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Of Icarus and Air Accident Investigations

Some of you may be familiar with the fable of Icarus. This ancient Greek hero attempted to escape from Crete using wings made of wax and feathers. Unfortunately, despite warnings, he flew too close to the sun, the wax melted and he plunged to his death. His black box flight recorder was never found.

This story came to mind when I set out to write about Wynyard Group, because it perfectly illustrates the calamity that can befall a high flying individual or company that fails to properly balance the risks of a particular course of action. Unlike Icarus, we also have the benefit of a veritable black box (or should that be wine box) of information. It is a complex story and I can only summarise many aspects.



The Flight of Icarus Jacob Peter Gowy (1615-1661)

Wynyard develops and sells its own ambitions. The difficulty (often through third parties) frequently lies in having to raise a range of security analysis software. This is a growth industry worldwide and Wynyard has made no secret of its to make large placements to institutional and eligible

investors while offering derisory share placement plans to its large retail shareholder base. It has raised \$70m in this way with a mere \$10m in SPP's. Unsurprisingly, NZSA has consistently complained about the inherent unfairness and dilutionary effect of this process on the existing loyal retail shareholders.

On 12 November 2015, Wynyard sought shareholder approval to make a further placement of 15m shares at a price not less than \$2 each. Approval was necessary as Wynyard had already used almost all the 20% issuance cap for the financial year. The price at the time was \$1.38. The SGM was held on 11 December by which time the share price was about \$1.90. Management and the Chair were very confident that they could make the placement to what was described as "strategic" investors. NZSA ultimately did not oppose as, if successful, there was value upside despite yet another dilution. We did however re-iterate our preference for rights issues.

On 28 January, Wynyard announced a further SGM to "ratify" the June 2015 placement. This would have the effect of taking it outside the 20% cap.

The company said world market turbulence had made it impossible to achieve the \$2 minimum, but they remained confident the shares could be issued at a lower (but undisclosed) price. NZSA made media statements and pulsed members with our view that insufficient detail was available for investors to make decision and pointed out that this undermined the whole rationale behind the support most investors had given to the December resolution. On 17 February, one day before the SGM, it was cancelled. Apparently the so-called strategic investors were no longer interested.

On the same day, Wynyard applied for a trading halt, saying they had a "material need" to raise capital. The reason became apparent on 23 February when unaudited accounts were released showing Wynyard's revenue of \$26.3m was \$19m (42%) below November's guidance. OPEX had increased from \$38.7m to 57.1m (47%), the loss was \$21.8m (98%) higher than the previous year at \$44.1m and the company was only weeks away from running out of cash. Wynyard then announced a renounceable

rights issue to existing shareholders at the hugely discounted figure of 85c per share. The market was deeply shocked at the financials and the dire position of the company, and the share price plunged from 150c to 92c - where it has remained close to ever since. To ensure it did not fail while the rights issue proceeded, Wynyard was forced to obtain an emergency standby facility of \$10m from its largest shareholder.

The trading halt was lifted on 24 February and the rights issue has now been completed, (including a 75% uptake by existing investors). Institutions also squeezed a further 4% "fee" payable in shares for agreeing to participate in the offer, meaning their effective entry cost was 81.6c per share. From 27 October 2015 through 10 February 2016, Wynyard released six notices announcing sales of product. Five of these totalled \$13.9m - we understand several remain outstanding. The sixth was a whopping \$27m sale conditional on a third party vendor completing commercial agreements with the customer. This notice which was dated "31 December, London" was released to NZX on 5 January, several

days after it was apparent the conditions had not been met and the "sale" could not be included in the 2015 accounts. Three months later, they still appear to have not been satisfied.

This is significant because the company needed to "bank" this deal to get anywhere near the \$40-45m revenue figure it confirmed in November. Forsyth Barr analysis (the only retail one available as UBS is institutional) picked a similar figure and loss in line with company projections. Generally, companies have an obligation to correct broadly available analysis if it is materially different from reality. Wynyard did not do so even after it was obvious that guidance had been woefully astray.

So, what had NZSA been doing through all this? Prior to the move to ratify the June placement, we had discussions with a leading fund manager, twice spoke with Wynyard management and twice wrote to the board. One letter included fund raising options. Broadly, they were a rights issue, placements at a small agreed premium to the share price, an underwriting option and a hybrid placement/rights option. Had a same -class rights issue been undertaken

then, it is likely that a discount of perhaps 20-25% would have been needed, resulting in an issue at perhaps 113-120c per share. Surely much better than the 85c (or 81.6c) that resulted in the crisis situation?

When the company went ahead with its placement option, we were vocal in criticising the lack of information about the price and the further dilutionary effect. In the event, the "strategic" investors who had been so keen cut and ran - so much for their "commitment".

Subsequently we have twice talked with the Wynyard Chairman, Murray Horn and discussed the matter with both NZX Regulation and the FMA. I am unable to share the nature of these discussions at the present time other than to say that the Wynyard Chairman accepts they should have used an investment bank at the beginning rather than try to do the raising themselves. The black box of information available to us clearly illustrates the chronology of events. It is less clear how the situation was allowed to develop, but like Icarus, it is hard to avoid concluding that pilot error played a significant role. In no

particular order, the following questions come to mind:

- Why did the board go to shareholders with the \$2 proposal when no formal agreement was in place? (We understand due diligence had not even started in early November)
- Why were retail analyst reports not corrected?
- Why were Wynyard's own guidance figures not updated promptly when it became obvious (even before the January 5 media release) that the \$27m "sale" could not be included in 2015 revenue figures?
- How was management allowed to burn through almost all the reserves and funds raised earlier in the year?
- Why were staff numbers allowed to balloon from 228 to 297 (a 30% increase) in just one year?
- What sort of stress testing did the audit and risk committee apply to management's cash flow predictions? And was this suitably robust?
- Did the CFO raise concerns over cash flow, and if so, were these ignored?

- Did the CEO present overly optimistic projections that were insufficiently challenged?
- Was the board captured by management?
- Why was an investment bank not employed at the beginning?
- Were performance incentives a factor? (CEO Mark Richardson was paid \$866,499 in 2014 and held 3.16m part paid redeemable ordinary shares that vest between \$1.242 and \$1.92 (average \$1.66) over the next three years.)
- Did the company begin to believe its own PR spin?

The very fact that these questions even arise indicates that there have probably been serious governance and

management shortcomings at Wynyard. Shareholders are constantly told that we must pay huge salaries and incentives to get the "most skilled" CEO and executives. Directors are always "highly knowledgeable and experienced".

When companies fly, that may be easy enough to justify. When they approach too close to the sun and their wings melt, we expect and should demand accountability. In this case, we do have the black box recording of what happened. Let's hope the air accident investigators (and shareholders) do their job and those responsible are held to account. After all, Icarus paid the ultimate price for his folly!

John Hawkins
Chairman

NZSA AGM and Annual Conference

NZSA's AGM will be held this year in Auckland, on 3rd September. Please mark this date in your diaries. If you have any special issues you would like to have aired during the conference or AGM, please advise a branch committee, or board member.

Bank Capital 101

A number of readers would like to have a better understanding of the various types of bank capital instruments and their risks. What are Basel III, tier 1 & 2 capital and an Open Bank Resolution? What do those financial terms mean to investors? The Global Financial Crisis was the major driver for these changes. New regulations are tools for authorities to prevent financial systemic risk; while in the short term they may increase a banks cost of raising money, a stable financial system in the long term can reduce risk premium and lower their business costs. Investors will be the ultimate beneficiaries of a stable financial system and safe banks.

So what is Basel III?

The Basel Committee on Banking Supervision (BCBS) established Basel III, the current global regulatory standard for bank capital adequacy and liquidity. The Reserve Bank of New Zealand (RBNZ) started the implementation of Basel III on 1 January 2013. The new standard is aimed at increasing banks capital reserves and decreasing leverage. Without going into too much detail, under Basel III New Zealand banks now need more capital to run the same business than they did previously under Basel I & II.

