

Viewpoint

Pyne Gould Corporation Limited Newsletter

August 2009

The past few months have been busy ones for Pyne Gould Corporation (PGC). We've made some important progress towards PGC achieving its goal of becoming New Zealand's only publicly listed banking and asset management company.

Unfortunately, we have not been immune from the global financial crisis, which has been particularly severe on the property sector as a whole. This has meant that the impairment on MARAC's property development loans is higher than we initially expected and has also led to MARAC's rating being downgraded to BB+ (Negative) by Standard & Poor's following its annual review. The directors and management alike are disappointed with this.

Some uninformed media have described this new rating as "junk". That is certainly not the case and it is not a term used by Standard & Poor's. Moreover, it is not reflected in their report. Here is an extract:

"We retain our view that MARAC is one of the stronger finance companies in New Zealand, despite the company's recent asset quality pressure. Other factors that remain supportive of the rating include MARAC's sound business profile, underpinned by its market position as one of the largest domestically owned finance companies in New Zealand. Also supporting the rating is MARAC's sound funding and liquidity positions, and its parent's financial flexibility as a public listed company."

We know what MARAC has to do to earn back its BBB- (Stable) rating – a rating which is commonly recognised amongst the investment community as "investment grade". We are already well advanced with a strategy to achieve this.

To strengthen MARAC's business, there has been the recent appointment of a new CEO (outlined on page 2) and changes at the operational level, including ceasing lending on property development, a refocus on MARAC's core business of plant, equipment and vehicle finance and a tightening of credit processes. It remains our intention for MARAC to become a bank.

The group has also embarked on a range of structural changes. A key part of this is our intention to raise capital. We have appointed the respected stockbroking firm First NZ Capital to assist us and we expect to be in a position to tell you more about the capital raising in mid September after our annual results announcement on 28 August.

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Chairman

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We also recently announced a move into asset management with the creation of Perpetual Asset Management. We recently completed the purchase of established New Zealand-based asset management firm, Equity Partners Asset Management Limited (EPAM). From day one, Perpetual Asset Management, through the purchase of EPAM, will have an interest via management rights and direct equity in the EPIC Fund, which focuses on infrastructure. Another key consideration behind the purchase was that it delivers us the expertise to manage the Torchlight Credit Fund (Torchlight), which will focus on real estate.

The identified benefits of Torchlight to PGC are two-fold. Torchlight allows MARAC to exit the property loans no longer aligned with its banking strategy. Second, Perpetual Asset Management, through its interest in Torchlight, gets to benefit from the potential of any increase in margin on the MARAC loans which will be acquired at a discount to face value.

Perpetual Asset Management will be headed up by John Duncan as Chief Executive Officer, and chaired by PGC director and substantial shareholder George Kerr (read more below). John and George are two extremely capable and experienced businessmen who I am confident will ensure the success of this asset management business.

Even though the market environment continues to be challenging, these changes will create a stronger and more diversified PGC. They will also provide more choice for our customers and investors, and ultimately better returns for you.

A warm welcome to Jeff Greenslade

Our next piece of news is to welcome Jeff Greenslade to his new role as Chief Executive Officer of Pyne Gould Corporation and MARAC. Jeff is responsible for the overall strategy and operations of both businesses and his banking experience will be invaluable.

MEET A DIRECTOR OF THE BOARD

Introducing George Kerr



George Kerr

George Kerr's family ties with Pyne Gould Corporation (PGC) go back many years. He is the great-great-grandson of F H Pyne, who started one of PGC's founding businesses, Pyne & Co, in 1887. Since then, his family has been closely aligned with the company as shareholders and today George is PGC's largest sole shareholder.

George was appointed a director of PGC less than a year ago and brings more than twenty years' experience in the banking and asset management industry to the board. He has also been appointed as Chairman of PGC's new asset management arm – Perpetual Asset Management.

Looking at the current market environment, George compares it to the 1970s, and believes that a clear, strong strategy and sound finances are the keys to thriving through the lows of these market conditions.

According to George, success is also driven by focus – whether in a business or personal context. He was once given a book written by Friedrich Nietzsche, which included a quote which has always stayed with him: "Stop searching for the meaning of life, because what you choose is the meaning of life." George has taken this philosophy to heart. He believes that it's important to set your own values and goals and live life accordingly.

Jeff had a long and distinguished career with ANZ National Bank – holding a number of relationship banking roles, most recently Managing Director Corporate and Commercial Banking. Jeff also held several other senior positions at the National Bank and was a board member of UDC. This banking experience will be invaluable to us.

Congratulations to Perpetual Trust

2009 is going to be a significant year in our history as the business further evolves. It is also noteworthy in that it marks Perpetual Trust's 125th anniversary, and the 75th jubilee of PGG Trust.

