

# absolute

Harbert Management Corporation

2006  
ANNUAL  
REPORT





# absolute approach absolute returns

There are few absolutes in the world of alternative investments. Every portfolio, every investment, every deal is unique. But at Harbert Management Corporation, there are several absolute principles that guide us. Since its founding, this handful of beliefs has defined our company. These beliefs continue to guide our actions, and they are absolute and non-negotiable.

At Harbert, we approach every transaction as an investor. Our chief product is opportunity. We are always looking for opportunistic ways to deploy our investors' and our own capital. We are not asset gatherers; we are not advisors or allocators. We and our affiliates invest our own capital in every fund, in every transaction, on equal terms with our partners. Because we commit our own money to every fund, our interests are aligned with those of our investors. Our only measure is absolute returns. Measuring our performance against traditional benchmarks offers little comfort when those benchmarks are below the goals we set for ourselves. That said, we are disciplined enough to stay out of the market or sell assets when timing and conditions dictate.

We are absolute, devout believers in diversification, across asset classes and within portfolios. Diversification is our primary tool for managing risk.

We use fundamental investment-by-investment underwriting to absolute thresholds. We do not invest based on trends, momentum, non-fundamentally based models or similar techniques. We believe in diligence, patience, creativity and thorough analysis of every opportunity.

Our investors are our partners; they have a right to transparency and to understand how their money is deployed. We employ a sizeable team of legal, accounting, compliance and risk management professionals to support all of our investment teams. They endeavor to ensure that we comply with all relevant laws and regulations, they help us manage risk and they free our investment professionals to concentrate their energy on investing. Our support team provides our investors timely access to performance information and provides current and relevant information to our investment teams to support their investment management process. We have never hesitated to invest in or upgrade this infrastructure.

Finally, we believe in talent. Without question, our greatest strength lies in the people we hire. So we seek out talent, we invest in our people and we reward their performance. Given the nature of our business, smart, motivated people are a differentiating factor.

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*The annual report contains certain "forward-looking statements" that are based on our assumptions and judgments with respect to, among other things, future economic, competitive and market conditions, subjective evaluations of current investments and their prospects and future business decisions, all of which are difficult or impossible to predict or evaluate accurately and many of which are beyond our control. Because of the significant uncertainties inherent in these assumptions and evaluations, you should not place undue reliance on these forward-looking statements, nor should you regard the inclusion of these statements as our representation that any fund will achieve any strategy, objectives or other plans. All forward-looking statements are made as of the date of this report. There is no obligation to update these forward-looking statements to reflect events or circumstances after the date hereof, nor is there any assurance that the policies, strategies or approaches discussed herein will not change.*

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# Harbert® Management Corporation

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# corporate profile

Harbert Management Corporation is an investment management firm managing over \$7.5 billion (as of January 1, 2007) of assets and committed capital in 10 alternative asset classes in three areas of concentration: real estate, private capital and absolute return strategies.

Harbert and its affiliates make significant co-investments on a pari passu basis in each strategy offered to their investors. Harbert's investors include endowments, foundations, funds of funds, family offices, pension plans, banks, insurance companies and high net worth individuals. Harbert makes each commitment of capital with a disciplined focus on risk, absolute return and diversification.

Harbert has put in place the risk management and compliance infrastructure demanded by the growth of its diverse set of investment strategies. This commitment to management and compliance is demonstrated by the breadth and professionalism of the legal, accounting, compliance and risk management teams centrally located at our headquarters in Birmingham, Alabama.

Harbert's investment teams are located in Birmingham and in satellite offices in New York; London; Richmond, Virginia; and Nashville, Tennessee, so that they are close to the relevant markets for their respective strategies. Harbert's centralized risk management and compliance program enables these teams to concentrate on their goal of delivering risk adjusted returns for their respective strategies.

## *Real Estate:*

- Domestic
- European

## *Private Capital:*

- Private Equity
- Venture Capital
- Mezzanine Capital
- Independent Power

## *Absolute Return Strategies:*

- Distressed/Event
- Emerging Markets
- Capital Structure/Convertible Arbitrage
- Merger Arbitrage/Event Driven

Harbert's Real Estate and Private Capital Investments (Including Managed Assets)  
as of December 31, 2006



# 20 06 the year in review

Our individual investments are as varied as the mood of the capital markets. Our approach to investing is not. We operated this year, as we do every year, guided by a few absolute principles, and the results have been reassuring.

## LETTER TO PARTNERS, ASSOCIATES AND FRIENDS

For the past several years, our letter to you has described the investment environment as challenging or, to quote our last year's description of 2005, "a very difficult year for investing and investment management." Viewed from a distance, things have not changed that much. The world is still awash with liquidity, credit spreads are at or close to

*We have closed the year on an especially strong note and believe the last two quarters of 2006 were the best in HMC's 13-year history.*

all-time lows, leverage ratios in buyout deals are continuing to increase and the valuation of investments in the public and private markets still appear excessive to us.

