2007/08

AUSTRALIAN AGRIBUSINESS GROUP

# AGRIBUSINESS MIS INDUSTRY REPORT OF FUNDS RAISED

July 2008

## Executive Summary

### Introduction and Methodology

- The 2007/08 financial year was once again a year of uncertainty for the MIS industry, particularly the non-timber sector. However, the industry as a whole performed very well in terms of capital raised.
- All project managers that released MIS products in 2007/08 were sent a survey.
- Survey responses were collected on the basis that information was confidential if requested and the results of no one project in particular could be identified from this report.
- This report extends on similar reports undertaken by AAG annually since 2001/02.

### Number and Type of Projects

- **AAG identified 57 agribusiness offerings that were open for investment in 2007/08**. This compares to **67** in 2006/07.
- Of the 57 projects open for investment, 37 were released in 2007/08, with the balance continuing on from the previous year. The number of new projects represents a **23% decrease** on 2006/07 figures.
- **Timber projects represented 38% of products on offer compared with 40% in the previous financial year**.
- **Horticulture projects accounted for 35% of new products, down from 38% of projects in 2006/07**.
- **There were 28 agri-sectors on offer in 2007/08, compared with 29 in 2006/07**. There were no new agri-sectors in 2007/08.

### Funds Raised

- The **agri MIS industry raised $1,079 million in 2007/08, a decrease of 5% from the previous financial year of $1,139 million**.
- **Timber offerings** accounted for the vast majority of funds raised in 2007/08 ($705 million or **65% of total funds**), slightly up on the 2006/07 result of $672 million (59% of the total).
- Inflows for **horticulture increased by 4% to $246 million** in 2007/08, while wine grape and other categories were significantly down on the previous year.
- There were approximately **24,300 individual investors** who participated in MIS projects in 2007/08, 5% below the corresponding figure last financial year.

### Companies

- AAG **identified 31 project managers who released investment offerings in 2007/08**.
- Of the of 29 companies that released investment products in both 2006/07 and 2007/08, 45% achieved better results in 2007/08.
- Only one-quarter of projects open for investment in 2007/08 achieved funds raised equal to or in excess of their stated target.
- Whilst listed companies represented only 29% of the companies operating in the sector, they raised approximately $916 or 85% of the funds raised during 2007/8.

### Revenue, Tax and Finance

- The **2007/08 investments will contribute approximately $6.5 billion in farm gate revenue over their term**.
- AAG estimates that the projects established since AAG started this survey in 2001/02 will produce a total of **$29.0 billion** in farm gate revenue.
- An estimated $482 million will be received by investors as tax refunds following the 2007/08 capital raising. These refunds will be far outweighed by the tax paid from the activity of these projects.
- The weighted average of total investment dollars which were geared in 2007/08 amounted to 73%, down from 77% in the previous year.

### Flow-on Effects

- **Victoria** will receive the largest proportion of **funds raised** from the 2007/08 capital raising, while **Western Australia** will receive the largest proportion of **new project development by area**.
- As a result of the 2007/08 capital raising, a significant area of land will be established to timber plantations (78,289 hectares), of which 54,500 hectares will be for woodchip purposes.
- The area of land to be established to horticulture and vineyards stands at 7,025 hectares and 1,122 hectares respectively.
- The companies involved in the industry employ more than 2,300 persons directly and a further 3,100 persons on a contract basis.

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## 1. Background

AAG has researched Managed Investment Schemes (MIS) since 2000 and has produced the industry leading End of Year Round-Up Report every year since 2001/02. The 2007/8 report builds on the previous six years of data with another year of detailed information.

The 2007/08 financial year was once again a year of uncertainty for the MIS industry, particularly the non-timber sector. Concerns over the future of non-timber MIS projects, within the context of the poor performing equity market, higher costs of finance and continuing drought conditions in south eastern Australia were all influencing factors to this year's capital raising.

Whilst the taxation legislation for non-timber MIS projects is assured, uncertainty regarding the ATO's interpretation of non-timber MIS projects going forward had a negative influence on sales.

A test case will be heard in August 2008 between industry and the ATO and is expected to clarify the standing of deductions for non-timber MIS from 2008/09 onwards.

Compounding the legislative uncertainty for non-timber investments is the continuing drought conditions across south eastern Australia. The impacts of the continuing drought and of climate change on future water allocations, particularly in the Murray-Darling Basin, was apparent across both print and television media during the year. We are aware that this perception of drought was a determining factor for a number of financial planning groups when deciding which investments to recommend to their clients.

Investor demand for MIS projects is largely driven by strategies associated with tax minimisation, and as such the performance of the domestic economy, and returns from the equity market in particular, had a large bearing on sales.

