market volatility, increasing interest rates and of the potential impact of increasing regulation. The speculation that we are nearing a peak in the economic cycle has not abated since last year.

Investment in private New Zealand companies continues to provide prospects for good managers to accelerate growth and build capability. Institutional investors continue to increase mandates targeting private equity.

Industry development

As an industry body, we continue to explore ways to promote excellent outcomes for all stakeholders. We have recently undertaken research to better understand the perceptions and priorities of members and stakeholders in the community. This work has reinforced our focus on being more vocal about the combined strength of investors, fund managers and company owners in building strong and enduring New Zealand companies.

I encourage you to support the Association's efforts and wherever possible, to contribute to the conversation around accelerating growth and improving productivity through the continued development of New Zealand's private capital markets.

Outlook

“The focus of fund managers on investment in export growth, new markets, recruitment and R&D is proof of the need for private capital investment.”

Brad Wheeler, Partner, EY

Industry outlook

The outlook for the New Zealand private equity and venture capital market is generally positive. VCs see challenge in demonstrating strong returns and the ability to execute divestments. PE fund managers continue to see the impact of strong demand for assets and its impact on pricing, and are increasingly seeking to bridge valuation gaps through structures which share risk with business owners.

As for the investee companies, currency volatility and potential increases in interest rates are key areas of concern, together with the availability of skilled and experienced personnel.

The New Zealand IPO market saw minimal activity in 2017, whilst private M&A activity remained buoyant.

Plans for investee companies

Respondents were asked their plans in relation to new investee companies. In 2017 these plans included:

- ▶ Increasing capital expenditure
- ▶ Acquisition activity
- ▶ Growth in exports and expansion into new markets
- ▶ Increasing recruitment, R&D and marketing spend
- ▶ New product launches

Challenges and opportunities

Respondents identified the following factors which they consider will impact venture capital and private equity activity in New Zealand over the next 12 months:

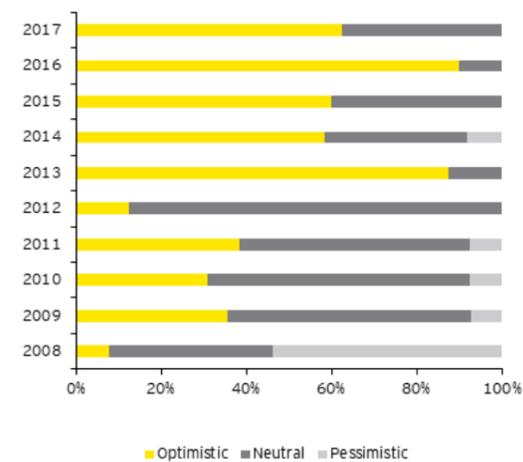
- ▶ Large amounts of capital available for deployment and heavy demand for the same opportunities.
- ▶ The recycling of capital from exits in order to raise new funds.
- ▶ Mixed views as to the potential impact of regulatory constraints to offshore investors into New Zealand.
- ▶ Valuation expectations of target companies and ability to structure deals which share risk with the business owners to meet these expectations.
- ▶ Restrictions placed on foreign direct capital investment into New Zealand owned assets.

Respondents were also asked to comment on key factors expected to affect their investee companies over the next two to three years, which included:

- ▶ Global economic volatility and currency fluctuations
- ▶ Cost of debt
- ▶ Currency fluctuations and interest rates
- ▶ Rising labour costs and limited availability of skilled labour in New Zealand
- ▶ Ability to achieve growth in exports and expansion into new markets
- ▶ Increase in R&D spend in light of government’s planned tax credits

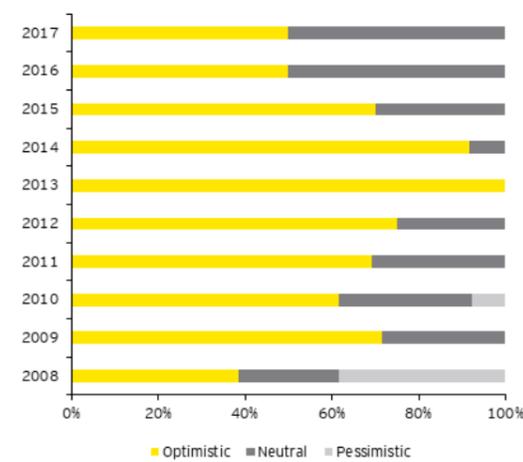
Next six months

Respondents’ short term outlook is slightly less positive than last year but still largely optimistic, reflecting the New Zealand economy’s relative resilience compared to global markets.



