

December 2020 Update

Pencarrow Newsletter

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Pencarrow has had another busy year in 2020

It has been a fair while since we produced our last newsletter which was dated February 2019. In that newsletter we announced the first three investments of Fund V following the raising of that fund in April 2018. Those investments (The Collective, Seequent and Avanti Finance) have all made solid progress including two significant add-on investments by Seequent. Since that update, Pencarrow has been busy and undertaken three further platform investments for Fund V (RedShield, NZ Frost Fans and Skin Institute) and made a significant add-on acquisition for Bridge Fund investee, MMC, significantly enlarging the size of that business, acquiring the Aegis wealth platform business from ASB Bank. In Fund IV we have also re-shaped that portfolio (which has three remaining investments) by divesting significant components of both Umbrellar and BeGroup. We provide more detail later in the newsletter on each of these transactions.

Pencarrow manages over \$450 million of aggregate committed capital across three funds with virtually all the aggregate committed capital of the older two funds, Fund IV (\$124 million) and the Bridge Fund (\$80 million), now deployed. In total with the three new investments in Fund V, Pencarrow has a portfolio of 12 investments across three funds with one of those investments (The Collective) spanning two funds.

Fund V Investment Stage Making Good Progress

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. With just under three years of the Fund V investment stage now elapsed the fund has made six platform investments, completed two add-ons and called 58% of its capital. A healthy deal pipeline ensures the pace of investment should continue into 2021 despite the impacts of the coronavirus pandemic.

Impact of Covid-19 on the Portfolio

The onset of the Covid-19 pandemic and subsequent lockdowns in New Zealand and around the world have had a far-reaching effect on businesses. Fortunately for New Zealand, we appear to be one of the few countries in the world that has had success in elimination of local transmission of the virus. By May, citizens and businesses were able to return to operating largely as normal other than having our

border effectively closed (notwithstanding the second lockdown in Auckland during August).

Across all three funds, Pencarrow has been fortunate that it has a relatively small exposure to those industries most effected by the global pandemic such as travel, tourism, hospitality and retail. Portfolio companies with consumer facing products such as The Collective (yoghurt) and Essano (skincare) faced changing consumer demand patterns but were able to trade through the lockdowns well given the majority of sales are made through the grocery and pharmacy channels. Skin Institute, which undertakes medical and cosmetic dermatology, was required to shut its appearance medicine retail stores during the level three and four lockdown periods but was able to continue operating its core medical services business.

Overall, Pencarrow's portfolio continued to perform well following the onset of Covid-19 with the key theme across the portfolio being the focus on employee safety, which has been at front of mind in all executive decision making.

Strong Flow of Deal Activity

Pencarrow has delivered a strong cadence of platform investments in Fund V alongside a number of transactions within the existing portfolio.

In October 2019, Fund V made its fourth investment by providing \$11.5 million of expansion capital for Wellington-based cybersecurity business, RedShield,

giving Fund V an ownership stake of 21% with the potential to provide additional expansion capital as the company grows. RedShield is an emerging global leader in the provision of advanced shielding and protection of web applications and application programming interfaces. The software is easily deployed over the top of an entity's existing code base to rapidly protect against cyber threats. Sales are primarily to large healthcare providers, financial services businesses, governments and corporates with customers located in New Zealand, Australia, US and the UK.

In November 2019, Fund V acquired 75% of leading global frost protection business, NZ Frost Fans, which designs and manufactures frost fans that protect a wide range of horticultural products. The company is the leading supplier of frost fans in New Zealand and Australia and has a top three position globally with products also sold in Turkey and Chile. The company has a strong competitive position through its blade design creating lower noise and greater effectiveness than competing designs. Remote monitoring is also undertaken through its subsidiary Loncel Technologies.

In April 2020 Fund V made its sixth investment, acquiring an 17.6% stake in the Skin Institute alongside the founders and management team (who are largely shareholder medical practitioners). Skin Institute is a leading domestic dermatological medical practice. The company also operates in the appearance medicine market, through its two retail brands; Lovely (by Skin Institute) and Off & On. Further expansion capital is likely to be provided to Skin Institute to support growth plans and potentially purchase shares from existing shareholders.

