

Equity Strategy

Market Ownership Largely Unchanged

Equity Strategy | New Zealand

Event:

- We have updated the GS&PNZ survey of the New Zealand equity market structure for the June Quarter 2011.
- There are 51 stocks in this year's market structure survey with one addition (DNZ) and one removal (PRC) from the previous year.

Highlights:

- Foreign ownership of the NZ equity market was flat at 35.9% from 36.1%. There were minimal changes to foreign ownership levels, of the 51 companies surveyed; the only notable changes is the increased stake of Agria in PGW and the sell down of TUA from White River Partners.
- NZ Managed funds' share of the equity market increased 1.9%pts from 20.5% to 22.3%. The highest level since the initiation of this survey.
- Total strategic stakes reduced from 35.2% to 33.0%.
- One of the trends our Offshore Ownership Survey has captured over the years is a steady leakage of equity supply into the unlisted sector, primarily via takeover activity. We consider improving the flow of equity supply as critical to restoring the NZ market's role in the economy.

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Key Data:

	Jun-11 Qtr	Change (Jun-10 Qtr)
NZ Managed Funds	22.3%	1.9%pts
NZ Retail Investors	22.3%	0.2%pts
Total Foreign Ownership	35.9%	-0.2%pts
NZ Strategic Stakes	19.5%	-1.9%pts
Offshore Strategic Stakes	12.8%	-0.4%pts

