



30 April 2009

**Dear Xero Shareholder,**

## **NOTICE OF SPECIAL MEETING OF SHAREHOLDERS**

This letter and the accompanying documents contain important information about the Special Meeting and the Share Purchase Plan.

### **Introduction**

On 7 April 2009, the Board of Xero ("Board") announced a strategic capital raising of NZ\$23.2 million at NZ\$0.90 per share from some key investors (the "Fundraising"). The Fundraising will enable Xero to accelerate its growth plans in the UK, Australian and US markets.

The strategic groups of investors include:

- Craig Winkler, a founder and former major shareholder of Australian based accounting software company, MYOB, has subscribed for NZ\$18.0 million of new Xero shares (subject to Xero shareholder approval). This includes NZ\$0.45 million from parties associated with Craig Winkler;
- the Bank of New Zealand ("BNZ"), an existing Xero shareholder, has subscribed for NZ\$1.6 million of new Xero shares;
- two Independent Directors of Xero, being Sam Morgan and Graham Shaw, have subscribed (in aggregate) for NZ\$1.45 million of new Xero shares; and
- other investors, including an institutional investor, have subscribed for the remaining NZ\$2.15 million of new Xero shares.

Craig Winkler was a founder and major shareholder of MYOB (the Australian based accounting software business), which was recently acquired by private equity investors. He is no longer involved in MYOB as a director, executive, shareholder or in any other capacity.

The Fundraising price of NZ\$0.90 represents a premium of approximately 4.7% to the volume weighted average ("VWAP") share price of Xero of NZ\$0.86 per share over the 5 trading days prior to Xero's announcement, on 2 April 2009, of a potential capital raising.

The addition of this strategic capital into the business should create value for all shareholders and provide sufficient resources for the next stage of expansion. However, the Board of Xero considers it is also important to offer a share purchase plan ("SPP") to the existing New Zealand shareholders of Xero to enable them to participate in the capital raising and acquire new shares in Xero. The SPP enables existing Xero shareholders to subscribe for up to an additional NZ\$5,000 of Xero shares at NZ\$0.90 per share. The SPP is not subject to shareholder approval.

## **Background to the Fundraising**

Xero listed on the New Zealand Stock Exchange (“NZSX”) on 5 June 2007, raising NZ\$15 million at NZ\$1.00 per share (the “IPO”). The volume weighted average share price of Xero since listing on the NZSX is approximately NZ\$0.88 per share (*Source: Bloomberg*).

Since listing on the NZSX, Xero has managed its costs in accordance with its plan and has proven its business model. Xero’s announcement on 7 April 2009 of the Fundraising also follows the recent announcements of the achievement of a significant growth in customer numbers and a major strategic partnership with Telstra in Australia. On 31 March 2009, Xero announced that it had passed the 6000 customer number milestone, double the customer figure at December 2008. On 1 April 2009, Xero announced that it had entered into a strategic partnership with Telstra in Australia.

Xero is poised for further growth. The raising of new capital will enable it to push further ahead in the UK and Australian markets and enter the US market. As part of these plans, Xero announced in March 2009 that it had appointed Andy Lark as its US advisor. He will establish Xero’s US Advisory Board. Andy Lark is a New Zealander and a Senior VP of Global Marketing for Dell Computer.

The Board and its advisors considered various fundraising alternatives for Xero to raise growth capital, against a backdrop of volatile and uncertain global capital markets.

The fundraising options included raising capital from strategic investors and the possibility of a rights issue to all existing Xero shareholders. The Board concluded that a rights issue was unlikely to raise the amount of capital required to fund its growth opportunities and would not provide the strategic benefits to Xero which a placement to the BNZ and Craig Winkler was able to offer. In addition, a rights issue would most likely have been priced at a significant discount when compared to the Fundraising price of NZ\$0.90 per share, given the volatile global capital market environment. Furthermore, a rights issue would also have taken significantly longer to conclude with an uncertain outcome for Xero’s shareholders and the business generally.

## **Summary Reasons for the Fundraising**

In summary, the Board has concluded that the Fundraising from strategic investors is in the best interests of all Xero shareholders, given:

- it provides sufficient capital to enable Xero to accelerate its international growth opportunities;
- it provides Xero with access to strategic capabilities, including the considerable experience of Craig Winkler in the small business accounting software and services market. This will assist in the further development and execution of Xero’s strategy;
- it has strengthened the shareholder base by adding an institutional shareholder;
- it has raised capital from a group of knowledgeable and informed shareholders at a price of NZ\$0.90 per share, which is above the Xero VWAP share price of NZ\$0.88 since the time Xero listed on the NZSX. The Fundraising price is also above the Xero VWAP share price of NZ\$0.86 over the 5 trading days prior to Xero’s announcement, on 2 April 2009, of a potential capital raising; and
- Xero will be well funded with a strong balance sheet, which will help to instil customer confidence and accelerate the development of additional strategic partnerships in Xero’s international markets.

Xero was advised on the Fundraising by Cameron Partners Limited, New Zealand’s leading independent investment bank.

## **Notice of Special Meeting of Shareholders**

Given that the funding from Craig Winkler and his associated parties will result in them owning over 20% of the shares of Xero, their investment is subject to Xero shareholder approval under the NZX Listing Rules and the Takeovers Code.

In addition, as required by the Takeovers Code an independent appraisal report has been prepared in respect of the investment by Craig Winkler and his associated parties. This report has been independently prepared by Deloitte and is enclosed.

Accompanying this letter is a notice of the Special Meeting of Shareholders and Proxy Form. The meeting of shareholders will take place at 4.00pm at the NZX Centre, Level 2, 11 Cable Street, Wellington on Thursday 14 May 2009.

You may either exercise the right to vote by being present in person or represented by proxy. A proxy need not be a shareholder of Xero and may be the Chairman of the meeting. If you are unable to attend the meeting and you would like to vote, please complete and return a proxy form by 4.00pm on Tuesday 12 May 2009.

### **Share Purchase Plan**

As explained above, the SPP will enable shareholders who have been supportive of Xero, including those existing shareholders who acquired shares at the time of the IPO, the opportunity to subscribe for new shares. Each existing New Zealand shareholder of Xero is entitled to subscribe for a maximum of NZ\$5,000 of Xero shares (being the maximum amount currently permitted under the NZX Listing Rules) at NZ\$0.90 per share.

We appreciate that many of our early shareholders would like to subscribe for more shares under the SPP, but the business does not require the additional capital at this time.

Xero shareholders with registered addresses in New Zealand may participate in the SPP if they were on the Xero share register at the close of business on Thursday 23 April 2009.

The SPP is not subject to shareholder approval and the SPP documents, including an application form, are enclosed with this letter. Applications for the SPP will close at 5.00pm on Monday 18 May 2009.

### **Summary**

We encourage you to carefully read the enclosed documents.

We thank you for your continued support of Xero.

Kind regards.

Yours sincerely



Phil Norman  
**Chairman**