Under Basel III, bank capital securities (aka regulatory capital instruments) must contain explicit terms, that under certain conditions, impose losses on investors.

The terms are about equity conversion and loss absorption, which will be discussed in detail later. The conditions are: (1) the regulator can determine that the bank is reaching non viability; (2) The bank is over leveraged, its equity to debt ratio is below Basel III requirement Because of the explicit terms about imposing losses, Basel III bank capital securities are deemed to be more risky than Basel I & II bank capital securities.

The table below shows various types of bank capital and their risk ranking in the event of a bank winding up

Tier 1 capital

Tier 1 capital is a bank's core capital including common equity; retained earnings and Alternative Tier 1 capital. Basel III has set a minimum ratio (6%) on tier 1 capital to total risk-based assets¹ (e.g. commercial loans & mortgage). The ratio is a measurement on bank's financial health.

Common Equity, or ordinary shares, is classified as Tier 1 capital (CET 1). Basel III has set a minimum ratio (4.5%) on CET 1 to total risk based assets. The security characteristic remains the same as you would expect for common equity. As

¹ risk based assets is not a direct add up of all loans and mortgages

The table shows how Subordinated Notes ("Notes") would rank upon a winding-up of the issuer if conversion does not occur and the Notes are not written off

Higher Ranking/ Earlier Priority/ First to be repaid	Types of Obligations	Examples
Higher Ranking Obligations	Secured Debt and Creditors Preferred by Law	Secured creditors such as money held with clearing systems and covered bond programmes. Liabilities given preference by law including employee entitlements and taxes.
	Unsubordinated Debt	Deposit accounts, senior bonds and trade and general creditors.
Equal Ranking Obligations	Term Subordinated Debt	Subordinated loans
	Perpetual Subordinated Unsecured Debt	
Lower Ranking Obligations	Preference Shares and Other Equally Ranked Instruments	Perpetual preference shares
	Ordinary Shares	Ordinary shares
Lower ranking/ Later Priority/ Last to be paid		

Examples listed in the table: Covered Bonds, Senior Unsecured, Tier 2 or "T2", Alternative Tier 1 or "AT1", Equity.

the owner of the bank you enjoy the growth of the business, the dividend and capital gain during good times, but may experience volatility of the share price and be the last to be paid in the event of a bank winding-up.

Perpetual Subordinated Unsecured Debt, Preference Shares and other Equally Ranked Instruments, such as Perpetual Preference shares are classified as Alternative Tier 1 (AT1). Issues after 2013 contain the same conditions (1) and (2) about equity conversion and loss absorption mentioned earlier. CET1's loss absorption capability is greater than AT1.

Tier 2 capital

Tier 2 capital is supplementary capital including various reserves, hybrid and subordinated securities. Basel III has set a minimum ratio (8%) on total capital to total risk based assets. Total capital = Tier 1 capital + Tier 2 capital.

Term Subordinated Debt and Subordinated loans and hybrid capital instruments are classified as Tier 2 capital (T2). They also contain the explicit terms on loss absorption and equity conversion conditions as stated in (1) & (2) earlier. Tier 2 Capital ranks ahead

of Tier 1 capital.

What does this mean for my investments?

When things are going well and banks' lending business is growing, they need to maintain a specific capital to debt ratio. Banks are required to maintain additional 2.5% capital on top of above three minimum ratios. To do this they have to issue more CET1, AT1 and T2 capital, which mean more investment opportunities for you. AT1 and T2, with above explicit terms and conditions, is considered more risky and has a lower credit rating so banks need to compensate you with higher interest rates.

If things go wrong and conditions (1) or (2) are triggered, there are two scenarios for Basel III capital securities loss absorption: (a) In the case of Basel III capital securities converting into common equity, investors' claims on the bank's assets then rank equally with common equity in terms of the bank's loss absorption; (b) In the case of a write-down, investors in Basel III capital securities would effectively absorb losses even before common equity holders.

There is additional fine print that investors should be aware of.

Basel III capital securities issued by overseas owned banks, such as the big four Australian banks which are governed by both the RBNZ and Australian Prudential Regulation Authority (APRA), can be deemed non-viable by either organisation. Only two of the big four Australian banks are dual listed in Australia and New Zealand so if a conversion happens, investors may end up with some Australian listed shares.

May 2015 Kiwibank issued Perpetual Capital Notes. Kiwibank is 100% owned by the NZ government by legislation. The compromise solution was to set up a separate vehicle, Kiwi Capital Funding Limited, to hold those debt securities. So in the unlikely event of equity conversion, Kiwibank ownership will not be diluted. It's very important for investors to read the terms and conditions of each issue, and if you are still not sure, seek professional advice.

What is Open Bank Resolution (OBR)?

Basel III is the first layer of safe guarding to prevent bank failure. The aim is to prevent failure through regulatory capital loss absorption; a problem bank

would be allowed to get back on its feet and continue its normal operations. If things get worse and the bank fails, OBR will kick in to allow it to stay open. The RBNZ has introduced OBR for banks with \$1billion+ in deposits, but smaller banks have the ability to voluntarily opt in to the OBR scheme. New Zealand has not adopted a deposit guarantee scheme as many other overseas countries have. OBR is the second and final layer of safeguarding. .

How does OBR work?

In the event of a bank failure, instead of a bank ceasing its operations and going straight into liquidation, the bank will be placed under statutory management and some money will be frozen. The next day customers can access the non-frozen portions of their money, which is guaranteed by the government. They can withdraw most of their money in transaction and on-call saving accounts.

Term deposits are not guaranteed by the Government, but depositors can still claim the frozen funds as unsecured creditors, which rank after secured debt and creditors preferred by law, such as wages and tax obligations.

Senior bonds are ranked below

term deposits and above tier 2 capital, and do not contain above explicit terms and conditions.

In addition, people used to be able to break their term deposits anytime (with penalties applied), but are no longer able to do so if they are with Australian owned banks. The Australian Prudential Regulation Authority (APRA) introduced a "liquidity coverage ratio". We will not go into the details of how the ratio works, however the result is that all four Australian owned banks introduced a 31 or 32 day notice period for breaking a term deposit, unless financial hardship can be proved. Non-Australian owned banks do not have this requirement. So in the unlikely event of their Australian parents' failure, the RBNZ can take control of the situation to protect NZ depositors.

Ally Cui, AFA, MMgt (Fin), BEcon, JBWere

Source:

Moody's Investors service Issue In-depth 9 March 2015

RBNZ: www.rbnz.govt.nz/

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Whistling in the Winds

Several media reports recently have prompted NZSA board to consider the role of whistle blowers in our listed companies. Firstly, there was the report of an Australian court action involving Origin Energy. Sally McDow an experienced company lawyer was made redundant from Origin, in a large rationalisation involving 800 employees, after having "blown the whistle" and sought protection under the company's protected disclosure policies. She sued. During press reports it was noted that in USA whistle blowers can be awarded a bounty of up to 30% of a successful court proceeding against a company which is breaking the law. In New Zealand we have the Protected Disclosures Act under which the Ombudsman's office acts as the external adviser to would-be whistle blowers. However, the Ombudsman's annual report reveals that an average of only 10 requests per year have been serviced. In 2015 for instance, there were 43 informal requests and 16 requests for guidance, and those were completed within 6 months of the request being made. The report suggests that most requests failed to meet the test that the whistle blowing should be for "serious wrong doing." The report also observed that potential whistle blowers are often unaware of the protection under the Act, and that they usually felt that the protections were inadequate in the face of smear campaigns, bullying, job loss, and expensive court battles.

The second issue that has been raised locally is the current cases involving fraud and theft as a servant in our companies. It is a continuing risk which is accelerated by retrenchment and rationalisation of job functions. The best protection within a company is engaged and committed staff who discuss their fears and limit the risks of illegal activities with the appropriate internal authority, and ultimately the Audit and Risk committee of the board. Even then, a company can have all the policies in the world, but fearful or corrupt management and directors will do everything in their power to avoid the bad publicity of illegal practices inside the organisation. A survey by chartered Accountants in NZ and Australia of 1000 companies revealed that only half the companies would report an illegal request, and that bribery and corruption in businesses was on the increase.