Fortunately, HMC has been able to navigate extremely well in this environment. We have closed the year on an especially strong note and believe the last two quarters of 2006 were the best in HMC's 13-year history. This letter not only conveys our views on the firm's investment performance, but also reflects how we feel about HMC's progress in achieving its strategic objectives and how HMC is positioned for the future.

When we examine the discrete achievements that resulted in a great year, we find that the factors that drove our overall performance were complex and difficult to pinpoint. However, the word that surfaces again and again in this analysis is "cumulative," the cumulative effect of the consistent

application of our business and investment principles, across a diverse set of asset classes, over an extended period of time.

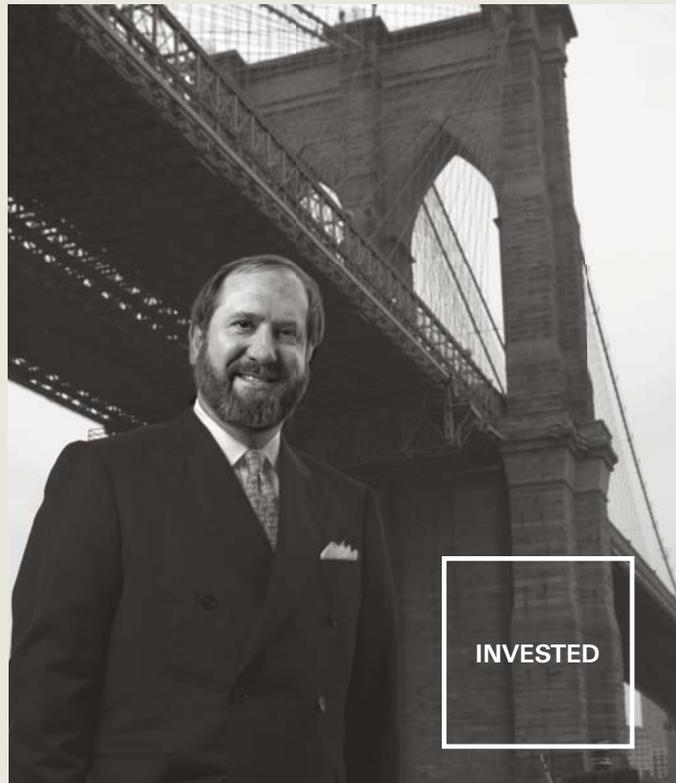
Here are some examples of our 2006 successes that contributed to that cumulative result and why we are so excited about the future.

- The Harbinger Special Situations Fund was launched in August. The returns for its first five months are spectacular, and we are rapidly raising capital for that partnership. This Fund has been under consideration for over three years and is a natural extension of the strategy of an existing investment that itself has been evolving for more than five years.

- In Private Capital, Real Estate and Power, we struggled to make new investments that met our absolute return thresholds in 2004 and 2005. However, during 2006, in the face of what almost any observer would classify as excessive liquidity in all markets, our Private Equity and Mezzanine teams had record years in terms of dollars deployed, which included the establishment of multiple new investment platforms by the Domestic and European Real Estate groups and the Power group. The reasons: the long-term impact of years of direct deal flow development; becoming the dominant regional provider of mezzanine capital in our segment; relationships with entrepreneurial real estate owners and developers and operational expertise that enables us to develop as well as buy our power investments.

- Our marketing team had a record year as well, bringing our aggregate assets and committed capital under management as

*...We are thrilled by the number of dollars, but even more pleased that some of the most sophisticated investors in the U.S., Europe and Asia have partnered with us.*



Raymond J. Harbert / Chairman & CEO

of January 1, 2007, to over \$7.5 billion. These totals include the new Special Situations Fund and follow-on funds for Power, Domestic Real Estate, European Real Estate and Mezzanine. We are thrilled by the number of dollars, but even more pleased that some of the most sophisticated investors in the U.S., Europe and Asia have partnered with us. Our fundraising successes are not only the result of

long-term investment performance, but also relationships developed over many years.

- On the strategic front, we believe our newest hedge funds—Emerging Markets, Capital Structure/Convertible Arbitrage and Merger Arbitrage/Event Driven—are positioned to take advantage of opportunities in each of these markets. New issue volume has begun to pick up in the convertible markets, and we believe that the current low levels of volatility are almost certain to trend up. The volume of public M&A deals available for investment is near all-time highs while a tremendous amount of capital still remains on the sidelines. And, the key emerging markets around the globe continue to experience high rates of economic growth and progress toward more open and transparent political and economic systems, which we expect will result in valuations converging with those in developed countries.