The financial environment in Australia during the 2007/08 financial year was characterised by a flagging equity market and increased inflation. Despite this, the capital raised result suggests that there was still a considerable number of investors with a need for tax minimisation strategies. If the economy was stronger, it is likely that the capital raised this year would have exceeded that of 2006/07.

Traditionally, a large proportion of MIS investors borrow to finance their investments in MIS. As a result, the increasing costs of borrowing and the consequences of the significant tightening in the finance market were negative influences on MIS sales during 2007/08.

There is no doubt that the MIS industry faced an uphill battle during 2007/08 to raise capital. The capital raised by the non-timber sector was down on the previous year, while a large number of MIS participants failed to achieve targeted sales figures.

Despite the issues faced by the industry, the total subscription monies raised by the industry indicated a relatively successful capital raising year, propped up by a late surge of investment in several forestry MIS projects.

## 2. Methodology

AAG created a list of project managers whom we were aware released MIS projects during 2007/08. Each project manager was contacted and sent a survey form to be completed. All responses were collected and analysed.

This review only looks at projects which raised funds during 2007/08. Given that not all projects close by 30 June, some of the investments on offer in 2007/08 were investments that were actually released in the previous financial year. For these investments, we have only included the portion of the project's fund raising that was undertaken in 2007/08.

This review looks at both retail and wholesale investments which were released during the financial year through Product Disclosure Statements (PDS) and Information Memoranda (IM) respectively. The vast majority of projects released in 2007/08 were into the retail market.

  

The wholesale market includes investments which are released by easily identifiable project managers, as well as investments released by discreet non-public participants where contact details are very difficult to find. AAG has only included those that were released with a product ruling and those where the offer documents were publicly obtainable.

An important feature of our end of year survey is the fact that AAG is fastidious in maintaining confidentiality of those product managers which do not want their information to be identified publicly.

AAG relies on the integrity of the product manager in completing this survey honestly and accurately. Given the confidentiality of the surveys and the relationships we have developed with the product managers over time, AAG deems the accuracy of information provided to be very strong.

The end of year survey form which AAG sends to the product managers is standard for all projects. The results from each product manager are therefore uniform and readily able to be compared against previous year's figures.

It is important to note that our capital raising estimate is based on the upfront fee payable upon application. It does not include any ongoing fees and excludes GST.

## 3. Responses to this Survey

AAG identified 31 project managers which released investment offerings in 2007/08.

AAG contacted all project managers and provided them with a survey form to complete. We received responses from all but 4 companies, resulting in a response rate of 87%.

Those that did not respond to the survey included:

- Oak Valley Truffles
- Watershed Premium Wines
- Paulownia Farm Management
- DDR Funds Management

Oak Valley and Watershed Premium Wines have some common management. The other two are not related.

For the projects which we did not receive sales information for this financial year, we have made estimates based on the targeted subscription, capital raisings from similar projects and previous capital raisings from these offerings in previous years. It is important to note that these projects have traditionally accounted for a very small volume of sales and as such do not have a material impact on industry wide numbers.

## 4. Number and Type of Projects

A total of 57 projects raised funds in 2007/08 with 37 (65%) of these projects being and released specifically in 2007/08 (Figure 1). The number of new projects released during the year represents a 23% decrease on the previous financial year.

The remaining 20 projects (35%) which raised money during 2007/08 were offerings which continued over from 2006/07. The chart below clearly indicates the reduction of projects offered, some of which is due to industry consolidation.

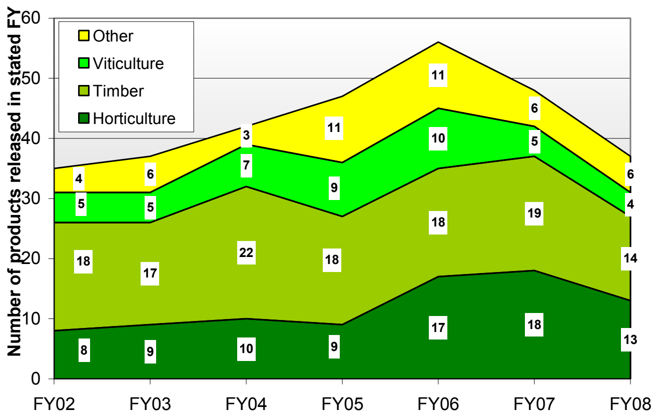


***Figure 1 – Number of newly released agribusiness offerings by year and industry.***

The proportion of carry over projects to new projects in 2007/08 was higher in 2007/08 (35% carry over; 65% new), than the previous financial year (28% carry over; 72% new). AAG believes this was largely due to the uncertainty of the non-timber sector, with companies preferring to carry over projects from the previous year instead of incurring the costs of releasing new projects.