Source: GS&PNZ Research estimates, RBNZ, IRESS, Merlin IR

Market Structure

Figure 1: Offshore Ownership unchanged
Ownership Structure of NZ Equity Market

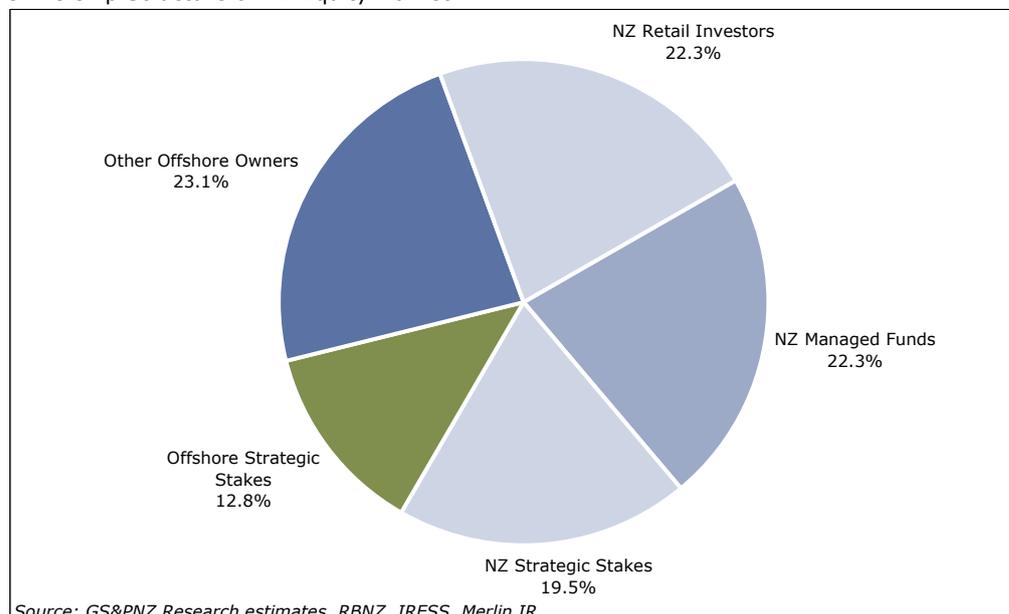


Table 1: Ownership Structure of Sample NZX Primary Listings

	Dec-97	Dec-98	Dec-99	Dec-00	Dec-01	Mar-03	Mar-04	Mar-05	Mar-06	Mar-07	Jun-09	Jun-10	Jun-11
NZ Managed Funds	14.0%	15.2%	14.6%	16.1%	15.1%	14.2%	16.1%	15.6%	16.7%	15.8%	19.1%	20.5%	22.3%
NZ Strategic Stakes	9.9%	9.8%	10.0%	13.3%	16.6%	18.1%	15.1%	17.1%	16.0%	16.6%	21.1%	21.3%	19.5%
Offshore Strategic Stakes	29.4%	27.0%	23.2%	21.8%	24.9%	18.9%	16.5%	15.9%	12.0%	13.2%	15.2%	13.1%	12.8%
Other Offshore Owners	30.9%	28.1%	31.3%	25.4%	22.1%	26.5%	29.5%	28.4%	29.4%	25.9%	22.9%	23.0%	23.1%
NZ Retail Investors	15.8%	19.9%	21.0%	23.5%	21.3%	22.3%	22.7%	23.0%	26.0%	28.4%	21.7%	22.1%	22.3%
Total Foreign Ownership	60.3%	55.1%	54.5%	47.2%	47.1%	45.4%	46.0%	44.3%	41.4%	39.1%	38.1%	36.1%	35.9%

Source: GS&PNZ Research estimates, RBNZ, IRESS, Merlin IR

Offshore Ownership: Downward trend likely to continue

Foreign ownership of the listed NZ equity market was more or less flat at 35.9% from 36.1%. The lack of new listings and M&A activity (a major driver of structural changes in foreign ownership) over the past year meant there were minimal changes to the sample of the companies surveyed, with one addition (DNZ) and one removal (PRC) from the previous year.

The overall level of offshore ownership is relatively unchanged, of the 50 recurring companies that we surveyed, there were 24 decreases, 22 increases and 4 recorded as no change. Because the measure of foreign ownership is market weighted, the larger companies typically dominate our headline estimate. Our analysis of the NZX10, which account for over 75% of total foreign ownership in the New Zealand market, suggests that the aggregate offshore ownership of the largest 10 primary-listed companies is flat compared to last year.

Outside of the NZX10, notable changes were the increased stake of Agria in PGW and the sell down of TUA from White River Partners.

While the level of foreign ownership has been steadily trending down since the inception of the survey, on an international basis the level of foreign ownership in NZ remains high. We see a good chance that the level of foreign ownership will fall further going forward, given the potential for partial flotation of various State Owned Enterprises which are likely to be domestically biased.

Figure 2: Historical Level of Foreign Ownership

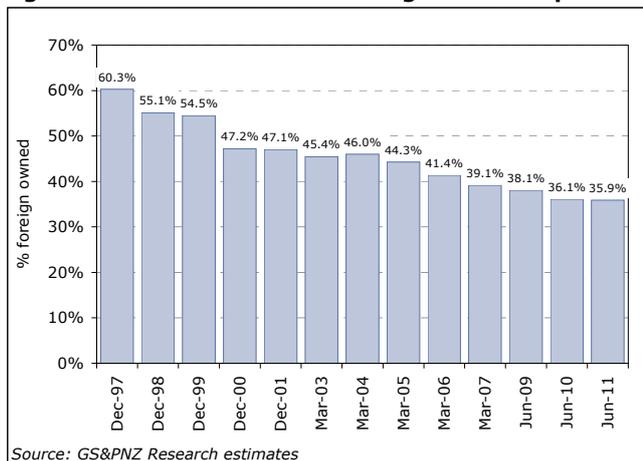
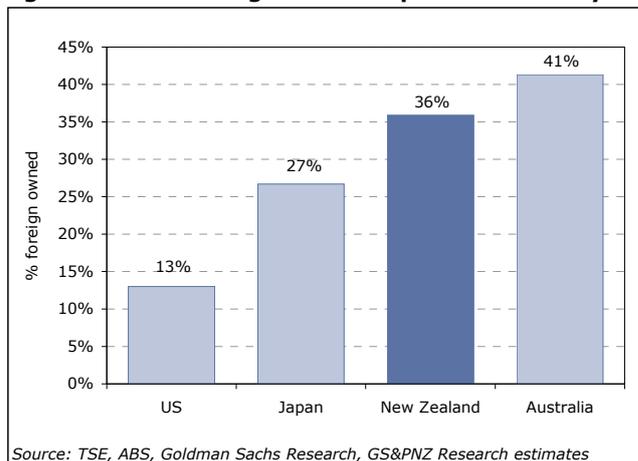


Figure 3: CY11 Foreign Ownership Internationally



Strategic Stakes: A slight drop

Strategic stakes fell from 35.2% to 33.0% (strategic stakes are defined as ownership blocks of 10% or more). Notable changes in strategic shareholders include the increased stake in PGW after the Chinese cornerstone investor Agria took a controlling stake after its partial takeover offer, the selling down of the Turner's Auction stake by White River Partners, and the reduction of Tainui's stake in Ryman.

