

Colonial First State Diversified Private Equity Fund Newsletter

September 2005

- The Colonial First State Diversified Private Equity Fund ('the Fund') gives investors exposure to unlisted companies across a broad range of industries at various business life cycle stages.
- The Fund aims to achieve returns for investors that are 5% p.a. greater than traditional listed investments over its ten-year life.
- The Fund will commit no more than 40% of its total committed capital to 'Early Stage' investments and at least 60% of its total committed capital to 'Later Stage' investments.
- The Fund is managed by a team of seven investment professionals (headed up by Steve Baldwin) and also has the benefit of an Investment Advisory Council (chaired by Bill Beerworth).

The Fund at a Glance – as at 30 June 2005

Fund size (four equal instalments – all received from investors):	\$103.1 million
Cumulative cash distributions paid to investors to 30 June 2005:	\$54.2 million
Remaining Net Assets of the Fund as at 30 June 2005:	\$82.4 million
	\$136.6 million
Analysis of Fund's Net Assets as at 30 June 2005:	
→ Current investment portfolio, at valuation (audited):	\$40.6 million
→ Cash distributions paid on 22 September 2005:	\$17.5 million (note 1)
→ Contingent investment commitments (currently undrawn):	\$5.4 million (note 2)
→ Cash available for new and follow-on investments	\$18.9 million
	\$82.4 million
Current Investment portfolio, at cost:	Australian Vinyls – \$11.2 million SG Fleet Services – \$8.1 million Endeavour Healthcare – \$7.8 million Mincom – \$4.6 million Integration Management – \$4.1 million Technisyst – \$3.8 million AtCor Medical – \$2.5 million

Note 1: \$16.0 million of this distribution relates to proceeds from the Penrice IPO (company listed on ASX in July 2005) and \$1.5 million relates to a further return of capital received from Endeavour Healthcare (September 2005).

Note 2: \$2.8 million of this contingent investment commitment relates to the Australian Vinyls investment and \$2.6 million relates to the SG Fleet Services investment.

Market conditions and investment activity in the June 2005 half-year

After unprecedented levels of capital raising for new private equity funds in the December 2004 half-year (particularly for listed vehicles with very broad investment charters), the June 2005 half-year has seen a return to more normal levels. The amount of capital recently raised, however, has undoubtedly increased pricing pressure for new investments, particularly for larger transactions. This is further amplified by the increasing leverage that is being offered to private equity sponsors by some of the more aggressive lenders in the market.

The benefits of the above-mentioned developments are that there are now an ever-increasing number of examples where offers from private equity managers are considered very competitive (and in some cases, even superior) to the offers from trade purchasers. The private equity asset class can also now claim to have a large database of both completed investments and successful realisations. Over the past six months, the Fund has participated in another two of the industry's success stories (**Flexirent** and **Penrice**).

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The Manager's private equity team continues to focus on buyouts and expansion opportunities in the 'mid-market', being private businesses which typically have an enterprise value in the \$30-200 million range. Although there are still pricing pressures in this segment of the market, we believe that this segment offers the greatest number of prospective attractive investment opportunities.

Following the significant new investment commitment (\$14.0 million) to **Australian Vinyls** during the June 2005 half-year, the Fund is now close to being 'fully committed'. The Manager intends to reserve some of the residual cash in the Fund to support any acquisitions that are value-accretive for the existing portfolio companies, with the balance of the residual cash being targeted for one new large investment.

This final new investment for the Fund has been identified and terms have been negotiated with the vendors. The final investment commitment for the Fund should be in the \$12-13 million range and due diligence is well advanced. Final completion of the investment is expected in November 2005.

In addition to finalising new investments for the Fund, the Manager has also completed follow-on investments in some of the existing portfolio businesses. To that end, the Fund committed to a further \$0.8 million investment in **Mincom** in March 2005 (through a secondary purchase from an existing shareholder) and also committed a further \$2.0 million to **SG Fleet Services** in May 2005 (in order to take up the Fund's pro-rata share of a capital raising to finance the SMB Fleet acquisition).

While the proposed Initial Public Offering ('IPO') of **AtCor Medical** discussed below is a capital raising transaction rather than a realisation, it clearly moves the Fund's investment much further along the path to ultimate liquidity.