In addition to the three platform investments mentioned above, Fund V investee company, Seequent, completed an add-on investment of Calgary-based geotechnical software business, Geoslope during October 2019. This will enhance Seequent's geosciences platform following the earlier acquisition of geophysics software business, Geosoft.

In addition to the activity of Fund V, another portfolio company of Pencarrow in its Bridge Fund, MMC, made a very sizeable add-on acquisition of Aegis, the wealth management platform owned by ASB Bank. This acquisition will considerably accelerate MMC's move into private wealth administration complementing its other activities in fund accounting, unit pricing and registry services.

In November 2020, Fund IV completed the 100% sale of

Freeparking, a division of Umbrellar, to Dreamscape Networks. Freeparking is New Zealand's leading domain name registrar and web hosting provider with more than 90,000 customers. Robert Rolls, Umbrellar Group CFO and General Manager of Freeparking, has moved with the business, along with ~42 Freeparking employees. The remaining investment in Umbrellar is now solely comprised of the cloud business (Umbrellar Cloud). Umbrellar Cloud will continue to be owned and operated by Fund IV and the leadership team. Michael Foley, Chair, will continue to oversee Umbrellar Cloud and support the business's CEO, Dave Howden.

Personnel Changes and New Office

Since our last newsletter there have been two additions to the team at Pencarrow. Susan Trinh has joined as AML Analyst from Jarden and Jessica Monaghan has joined as Office Manager.

The Pencarrow Auckland office moved premises in early 2020, from 125 Queen Street to 33 Federal Street. In terms of Pencarrow staff, Jonathan Goldstone and Hazel Martin are permanently based in Auckland, with the remainder of the team based in Wellington.

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 (called the Bridge 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 April 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 six investments and will seek to undertake a further two to three 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 and the opportunity to create significant value.

Portfolio Investments

Pencarrow currently has three investment funds with 12 active portfolio investments across those three funds. Fund IV concluded its investment period in September 2016 with six portfolio investments which has since been reduced to three following the successful sales of Icebreaker, BrewGroup and Seequent. The Bridge Fund concluded its investment period in May 2018 with four portfolio investments including one, The Collective, shared with Fund V. Fund V was raised in April 2018 and to date has deployed over half of its committed capital of \$250 million into six investments. Each of the investments in Fund IV, Bridge Fund and Fund V is described in more detail below.

BeGroup

BeGroup

BeGroup is an aged care and retirement village operator established by Pencarrow in conjunction with Guy Eady, a highly experienced aged care executive. BeGroup currently operates two villages; The Falls Estate in Whangarei and The Rawhiti Estate in Remuera, Auckland.

In September 2020 BeGroup sold a development site in Auckland's Half Moon Bay to NZX-listed aged care company Summerset. The sale has strengthened BeGroup's balance sheet and enables the Executive Team to focus on the management of the other two operational villages.



SolarZero

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



Umbrellar

Umbrellar, a leading NZ domain name and cloud hosting business, recently completed the 100% sale of Freeparking (domain name segment of the business) to Dreamscape Networks in November 2020. The focus of management is now solely on growing the Cloud side of the business, which has been renamed Umbrellar Cloud Limited.

Umbrellar Cloud leads the New Zealand market in the promotion and delivery of cloud services, specifically Microsoft Azure and Azure Stack. Umbrellar offers a number of cloud solutions for businesses, including options for data to be hosted domestically whilst retaining all the benefits of the public cloud.



MMC

MMC is a leading New Zealand outsourced fund and investment administration business with over \$85 billion of client funds under administration. MMC's intuitive and easy-to-use web interface is a key differentiator in the fund administration market. In December 2019, MMC successfully acquired Aegis, a leading wealth management administration platform, owned by ASB Bank. The acquisition has enabled MMC to accelerate its growth into the wealth management administration space, which it had entered organically in 2018.



Essano (formerly Mix)

Essano is a leading New Zealand personal care products business. Essano 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. Its brands have a mid-market price point, positioning it at the top end of the mass market.



Netlogix

Netlogix is a 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.



