

IN PRIVATE

NEWSLETTER WINTER 2008
NEW ZEALAND EDITION



Beyond the mainstream – alternative investment opportunities

By leveraging the specialist resources of our wider organisation, we can offer investment opportunities tailored to the individual needs of Private Bank clients.

Making a difference

Wealthy philanthropists are making an increasingly important contribution to their communities – and they're becoming increasingly hands-on.

An enduring legacy

One family's 40 year commitment to a disease-free New Zealand has helped create one of the world's leading medical research facilities.



TAKING THE LEAD

THE RECENTLY ANNOUNCED CHANGES TO NEW ZEALAND TAX RULES ON CHARITABLE DONATIONS ARE A WELCOME ACKNOWLEDGEMENT OF THE IMPORTANCE OF PRIVATE GIVING TO ORGANISATIONS MAKING A DIFFERENCE IN OUR COMMUNITIES. THEY ARE ALSO VERY TIMELY, AS THE THEME FOR THIS ISSUE OF IN PRIVATE IS PHILANTHROPY.

Many Private Bank clients give very freely of both their time and their resources to support causes they believe in. In our experience, they are not driven by any desire for recognition. They do it simply because they are in a position to make a contribution. In this issue we look at the increasingly significant role wealthy philanthropists are playing and the changing nature of philanthropy. We also profile some of the ways that our clients, and indeed ANZ, are helping to make a positive difference.

One of the advantages of the Private Bank service is our ability to leverage the specialist resources of our wider organisation. In this issue we also introduce some of the ways we can use those resources, to provide alternative investment options for clients with differing needs and interests.

Whatever your needs and interests may be, in an economic environment that remains uncertain the value of a clear strategy and a disciplined approach are more apparent than ever. As we continue to extend and enhance our offering, you can be sure that those qualities will continue to remain at the heart of the Private Bank approach. **IN PRIVATE**

Catherine McDowell
Managing Director, Private Banking

Lending watch

Financial market sentiment appears to be improving around the globe. Credit and swap spreads are narrowing, equity markets are recovering, and iTraxx measures have fallen quite sharply. Are we out of the woods? It is too early to say.

Certainly, we have been encouraged by continued write-downs and disclosures on poor derivative assets, along with recapitalisation moves. Recent data in the US (leading indicators such as the ISM) have taken on a better tone, albeit off recessionary lows. Yet inter-bank interest rates remain elevated.

A key area we are watching is the behaviour of the banking system itself, given the significant role financial intermediaries play within the economic cycle. The past decade has seen a growing portion of literature devoted to the credit channel of monetary policy, an implicit recognition of the role financial intermediaries play in the economic cycle. Bernanke (yes, the current Chairman of the US Federal Reserve) and Gertler (1995) identified two legs – the balance sheet and the bank lending channel. The balance sheet channel is where changes in interest rates (monetary policy) affect asset values, the cash flows of borrowers, creditworthiness and the external finance premium they face. The bank lending channel relates to the outright supply of loans. One of the reasons the 1990/91 US recession was thought to be a long and drawn out process has been put down to ‘financial headwinds’ arising from a shortage of capital (Bernanke and Lown, 1991).

The US Federal Reserve and the European Central Bank have recently released surveys on lending practices in their respective economy’s banking sectors. The surveys ask banks about changes to the supply and demand of bank loans to businesses and households over the past three months.

The key and clear message from these surveys is that credit standards are tightening. Such a tightening represents a prudent step in relation to a turn in the economic and credit cycle. Yet it also gives the real side of the economy a further headwind to worry about.



Beyond the mainstream

ALTERNATIVE INVESTMENT OPPORTUNITIES

The tightening – comparing the 1990/91 and 2001 episodes – is consistent with the US economy being in recession. It is also consistent with the momentum within the European economy slowing.

With lending standards tightening, we believe it is too early to extrapolate out recent marginal improvements in US indicators such as the ISM surveys as evidence that the trough for the US economy has been reached.

This does not mean we should be slavishly watching lending gauges, as these are notoriously late cycle indicators. However, the significance of lending standards should not be downplayed given the major role the credit channel of monetary policy and risk appetites has played supporting asset values, and the influence the wealth effect has had on consumer spending. Estimates suggest the wealth effect from rising asset values could have added close to a full percentage point to growth each year. How households' spending behaviour adapts to a more stable (outright declining) near-term housing environment remains a key issue. Ultimately, the de-leveraging, and tightening in lending standards across financial institutions must be met by the same belt tightening in the real economy. This adjustment will be the next leg of the cycle to watch.