Next 18 months

The outlook for the next 18 months remains consistent with recent years, with continued global geo-political uncertainty a factor.

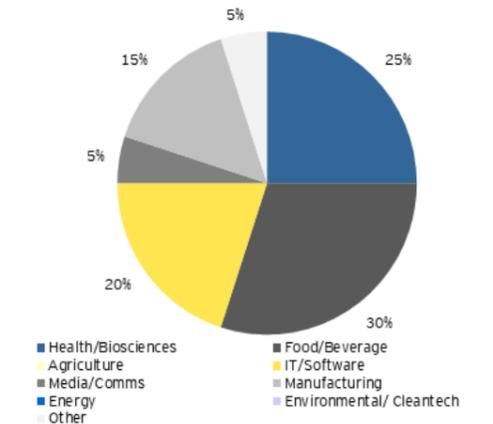


Outlook by sector

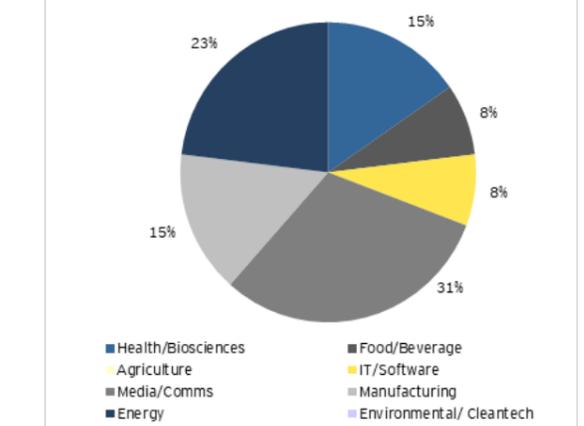
For 2017, respondents were asked to identify which sectors they were most optimistic and most pessimistic about.

Food/Beverage and Health/Biosciences were sectors generating significant optimism whilst fund managers have a more pessimistic view of Energy and Media/Communications sectors. Managers have a split view regarding Manufacturing, potentially demonstrating that niche opportunities still exist in New Zealand.

Sectors most optimistic about



Sectors most pessimistic about



Activity summary

Currency: NZ\$m	FY03	FY04	FY05	FY06	FY07	FY08	FY09
Investment							
Venture capital	43.6	50.2	63.0	75.6	81.9	66.1	34.0
Mid-market PE	44.1	157.0	184.7	84.8	203.7	127.8	58.7
Buy-out PE	0.0	0.0	136.9	1,048.5	937.7	40.1	62.7
Total	87.7	207.2	384.6	1,208.9	1,223.4	234.0	155.4
Investment (no. of deals)							
Venture capital	42	44	50	77	60	52	63
Mid-market PE	7	18	25	18	23	31	12
Buy-out PE	0	0	4	17	2	1	3
Total	49	62	79	112	85	84	78
Divestment (NZ\$m)							
Venture capital	0.0	0.0	1.8	2.1	10.0	0.0	17.1
Mid-market PE	85.5	10.7	28.4	28.2	76.3	46.5	60.8
Buy-out PE	0.0	0.0	154.6	172.0	200.0	301.5	391.5
Total	85.5	10.7	184.8	202.3	286.3	348.0	469.4
Divestment (no. of deals)							
Venture capital	0	0	1	4	3	1	1
Mid-market PE	7	2	5	5	7	12	6
Buy-out PE	0	0	1	1	1	1	2
Total	7	2	7	10	11	14	9
Total activity – investments and divestments (NZ\$m)							
Venture capital	43.6	50.2	64.9	77.6	91.9	66.1	51.1
Mid-market PE	129.5	167.7	213.1	113.0	280.1	174.3	119.5
Buy-out PE	0.0	0.0	291.5	1,220.5	1,137.7	341.6	454.2
Total	173.2	217.9	569.4	1,411.2	1,509.7	582.0	624.8
Average Investment deal size							
Venture capital	1.0	1.1	1.3	1.0	1.4	1.3	0.5
Mid-market PE	6.3	8.7	7.4	4.7	8.9	4.1	4.9
Buy-out PE	0.0	0.0	34.2	61.7	468.8	40.1	20.9
Average for all	1.8	3.3	4.9	10.8	14.4	2.8	2.0