In addition to the 57 projects that raised funds in 2007/08, we are aware that several others received Product Rulings, but were removed from the investment market and subsequently did not accept investment funds. These projects have not been included in the survey analysis.

Timber investments accounted for the majority of projects that raised funds during 2007/08 (38%), with horticultural offerings coming a close second (35%) (Figure 2).

Timber has been the largest category by number of projects since AAG started this survey in 2001/02.

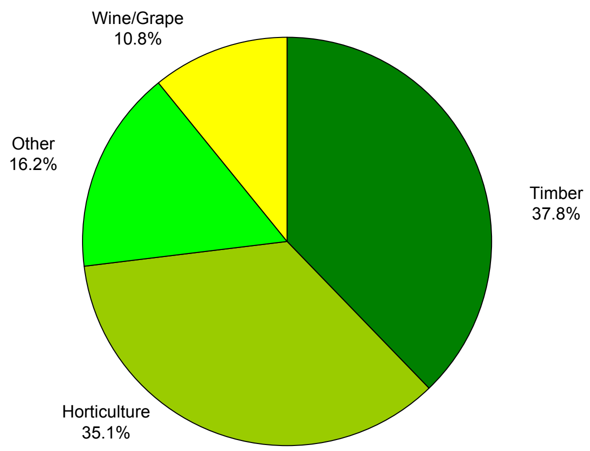


***Figure 2 – Proportion of 2007/08 agribusiness offerings that raised funds by industry.***

The remaining projects on offer 2007/08 were taken up by those in the Other and Wine/Grape categories (Figure 2).

The Other category included projects in the following agri-sectors:

- Abalone;
- Cropping;
- Dairy;
- Diversified;
- Ginseng;
- Infrastructure;
- Livestock (including beef cattle and chickens);
- Pearls;
- Truffles; and
- Water.

There was a broad range of projects on offer in 2007/08, with 28 agri-sectors recorded by AAG compared with 29 in 2006/07 (Figure 3). There were no new agri-sectors in 2007/08.

Woodchip projects accounted for the largest number of offerings in 2007/08, with almond, sawn timber and wine grape projects also having a large number of offerings available for investment (Figure 3). A significant number of sectors had only one project offering.

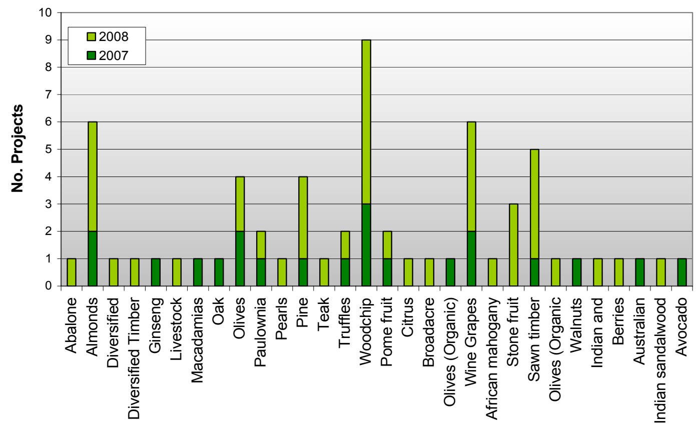


***Figure 3 – Number of products on offer in 2007/08 by agri-sector and year of release.***

## 5. Funds Raised

AAG estimates a total of $1,079 million was raised for agribusiness MIS in 2007/08, a decrease of 5% from the previous financial year (Figure 4). Given the issues faced by the industry during the year (refer to Section 1), AAG believes this year's capital raising was a very good result for the industry.

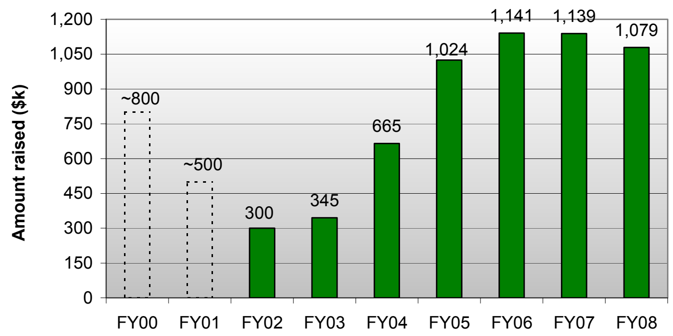


***Figure 4 – Funds raised in the agribusiness investment industry over the past 9 years (Note: 1999/00 and 2000/01 figures are estimates only while all other years are determined from AAG's end of year surveys).***

AAG's methodology provides for the only accurate and precise measure of industry performance. All data is collected on a standardised basis with GST excluded and only funds actually invested in 2007/08 included. We do not include any commitments for future payments.

