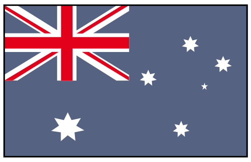
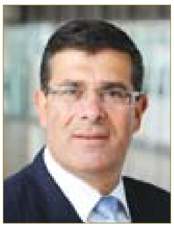


Australia

Significant stimulus packages have underpinned the resilience of the economy which has filtered through to M&A volumes in Q2. The remainder of 2009 is expected to continue on this track with financial services, resources and government infrastructure sales driving deal volumes.



Tom Fenton
Corporate Finance Leader
Australia

Current Environment

The Australian economy has shown resilience during the first half of 2009, which is partially attributable to the responsive fiscal and monetary measures implemented by the Australian government during this period. The combination of consumer expenditure, export growth and increased public spending has helped to expand GDP by 0.4% in the first quarter to an annual rate of 0.4%. Rising unemployment rates, lower household incomes and global uncertainty in the financial markets are expected to cause the economy to contract in the remainder of 2009.

The Australian government has implemented spending initiatives specifically aimed at boosting economic activity. The first (AUD$8.7 billion) and second (AUD$12.7 billion) stimulus packages have shown their effect in the second quarter results through an increase in consumer spending. The 2009-2010 Commonwealth budget has commitments for several capital spending projects, such as the National Building Infrastructure project (AUD$22 billion) and partnering with the private sector to build the National Broadband Network (AUD$43 billion). However, these policies are forecast to put Australia into a budget deficit.

The Consumer Price Index rose by 0.1% in the first quarter to an annual rate of 2.5% compared to a fall of 0.3% in the final quarter of 2008. The first quarter current account deficit fell to AUD$4.6 billion from AUD$6.4 billion. Non-rural goods drove the majority of the decline, falling 15.3% in value for the quarter; this was offset by rural volumes which performed strongly due to this sector's recovery from periods of drought.

The Australian dollar appreciated significantly against the US dollar through May and early June to the mid 70c range, with a surge to 82c later in June. Interest rate spreads, stronger equity markets, a growing appetite for commodity exposure, relative growth and external financing were factors specific to Australia that drove this appreciation.

In calendar year 2008, the Reserve Bank of Australia ("RBA") cut the overnight cash rate by a total of 300 basis points. In the first quarter of calendar year 2009, the RBA has cut interest rates twice by a total of 125 basis points to 3.00%.

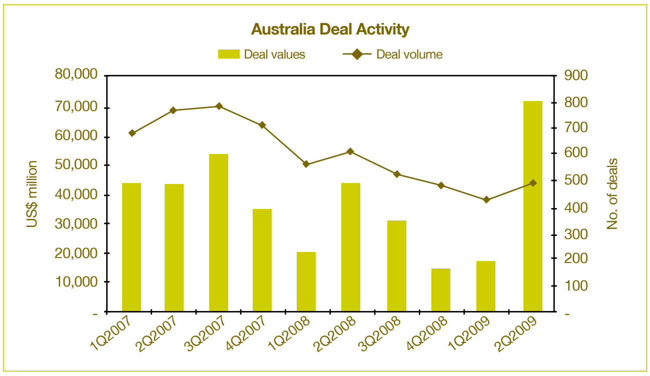
Business investments appear to have been delayed or reduced during the first quarter. Additionally, difficult economic times, a rise in uncertainty, risk aversion and poor trading results impacted the capacity for businesses to continue their historic levels of discretionary spending.

The unemployment rate has increased to 5.8% at the end of June while incomes contracted by 1.1% in the first quarter of 2009. Forward-looking indicators such as job advertisements remain at levels which indicate further deterioration over the second half of the year which points towards a rise in unemployment to an estimated 8% by the end of 2009.

A rebound in the global stock markets began in early March, with the ASX S&P200 rebounding 26% from its low on 6 March 2009 of 3,145 points to close the first half of 2009 at 3,954 points.

During the first half of 2009, there has been a significant amount of equity raised in the Australian stock market, with AUD$17 billion alone raised in the first quarter of 2009. With companies seeking to bolster their balance sheets and pay down debt, these new issues have typically been placed at a heavy discount to the prevailing share price.

Deal Activity



Source: Thomson Reuters, based on total domestic, inbound and outbound deals announced as of 30 June 2009.

Deal volumes have increased slightly from the previous quarter, with 422 and 492 transactions completed in the first and second quarters respectively.