Investment activity in June 2005 half-year: \$14.0 million new commitment to Australian Vinyls



Australian Vinyls Corporation Limited

Melbourne-based Australian Vinyls Corporation ('AVC') is Australia's only manufacturer of polyvinyl chloride resin and was originally formed as a joint venture between Orica (formerly ICI), and PolyOne in 1997. Following a management buyout of the business from Orica in 2002, the business was established with an independent head office and manufacturing plant in Laverton, Victoria. PVC resin is sold largely to pipe manufacturer, for use in residential, commercial and infrastructure construction.

Our Fund completed what is known in the private equity industry as a 'secondary buyout' (ie. the management team remain as shareholders, but the initial financial investor is replaced by a new financial investor) in June 2005. The Fund is represented on the AVC Board by Tom Fennell.

AVC was considered an attractive investment for the Fund due to its very strong management team with a proven track record in leveraged buyouts, long-standing customer relationships and the company's position as sole Australian manufacturer with a plant running at full capacity. Opportunities for the future include both development of new products and potential acquisitions of chemical trading businesses.

AVC's performance for the September 2005 quarter has been well ahead of the business case on which the Fund invested. With annual revenues in excess of \$250 million, AVC is of sufficient scale for either a sale or IPO to be considered as an exit strategy.

Investment activity in June 2005 half-year: Flexirent investment realised for a \$17.8 million profit



Sydney-based Flexirent is a market leader in the Australian 'microticket' leasing segment, operating mainly via retail distribution channels including Harvey Norman, Australia's largest retailer of IT equipment. The Fund had acquired its original investment of \$12.8 million in February 2003.

The Flexirent business grew significantly from the date of the Fund's initial investment – assisted by a strong retail environment, but primarily through the performance of a new Chief Executive Officer and his senior management team. During 2003 and 2004, there was also a significant expansion in both the number and size of funding facilities for the underlying IT equipment.

In February 2005, the Fund realised its Flexirent investment for cash proceeds of \$30.6 million through a share buy-back agreement with the company. The investment was a very good one for the Fund and an internal rate of return ('IRR') of approximately 60% p.a. was achieved over the holding period of two years.

All proceeds from the Flexirent sale were distributed to the Fund's unitholders as part of the 23 June 2005 distribution.

Investment activity in June 2005 half-year: Penrice investment fully realised for a \$16.0 million profit



Adelaide-based Penrice is a manufacturer of soda ash, sodium bicarbonate and other related products. The Fund had originally acquired its investment for \$11.2 million through a secondary buyout in May 2004, alongside another private equity group and the existing Penrice senior management team.

With annual revenues in excess of \$100 million at the time of the Fund's investment, Penrice is a mature business with a 'blue chip' customer base and strong profit margins. Soda ash is a key input to the glass manufacturing industry and Penrice satisfies in excess of 80% of the Australian domestic demand. Penrice also owned very valuable salt fields at the time of the Fund's investment.



The group's salt fields (together with a long-term supply agreement) were sold to an ASX-listed group in May 2005 for what the shareholders considered to be a very attractive price. In addition, strong soda ash prices in the second half of the 2005 financial year enabled Penrice to renew a number of their customer contracts, which in turn provided sufficient future revenue certainty for an IPO to be completed in July 2005.

Proceeds from the sale of the salt fields (\$11.2 million) were distributed to the Fund's unitholders as part of the 23 June 2005 distribution, while proceeds from the Penrice IPO (\$16.0 million) have been distributed to the Fund's unitholders as part of the 22 September 2005 distribution.

Investment activity in June 2005 half-year: Agrilink realised at a \$2.1 million loss

AGRILINK

Adelaide-based Agrilink provides irrigation technology services to enable growers to make better decisions on water and

fertiliser usage. Customers include the major wine, cotton and tropical producers in Australia.

The Fund invested in Agrilink in May 2002. A number of external factors adversely affected the company soon after the Fund's initial investment, in particular the Australian drought. As part of a capital raising in June 2005, the Fund realised its investment for a nominal amount through a sale to other Agrilink investors.