Currency: NZ\$m	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17
Investment								
Venture capital	94.4	36.6	26.8	54.8	55.8	62.5	92.3	217.3
Mid-market PE	130.0	223.0	84.6	191.5	243.5	284.1	100.8	333.7
Buy-out PE	70.0	294.5	0.0	210.0	0.0	0	1,005.6	325.0
Total	294.4	554.0	111.4	456.2	299.3	346.6	1,198.7	876.0
Investment (no. of deals)								
Venture capital	67	70	50	66	62	69	50	48
Mid-market PE	14	12	12	15	19	17	11	17
Buy-out PE	1	2	0	1	0	0	5	3
Total	82	84	62	82	81	86	66	68
Divestment (NZ\$m)								
Venture capital	1.8	0.0	0.0	0.0	0.4	0	0.0	51.2
Mid-market PE	108.2	116.3	76.7	2.9	148.3	147.8	134.9	62.4
Buy-out PE	0.0	791.6	0.0	662.5	471.6	0	223.4	0.0
Total	110.0	907.9	76.7	665.4	620.3	147.8	358.3	113.6
Divestment (no. of deals)								
Venture capital	2	0	0	0	2	0	0	2
Mid-market PE	5	7	5	3	5	4	5	2
Buy-out PE	0	3	0	4	2	0	4	0
Total	7	10	5	7	9	4	9	4
Total activity – investments and divestments (NZ\$m)								
Venture capital	96.2	36.6	26.8	54.8	56.2	62.5	92.3	268.5
Mid-market PE	238.2	339.2	161.3	194.4	391.7	431.9	235.7	396.1
Buy-out PE	70.0	1,086.1	0.0	872.5	471.6	0	1,229.0	325.0
Total	404.4	1,461.9	188.1	1,121.7	919.5	494.4	1,557.0	989.6
Average Investment deal size								
Venture capital	1.4	0.5	0.5	0.8	0.9	0.9	1.8	4.5
Mid-market PE	9.3	18.6	7.0	12.8	12.8	16.7	9.2	19.6
Buy-out PE	70.0	147.2	0.0	210.0	0.0	0.0	201.1	108.3
Average for all	3.6	6.6	1.8	5.6	3.7	4.0	18.2	12.9

About the survey

The survey

The New Zealand Private Equity & Venture Capital survey is based on responses received from venture capital and private equity participants in the New Zealand market, including firms from both New Zealand and Australia. The values reported represent the equity component of transactions only. We have also included in our analysis any publicly announced information, acknowledging S&P Capital IQ as a source of data, in addition to venture capital activity as reported in Startup Investment NZ publication. We do note that there are a small number of industry participants that elect not to participate.

Data integrity/privacy policy

All data received through The New Zealand Private Equity & Venture Capital survey process is the property of the NZVCA and Ernst & Young. Other than for use in the monitor document, all data is subject to the principles of Ernst & Young's Privacy Policy and will not be sold or released to any other parties.

If you are aware of a colleague that did not receive a copy of the New Zealand Venture Capital and Private Equity Monitor or if you would like to participate in future surveys, please contact either Brad Wheeler or Tom Goad at EY or Colin McKinnon at the NZVCA. Contact details are provided below.

About EY Transaction Advisory Services (TAS)

How organisations manage their capital agenda today will define their competitive position tomorrow. We work with our clients to help them make better and more informed decisions about how they strategically manage capital and transactions in a changing world. Whether you're preserving, optimising, raising or investing capital, EY's Transaction Advisory Services bring together a unique combination of skills, insight and experience to deliver tailored advice attuned to your needs - helping you drive competitive advantage and increased shareholder returns through improved decision making across all aspects of your capital agenda.

For more information about the New Zealand Private Equity and Venture Capital Monitor or to find out more about EY, please contact one of the specialists noted below:

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ey.com/nz/transactions

About the New Zealand Private Equity & Venture Capital Association (NZVCA)

The NZVCA is a not-for-profit industry body committed to developing the venture capital and private equity industry in New Zealand. Its core objectives include the promotion of the industry and the asset class on both a domestic and international basis and working to create a world-class venture capital and private equity environment.

Members include venture capital and private equity investors, financial organisations, professional advisors, academic organisations and government or quasi-government agencies.

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