These reports posed serious questions for shareholders who look for the long-term governance and growth of their company. Why have so few cases have come before NZ courts under the Protected Disclosures Act? Why do the forward-looking companies like Michael Hill International which disclose policies of speaking up and challenging the accepted culture, not layout protections for whistle blowers? Should NZSA be active in this area? Should we promote the idea that compensation for whistle-blowers be part of a successful court action? Is the issue of

whistle blowing part of a wider concern involving the whole culture of a company?

From the NZSA board discussion, it was clear that whistle blowing is part of a wider company environment. It is concerned with bullying, harassment, risk management, disclosure and transparency, a vital part of the health and safety of employees. It was also accepted that in its negative or protective aspect, it is an emotional issue that many boards don't get round to talking about. However, engaged employees who know they are backed by an Employee Assistance Programme are more likely to be productive employees, and this is surely the business of the board and its audit and risk committee. So NZSA now has a policy towards employee engagement and whistle blowing. You can read it in the public section of the website.

"The Association recommends that all companies have an appropriate policy around employee engagement including the safe reporting of illegal and other inappropriate behaviour.

The company should disclose its policy, or explain why it doesn't have a policy in its Annual Report.

Where the company has a policy, it should also disclose sufficient details of the mechanisms which allow employees to report such behaviour in a manner that will inform a reader of the report about the efficacy of the policy.

Where it can be demonstrated that harm was caused and the company concerned did not have an appropriate policy around employee engagement or failed to uphold this, the NZSA will consider appropriate voting against the re-election of Directors."

What do members think? Do you think we should go further? We feel a company should describe a pathway to an independent authority which can hold directors and staff to account. We also believe that a whistleblower reporting verifiable illegal activity should be completely protected against intimidating actions by the company's officers. Could NZSA even be a port of independent appeal in the event that a company covers up its illegal dealings? We are interested in members' feedback on this live issue.

Alan Best

Quotas for women on NZX Boards

Thanks to Des Hunt, I read Susan McLean's MBA thesis on the issues surrounding gender diversity on NZ board of directors. Susan tackles the thorny question, whether enforced quotas are an effective way of increasing the number of women on boards. Susan's chart of countries which have adopted targets and mandatory quotas makes interesting reading. The classic case is Norway, a country of similar size to NZ, but with a stock market capitalisation of nearly 2.7 times ours. Norway was the first country to commit to a 40% female target,

making it voluntary in 2003, and mandatory in 2006, expecting to achieve the target in 2008. However, Norway did not reach the target until 2015, and the controversy amongst business leaders took 7 years from 2006 to die down. So what difference did the increase of women make to the performance of the boards? Susan quotes research which showed that despite experiencing more governance-related controversy, Return on Equity increased to 10.1% from 7.4% with the increase of women. Growth in GDP was consistent with this increase, and the



increase was more marked after the representation became mandatory in 2006. Susan concludes that mandatory quotas do accelerate the participation by women on boards, and although fraught with debate, this has a positive effect on the company and the economy.

In NZ the government has led the way with the representation of women on state boards and committees exceeding 40% since 2009. What then is the result of the NZX rule 10.4.5 reporting on gender diversity which began in 2013. From 12% of board members then, it has grown to 17% today. If this pace of change were to continue equality of gender would take another 25 years. In 2015 an IOD survey revealed that only half the board member respondents agreed that their board was fit for purpose, had the right capabilities, and was able to deal with the increasing complexity and risk. Members also confirmed that they met every 2 years to consider their own performance. While only 5.6% of board chairs are women, the top industries for women board members are as follows:

INDUSTRY	% BOARD MEMBERS
Telecom - Media - Technology	25
Manufacturing	22
Energy - Resources	21
Life Sciences and Health	13
Consumer	12
Average	17.5

It is surprising to note that the very activities in which women wield the most purchasing power are the ones which weigh the average down.

Perhaps the most challenging section of the thesis occurs when Susan moves on to consider the barriers to the entry of women and the ways to overcome them. Claims that it is difficult to find a supply of suitable women candidates are roundly disproved by the number and quality of candidates in our own Future Directors programme. The inertia of successful male boards who claim to achieve diversity of talent and experience without female participation is questioned. Old assumptions of feminine prototypes are also disproved by male executives who admit the diverse managerial talent of a dominant mother in their homes. Even the "queen bee syndrome" where a chief woman sees applications from another woman as unhealthy competition in restricted job market is not common in NZ. To overcome these barriers, Susan elaborates on 4 healthy recommendations for NZ boards:

- 1 Candidate profiling based on merit. This may mean waving the near automatic renewals for existing directors.
- 2 Active participation in supply initiatives (like Future Directors*, Appoint, and Champions for Change.)
- 3 Regular performance monitoring, with the corollary that poor performers would not hold their position on a board.
- 4 Mentoring by senior successful board members, (especially supportive female

mentors who act as role models.)

NZSA has a policy on diversity which is not aligned to gender equality though sympathetic to the cause, but rather embraces technical diversity regardless of gender. Nevertheless, research papers like that of this MBA thesis gives us all food for thought.

**Susan's thesis treats Future Directors in some depth, and provides the following list of those companies which are currently employing Future Directors from the IOD register: Auckland international Airport, AWF Group, Canterbury Scientific, Dunedin Airport, Fisher and Paykel Healthcare, Genesis Energy, IANZ, Kordia, Meridian, Mighty River Power, Service IQ, The Warehouse, Tower Insurance, Vector.*

Alan Best

User-Needs research by the XRB – Which users?



- Advisers, brokers and analysts (70 participants,)
- Regulators and compliance officials (8 participants.)

We see immediately that the sample is heavily weighted against retail investors. However the questioners were conscious of the reliance placed by the less knowledgeable investors on financial advisers, and commented on this several times in the report.

The survey involved questions on:

- the use of financial reports,
- types of decision made from the reports,
- the importance of the components – P+L, BS, Cash Flow, Changes in Equity (this last was the least useful),
- information that was not considered useful,
- information that is currently omitted,
- possible improvements, further sources

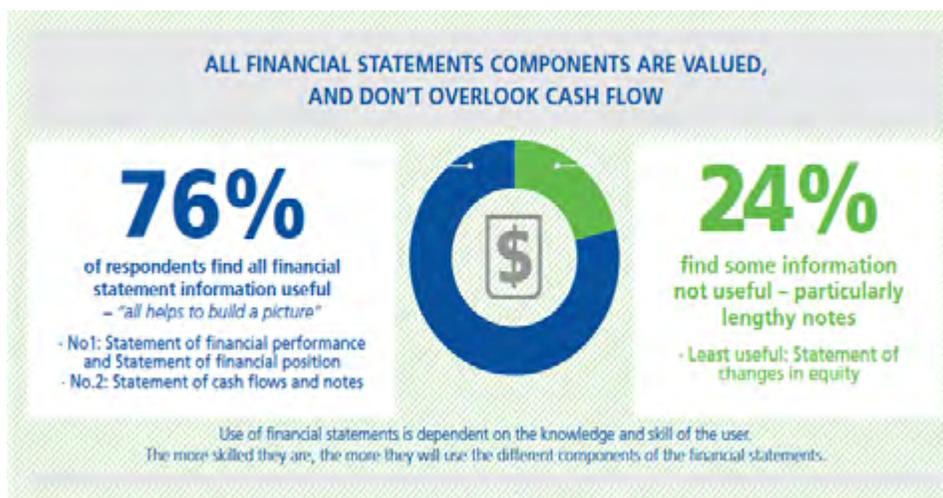
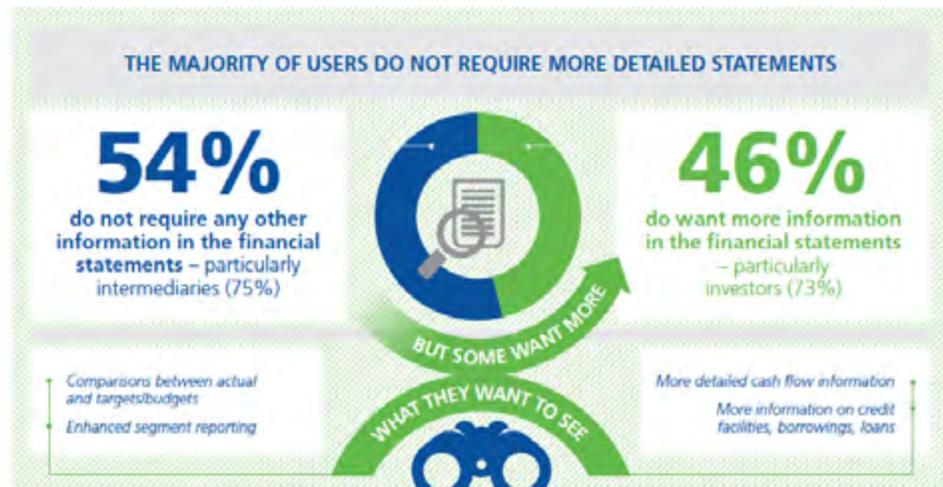
- of company information (here, analyst's reports were most important),
- supplementary information (like Chair and CEO reviews),
- and other important information (e.g. strategies, prospects, and narrative on the results).