  

The breakdown of the funds raised by each industry is detailed in Table 1.

***Table 1  Funds raised by industry***

| | Funds Raised in 2007/08 ($m) | % change in funds raised from previous year | % of funds in 2007/08 | % of funds in 2006/07 | % of projects in 2007/08 |
|---|---|---|---|---|---|
| Horticulture | $246m | +4% | 23% | 21% | 35% |
| Timber | $705m | +5% | 65% | 59% | 38% |
| Wine/Grape | $42m | -46% | 4% | 7% | 11% |
| Other | $86m | -44% | 8% | 13% | 16% |
| **TOTAL** | **$1,079m** | **-5%** | **100%** | **100%** | **100%** |

As Table 1 suggests, timber offerings accounted for the vast majority of funds raised in 2007/08 ($705 million or 65% of total funds). This figure was slightly above the total achieved in the previous financial year (+4%).

Inflows also improved for horticulture in 2007/08, increasing by 4% to $246 million (Table 1). AAG views this as an excellent result given the difficult investment environment for this sub-sector in 2007/08.

Unlike the horticulture sector, those in the wine grape and other categories were significantly impacted by the negative environment for non-timber projects. This is evident by the noticeable decrease in fund inflows into these sectors in 2007/08 (Table 1).

Despite a decrease in the proportion of product offerings open for investment (40% in 2007/08 compared to 38% in 2006/07), the timber sector increased its sales figures as a proportion of total sales from 59% in 2006/07 to 65% in 2007/08 (Figure 5). Given the MIS environment during the year, AAG was not surprised by these figures.

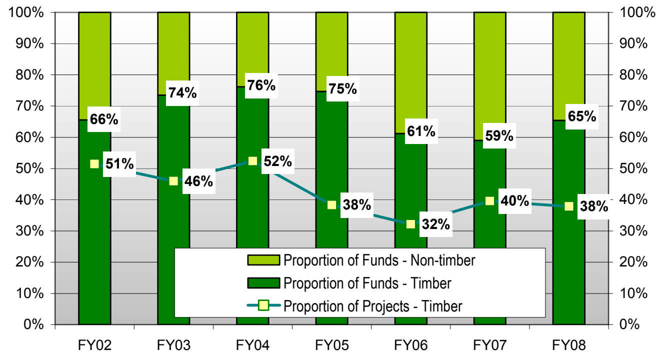


***Figure 5 – Proportion of timber vs. total MIS industry funds raised and number of product offerings.***

Figure 6 provides a breakdown of the changes in the funds raised between 2006/07 and 2007/08 for the major sub-sectors.

The woodchip segment was again the largest accounting for $398 million in 2007/08 (Figure 6). This was however, a 9% decrease on the previous financial year.

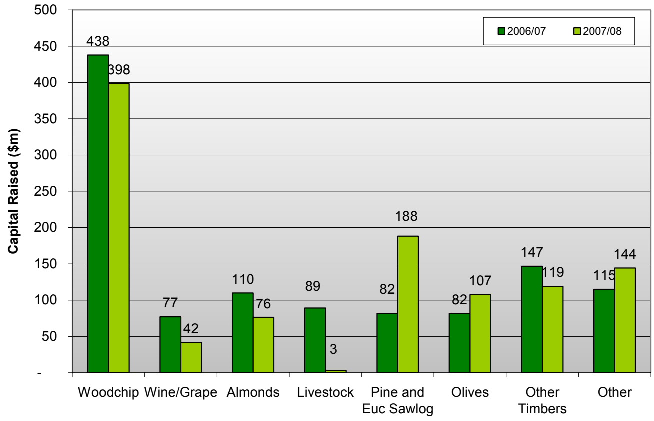


***Figure 6 – Year on year funds raised by the major agri-sectors showing percentage change.***

As Figure 6 suggests, the pine/eucalypt sawlog segment had by the far the largest increase in sales in 2007/08, increasing by 130% to $188 million. In doing so, the pine/eucalypt segment became the second largest by funds raised.

The other timber category, which includes African mahogany, sandalwood, teak and paulownia timbers, remained a major sector from a funds raised perspective, but did fall 19% from the previous year (Figure 6).

Olive offerings received a noticeable improvement in fund flows – up 32% on the previous year to $107 million (Figure 6). In contrast, both almonds and wine grape sales fell significantly from the previous year.