New Zealand has not been immune. Indeed, as noted by the Reserve Bank in their latest Financial Stability report '...a more cautious approach to lending on the part of the banks appears prudent. However, there are risks that if credit conditions are tightened excessively the slowdown in the economy will be exacerbated, putting additional financial pressure on households and businesses.' The risk to those addicted to the credit fix, is that it turns quickly into a case of cold turkey.

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Cameron Bagrie
Chief Economist

The fundamental principle behind the Private Bank service is that every client has unique needs. Our fundamental approach is based on meeting each client's needs in the most appropriate way.

For some clients, the primary focus is on preserving their wealth. Their investment portfolios reflect that goal, with a mix of predominantly share and fixed interest investments, structured with a long term view in mind. But along with these more traditional investments, an increasing number of clients are seeking to explore alternative investment options to broaden their portfolio.

Director of Private Clients Nigel Scott says our position as part of a leading global banking group means we can provide a number of alternatives for clients looking to spread their investment wings. "By drawing on the resources of our wider organisation we can structure investment opportunities outside the mainstream, tailored to individual clients' situations and interest," says Scott.

Those opportunities include options for private equity and commodity investments. In this article, we look at some of the options that are available for Private Bank clients.

EQUITY PARTNERSHIPS

One well established example is the opportunity to invest in the rural sector (particularly in dairy farming and dairy conversions) through Equity Partnerships. Equity Partnerships are particularly attractive to clients who have been successful in the rural sector and wish to retain an interest, without being involved in the day to day operation. Typically, an equity partnership is a company structure, with investors holding shares in the company. They normally involve a small group of investors who know each other or are introduced by a common party. Through our rural banking network, we have assisted many clients to become involved in successful equity partnerships.



PRIVATE EQUITY INVESTMENTS

Another example of private equity investment opportunities on a wider scale is the ANZ Business Equity Fund offered through our parent company Australia and New Zealand Banking Group Limited (ANZ Group). ANZ Group in Australia and ANZ National Bank Limited (ANZ) in New Zealand have been investing in private equity since early 2000.

The first Business Equity Fund was established in 2006 to provide an opportunity for high net worth investors to co-invest indirectly alongside ANZ and ANZ Group in private equity investments here and across the Tasman. The Fund invests in small to medium sized enterprises, with an average investment life of five years. Generally, the Fund will only undertake an investment where the expected internal rate of return on exit is expected to be at least 20%.

Potential companies are sourced and undergo a rigorous assessment process before investments are undertaken. The Fund, ANZ and ANZ Group (depending on the country) collectively have a significant level of influence over the activities of the companies.

“The results of the investment activity of the Fund to date have been very pleasing, and generally in line with our expectations” says Business Equity Fund Manager Brad Middleton. “The Fund was launched in 2006 and the emphasis to date has been on identifying the right investments. We now have a strong portfolio of businesses, and we’ll be looking to realise some of those investments over the next twelve to eighteen months.”

The Fund is now closed to subscriptions however, following its success, a second is in development and is expected to be launched in the third quarter of 2008.

COMMODITY LINKED INVESTMENTS

Commodity prices have been the subject of much media coverage in recent times, with the price of food and oil soaring. Gold has also enjoyed a sustained rise in value as a hedge against inflation and a safe haven with the upheavals in financial markets.

Traditionally, the only way to invest in a commodity like gold was to physically buy and hold it. Private Bank is working on a structure whereby clients can take advantage of commodity linked investments which offer exposure to a range of commodities, without having to physically hold them. These investments are linked to a specified commodity index and can also provide clients with a capital guarantee.

“Commodities can be a useful complement to traditional financial assets like stocks and bonds and this helps reduce portfolio volatility,” says Nigel Scott. “Commodities are one of the few asset classes that tend to benefit from rising inflation and as such, offer protection from the effects of inflation. Many countries around the world are currently experiencing a period of low growth and high inflation.

“Commodity linked investments can be tailored to reflect our investment view. For example, if we think that gold will continue to increase in value, we can structure an investment accordingly. Alternatively, if we take the opposite view and believe the price of gold will fall, we can also structure an investment to reflect that.

“Our approach has always been about understanding and meeting the individual needs of our clients,” says Scott. “For those clients who are interested in exploring alternative investments, we can provide a range of exclusive and innovative options tailored to their interests and particular situation.”

If you’d like to find out more about alternative investment options, talk to your Private Banker. **IN PRIVATE**

Making a difference



When Warren Buffet announced in 2006 that he would give away 85% of his \$US44 billion fortune to charity, it was one of the most notable examples in a long history of wealthy individuals and families using their resources to make a real difference to local and global issues.