From this, a short set of recommendations was assembled reflecting the need for simplification, the desirability of standardised presentation so that similar entities could be easily compared, a desire by some for comparisons between performance and budgets or targets, dashboard summaries to highlight significant figures, supplementary information involving narrative, prospects and strategies, and more detailed disclosures of segments and financial instruments.

The External Reporting Board is committed to assessing whether the changes in reporting standards embodied in IFRS are fit for purpose, and satisfy user needs. They have recently commissioned research from Massey University to check on this. The research involved a review of international literature, an internet questionnaire, and in depth interviews with a sample of those surveyed. The following groups were surveyed:

- Existing and potential investors (45 participants,)
- Lenders and creditors (22 participants,)





It is easy to be critical of the survey. There was almost no mention of the perennial interest by investors and media in remuneration reports, the renewed interest in health and safety -both its increased cost and benefit, and the critical importance of environment and sustainability, the need for a clear explanation of the tax obligations of the enterprise, and the social and charitable engagements by a company in its community.

We wonder how the financial community could be so divorced from its operating environment. The financial analysts will probably say that these are not really part of a financial report, but surely they have strategic and cost implications.

It is certainly worth taking a look at the graphic summary on the XRB website – XRB Summary Research Report_187224 pdf. The messages are simple and the percentages telling. It will be interesting to see how far and how soon the recommendations are implemented.

Where does the phrase “nest egg” come from?

- a 19th Century Russians investing their wealth in Fabergé eggs
- b 14th Century farmers using dummy eggs to get their hens to lay more eggs
- c 20th Century American children storing their allowance in plastic Easter eggs
- d 17th Century Spaniards eating eggy bread on Christmas to ensure a prosperous new year
- e Isaiah 10:14 Eggs left in a nest and gathered by foragers

See page 17 for the answer

Company Meetings

New Zealand listed companies now usually post AGM presentations by the chair and CEO, on their website. Our commentaries therefore concentrate on the flavour of the meeting and the questions raised by shareholders. We encourage members to use the company website, before attending the general meeting, to see what has been said previously, and to familiarise themselves with the latest news. Comments are those of the attendee, who will often be a shareholder in the company, and are not necessarily NZSA policy. **Run your cursor over the report heading for a link to the company website**

More moves for MHI 30th March

Michael Hill's communication consultant, Merlin Consulting arranged a meeting with NZSA to discuss the company's intention to move its primary listing to Australia.

CEO, Mike Parsell set the ball rolling by pointing out that 80% of the company's revenue was now gained from overseas and that 60% of that was in Australia. With head office functions and most company advisers based in Australia he saw a certain inevitability about registering in Australia, scheduling most directors' meetings beside the most accessible information, and holding AGMs there.

NZSA's John Hawkins and Alan Best asked a series of questions that shareholders will need to consider.

MHI has about 3500 shareholders with a total of about 383m shares. Director's interests hold about 240m of these. So where are the others based? Mike and CFO Phil Taylor said they were largely in NZ.

Was it intended to maintain a secondary listing on the NZX? Mike was very clear that

this was the intention and the company was committed to keeping things simple for NZ shareholders to trade MHI stock.

What is the cost benefit of Australian registration? Phil said that primary ASA registration at about A\$55k was only a little above NZX at about NZ\$45k, while savings on travel and incidentals would largely bridge the gap. The main advantages would be in head office and board communication, and potential for capital raising (though none is planned,) while the disadvantages of tighter regulations and remuneration reporting were largely covered by existing systems in the Australian head office.

We asked about the disadvantage of being a small fish in a big pond, compared with a position of substance amongst NZ listings. Both Mike and Phil were neutral about this. They said their recent market research had shown strong recall of the MHI brand in Australia. It was agreed that with a market cap of about A\$345m in Australia, MHI would be an index company, and NZ shareholders would not be subject to FDR tax, but would be taxed on the net dividend paid, without

imputation credits.

This raised the tax issue. We asked about the lack of provisioning, and it was clear that the company had taken very careful advice, involving both its barrister, auditor and tax consultant, to conclude that any provision above the tax pooling arrangement could not be substantiated. We suggested that the profit shifting involved in the IP payments to Australia were the reason that imputation credits were not available to NZ shareholders, and that if NZ's IRD gained a significant settlement which set a lower precedent for IP payments, NZ shareholders might once again benefit from imputation. Discussion around this topic confirmed that the move to Australia would not benefit the company's existing claim (no backdating,) but that it may make the IP payments more acceptable to the NZ IRD in future. Although the company denied the tax dispute was involved with the decision, we still wonder if it was a factor.

We also asked whether executives would gain under the transition to ASX, (perhaps under the existing incentive schemes,) and both

Kirkcaldie and Stains AGM 23rd February

MHI staff denied this, claiming that Rob Fyfe, Remuneration Committee chair, was insisting the conversion be neutral.

Annual Meetings were also discussed including NZSA's preference for interactive, remote meetings, and the potential for internet communication with NZ shareholders.

Voting in the Special meeting required to approve a shift to primary ASX registration would be conducted in categories, so that the dominance of the Hill family shareholding can be taken out of the voting.

Phil Taylor estimated that the MHI board would probably review the registration in its April meeting and that the company would be in a position to call a special meeting shortly after. We suggested that many NZSA members would probably be opposed to the move, and that we would take an objective view in our voting intentions once the notice of meeting and explanatory notes had been circulated.

Alan Best and John Hawkins

There were between 120 and 180 people at the Kirkcaldie & Stains AGM.

Voting was by a show of hands. There were no proxies available for me to action on behalf of NZSA. I spoke to Michael Curtis (Director) and Orsola Del Sante-Bland (acting CEO and Company Secretary) as Link Market Services had not sent them through. They said they had enough proxies lodged with the chair to pass the resolutions (51% of the issued capital).

Since the Special General Meeting in July 2015 that approved the sale of the Kirkcaldie & Stains Trading company to David Jones, the Harbour City Centre building has been sold, 'Kirks' store has closed, the stock sold or donated to charity and good progress is being made on the assignment of two of the three outstanding leases without loss to the company. The company archives have been donated to the Wellington Museum, The Alexander Turnbull Library and Te Papa. \$2 million has been set aside in escrow as part of the David Jones sale for bad debts.

A capital return of 80% of shares was distributed on 29 February at \$2.36 per share. This distribution did not alter the voting or distribution rights of shareholders in the remaining 20% of issued capital. The remaining 2,250,000 shares have a NTA value of between \$0.63 and \$0.73 per share. The company may be on sold as a

shell company for a backdoor listing or will otherwise be liquidated and delisted. Once resolved, the remaining distribution will occur. A schedule for this was not announced that the meeting.