The most significant fall in sales during 2007/08 was in the livestock sector (96% decrease). This was primarily due to the reduction of projects open for investment in this sector.

As Figure 7 illustrates, the average investment by project was similar to the previous year. The average project investment was $56,800 compared to $55,500 per investor in 2006/07. The median project average decreased slightly from $45,500 in 2006/07 to $43,600 in 2007/08.

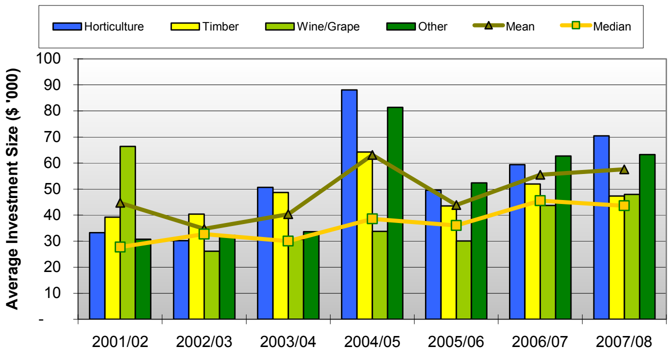


***Figure 7 – Average project investment size by industry and year with the mean and median shown across all types and for each year.***

The fact that the average is greater than the median indicates that several products with large average investments brought the overall average up.

Horticulture investment has the highest average per investor at just over $70,000 (17% increase on previous year), while the timber segment received the lowest average at around $45,000 per investor (13% decrease on previous financial year).

## 6. Companies

AAG is aware of 31 companies who released products in 2007/08. This compares with 37 companies who released projects in the previous financial year (16% decrease).

A total of 29 companies released investment products in both 2006/07 and 2007/08. As the chart below suggests, 13 companies (45%) achieved better results in 2007/08 in terms of funds raised than in the previous financial year.

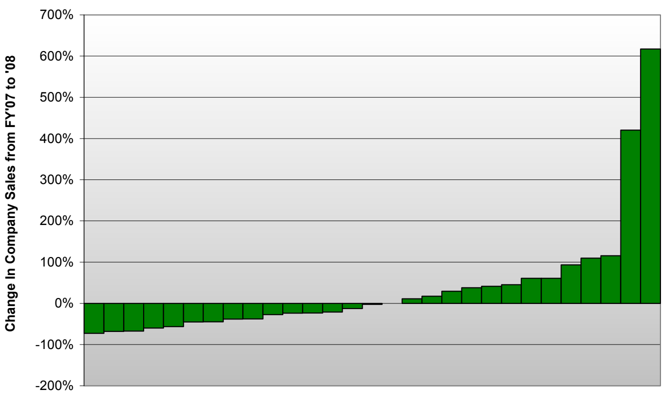


***Figure 8 – Change in sales from 2006/07 to 2007/08 for companies that had investments available in both years.***

While the average of funds raised by companies in 2007/08 compared to 2006/07 was a 37% increase, we do note that the companies which had the most improvements were ones which had a relatively small base to begin with and as such can be seen as anomalies. Taking away the two companies with the largest improvements in sales brings the average back to only a 1% increase on the previous year's raising.

While some companies will measure their performance by how well they did against last year (as per Figure 8), others will measure how successful the year was by a comparison between the actual funds raised against their initial targets.

Only 25% of projects achieved funds raised equal to or in excess of their stated target figure (Figure 9). This compares with 33% in the previous financial year. Of concern was the fact that 40% of the projects offered during 2007/08 achieved sales less than 50% of what was originally targeted.

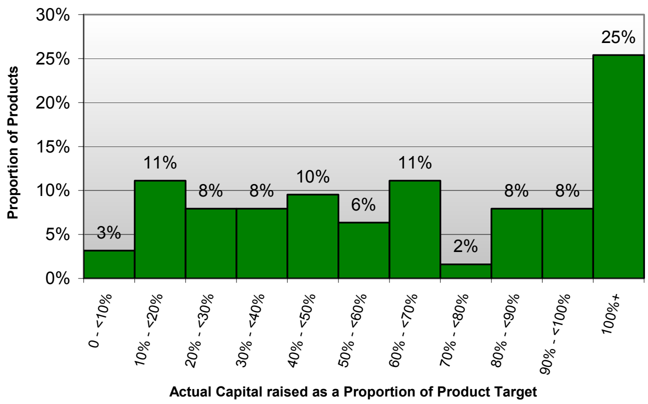


***Figure 9 – Proportion of products by actual funds raised against targets.***

In 2007/08, only 43% of projects achieved better than 70% of stated targets compared to the previous year when 50% of projects achieved better than 70% of stated targets, showing that it was a significantly tougher year for fund raising in 2007/08 than in the previous financial year.