Existing investment – proposed Initial Public Offering ('IPO') of AtCor Medical



Sydney-based AtCor Medical develops and markets the SphygmoCor range of cardiovascular diagnostic devices, which provide physicians with important data about the condition of the heart and the

arterial vascular system that currently can only be measured by the insertion of a catheter. The Fund acquired its shareholding in February 2004 and is represented on the AtCor Medical Board by Peter Jenkins.

Over 13 million people in the USA have hypertension which cannot be controlled with current diagnostic and therapeutic regimens. SphygmoCor has already gained regulatory approval in key markets, including the US, Europe and Japan. The device has achieved significant penetration into the research and clinical trial markets, with over 750 units currently placed in leading cardiovascular clinical research centres in 40 countries worldwide. Leading institutions such as The Mayo Clinic have endorsed the technology.

AtCor Medical is currently considering an IPO on the Australian Stock Exchange to raise expansion capital of \$15.0 million. It is considered likely that the Fund will have some period of trading escrow over its shares, which will subsequently be realised in an orderly manner over time.

Existing investment – SG Fleet Services on acquisition trail



FLEETAUSTRALIA

Sydney-based SG Fleet Services was originally established by JSE-listed Super Group Limited, a South African

fleet management and automotive supply chain business, to acquire the Commonwealth Bank of Australia's fleet management business. Super Group had expressed a strong desire to have an Australian private equity partner in the transaction, and the Fund acquired its shareholding in SG Fleet Services in June 2004. The Fund is represented on the SG Fleet Services Board by Steve Baldwin.

The former Commonwealth Fleet Lease business (now renamed Fleet Australia) manages approximately 30,000 vehicles in a diverse portfolio, under either lease or long-term management contract. In May 2005, SG Fleet Services acquired SMB Fleet Management, Australia's premier provider of novated lease fleet management services. The acquisition was primarily debt funded, but the Fund participated in the equity requirement on a pro-rata basis alongside other shareholders.

The SMB acquisition has added approximately 15,000 vehicles to the SG Fleet Services pool of vehicles under management, but has also been important in both diversifying the group's vehicle funding sources and also reducing the group's residual value exposure (due to the fact that SMB's business is focused on novated finance leases, rather than operating leases).

Performance by SG Fleet Services for the June 2005 half-year was in line with plan and, even before taking account of synergies from the SMB acquisition, there is a reasonable outlook for the 2006 financial year. The Fund's most likely mode of exit from this investment will be through an IPO or sale.

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Existing investment – Mincom appoints new CEO and secures Australian defence logistics contract



Headquartered in Brisbane since its formation in 1979, Mincom is Australia's largest commercial software

development company with approximately 1,100 staff in 18 different international offices. Mincom is the fourth oldest Enterprise Resource Planning ('ERP') company in the world and its technology is used in customer sites within the mining, oil and gas, utilities, transportation, defence and government industries. The Fund acquired its original shareholding in October 2002 and is represented on the Mincom Board by Steve Baldwin.

During the June 2005 half-year, Mincom appointed a new Chief Executive Officer, Richard Mathews – who has subsequently augmented his senior management team through recruitment of executives with significant experience in international markets. Mincom's current focus is on improving its financial performance and creating a robust business in anticipation of rapid growth.

In July 2005, Mincom announced that the company and the Australian Defence Force (ADF) would develop the world's first fully deployable, fully integrated, tri-services military logistics solution, in an agreement approved by the Federal Government. Importantly, it is believed that this model being adopted with the ADF will foster a common global defence industry solution and enhance interoperability – a critical factor for all of the global defence forces with whom Mincom is currently engaged.

Financial performance for the June 2005 half-year was a significant improvement from the prior corresponding period and the outlook for the 2006 financial year is very encouraging. The global nature of Mincom's operations would indicate a more likely exit strategy via trade sale, although the business is also of sufficient size to also consider an IPO.

Further Information

If you would like further information on your investment in the Diversified Private Equity Fund or know of a business that requires funding, please:

- Contact your financial adviser; or
- Contact the Investor Service Centre on **13 13 36**; or
- Visit the Colonial First State website: www.colonialfirststate.com.au/privateequity

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