The Collective

The Collective is a New Zealand headquartered dairy company that manufactures and distributes premium yoghurt, dairy and dairy-alternative products through the grocery channel. The Collective has operations in New Zealand, the UK, Australia, and France.



Seequent

Seequent designs and develops world-leading 3D geological modelling solutions for the mining, energy and environmental markets. Seequent's suite of geoscience software is a crucial part of mining, engineering and energy companies' workflows and daily decision-making across the globe.

Fund IV originally invested in Seequent in July 2014. In May 2018, Fund IV accepted an offer from a consortium led by Accel-KKR to acquire 100% of Seequent, a very successful outcome for Fund IV investors. The acquiring consortium included rollover investment from Seequent founders and management as well as participation of Fund V which took a 10% stake in the enlarged company.



Avanti Finance

Avanti is a leading New Zealand 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. Since its establishment in 1989 the company has provided secured personal and motor vehicle loans and, more recently, has diversified into providing first residential mortgages and SME loans.



RedShield

RedShield is a Wellington-based web application security-as-a-service business that provides advanced shielding and protection for web applications and application programming interfaces. The product is rapidly deployed over the top of an entity's existing code base to prevent cyber threats. RedShield's technology platform and service offering includes scanning (through other parties' scanning tools), security policy tuning, shield development and ongoing customer management of shields and vulnerabilities.



New Zealand Frost Fans (NZFF)

NZFF designs and manufactures frost protection solutions for a wide range of crops including grapes, almonds, citrus, apples and avocados. NZFF is the leading supplier of frost fans in Australia and New Zealand and has a top three position globally. Frost fans are manufactured in Hawke's Bay and are currently sold to customers in New Zealand, Australia, Turkey and Chile. NZFF also offers remote monitoring of frost fans through Loncel Technologies, a wholly-owned subsidiary.



Skin Institute

Skin Institute is a leading New Zealand dermatological medical practice. Its core medical services business was established in 1994 and its treatments and services include skin cancer, veins, cosmetic surgery, and appearance medicine. Dermatological services are provided by trained surgeons, specialists, doctors and nurses. It is the largest practice of its kind in New Zealand with nearly all of Skin Institute's competitors currently operating in a handful of locations.

Skin Institute also has two retail brands, Lovely (by Skin Institute) and Off & On. The two brands leverage Skin Institute's reputation as a leading dermatological practice to bring appearance medicine to the mass-consumer market.

Outlook

Despite numerous Covid-19 related disruptions across the globe in 2020, Pencarrow has continued its strong momentum from 2019, with the successful investment in Skin Institute in April and the sale of Freeparking from the Umbrellar Group in November as well as add-on investments to portfolio companies. Pencarrow portfolio companies (across all three Funds) continue to make progress towards achieving their respective investment theses following relatively robust trading through the Covid lockdown periods.

New Zealand remains well placed heading into 2021 as one of the few countries in the world which has effectively eliminated Covid-19, particularly relevant as we see significant second waves of the virus and daily infection records being broken in North America and Europe. This indicates our border in terms of travel will likely remain closed for the foreseeable future. The inability to travel internationally is probably one of the most significant issues affecting the operations of private equity firms and their portfolio companies while the pandemic persists. For globally oriented portfolio companies it is slowing down the entry into new markets and for mergers and acquisitions involving cross-border deals it is creating hurdles for add-on investments to portfolio companies.

Globally, hope of returning to "normality" remains pinned to development of an effective vaccine. Encouraging news out of companies such as Moderna and Pfizer provides hope, with recent developments indicating vaccines can achieve over 90 per cent effectiveness. Ultimately there remain many hurdles before a vaccine is ready for mass distribution across the globe.

Nevertheless, with record levels of dry powder (uncommitted capital) held by private equity firms there is pressure on these firms to invest and we are seeing merger and acquisition activity re-emerging to levels seen before the pandemic, albeit with deals being undertaken via video-conferencing and remotely rather than face-to-face. This is easier in some industries such as technology than in others more necessitating on-the-ground presence.

We hope that all readers, their staff and families remain safe and well.

Our Team

The Pencarrow Team



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