Perpetual Trust commenced operation in Dunedin in 1884, and PGG Trust achieved Trust Company status by an Act of Parliament in 1934.

Perpetual Trust today employs a hundred people in seven branches, has over five thousand clients, administers almost \$1b of assets for private clients, trusts and estates, oversees more than \$250m in managed funds, and supervises more than \$21b as a corporate trustee.

Congratulations to Perpetual Trust on reaching this important anniversary.

Inside this Viewpoint

As always there is a wealth of interesting reading inside this *Viewpoint*. Below you'll find a profile on director George Kerr, the great-great-grandson of one of PGC's forerunning company founders. Jeff Greenslade brings you his first business update as Chief Executive Officer, and there are some questions and answers to help you interpret the business changes.

We will be in touch in September with the announcement of our annual results. Until then, you are welcome to contact us with any questions.

Sam Maling

Chairman

As well as his shareholding in PGC, George has interests in investment and asset management firms in Sydney and London. Some of his other business investments are more aligned with personal interests – such as an interest in Amisfield Vineyard in Central Otago and Treble Cone Skifield near Wanaka. George, his wife Kym and their four children are all skiers or snowboarders of varying degrees of enthusiasm and ability. His daughter Jeanie is one of the top junior snowboarders in the USA.

As a more leisurely pursuit, George also enjoys reading and usually has four or five books on the go. His favourite quote from *The Prince* by Niccolò Machiavelli, written in 1532, is very relevant in today's market: "Entrepreneurs are simply those who understand that there is little difference between obstacle and opportunity and are able to turn both to their advantage."

George is also involved with several charities, including Oasis Africa which runs a school for orphans in Kibera, Kenya; and the Black Dog Institute in Australia, which supports people with depression and bipolar disorder.

With George's family ties to PGC's history, he has a strong personal interest in ensuring that PGC continues to play a significant part in New Zealand's financial and rural sectors. He is looking forward to using his investment and asset management experience as PGC moves ahead with its future growth plans.

Questions and Answers on the Business Changes

The last *Viewpoint* noted our plans to establish PGC as New Zealand's only publicly listed banking and asset management company. This has received a lot of media coverage and there is speculation around what changes will occur for PGC to achieve this goal.

We will announce our annual results on 28 August and we expect to be in a position to announce the details of capital raising and other strategic moves in mid September. Meanwhile, we take this opportunity to answer some questions that can be clarified at this time. We look forward to bringing you further information on our value-enhancing changes for the business as they come more fully into focus.

1. Did PGC pay a fair price for EPAM?

We believe the price is fair. We sought independent advice in agreeing to the purchase price. We have also reached agreement that under certain circumstances, there could be a reduction in the price paid for EPAM.

2. When will we know the remaining details about changes within the group?

Due to legal and regulatory constraints, we're not able to provide full details now; however we expect to be in a position to announce all details of the planned changes for the group in mid September.

3. How much capital does PGC intend to raise and what will the funds be used for?

This will be announced in mid September as the details are still being worked through.

The requirement for funds is driven by a desire to take advantage of the many consolidation and investment opportunities in the non-bank and asset management sectors. We currently expect that all shareholders will be given the opportunity to invest in aspects of the capital raising and we hope that you will take advantage of this offer. Shareholders will also have the opportunity to vote on key aspects of the capital raising at a shareholders meeting intended to be held in early October.

4. When will MARAC receive its banking licence?

Neither the timeframe nor the outcome can be pre-judged. The Reserve Bank, as expected, has a rigorous process, and all we can say is that MARAC is working hard to achieve what we believe to be the right levels of capital, asset mix, personnel and systems to position MARAC in the best way possible to apply for a licence.

5. Is MARAC going to merge with or purchase any other finance companies?

We remain open-minded about the potential to build value through industry consolidation with good-quality partners. Following our capital raising, we expect to play an active role in industry consolidation if we see opportunities to create excellent value.

6. Why are MARAC's impaired property development loans higher than initially indicated?

The board and management of PGC are disappointed at the level of impairments that MARAC has suffered. Unfortunately we have not been immune from the global financial crisis, which has been particularly severe on the property sector as a whole. We announced the expected level of property asset write-down last month – ahead of our full-year result to be announced on 28 August – to keep the market well informed. We are, however, confident that the Torchlight Credit Fund will be able to manage these loans in a way that offers maximum return to PGC (through its investment in Torchlight) over the long term.



7. Has MARAC lost \$160m in property loans?

No. The MARAC portfolio of impaired property loans is to be transferred to another PGC subsidiary at its \$160m face value with payment to be made on commercial terms, so there is no loss to MARAC (although the PGC group will take the loss in a subsidiary other than MARAC). PGC has provisioned for a \$60–65m after-tax loss so Torchlight can acquire the portfolio of loans at market value.