The key private equity transactions during the first half of 2009 were:

- The Cayman Islands-based private equity firm Harmony Capital purchased Western Australia's largest abattoir, Harvey Beef for an undisclosed sum.
- Waste management group Transpacific announced an AUD$800-million cornerstone investment from Warburg Pincus through an equity placement.
- Consortia including Carlyle Group and TPG were bidders for Asciano during its sale process, until Asciano decided to go to market and raise equity capital of AUD$2.35 billion.
- Australian Discount Retail Group owned by Catalyst and CHAMP was placed into receivership in January and subsequently sold to Retail Adventures, a privately owned Australian company.
- Archer Capital is reported to be seeking to acquire a clean energy company, Energy Developments, which owns and operates power generation facilities in Australia, US, UK and Europe.
- Vodafone group merged its Australian telecommunications businesses with Hutchison Telecommunications with a deal value of AUD$3.62 billion. The merged entity will operate as a 50:50 joint venture.
- Canada Pension Plan Investment Board acquired the entire ordinary share capital of Macquarie Communications Infrastructure Group for AUD$1.6 billion.
- Kirin Holdings Co Ltd of Japan acquired the remaining 53.87% interest in Lion Nathan Ltd for AUD$3.31 billion.
- Viterra Inc of Canada acquired the entire share capital of ABB Grain Ltd, an Adelaide-based wholesaler of agricultural products, for AUD$1.64 billion.

Other key transactions include:

- Nippon Paper purchased a significant portion of Australia's third largest paper company, Paperlinx for AUD$375 million.
- OZMinerals completed an assets deal with China Minmetals with total proceeds of US$1.35 billion.
- BG Group acquired the entire ordinary share capital of Pure Energy Resources Ltd, a coal seam methane mining company from Arrow Energy. The transaction value was AUD$1.03 billion.
- Chinese state-owned China Metallurgical Construction Corp. acquired a 10% stake in Waratah Coal Inc., a Brisbane-based coal mining company for an estimated AUD$664 million.
- Red Back Mining Inc. of Canada acquired the entire share capital of Moto Goldmines Ltd in a stock swap transaction valued at AUD$562 million.
- Chinese state-owned Hunan Hualing Iron & Steel Group Co Ltd acquired a 16.38% stake in Fortescue Metals Group Ltd, an iron ore mining company for AUD$1.1 billion.
- China's Guangdong Foreign Trade Group purchased a stake of up to 19.9% in Australian copper and zinc miner Kagara for AUD$63 million.

Outlook

Financial Services

The Australian banking sector is considered one of the strongest in the world as its four main banks still carry an AA-credit rating. These banks are expected to capitalise on this relative strength with potential offshore acquisitions and domestic tie-ups taking place during 2009.

The potential offshore activity for Australian banks include Commonwealth Bank considering a bid for the fund management arm of Lloyds Banking Group in the UK for a transaction value of GBP£200 to GBP£300 million and ANZ's interest in RBS's Asian assets.

On the domestic front, there is an opportunity for the main banks to take strategic stakes in smaller banks and regional operators, with BOQ and Suncorp touted as potential targets. In funds management and life insurance, NAB recently agreed (in June 2009) to acquire the Australian operations of UK insurance giant Aviva for AUD$825 million.

Resources

The stabilisation of the Chinese economy and the scale of urbanisation and industrialisation are fundamental factors underpinning the demand for Australian resources. The apparent success of the Chinese government's stimulus package (US$590 billion), the World Bank's forecast for Chinese GDP growth of 7.2% in 2009 and a recovery in commodity prices are all encouraging signs.

Rio Tinto rejected a proposed US$19.5-billion investment from Chinalco in favour of contributing US$ 58 billion in assets to a Western Australian iron ore 50:50 joint venture with BHP Billiton and undertook a US$ 15 billion rights issue to strengthen its balance sheet. The strength of this combined business has raised tensions with the Chinese steel industry, culminating with Chinese government sources flagging potential conflicts with Chinese anti-monopoly laws as both Rio and BHP have significant operations within China and potentially are under the scope of such regulatory reviews.

Property

Asset valuations during the year for REITs have fallen up to 20% and continue to threaten loan-to-value ratio covenants. This has placed lenders in a position to demand asset sales, as reflected in ING Office Fund and Charter Hall Groups' disposal programme and the continued 'for sale' status of GPT's non-core assets (primarily hotels), and may drive further movements in this sector.

A desire to strengthen balance sheets has led to a continuation of discounted placements and rights issues from the likes of GPT, Mirvac, Stockland and Dexus.

The Goodman Group has suffered two downgrades to its issuer rating and has highlighted the continued weakness and strain on their liquidity. It is anticipated that the group will conduct an equity raising to meet its rising interest obligations.

Infrastructure

Potential activity in this sector includes the privatisation of NSW Electricity, and in the longer term, infrastructure asset sales announced by the Queensland government. Furthermore, there is activity generated by a number of listed infrastructure funds that are facing a closing gap between net asset value and share price. A number of sale processes are in place, including Babcock and Brown Power, EPIC and Dalrymple Bay Coal Terminal.

The government's proposed carbon emissions scheme has been postponed as its implications may further weaken the economy. However, interest in renewable energy projects is accelerating in the lead up to the implementation of the Renewable Energy Targets and Carbon Pollution Reduction Scheme.

Private Equity

Investment opportunities for private equity funds have changed in response to the deteriorating economic conditions. Unreasonable price expectations from vendors and a lack of funding availability are hampering deal activity. We expect a continued low level of LBO activity in the near future, with private equity funds focusing on enhancing value in existing portfolios including divestments of underperforming assets, strategic reviews and cash optimisation. Opportunities for investments in companies at "bottomed out values" as well as the investment in cornerstone equity stakes are expected to drive deal flow. ■