Managed Funds & Retail: Showing further benefits of KiwiSaver

Managed funds' share of the equity market increased from 20.5% last year to 22.3% in the current year; the highest level since the beginning of this survey. We continued to witness strong managed funds inflow from KiwiSaver, total funds under management of \$9.4bn as at

30 June 2011, up 63% from \$5.8bn in the pcp. The amount invested in NZ equities is also up an impressive 59% to \$900m from 569m. Interestingly, the percentage invested in New Zealand equities has actually reduced somewhat from a peak of 10.5% in the Dec 09 quarter; it will be interesting to see whether the potential partial flotation of the State Owned Enterprises would increase the percentage of KiwiSaver inflows into New Zealand equities.

Retail participation increased modestly from 22.1% to 22.3%, consistent with levels seen from 2000 - 2005, we suspect that as KiwiSaver continues to build momentum, there will be further substitution of direct holdings to managed funds.

Portfolio Investors

Our measure of portfolio-style investor ownership (managed funds + NZ retail investors, a measure of non-strategic holder who are likely to trade more actively) of the market has increased from 68.6% to 69.8%. This was driven by both an increase in managed funds ownership and a small expansion in retail investment. We have continued to see a highly positive-correlated relationship between portfolio-style investor ownership of the NZ equity market and market liquidity, since the significant decline since the GFC, median daily turnover has now risen by 24.1% to July 2011, consistent with the pick up in portfolio-style investor ownership.

Table 2: Portfolio-Style Investor Breakdown of NZSX Primary Listed Stocks

	Dec-97	Dec-98	Dec-99	Dec-00	Dec-01	Mar-03	Mar-04	Mar-05	Mar-06	Mar-07	Jun-09	Jun-10	Jun-11
Strategic Stakes: Offshore Managed Funds	2.9%	2.2%	0.6%	1.1%	4.1%	4.7%	2.2%	3.0%	2.2%	3.1%	2.9%	3.0%	2.0%
Other Offshore Owners ¹	30.9%	28.1%	31.3%	25.4%	22.1%	26.5%	29.5%	28.4%	29.4%	25.9%	22.9%	23.0%	23.1%
Strategic Stakes: NZ Managed Funds	1.1%	1.5%	1.2%	1.5%	1.1%	0.9%	0.3%	1.4%	2.1%	2.6%	1.3%	0.7%	0.8%
Other NZ Managed Funds	13.0%	13.7%	13.4%	14.6%	14.0%	13.3%	15.8%	14.3%	14.6%	13.3%	17.7%	19.7%	21.5%
Total Managed Funds	47.8%	45.5%	46.4%	42.6%	41.3%	45.4%	47.8%	47.0%	48.2%	44.8%	44.9%	46.5%	47.5%
Managed Funds + NZ Retail	63.6%	65.4%	67.4%	66.0%	62.6%	67.7%	70.5%	70.0%	74.2%	73.2%	66.6%	68.6%	69.8%

¹ Mainly managed funds, but a small portion are retail investors.
Source: GS&PNZ Research estimates, RBNZ, IRESS, Merlin IR