8. Is George Kerr launching a takeover?

No. George Kerr has strong family links with PGC and has been the company's largest shareholder for a couple of years. PGC is fortunate to have George as a cornerstone shareholder (which he intends to remain) who will contribute both capital and substantial time as Chairman of our new asset management company, Perpetual Asset Management. PGC is expected to continue to be a public company owned by the descendants of the founding families and other small shareholders and institutions.

9. Will George Kerr be selling unwanted assets he owns into Torchlight?

There is no current intention for PGC to acquire any property assets from George Kerr. Neither PGC nor its subsidiary MARAC has lent any funds to George Kerr or his companies. PGC and its subsidiaries have strong governance processes to ensure that any transaction undertaken is in the best interests of all shareholders.

10. Why has the PGC share price fallen?

It can be a difficult exercise to read the mood of the market on any issue. Our observation is that it's a common response for investors to hold back when they perceive that a capital raising might be at hand. At this point, some of the details are not settled, and as a result, the capital raising remains an incomplete proposal, which must remain confidential. We will be moving to deal with the market's desire for information as quickly as possible, but we are mindful of making quality decisions to position the company for the medium and long-term rather than merely addressing short-term issues.

11. What does the rating change from BBB- (Stable) to BB+ (Negative) mean for MARAC?

As Standard & Poor's stated in its report, "MARAC is one of the stronger finance companies in New Zealand, despite the company's recent asset quality pressure." We agree with this statement. Whilst the change is disappointing and we will be doing all we can to earn back a BBB- (Stable) rating, this is still a comparatively good rating for MARAC. It will still continue supporting small and medium-sized New Zealand businesses, which are the economic backbone on the country.

Sam Maling
Chairman

PGC Business Update



Jeff Greenslade

It's an honour to have been appointed Chief Executive Officer of Pyne Gould Corporation and MARAC. Having been brought up in Otago and schooled in Canterbury, I am deeply conscious of PGC's long heritage and status.

While I come into the role at a time of great challenge I am convinced that this is also a time of significant opportunity for a company such as ours that is strong financially and has a clear strategy.

As Chairman Sam Maling mentioned on page 1, there has been a lot of activity going on in progressing us towards our desired business structure. I am pleased that the Board has entrusted me with their support to lead your company through this important transition period and beyond.

I am confident that the changes we are making will in time create value, not only for the many customers across the PGC group, by offering them new products and services, but also for you, our shareholders.

A key opportunity for the business

A key to our success will be our ability to utilise our significant customer base. Spread across PGC's businesses are 50,000 to 80,000 customers reflecting 'middle New Zealand' – urban and rural small businesses, their owners, and mid-to-high-income earning individuals. This is not just a valuable demographic – it is also one that is increasingly under-served by financial institutions. When you add this to our many ancillary business relationships, our potential customer base increases significantly.

The creation of Perpetual Asset Management

The purchase of EPAM and the creation of Perpetual Asset Management provides an exciting new opportunity to service this customer base and is a great foundation to build a market-leading business. Perpetual Asset Management will be led by two of the best people in the asset management field: John Duncan as Chief Executive Officer and George Kerr as Chairman.

MARAC becoming a bank

It was unexpected and disappointing that MARAC's credit rating was recently downgraded by Standard & Poor's to BB+ (Negative). Steps have been taken to strengthen MARAC's position including ceasing lending on property development and tightening our credit process. We know what to do to earn back the "investment grade" rating for MARAC and to ensure that it is not put in this position again.

Once that is achieved, a real focus of mine will be transitioning MARAC to become a bank. We're continuing working hard to achieve what we believe to be the right levels of capital, asset mix (thus the move away from property development lending), personnel and systems to position MARAC in the best way possible in its application for a banking licence.

MARAC's loan portfolio

The divestment of MARAC's impaired property loans will see MARAC focusing on what currently makes up 80% of its lending portfolio – financing the quality end of the market for plant, equipment and business assets, as well as new and near-new vehicles. This part of MARAC's loan book continues to perform well.

Perpetual Trust is business as usual

Perpetual Trust will continue to provide estate management and trust services, as well as corporate trustee services. We expect distribution of Perpetual Asset Management and Perpetual Trust's products to widen through offering wealth management and trust services to MARAC customers.

Looking forward for the group

We are fortunate to have the skill base, capital resources and clear strategy to see the PGC group and their businesses through this recessionary environment. The proposed capital raising will play an important role in allowing us to take advantage of the significant consolidation and investment opportunities that have and will continue to present themselves and, in turn, add value to your shareholding. We look forward to you coming on this journey with your company, and hope that you will take part in the capital raising.

I will keep you up-to-date with progress over the coming months.

Jeff Greenslade
Chief Executive Officer



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