AxleTree Capital

QUESTIONS ABOUT THE FUND STRUCTURE

Why an evergreen fund and not a close-ended, fixed term structure?

The AxleTree NIF is investing in a theme, that is the long-term application of technologies to support a more sustainable future, and not a style of investment such as traditional venture capital or LBO/turnaround premised Private Equity, where entry and exit points are clearly defined and for which such structures were originally developed. Our entry and exit points will be determined by the risk-return trade off at any given point in time, overlaid with considerations of portfolio balance and the continuing ability to make material contributions to sustainability outcomes.

With an Evergreen structure, we can focus on the risk return trade-offs of a particular asset at any point in time and in its technology life cycle, maximising investor value.

The structure also recognises that despite the long term momentum for sustainable investment, that **it is a significant transition in approach.** This means that we will be subject to (relatively) short-term reversals in government policy (particularly in the energy sector), continued technological change, and broader market downturns. With the overall investment thesis of sustainability remaining intact, the structure allows us flexibility to ride out the troughs rather the being forced to sell long-term assets at a discount; or to distract the attention of management through the raising of new, secondary funds. Exits and new raisings can be based purely on portfolio balance, value and the pipeline of opportunities.

Why so big for a first fund from a new Manager?

Application of technology to sustainability issues is highly capital intensive – we will be investing in manufacturing/processing capacity and/or deployment of technologies on commercial demonstration projects; or even in utility scale projects where this ensures the deployment of our portfolio company technologies. Any of these types of projects may have total capital costs in excess of AUD100M, and high levels of debt may not be initially sustainable. We expect to be making investments in the AUD5-25M range, so the target size also reflects the desire to achieve meaningful diversification.

This is unlike, for example, software development, where scalability is dependent on variable resources (developers, sales and marketing, support) or trading platforms; or where the company is merely the licensor of the technology. Similarly, Impact Funds outside of those sectors where technology is critical, may benefit from relatively small investment, with access to working capital and training resources being a primary obstacle for many social enterprises; allowing smaller sized funds to be effective in delivering the desired outcomes.

Software development will be vital to support the transition to a more sustainable World as well, but not without the physical assets for it to assist in managing.

How is your Performance Benchmark set? How is Performance calculated?

The benchmark return for the Fund will be a blend of:

- S&P ASX Infrastructure Index (30%)
- S&P ASX Emerging Companies Index (30%)
- S&P Australian Private Equity and Venture Capital Total Return Index (40%)
- Plus 3.0% p.a.

AxleTree has constructed a benchmark to reflect the risk profile/maturity of its target portfolio, with an additional premium to compensate for:

- lack of initial liquidity,
- heavier level of political risk compared to the underlying portfolios in the benchmark components,
- to amortise the entry fee.

These indices are publicly available other than the S&P Australian Private Equity and Venture Capital Total Return Index which is a subscription service, and which AxleTree will make available to the Trustee. The evergreen nature of the fund makes a fixed upfront return target inappropriate.

This benchmark is in turn used to determine the Manager's rights to receive a performance bonus on the one hand; and the right for investors to terminate the Manager for underperformance, on the other.

The fund's actual performance is calculated as an Internal Rate of Return using the opening Net Asset Value of the fund as a inflow, the closing Net Asset Value as an outflow, and accounting for all cash flows in and out of the fund, whether capital or income, during the calculation period.

How is the Manager's Performance Bonus calculated? Is this paid on Unrealised Gains? Is it paid simply for the "clawback" of previous underperformance?

The Manager is entitled to receive a performance bonus equivalent to 20% of the annual return above the benchmark return. This is paid in the form of B Units rather than cash, which are not transferrable, distributions attributable to them must be reinvested in additional B units, and which convert to A Units only after 4 years from issue date.

The bonus structure recognises the evergreen, open nature of the fund, where for accurate measurement of performance, equity between new and existing investors, and price signalling when liquidity measures are adopted in the future, requires inclusion of unrealised gains in the performance measure. The performance bonus aligns the managers interests with those of investors, while ensuring that the benefit of unrealised gains does not immediately fall to the manager, but rather relies on valuations being maintained in the medium to long term.

The Performance Bonus structure includes a high watermark mechanism that ensures that the manager does not benefit from any outperformance which is simply the recouping of earlier underperformance. A bonus is only payable if target returns have been met for the period since the later of inception or the last bonus payment, to the calculation date.

How are assets valued?

The evergreen nature of the fund requires annual independent valuations of assets for accurate measurement of performance, equity between investors, and price signalling in the future.

Most assets acquired will be reaching the stage of positive cash flow and will be suitable for Discounted Cash Flow valuation. These valuations will be verified annually by independent parties.

Assets which are pre-operating cash flow will be held at cost; publicly traded assets will be marked-to-market.

Comparable market transactions may also be considered.

Investments must stand alone as financial investments regardless of impact on sustainability; but must also demonstrate positive net sustainability. Hence the base case model will take the form of a balanced scorecard, defining both expected financial outcomes but also sustainability outcomes to be achieved by those cash flows.

Are your fees competitive?

AxleTree believes that ongoing management fees and the performance bonus are competitive. Typical ongoing management fees for Venture Capital and Private Equity generally start at 2% of FUM. AxleTree's lower fee structure recognises some economies of scale, with the more mature investments being more of the nature of Infrastructure Assets. The performance bonus of 20% above benchmark is in line with Private Equity norms, and lower than what would be expected in Venture Capital. This fee also covers all of the trustee and administration costs.

The Management Expense Ratio cap of 4% covers both fees and other direct expenses of the fund; in particular, it captures approved due diligence expenses not able to be capitalised into a successful investment. The Manager is at risk for expenditure above this amount.

The 7% Subscription Fee (4% cash to Axletree and 3% reinvested in B units) may seem high. AxleTree is a start-up manager and as such has additional expenses beyond those required for subsequent funds once the Manager is established. If the fund were totally reliant on external placement agents AxleTree believe that success fees of 5-6% cash would be payable, and indeed some will be used for this purpose. This is for the benefit of all investors in ensure the fund meets its closing target and can obtain the spread and scale of investment it seeks. It also recognises 2 years plus of sweat equity and cash contribution by the management team. The 3% reinvested in B units is at risk, hence the higher total fee, but is important in aligning management interests with those of investors.

Do I have an opportunity to co-invest?

Yes. AxleTree encourages co-investment where for portfolio balance it does not wish to provide the full amount of capital available for investment. Where these opportunities become available, AxleTree's policy will be to first offer these to its cornerstone investors (those committing $25M or more to the NIF), then to the remaining NIF investors and then to other funds that AxleTree may manage in the future, and to its partners in other ventures where a good working relationship exists. AxleTree would normally expect to manage this co-investment under a single asset mandate in which case the co-investment would be counted towards NIF Funds Under Management in calculating the marginal management fee.

How do I get my money back?

The NIF will be required to distribute all taxable income on an annual basis. It will also have the option to make returns of capital at it's discretion. Investors will have the opportunity to reinvest distributions. Units are freely transferrable although where associated undrawn commitments exist these will need to be to a creditworthy party. The Manager will use its Best Endeavours to assist any investor seeking to sell its units. Existing investors will have pre-emptive rights to purchase these. After 5 years a Unit Holder may request a proposal to list the fund which would be subject to 75% Super Majority vote. The manager may also recommend alternative liquidity mechanisms such as through online trading platforms. After 10 years the Trustee may consider providing a redemption facility.