  

Of the 31 product managers that had projects open for investment in 2007/08, 9 or 29% were ASX-listed or subsidiaries of ASX-listed companies. These included:

- Arafura Pearls (APB);
- Forest Enterprises Australia Ltd (FEA);
- Great Southern Plantations Ltd (GTP);
- Gunns Ltd (GNS);
- Integrated Tree Cropping Ltd (ITC), (part of Futuris Corporation Ltd (FCL));
- Macquarie Bank Ltd (MBL);
- TFS Corporation Ltd (TFC);
- Timbercorp Ltd (TIM); and
- Willmott Forests Ltd (WFL).

Listed companies again dominated the sector in 2007/08 in terms of funds raised. Table 2 outlines the collective results for the ASX listed sector compared to the un-listed companies.

***Table 2 ASX Listed versus Unlisted Companies***

| | Companies | Projects | Funds Raised |
|---|---|---|---|
| ASX-Listed Companies | 9 (29%) | 28 (55%) | $916 m (85%) |
| Non-Listed Companies | 22 (71%) | 23 (45%) | $163 m (15%) |

Whilst listed companies represented only 29% of the companies operating and accounted for 55% of the projects on offer, they raised approximately $916 or 85% of the funds raised during 2007/8 (Table 2).

## 7. Location of Projects

Figure 10 suggests there was a relatively even spread of funds raised across each of the states in 2007/08. As per previous years, the state where the most funds will be sent is Victoria (22%), with Western Australia (19%), Tasmania (18%) and New South Wales (18%) also receiving large volumes of funds.

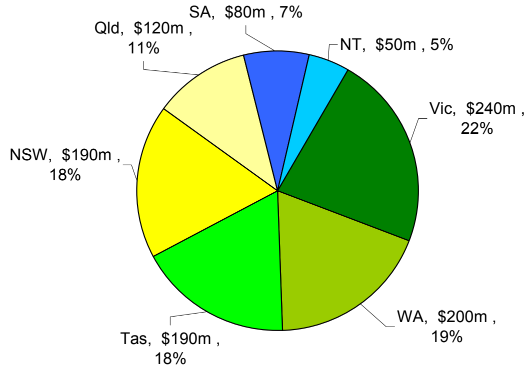


***Figure 10 – Percentage of agribusiness projects directed into each Australian state and territory in 2007/08, by funds raised (note: figures have been rounded).***

South Australia and the Northern Territory will receive the least amount of funds, but at $80 million and $50 million respectively, both are sizeable amounts (Figure 10).

Whilst non-timber companies will most likely know exactly the area and location of their areas to be developed, timber product managers have up to 12-months to find and plant the land for their projects. For that reason, we provide an estimate of the areas that will be established following the 2007/08 capital raising (Figure 11).

As Figure 11 suggests, Western Australia is clearly the leader from an area perspective, accounting for 69% of the total area to be developed from the capital raising, up from 57% last year. We do note that the area in Western Australia is significantly influenced by one project in particular where large areas of cropping land will be developed.

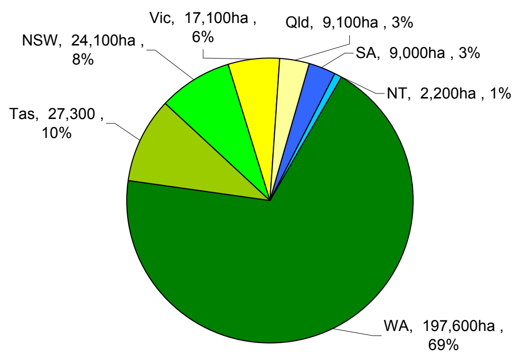


***Figure 11 – Percentage of agribusiness projects directed into each Australian state and territory in 2006/07, by area.***

The Northern Territory will have the least amount of development at 1% of the total or around 2,200 hectares (Figure 11).

  

## 8. Revenue, Tax and Finance

Our analysis suggests that approximately 93% of the total funds raised in 2007/08 was deductible in the same year. Assuming a marginal tax rate of 46.5%, $482 million or 45% of the funds raised will return to investors as a taxation refund. AAG has outlined this scenario in Figure 12.