Figure 4: KiwiSaver Inflows Boosts Managed Funds

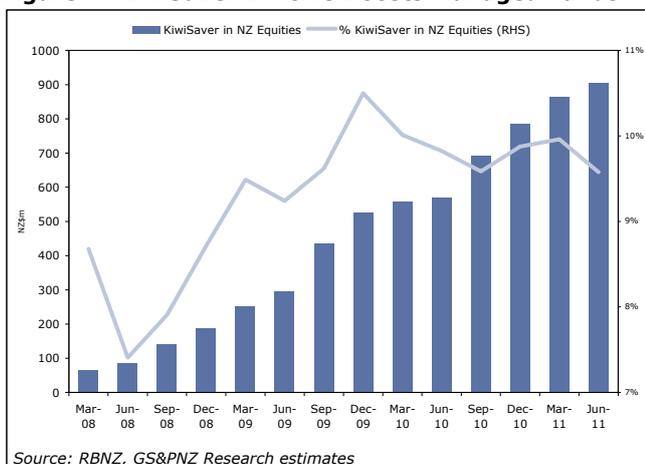
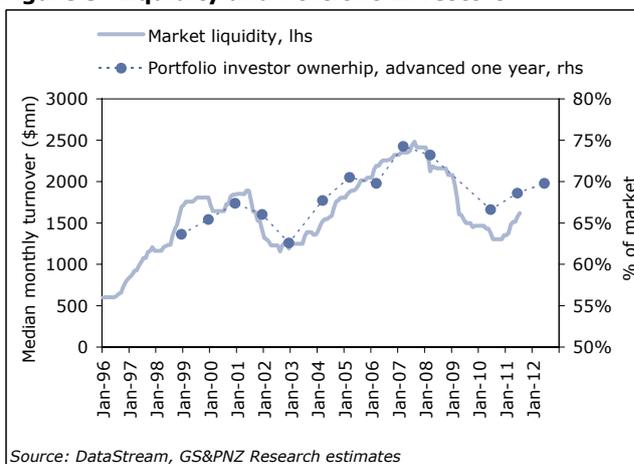


Figure 5: Liquidity and Portfolio Investors



NZ's Capital Markets At A critical Juncture

Our survey of equity market structure comes at an important juncture for the future of capital markets in this country. In particular, the trends in ownership structure mask two other developments that we believe threaten the critical mass of capital markets in this country:

1. The NZ equity market's low and declining **share in the economy**. We see this as indicative of a reduced role in the provision of risk capital. 15 years ago the NZ equity market's share of GDP was within range of our advanced economy peers, and close to Australia (56% versus 68%). NZ's share has since dropped to ~30%, while our advanced economy peer group has grown (below left).

2. A declining role in the economy has meant **market liquidity** has suffered. Daily trading volumes provide the best illustration of the tenuous state of institutional investing in NZ. Average daily turnover has oscillated around a flat trend for 15 years, and at current levels (~\$80m/day) is the same as in 1998. By contrast, daily trading in Australia has risen from an average of \$1bn/day in 1997 to \$5bn/day currently (below right).

Figure 6: NZ Equities play a small role in the economy

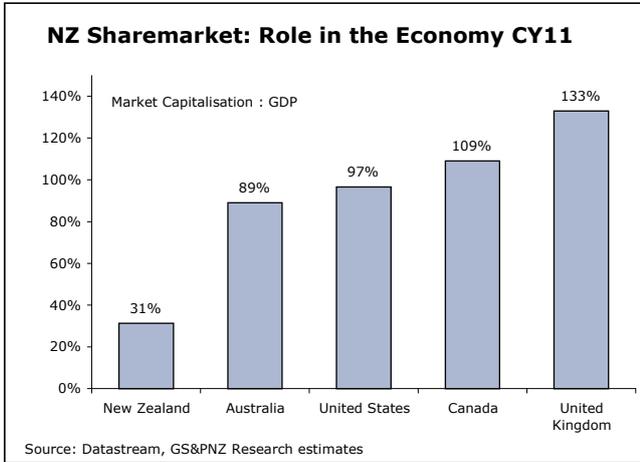


Figure 7: Liquidity has not grown sustainably



Equity Supply Needs to Respond

Encouragingly, the latest readings on equity market turnover are showing improvement (latest quarter ~\$90m/day). To some extent this reflects the recovery in portfolio investment discussed earlier (figure 4). We also believe improving demand conditions for NZ equities have helped, aided by: 1. the tailwind institutional ownership has been given by Kiwisaver and the NZ Superfund; and 2. solid relative returns versus Australia over the past year.