Buffet, the world's second-richest man, gifted shares in his Berkshire-Hathaway company to five foundations. The majority went to the philanthropic foundation set up by the world's richest man, Bill Gates and his wife Melinda. The Gates' had themselves pledged over \$US30 billion to set up their foundation, and are heavily involved in its operation. The other organisations that benefited from Buffett's decision were three foundations each headed by one of his children, and another set up by his wife.

Wealthy philanthropists come from a wide range of backgrounds. Along with successful businesspeople, musicians like Bono and Sting are these days involved as much in their philanthropic activities as their music.

New Zealand has its own high-profile philanthropists. One of the most recent examples is Gareth Morgan's decision to use some of the proceeds from his investment in TradeMe to set up the Morgan Family Charitable Foundation.

On the whole, though, the philanthropic activities of wealthy New Zealanders are carried out 'under the radar'. Private Bank Head of Private Clients Kieran Forde says while many Private Bank clients are involved in a range of philanthropic work, they prefer to keep their involvement private.

"They are driven to get involved for a number of reasons," says Forde, "but recognition is not one of them. These are people who have worked very hard and are now in a position where they are able to make a meaningful and lasting contribution to society. They want to make a difference in an area they feel passionate about.

"Making a real difference is the key. They are results driven in their professional lives and they want to achieve results in their philanthropic work as well. Increasingly, we're seeing examples of our high net worth clients looking for more hands-on involvement as well as donating money. Whilst money obviously makes a difference some of these people often can make a more enduring contribution by bringing their professional skills and networks to bear."

Philanthropy is often a family affair, with several generations sometimes being involved. "For many clients, getting their family involved is a major factor," says Forde. "It's a way of getting across the values of social responsibility to the next generation, and what that means in practice."

Involving children in the running of a foundation is also an excellent way of helping them build their business skills and experience. They deal with many of the same issues that all businesses face – raising funds, organising resources and managing projects effectively, so it can be an excellent grounding for the future.

Forde says the Private Bank service is about understanding the holistic needs of clients, and he is keen to understand how the Bank can help clients achieve their philanthropic goals.

"In some cases we have helped clients to become involved in particular organisations that align with their personal values by making introductions. Often, the right introduction at the right level can facilitate an enduring partnership.

"Philanthropy continues to be a major area of interest for many Private Banking clients, and the landscape is evolving," says Forde. "We are keen to hear from our clients about how we might be able to assist in organising their philanthropic activities." **IN PRIVATE**

Sharing the load

GIVING YOUR STAFF THE OPPORTUNITY TO GET INVOLVED IN COMMUNITY INITIATIVES IS GOOD FOR EVERYONE



In the twenty first century the notion of social responsibility is taking on an increasing significance for businesses, as well as individuals. And in some cases, businesses are successfully aligning their own social responsibility agenda with that of their staff.

The ANZ National Bank Staff Foundation is one example of a company and the people who work for it joining forces to achieve a common social goal. The Foundation is a charitable trust through which ANZ National Bank staff can support organisations and projects that make a real difference in their own community.

Staff members who join make a regular donation to the Foundation from their pay each fortnight. Their contribution is matched dollar for dollar by the Bank, which also pays all the running costs. Since being established seven years ago the Foundation has donated over one million dollars in grants to more than 300 community organisations.

A board comprised of Staff Foundation members meets quarterly to make funding decisions. Private Bank Regional Manager Neil Beattie is the current chairman. He says the focus is on helping smaller, grass-roots organisations where Foundation grants can have a significant impact.

“Our grants typically range from a few hundred dollars to a few thousand,” says Beattie. “To a small community-based organisation that can make a huge difference.”

Beattie has been involved with the Staff Foundation since the start. Most members, he says, get involved for similar reasons – the opportunity to do something for the community they live in, and the satisfaction of aligning their personal values with their working lives.

The Staff Foundation is one of a number of initiatives under ANZ National Bank’s Corporate Responsibility programme. Another is the staff volunteering programme, where each staff member is given one day’s paid leave a year to help out community organisations. Initiatives like these help support our Corporate Responsibility goals but, there’s a spin-off benefit for the Bank too. There’s no doubt these kinds of initiatives help to lift staff engagement and pride in the organisation.

Neil Beattie says over 1200 ANZ National staff are currently Foundation members, and that number is continuing to grow.

“The Staff Foundation provides our people with an easy and very powerful way to make a real difference in their community. For example, one of the things we have supported is the Loaves and Fishes programme which provides lunches for children who go to school without breakfast or lunch – or sometimes both.