There was one shareholder question, questioning the need to re-elect directors with the company being wound up. The chairman advised that the election was required to comply with the Companies Act 1993 which requires that a public company needs to have a minimum of three directors of which two must be independent.

The two directors up for re-election, Michael Curtis and Kerry Prendergast, were re-elected. The auditor, PwC, was also re-elected. It was agreed that the directors would fix the remuneration for the Auditor.

The mood of the meeting was peaceful, a sense that the shareholders had worked through the pain of the demise of Kirks. I spoke to two shareholders, both very longstanding. They were philosophical and felt the directors had done what they could.

The meeting closed after 20 minutes.

Christine Pullar

Gentrack AGM 25th February

The real success story around Gentrack's AGM was that shareholders were able to negotiate the labyrinth of Auckland's Maritime Museum alterations and find the meeting venue. Given the lower city location and 4p.m. start time, there was a reasonable attendance.

We listened to addresses by Chairman, John Clifford; former CEO/Executive Director James Docking; and new CEO (in the job for 1 month) Ian Black. Copies of their presentations are available on the Gentrack web site.

Gentrack has a 25-year history and was rebranded with its current name after diverging from UK company Talgentra in 2008. It floated as a public company in June 2014 at an issue price of \$2.40 and first traded at \$2.58. At the time of the meeting the price was \$2.15. Unlike many other companies in the tech sector, it is funding development out of revenue and paying a dividend (11c a share in 2015). The lack of questions from the floor at the meeting suggests that shareholders are happy with the way the business is being run

The company counts Genesis Energy, Meridian Energy, Mighty River Power, Australia's Origin Energy and the UK's SembCorp Bournemouth Water among the electricity and water utility customers for its Gentrack Velocity billing product. Airport companies using its Airport 20/20 management system include Auckland International Airport, Sydney Airport, Hong

Kong International Airport, London City and John F Kennedy International Airport.

Gentrack has customers at 51 utility sites and 61 airports. It won five new customers during the year and upgraded six existing ones. This year it plans to maintain its mature New Zealand market, secure its growing Australian market, and grow its UK market, where it increased projects 44% last year.

Mr. Clifford said that nothing has changed in terms of corporate strategy. The company is still assessing acquisition opportunities as they arise. Gentrack, which has no debt, would consider debt funding as an option should a suitable acquisition target be found. He noted that England is planning to move to a model of contestable water supply (similar to what we have for electricity) and this offered opportunities for the company's Gentrack Velocity business.

Mr. Docking said one of the biggest challenges facing the company is finding the right staff to work on the projects. The company's headcount increased 12.5% last year and is recruiting strongly in Auckland, Melbourne and London.

Mr. Black, who has had an international career at Oracle and SAP, including as its New Zealand chief executive, said he is looking forward to the challenge ahead. "We're on track to meet 2016 objectives which is a nice start for me," he said. "Markets are changing and for a tech company that presents opportunity. We're working to make sure we have

a clear view of the growth opportunities in our chosen markets." Looking ahead, half-year 2016 revenue and EBITDA are expected to be up 20% on half-year 2015. The full-year results are expected to be in line with guidance given in November, with 10% revenue growth. Full-year EBITDA is expected to be at the same level as 2015, as investment in staff and new systems reduces margins.

Messrs Clifford and Docking, who each hold over 10% of the company stock, were re-elected as independent directors with 99% of the 52.5 million proxies in favour.

Bruce Parkes

Cavotec Investors' Meeting 7th March

Cavotec de-listed from the NZX in 2011 and is now listed on the Stockholm NASDAQ with about 600 New Zealand shareholders still registered. Link Market Services has an arrangement with Cavotec to facilitate information and dividend dissemination. The Christchurch design office at Wigram has expanded over the last year and now employs 40 working on the designs of the MoorMaster system. Some 40 shareholders attended the meeting which was addressed by Michael Scheepers, the director for Investor Relations and PR. He commenced by forwarding the apologies from Chairman, Mr Stefan Widegren, who was unable to attend on medical advice.

Mr Scheepers gave a 40 minute presentation on the overall company's performance and was assisted by David Williams, the Managing Director of the MoorMaster division based in Wigram, Christchurch, who gave some short videos on the new capabilities of their MoorMaster system.

Mr Scheepers pointed out that while the company, when originally formed, concentrated on mining support this division now accounted for just 10% of their activities with the Maritime ports and airports division now accounting more than 50%. Most notable advances in recent years have been with increasing sales of the MoorMaster automated mooring system and the continued expansion of their

Airports division since its introduction in 2004.

Mr Scheepers invited shareholders to ask questions which he answered:-

Q Did they face any completion for their MoorMaster and airport systems?

There were no competitors for their fully automated mooring system although there was a semi-automated system using hooks and a magnetic system. Neither posed serious threats. For airports the competitors were diverse and uncoordinated in contrast to Cavotec's integrated approach.

Q Can the MoorMaster vacuum system cope with buckled plates?

Yes they can seal over these plates which has been important on the St Lawrence Seaway where ships sustain many bumps!

Q Has the litigation over INET in the USA been resolved?

The two cases have been resolved in Cavotec's favour but Mike Colaco (the former owner of INET Airport Systems) has given notice of appeal. He is not expected to succeed and it should be completed by mid-year. The expected award has not been entered into the accounts pending conclusion of the litigation.

Q Will the collapse in oil prices impact on the electrification of ports?

The growth of AMP (Alternative Maritime Power) is expected to grow, driven by

legislation like the Clean Air Act in the USA and similar in Europe.

Q Is there any manufacturing undertaken in NZ?

No the local team is employed entirely on design of the MoorMaster systems. All manufacturing is undertaken in Italy, USA and China.

Q Could they provide some projections on future profitability?

Not beyond what has been officially released and there are no forecasts for 2016 and 2017. There is considerable quarterly volatility so half-yearly or annual figures are more stable and reliable. There has been a move by some exchanges towards allowing half-yearly reporting because of the volatility in quarterly reports.

Q Is there any prospect of re-listing on the NZX?

Unlikely; but they are committed to visiting NZ for shareholders' meeting and providing a good flow of information. (One shareholder praised them for the quality of their website.)

Q Electrification of ports – is it dependent on local power supply?

They connect to the grid power and reliability has not been an issue. Would they use self-contained power supply? They have no plans to do so and they are concentrating on markets where power supply is reliable.

Pacific Edge Special Meeting 26th February

Q Would they include in their announcements the international time as well as CET (Central European Time)? CET is GMT plus one hour. However, they could do so.

Cavotec shares were valued at NZ\$2.45 when finally traded on the NZX in September 2011 but are currently trading on the Stockholm NASDAQ at (Swedish Kroner 24.50) the equivalent of NZ\$4.36

Robin Harrison

Chairman Chris Swann opened the meeting at 11.00am, 6 shareholders and 4 other people present in Dunedin.

Chris spent 15 minutes explaining the reason for the meeting, namely to obtain shareholder approval for a raise in directors' payments from \$198,000 to \$275,000.

The whole of this increase being used to fund a USA based director, a David Levison who has experience and interest in the Diagnostic and Healthcare market in the US.

A US recruitment firm was used to compile a short list of 8 possible candidates from which David was chosen. Chris also mentioned that US directors usually receive options as part of their payment, no details were given as to the NZSA's previously expressed concern on the pricing of these options. All the NZSA's 715,163 proxies were voted For, and with shareholders present the final result was 82.2% For the motion.

CEO David Darling took over at 11.15 and gave the meeting a rundown of Pacific Edge at this time. It operates in a very specific field of Bladder Cancer Diagnostics.

David outlined their first product now had a companion second product released on the 24-12-15 with a third product to be released very soon, this puts them ahead of other operators in this field who would only have one product, healthcare operators can therefore obtain a more comprehensive field of coverage from Pacific Edge at a greatly reduced cost over present methods. David also revealed they had made inroads with supplying some large

healthcare providers in the US.