Figure 8: Weak IPO activity over past decade

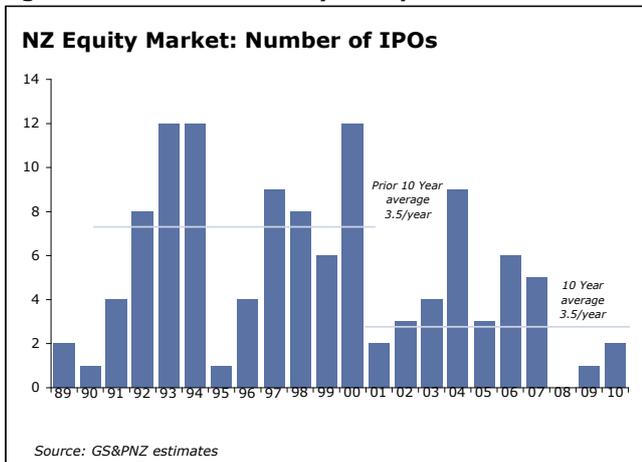
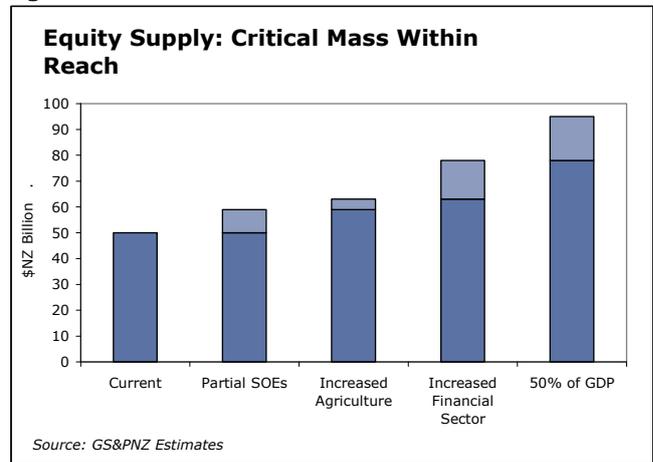


Figure 9: Critical mass within reach



However, while demand has improved, supply now needs to respond. One of the trends our Offshore Ownership Survey has captured is a steady leakage of equity supply into the unlisted sector, primarily via takeover activity. Over the past decade, this has been accompanied by a sharp fall-off in IPO activity (figure 8). With IPO's failing to replenish equities lost to the unlisted sector, net equity supply has been a significant drag on the equity market.

We see declining equity supply is a significant threat to the NZ equity market's critical mass. However we also believe that a self-sustaining level of equity supply, which we estimate is ~50% of GDP, is within reach. A number of potential equity market transactions would make headway in this respect:

- The potential partial floatation of various State Owned Enterprises.
- Increased share market participation from the agricultural sector, spearheaded by Fonterra.

- The potential float or partial float of one of the large Australian-owned banks.
- Further floats from the NZ unlisted sector, which is of significant size. The recently announced TradeMe float is an important positive step here.

The combined impact of these potential floats would provide a significant boost to NZ market capitalisation (figure 7). This is necessary to reverse the negative feedback loop of declining supply that has been in play over the past decade. Importantly, partial floatations are an ideal solution for the particular problem NZ faces –whereby a cornerstone holder retains a block stake preventing full takeover in the future.

Appendix 1: Survey Methodology

Construction of average	The survey is done as a weighted average, i.e. treating the New Zealand market as a pool of generic equity supply apportioned amongst a group of investors. This means that even if no significant trading was done, changes in overall ownership levels could still be influenced by the changing prices of individual stocks.
Survey coverage	Weights for the headline offshore ownership estimate are based on the NZSX All Ordinaries index. This index covers all companies that have NZ as their home exchange, ie it excludes Telstra, AMP and other offshore based stocks. This year, 51 companies were included in the survey, comprising 93% of the NZ All Ordinaries Index.
Layers of ownership	We calculate "1 st round" levels of ownership only. For example, IFT has partial offshore ownership as a stand alone company. IFT in turn owns 50.5% of TPW (at the time of the survey). However, we treat this 50.5% as a domestic stake, rather than calculating through the "beneficial" offshore ownership in TPW.
Data timeliness	The data used to compile the overall averages comes from various sources with variable lags. In this respect it is appropriate to view the data as a June Quarter "weighted average", rather than as a precise point estimate.
Revisions	Revisions are made to historical estimates from time to time. Unless these are judged to have a material impact on the survey, we will not explicitly highlight historical revisions. These can be made available on request.

Source: GS&PA Research

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