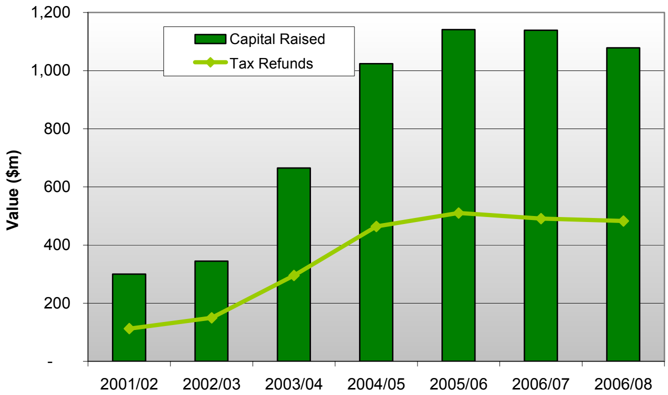


*Figure 12 – Approximate tax refund to investors compared to the amount outlaid on projects.*

We do point out that in reality, not all investors will be on the highest marginal tax rate (46.5%) and therefore this number will most likely be less than the $482 million indicated.

AAG has estimated that in **current dollar terms** (excluding any price or cost inflation), the 57 projects which were released in 2007/08 will produce $6.5 billion future farm gate revenue over their term (Figure 13). This is a 6.1 times multiple of funds raised.

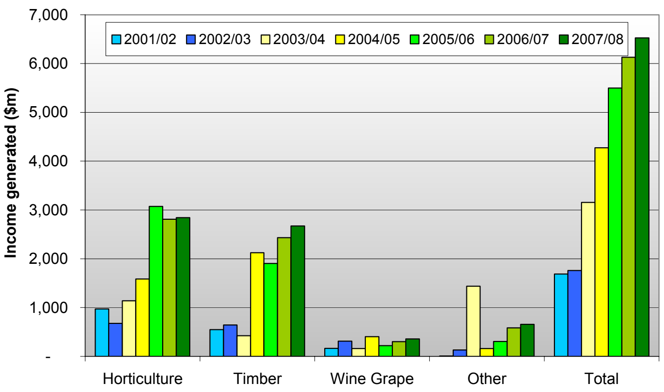


*Figure 13 – Estimated gross revenue for investors from sale of the crop by industry (note figures are gross income after harvesting costs but before any annual fees).*

Given that horticulture crops produce a higher crop value, this sector will account for the most income over time despite receiving less fund inflows than the timber sector.

As Figure 14 suggests, Victoria will receive the bulk of this years projects future farm gate income at $1.8 billion or 26% of the total generated. This is primarily due to the fact that several large scale horticultural projects will be established in this state.

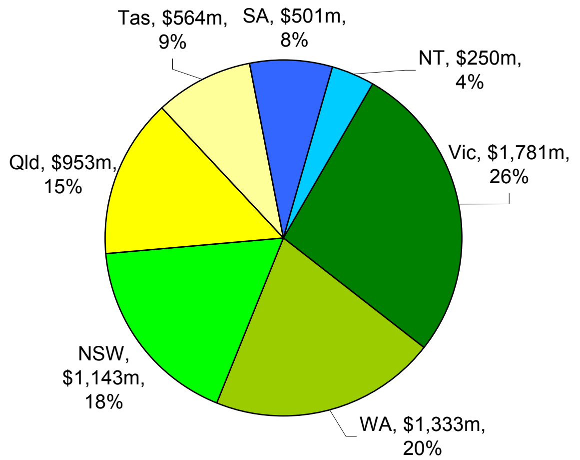


*Figure 14 – Estimated gross revenue from sale of the crop over the term of the 2007/08 investments by state (note figures are gross income after harvesting costs but before any management fees).*

If we allow for annual management, lease and crop marketing fees, our calculations suggests that project investors would receive net income of approximately $3.9 billion. Investors will pay tax on this net income. Assuming a tax rate of 46.5%, the total tax likely to be paid to the Government on the net project income is approximately $1.8 billion, which is 3.8 times the estimated tax deductions accessed in 2007/08.

In addition to the tax that will be paid by investors on their crop income, product managers will pay tax at 30% on the management, lease and crop marketing fees. Further, there will be tax paid on salaries and wages which will grow significantly as these projects develop.

Payroll tax and very significant amounts of GST will also be paid to the government and when combined with the tax on crop income after fees this industry contributes tax at substantially greater than 3.8 times the tax deducted upfront.

If we include 2007/08 offerings, AAG estimates that the projects funded since AAG started this survey in 2001/02 will produce a total of $29.0 billion in farm gate revenue. This is a very significant amount and will create very significant amounts of future tax revenues for the government.

  

The companies involved in the MIS industry currently employ more than 2,300 persons directly in head office and rural areas and a further 3,100 persons on a contract basis. Results from our survey suggests that approximately 220 new jobs were created from this years capital raising.