David then answered 4 questions from shareholders:

- 1 Are you covered by Patents for Intellectual property? A: yes but only for new or original products which will start to expire in 2023.
- 2 Is profit ahead of expectation? A: yes, and things are looking good for the future.
- 3 Is the fall in the share price a worry? A: yes, but that's the market.
- 4 Did David Levison know about Pacific Edges CX detection product? A: he was aware of it.

Summing up, David seems very driven and passionate about their products while being aware of possible competition and the need to keep ahead of the field.

The market must have liked what came out at this meeting as on Mon.29th I hear the share price went from 40 to 50 cents each.

Stephen Wesselingh

Editor: NZSA had discussed the issue of options with the CEO before the meeting. Our concerns were that there was no indication in the notice of how the price would be set, that it was unusual in NZ for non-executive directors to be issued with shares as part of their remuneration, and that we were strongly of the opinion that they should be issued at a premium to the market. It was clear that the board believed that the shares would be issued at the market price, (which they regard as low,) and that they would explain the pricing and exercise terms at the meeting. They did not, and it was disappointing that no clear thought had been given to the terms of the options.

Caught on the Net

The Big Short - A Federal Reserve Bank staffer's view

The key difference in his perspective to that of Michael Lewis is that for him, the crisis was largely caused by a widely held presumption that home prices would keep going up and could not come down at a national level. Now where have we heard that before? [More](#)

New Zealand Foreign Trusts, the Unaoil Scandal, Mossak Fenesco and much more: More chickens are coming home to roost

This story has been around in blogosphere for some time. I note that Tim Hunter - now with NBR picked up on it back in 2012. [More](#)

A quick investment checklist for selecting stocks

The Intelligent Investor offers a 12 point practical checklist to cover off the big issues before you buy a stock. [More](#)

The emotional and psychological risks of investing

Paul Merriman, in Market Watch, shares some truths about risk - and in particular, emotional risk. He says, "if you invest at all in the stock market you will lose money." He then offers some suggestions on how to react properly. [More](#)

Investors aren't countercyclical - but they should be

Investing's golden rule might be to buy low and sell high - but it is one to which even the most sophisticated investors have trouble adhering. Bradley Jones, from the International Monetary Fund suggests five structural and policy changes that would encourage institutional investors to behave counter to the market. [More](#)

The danger zone - when should we worry about how much households spend on their mortgages?

When households spend more of their income making payments on loans they are more likely to get into arrears. Identifying the danger zone where they will get into financial difficulty is often difficult. This Bank Underground post tries to identify the critical debt service ratios that indicate the danger zone. Unfortunately, this Bank of England whizz kid ended up with a woolly answer. [More](#)

The Callan Periodic Table of Investment Returns

Also known as an Asset Allocation Quilt is a useful tool for offering a visual display of the volatility of the various asset classes and the clear logic behind a diversification strategy. [More](#)



Stop paying Executives for performance

Dan Cable and Frank Vermeulen set out in a HBR article set out to show that performance based pay can actually have dangerous outcomes for companies that implement it. [More](#)

And a riposte

Alex Edmans, also in the HBR responds to the Cable and Vermeulen article. While he agrees with a lot of Cable and Vermeulen's findings, he says that the research which has been conducted on business leaders suggests that financial incentives can work and quite often do. [More](#)

Narcissistic leaders, mirrors in the boardroom and firm's risk taking behaviour

Guoli Chen, writing in the South China Morning Post describes his research which found that when narcissist chief executives interact with their board they often met not a moment of reckoning but their favourite thing: a mirror. That is, they had tried their best to select new board members similar to themselves. [More](#)

From Berlin to Basel: what can 1930's Germany teach us about banking regulation?

The main lesson from the German 1931 crisis is perhaps best expressed as 'misfortune rarely comes alone'. The German crisis had many causes – risky loans, due diligence failure by management, low capital, low liquidity, flighty funding, contagion and events outside a bank's control such as political risk.

There are striking parallels in the 2008 GFC. Regulators have had to painfully re-learn the lesson from Germany in the 1930's: a single tool, no matter how sophisticated, cannot guard against the manifold risks banks are exposed to, many of which are difficult to quantify. [More](#)

Key terms for tough times: The vocabulary of stressed markets

The Alert Investor offers some definitions for the common terms or jargon commonly used during stressed times in financial markets. [More](#)

The great investment advice hidden in Warren Buffett's annual letter

Joshua Brown, writing in Fortune, picks up 4 things Mr Buffett had to say about the disciplines that must be adhered to in the Insurance business and links them to the disciplines needed for managing an investment portfolio. [More](#)

Is passive investment actively hurting the economy?

Passive tracking funds just keep growing but could their continual success be their undoing? James Ledbetter says so in a New Yorker article. When these funds reach some threshold or tipping point they will become a circular transaction with no analysis of the company or market in which they are investing. It could all become rather messy. [More](#)

How reporters pulled off the Panama Papers, the biggest leak in whistleblower history.

A Wired article puts it down to an unknown source approaching a German newspaper *Suddeutsche Zeitung* in 2014. The newspaper involved the Washington, DC based International Consortium of Investigative Journalists. After much checking, the involvement of many media organisations and the transfer of terabytes of data, it has become the cause celebre of Spring 2016. [More](#)

The Federal Reserve and the Panic of 1907

When the Wild West (in the shape of F. Augustus Heinze from Montana) tried to

"short squeeze" the market it sets off a crisis that led to the creation of the US Federal Reserve. [More](#)

The Roll-Up Racket

In a New Yorker Financial page, James Surowiecki documents the rise and fall of Michael Pearson, CEO of drugmaker Valeant and the company he led. Valeant's stock price rose more than four thousand percent during his tenure. In the past six months the price has fallen almost ninety percent. What went wrong? Valeant had become known as a roll-up: a company buying lots of other companies trusting that they will be more profitable together. Roll-ups only work when they find a superior way to make money. Most, including Valeant, have no such ability.

[More](#)

Bruce Parkes

Nest Egg Answer

The practice of putting eggs into nests as an inducement to laying more is recorded from as early as the 14th century. The use of 'nest-egg' to refer to savings goes back to at least 1686. In 1927, Locke & Clarke printed a set of letters from that date, which included this:

"The rest, I perceive, he is not troubled should remain as a nest egg till a farther occasion."

Branch Reports

We recognise that branch reports in our newsletter do not adequately represent the expertise and preparation of those presenting to us. The work of these professionals who give their time is appreciated by all who attend. Members are encouraged to refer to the individual company websites for the latest news and disclosures.

Branch Contacts		
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Wellington	Martin Dowse	martin@dowsemurray.co.nz
Canterbury	Robin Harrison	robin.harrison@canterbury.ac.nz

Auckland

On 17th February, stimulating presentations were delivered by Ricky Ward, Equities Manager from JB Were, and Nigel Greenwood, CFO of Synlait. The former is available on the NZSA members' website

Upcoming Auckland Branch Meetings

All at Alexandra Park Convention Centre, Green Lane. 7pm tea & coffee – 7.30 pm start

Dates for 2016:

Wednesday 13th April	Chris Heaslip	CEO, Pushpay Holdings
	Mike Bennetts	CEO, Z Energy
Wednesday 15th June	Liz Stanford	Institute of Accountants, on new audit reporting
	Jane Elrick	CFO, Steel and Tube
Wednesday 14th September	Brian Gaynor	Milford Asset Management
Wednesday 16th November	Speakers to be advised	

Please mark the dates in your diary and have your questions ready for the speakers

Company Visits

Tuesday 17th May 10a.m. Airwork Holdings at Ardmore. Please register with

Fiona Gray – grayfion@gmail.com

Auckland Education Courses 2016

Western Springs Community College will run two more education courses in May 2016.

Website: www.leisuretimelearning.co.nz/businessandfinance

Our courses are right for new investors, for current investors who need more knowledge, and for those who want to understand their Kiwisaver investments.