“When you think about the benefits to those kids and the difference it could make to their lives, it’s very humbling. But it’s just one of many projects achieving fantastic things in our communities. It’s wonderful to have a mechanism like the Staff Foundation to be able to support them.” **IN PRIVATE**



An enduring legacy

A GIFT OF SHARES WAS THE CATALYST FOR A RELATIONSHIP THAT HAS CONTINUED FOR MORE THAN 40 YEARS, BETWEEN THE MALAGHAN FAMILY AND THE INSTITUTE THAT BEARS ITS NAME.



The Malaghan Institute of Medical Research is New Zealand's leading vaccine and immunology research centre. It is based in Wellington and has over 50 scientists who are dedicated to the prevention and treatment of cancer, asthma, arthritis, multiple sclerosis and infectious diseases. It has also earned an international reputation as a cutting-edge medical research and training facility. The scientific research and operations are overseen by Professor Graham Le Gros, while the Trust Board is spearheaded by a member of the Malaghan family, all of whom are still very much a part of the organisation.

Graham Malaghan has been the Institute's Chairman since 1990. The Malaghan family's involvement began in 1967 when his parents gifted shares in General Foods Corporation (the company his father helped establish) to the Wellington Medical Research Foundation. The funds were used to help sponsor the creation of the Wellington Medical and Cancer Research Institute, which later changed its name to the Malaghan Institute in recognition of the family's contribution.

Graham Malaghan is proud of the Institute, those who work there and the people who donate their time, energy and money to support it.

"The Institute is the only one of its kind in New Zealand, because while we collaborate closely with a wide range of organisations, we are completely independent. It's a unique environment for researchers. They are able to focus solely on their research, and benefit from access to first class facilities and a community of like-minded, dedicated colleagues. The chance to work in that kind of environment has attracted many talented young New Zealand researchers back from overseas, and that's a great thing for this country."

The quality of the work done at the Institute has been recognised by many awards, scholarships and research prizes.

It's also recognised by a great many New Zealanders. Institute Fundraising and Communications Manager Tanya Fulcher says the Malaghan Institute has attracted a national community following of

6,000 regular donors, and over 25,000 people in Wellington alone donate to the Institute's annual street appeal.

"The very strong feedback we receive from community groups is that they appreciate the independence of the Malaghan Institute and the strong focus on community involvement between our staff and ourselves," says Ms Fulcher.

Graham Malaghan says the discovery-based research approach is one of the key features of the Institute. "You never quite know what new breakthroughs might be just around the corner. The discoveries our scientists have made have led to some incredible advances in the treatment of disease. It's work that is immensely valuable and it's very exciting to be a part of it."

"It's also very satisfying to see bright young New Zealanders, high achievers who could earn considerably more overseas, coming back to make a contribution. Part of the Institute's role, in fact an essential part, has always been to foster and develop young scientists, and it's very pleasing to be able to give our bright young stars the chance to start their careers."

Operating at the leading edge of biomedical research means funding is always a major focus. As an independent body the Institute relies on contestable grants, corporate sponsorship, trusts, bequests and donations that enable it to continue working towards its vision of a disease-free New Zealand.

"We are very grateful for the incredible support we get from Friends of the Institute groups all over the country, and from the individuals, businesses and organisations who make such a contribution," says Graham Malaghan. "They do a fantastic job. But of course, fundraising is an ongoing need. We are always looking for people and organisations that share our vision and would like to play a part in helping to achieve it. I can say from my own experience that it is an incredibly exciting and worthwhile opportunity to make a very big difference."

For more information about the Malaghan Institute visit www.malaghan.org.nz. **IN PRIVATE**

Portfolio Investment Entities



Over recent months there has been considerable discussion in the media about the introduction of Portfolio Investment Entities. PIEs are a new type of investment entity that offer tax advantages to some investors.

HOW DO PIEs WORK?

Certain investment entities, such as managed funds, can apply to become PIEs.

Before PIEs, almost all managed funds were taxed at 33%, regardless of an individual investor's tax rate. Under the new regime, income from PIEs is distributed at each investor's prescribed investor rate (PIR). As the maximum PIR is 30%, there are obvious advantages for investors on higher marginal tax rates.

For example, an investor on a 39% tax rate who has \$500,000 invested in a non-PIE investment at 8.10% p.a. would receive \$24,705 per annum after tax from the investment.

In contrast, the same investor with the same amount (\$500,000) invested in a PIE fund at the same rate of return (8.10%) would receive \$28,350 per annum after tax – a difference of \$3,645 per annum.

If you would like to find out more about PIEs and how they could benefit your particular situation, talk to your Private Banker. **IN PRIVATE**

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