Future economic benefits from revenue generated, tax revenues, regional employment and the associated flow on benefits will all be reduced or eliminated from that proportion related to non-timber projects if the ATO test case is successful.

The weighted average of total investment dollars which were financed by debt (geared) in 2007/08 amounted to 73%, down from 77% in the previous year (Table 3). This was to be expected given the higher costs of finance this financial year. The percentage of individual investors who geared their investments in 2006/07 was similar to last financial year at 72%.

| *Table 3 Financing of investments* | |
|---|---|
| Proportion of investors that financed their investment – (weighted average) | 72% |
| Proportion of total cash investment that was financed (weighted average) | 73% |

There were approximately 24,300 individual investors who participated in MIS projects in 2007/08, 5% below the figure in the previous financial year.

## 9. Areas to be Established

As a result of the 2007/08 capital raising, a significant area of land will be established to timber plantations (78,289 hectares) (Figure 15). This figure is a decline of 4% in the planting rate from the previous financial year.

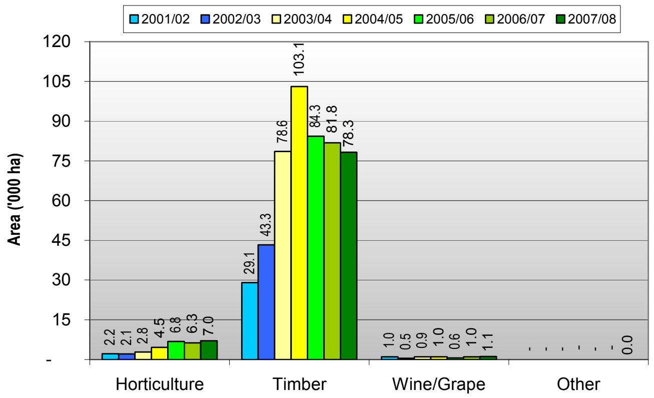


***Figure 15 – Areas that will be established resulting from 2007/08 funds raised.***

Due to their intensive nature, the area of land established to horticulture (7,025 hectares) and vineyards (1,122 hectares) is significantly less than that of timber crops (Figure 15). Of the horticulture crops to be established, olives (3,118 hectares) and almonds (2,580 hectares) account for the largest areas of land.

As not all projects require a land area (e.g. abalone and pearls), AAG has not outlined figures for the Other category (Figure 15). We do point out that the Other category includes significant area of broad acre land which will be planted to winter crops (approximately 200,000 hectares).

Of the Timber plantations to be established, a significant area will be established for woodchip purposes (54,500 hectares or 70% of the total area of plantations to be planted). This represents a decline of 12% from the previous financial year (Figure 16).

The 2007/08 capital raising will result in a significant increase in the area of land established to pine and eucalypt sawlog plantations, up 44% to 17,700 hectares.

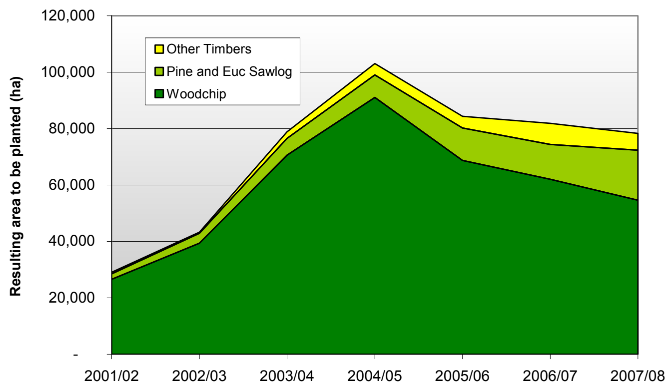


***Figure 16 – Areas of timber that will be established resulting from annual investment fund raising by product type.***

Areas to be developed for timbers such as African mahogany, teak and sandalwood fell 20% to 5,900 hectares despite some strong individual company results (Figure 16).

## 10. AAG Profile and Contact Details

The Australian Agribusiness Group was formed in 1997 and provides expertise in research, investment management and agribusiness consulting nationally.

AAG is the leading provider of research into the Managed Investments Sector (MIS) in Australia. It's research is read by over 9,100 financial planners and is distributed by Standard and Poors.

AAG sources and manages investments in the Australian agribusiness sector on behalf of national and international clients.

AAG undertakes research reports, feasibility studies, consulting projects and assists in facilitating funding for private and public clients. It provides the management skills, expertise, staff and office support to develop, incubate and launch new agribusinesses.

AAG focuses on agribusiness and particularly the commercial aspects of this dynamic sector.

For more information about AAG, please visit our website at www.ausagrigroup.com.au.