Course 1. Investing for your future – general investing principles - 2 x 2hr sessions

Commencing 11th May 2016; Tutor John Hawkins

Price \$69.95 incl GST; plus \$20 for the NZSA course book

Course 2. Sharemarket basics – understanding how and why to invest in shares.

Commencing 23rd May 2016; Tutor Jacquie Hagberg – 2 x 2hr sessions

Price \$67.95 incl GST; plus \$20 for the NZSA course book

Tell your friends, family, and work colleagues about these informative courses. You don't have to be an NZSA member – just keen to develop your understanding

Waikato

Quaystreet Asset Management 23rd February

It has been customary to start the year with a presentation by a market analyst from our valued and supportive sponsors, Craigs Investment Partners on their forecast for the coming year. This year we were addressed by Andrew South, an Investment Manager for Quaystreet Asset Management, (QAM) which is a newly acquired wholly owned subsidiary of Craigs. Andrew emphasised that the two firms are operated separately, and that QAM deals with every area of the market, not only Craigs Investment Partners. The small team have 60 years' experience between them in managing high performance investment funds, have \$450 million under management, and 10 active funds. All funds are PIEs with a minimum investment \$1000. The QAM philosophy is that an actively managed fund with a diversified and sector specific selection of investments can provide better returns than market benchmarks. Andrew said that market inefficiencies provide attractive investment opportunities. However, turnover is low – only 20% last year. QAM are not traders. The important areas in company selection are management, governance, competitive

positioning, volatility and visibility, and how much exposure there is to regulatory change. The latter is very evident in New Zealand. All funds are holding a cash buffer, and although interest rates are low, the dollar is drifting lower, and the local economy is resilient there are risks ahead for 2016.

The known risks are that the resource boom is over, there is world bank debt, social unrest, a bear market, re-regulation of the financial sector and a generational shift in employment with high turnover – all of which cause volatility in the share market.

The unknown risks are the future of oil, emerging markets, China and the effects of the strong US\$.

On the positive side, companies are not carrying a lot of debt, both the US and Europe markets are improving and oil prices are low. The market is improving from lows of -22% in Europe, -17.9% Australia, -11.2% in the US and -3.9% in New Zealand.

In New Zealand we are doing well in healthcare, tourism, Telco's and utilities. The forecast gain for 2016 is 2.4%, and for Australia 2.9%. The exchange rate between the two countries needs to improve in our

favour. Interest rates remain low – 2.5% in New Zealand and 2% in Australia and negative in Europe. Our market is kept up by yield, making for high valuations and so the market is expensive. Andrew said under present conditions the market is still good value, however there needs to be earnings growth globally.

Although Europe and Japan are improving, many of the emerging countries are not. The market is not accepting the Chinese official GDP growth numbers and the currencies in emerging markets are declining against the \$US.

What might derail us? Our housing market is overheated, with a large housing debt, external borrowings are high, the dairy price is too low, China and Australia slowing more than expected, though a recession is unlikely,

Angela Buglass of Trilogy 22nd March

First listed as Ecoya in 2010, the company changed its name to Trilogy in June 2013, and the share price has gone from 60 cents to \$3.35. It now comprises 4 brands– Trilogy, Ecoya, Goodness, and CS & Co, (bought last August). There are now 170 staff globally, based in Auckland. Trilogy's January 2016 forecast of 75 – 79 million revenue and 12 – 14 million EBIT became an actual in March of \$83 million and \$18 million respectively. How to explain the success? Angela put this down to the use of natural products with no additives; New Zealand's clean green image; and cosmetics at an affordable price. In particular, the Trilogy brand owes its success to rosehip oil and to

and there is the possibility of a global shock. Returns will be lower, and volatility higher, and he prefers developed over emerging markets. QAM is neutral on Europe and likes the United States. Interest rates will remain lower and companies with sustainable dividends will be well supported. In New Zealand he mentioned F & P Healthcare, Contact, Mainfreight and Auckland Airport as being good companies, and in Australia the healthcare companies CSL, Ramsay, Sirtex, and companies like Lend Lease and Amcor.

Questions

- 1 Were not the regulatory issues for AIA a negative? **A:** It is an issue for NZ but not for overseas investors who see an excellent growth rate.
- 2 Dairying concerns, with subsidies in Europe? **A:** Now oversupply but the volatility can change overnight.

its use by the Duchess of Cambridge and the supermodel Cara Delevingne. The biggest market for the company is Australia, 44%, and New Zealand, 30%. Trilogy is bigger in New Zealand, and Ecoya in Australia.

Trilogy appeals mainly to women born from 1985 onwards who are against chemical additives. The cosmetic range has maximum effect on the skin and minimum effect on the environment. The rosehip is sourced from Africa and harvested from May to July. Boxing is kept simple, and the marketing slogan is affordable luxury. There are now 414 outlets and the market is growing.

Goodness is marketed in grocery stores and

- 3 Oil situation? **A:** OPEC is driving prices down to bankrupt shale oil industry, and also to get as much income from it before technology changes like electric cars.
- 4 QAM fee levels? **A:** Fairly standard, 0.65% up to 1.25%.
- 5 Tourism? **A:** agreed limited stock in NZ.
- 6 Air New Zealand? **A:** Do not like airlines, as too competitive. Air New Zealand is doing well with low oil price, but increasing competition and regulatory risks.
- 7 Shares in Banks? **A:** Good yield here, but negative overseas, and banks are not spending on capital structure.

For further information on QAM go to www.quaystreet.com

John Davies

is aimed at the mass market. Its main ingredient is chia seed oil from Mexico. There are five products covering a complete skincare regime. The brand was launched in April 2015 and has over 12,000 Facebook fans.

Ecoya was started in Australia and the range of candles, soaps and lotions have a fragrance which appeals to the senses. Christmas sales are large and the main stockists are department stores such as David Jones, John Lewis and Farmers and also gift shops. Ecoya is largest in its field in New Zealand and second largest in Australia.

CS Company was founded in Auckland in 1976. It is a leading beauty cosmetics

distributor, with 1900 outlets and 60 plus names, such as Gucci, Cutex ad Max Factor. It was bought by Trilogy International in 2015 for its synergy benefits, international distribution contacts and for scale.

There were a large number of questions.

Shareholding? A: Not enough free float but now getting more retail.

Debt level? A: Very manageable \$34 million, as debt cheap at the present time.

Point of difference? A: NZ founded, natural and environmental, not the traditional type multinational company.

Men's care? A: Discontinued, but will start again when the right opportunity comes.

R&D? A: Becoming more important. Now must show why Trilogy differs from other natural products.

Dividend? A: Paid last year, and will continue to be paid.

Conflicting Brands? A: There were 2 direct competitors, and we talked this through with them before purchase. Sales can benefit all 3 brands, instead of just Trilogy.

Why do people change to Trilogy? A: Natural skin care.

Packaging? A: Point of difference, simple clean look.

Recycling? A: Ecoya customers can use base of candle, after candle burnt down.

On-line? A: 500,000 turnover. Sales are mainly through department stores after looking at web site.

Natural deodorants? A: Not yet, but with product development.

Manufacturing locations? A: Trilogy - New Zealand, Ecoya -Australia but some manufacturing elsewhere. Head office here.

Helen Glyde

Bay of Plenty.

On the last Friday of February, we had our first Discussion Group Meeting for the year which was well attended.

Bill Murphy from Enterprise Angels gave a 10 minute run down on a second fund (EA Number 2) they have opened which has slightly different rules. In total minimum investment would be \$30,000 but one would only have to pay \$6,000 pa rather than one lump sum. He was very upfront in saying such an investment is not for every one and the risk can be high but success can be very rewarding.

Jon Murie Advisor from Craigs Investment Partners then gave a very interesting presentation of the year ahead which could be "uncertain, have risk and be volatile." He did start with briefly summing up on the year that was Thursday, 28 April 2016, we

have an "After 5" event @ Mount Maunganui Golf Club with Tim Brown, Capital Markets & Economic Regulation @ Infratil. Tim is Chairman of Wellington Airport, and Director of NZ Bus, and will present to members and guests with an "interesting message."

Our AGM will be held on Thursday 26 May 2016 @ Mount Maunganui Golf Club @ 6 pm. Our guest speaker will be David Darling, CEO, Pacific Edge.

Jane Lyndon

Taranaki

We started the year with an event where we were hosted by NZAM and Castle Point on the 18th February. Greg Peacock from NZAM spoke about funds with an "Absolute Return" and Hedge funds. Steven Bennie from Castle Point then spoke about the things they look for when selecting the stocks they choose to put in their portfolio. A lot of it was common sense, but it still generated a good discussion. Both companies were very generous in their sponsorship and our thanks go out to them.

March 30th we will hold our AGM and Martin Watson from the Executive will also address us.

April 7th We plan a visit to the Fonterra plant at Whareroa just south of Hawera where we will have a short tour and a talk about how the listed Fonterra Shareholders Fund works and how that relates to the fund that suppliers (shareholders) invest in.

May 4th. Craig Investment Partners plans to invite us to their function when Mark Lister will be speaking.

Grant Langdon

Wellington

Our first meeting this year was a presentation from Julian Cook from Summerset. A nice way to start the year, and for our April meeting we have Ray Jack with a macro and micro view of the investing world.

We have been fielding a lot of enquiries about investor education courses and so for our May meeting we will run a new and prospective members evening with focus on investing basics and getting started. We will also slip in a quick branch AGM.

This time last year we were getting ready to set off for the Berkshire Hathaway AGM in Omaha

Nebraska. It was a great event and this year for the first time ever the Q&A part of the AGM (all 5 hours of it) will be webcast live – not to be missed! The time zone means a late night, 10am Eastern Time on Saturday 30 April will be 2am Sunday 1 May in NZ. Still it is easier and much cheaper than travelling to Omaha. Check it out at <https://finance.yahoo.com/brklivestream>. For background reading you can download the 2015 annual report (a cracking good read as always) www.berkshirehathaway.com/2015ar/2015ar.pdf

Martin Dowse

Canterbury

Our first event of 2015 for branch members was a discussion evening led by Branch Chair, Robin Harrison, under the theme "Surviving in a Deflationary Economy". It was not as depressing as the title may suggest and generated a lively and informative exchange of views.

Our next event for members will be a talk from Bruce Sheppard, founding Chairman of the NZSA, on Tuesday, 26th April. Details of the venue and time have yet to be confirmed but will be notified to Branch members shortly. We expect an energetic and politically incorrect presentation from Bruce! As this will be open to members and their guests we will be holding the event at a larger venue than our usual meeting spot at the Fendalton Croquet Club.

For later in the year we are planning a larger public event as part of Money Week which runs from 5th to 11th September

Robin Harrison

Members' Issues

Rubicon –The questions remain

In our February Scrip we reported on the Rubicon AGM in which shareholders expressed concern over the claims of former staff members over ArborGen which is 31% owned by Rubicon. The other Rubicon investment is in Tenon, the wood processor and distributor. Both of these subsidiaries are self-managing, and the question has been asked as to why an expensive board of directors is at all necessary for Rubicon.

ArborGen is a large producer of forestry seedlings with 160 staff, 15 nurseries, 16 seed orchards, and 32 distribution centres in USA, NZ and Brazil. A South Carolina court awarded \$53m to the former employees, making strong criticisms of the ArborGen directors including the current MD of Rubicon Mr Luke Moriarty. On 23rd March, Rubicon announced that the USA court had vacated its award to the plaintiffs in favour of a confidential settlement. The directors say that the cost to Rubicon is immaterial, and that

there will be no further impact on the company, or further comment. NZSA had 3 concerns over the judgement:

- 1 That the initial contract with the employees was poorly framed and not in the best interests of shareholders.
- 2 That the actions by the company in not adhering to the contract could never have measured up to the "high ethical standards" claimed in the company's policies
- 3 That the forecast decision by the judge was known at the time of the annual report and should have been provided for in the annual accounts.

These concerns were never answered by the company, and the court's criticism born by Mr Moriarty should have made his position untenable. NZSA is investigating the American court judgement. Shareholders may decide this year whether the composition of the board is still satisfactory.

Company Tax and the Avoidance Game

The Herald has recently published a series of articles on profit and base shifting by international companies to avoid paying tax in New Zealand. After reading our article on the MHI tax dispute, Grant Diggie gave his personal view:

- 1 I believe governments have a fundamental duty to govern with certainty and equity. So their agencies must do likewise. They must act in good faith and like the Courts justice delayed is justice denied. If they can't resolve an issue within a reasonable time frame, they should be disbarred by law from being able to extract both the tax and any penalties. This would concentrate their minds and avoid them using their power in an oppressive manner. The same principles that apply to citizens must apply to government and their agencies. You will recall in the good old days almost every statute had as its second clause "The Crown is not bound by this Act." Well those days are gone, and we are in a new era where the Crown must have the same liabilities as its citizens.
- 2 Tax minimization instruments: I am philosophically opposed to these. I believe every citizen including corporates must pay the tax due without using artificial constructs not available to all. Now the lawyers will argue the case but what are brands and IP really? And what are they worth? Take VW. In one incident its brand was devalued overnight. I believe the coming generation will fix the problem, because they won't stand for this stuff. Already we have seen protest in the UK over Starbucks, Google, Apple and others - and this will continue. So governments will and I suggest, will be quite happy to ignore these instruments and tax within a jurisdiction, on a very simple income less expenses equals taxable income. Governments must surely be getting to the point of understanding that, at present, it's the corporates who are winning not them.

We must let the Court decide

Recently we have been asked to comment on cases which are before the court involving theft by staff members of listed companies. NZSA board has resolved that we must not let our abhorrence of a crime interfere with the course of justice.

Chairman John Hawkins expressed it well to one of our correspondents.

- 1 Regardless of the circumstances, anyone accused has a presumption of innocence until proven otherwise. Any comment NZSA makes prior to the judgement could be construed as implying guilt.
- 2 Any comment NZSA made prior to judgement in regard to perceived problems with the companies' systems would be based on speculation. The fact is that we don't know how any alleged offense has occurred.
- 3 All the systems in the world will not prevent fraudulent activity if the perpetrator is hell bent on carrying it out. There are many ways this can be done (some very sophisticated) and audit and risk processes may take some time to pick them up. We note that Sky City, which probably has the most oversight and audit of any listed company also has a case before the court at present.

- 4 From reports, it usually appears that at some point, the company's systems did discover an irregularity and action was taken - perhaps too late, but again we don't even know if that is true.
- 5 I am meeting directors and CEOs regularly and will be discussing the general topic of risk management. I would not expect that they can share any specific detail of a case before the court. We will also be raising the topic of "whistle blowing" which we have been developing some policy around. This is a very effective way to minimise fraud and show up significant shortcomings, but experience has shown that often whistle blowers end up suffering consequences, something that the current law does not adequately address.
- 6 We understand your frustration as a shareholder, and it is always galling when we are told that \$1m+ off the bottom line is not material. This of course is the correct legal and listing rule interpretation (less than 5-10% is not "material"), but it is nevertheless a lot of money.
- 7 Realistically, can we expect directors to carry the can for the fraudulent activities of some

person in an operational position - assuming always that there were reasonable protocols and systems in place? The NZSA board thinks not, but will look at each instance on its merits at the time a judgement is made. Should it transpire that the company did have poor systems and a relatively unsophisticated fraud was perpetrated as a result, you can be assured that we will be quite blunt with the directors and management, including comment in the media if appropriate.

Upcoming Events

For more information go to Branch section of NZSA website

2016

April 7	Taranaki Branch visit
April 12	Wellington Branch meeting
April 13	Auckland Branch meeting
April 26	Waikato Branch meeting
April 26	Canterbury Branch meeting
April 28	Bay of Plenty Branch meeting
May 4	Taranaki Branch function
May 10	Wellington Branch meeting
May 26	Bay of Plenty Branch AGM
June 15	Auckland Branch meeting

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