*...we are pleased to be able to continue to report that HMC's long-term absolute investment returns remain above our established target of 15%, net of all fees and expenses.*

In 2007, we will continue our long-term commitment to seek out new investment opportunities for ourselves and our partners and to promptly recognize and deal with underperforming investments.

All of these words are worth little to us as investors without performance. On that front, we are pleased to be able to continue to report that HMC's long-term absolute investment returns remain above our es-

tablished target of 15%, net of all fees and expenses. To remind you, the measure we established and report to you each year is the weighted average internal rate of return that an investor would have earned by allocating to every investment platform we have created since the close of our first fund in 1995, in the same proportion and at the same time as the Harbert affiliated entities. The 2006 calculations are an estimated internal rate of 16% and a realized cash-on-cash return also of 16%, net of all fees and expenses. We do not pay much attention to relative returns, but comparing this performance to the S&P 500 and Lehman Bond Index returns of 9.7% and 6.5%, respectively, during the same period, says volumes about the value of a long-term, diversified alternative investment program.

While we certainly made some mistakes and had some setbacks, overall, 2006 was Harbert Management Corporation's best year ever from both qualitative and quantitative perspectives. Because of the cumulative effect of choices we made in the year just ending, and more significantly in the 13 years since the Company's launching, the future has never looked brighter.

But 2006 is now history. To quote our long-time friend Ace Greenberg of Bear Stearns, "it is a new year and the score is zero/zero." Achieving another winning year may seem a somewhat daunting task, but at Harbert Management Corporation, we are confident in early 2007 because of where we find ourselves from a qualitative perspective. We believe we are entering the new year with our investment portfolios in

CLARITY

Michael D. Luce / *President & COO*

Raymond J. Harbert / *Chairman & CEO*

the best shape ever, our investment management personnel have never been stronger and our investment strategies appear to be positioned correctly in the markets.

We continue our commitment to all of our constituencies that Harbert Management Corporation will work hard and strive to deliver the best risk adjusted returns and to be the best provider of investment manager services in the alternative asset universe.



Raymond J. Harbert, *Chairman & CEO*



Michael D. Luce, *President & COO*

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real estate

# domestic real estate



Our Domestic Real Estate team's experience stretches back more than 20 years, beginning with proprietary investments and continuing with the launch of the first real estate fund in 1995. We have developed

*We create a rigorous asset-specific management plan to improve each property's competitive position, with the intent of increasing the overall value of the portfolio.*

an extensive network of professional relationships, through which we find most of our investment opportunities. Rather than follow trends or "hot markets," we look at individual opportunities, scrutinizing each opportunity's fundamentals in detail. However, our deep experience as developers, owners and managers of real estate has the most influence on which opportunities we choose to pursue.

The Domestic Real Estate team targets mid-sized, entrepreneurial commercial office space and industrial properties, as well as opportunities in the multi-family, retail and hospitality segments of the market. We typically invest in properties ranging in value from \$10 million to \$50 million. This is a less efficient market where our skill set can have a meaningful impact.

We are not passive investors. When we consider an opportunity, we evaluate whether, through income growth and operational improvements, we can increase the property's value. We create a rigorous, asset-specific management plan for each investment to improve the property's competitive position, with the intent of increasing the overall value of that property. We strive to mitigate risk through diversification by property type, geography and investment profile.

*“At Harbert, our domestic real estate team began developing its expertise years ago by developing, owning and managing properties for Harbert Corporation’s account. Today we use this expertise as developers, owners and managers to judge every opportunity that we review.”*

*Michael White / Vice President & Director of Investments / Domestic Real Estate*

DIVERSIFIED

Michael P. White  
VP & Director of Investments

Alan C. Fuller  
VP & Director of Investments

## 20 06 IN REVIEW

- We completed the dispositions of Interstate Northwest Business Center, located in Atlanta, Georgia, and West Volusia Shopping Center, in Orlando, Florida.
- We initiated a disposition effort for Morgan Falls Office Park with one building sold in 2006.
- We executed a preferred equity recapitalization of Vista Centre Shoppes, in Orlando, Florida, allowing the return of a substantial portion of the original equity to investors. The recapitalization preserved future upside in the project while mitigating equity risk and enhancing investment returns.
- In Washington, D.C., we completed the close-out of the Meridian Crescent condominium development. Sales prices exceeded our initial expectations.
- We actively sought acquisition opportunities and acquired four office and office/flex properties. The portfolio now contains nearly 2 million square feet of space across nine properties in four states and five cities.
- Hartwell Smith joined Harbert as Vice President of Asset Management in August 2006.
- Harbert Real Estate Fund III had a final close of approximately \$161 million.

# 2006 Domestic Real Estate Transactions

## Acquisitions

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During 2006, the domestic real estate team acquired four properties totaling 947,000 square feet of office and office/flex space. These investments were:

### **East Pointe Business Center**

This 287,000-square-foot office/flex park in Memphis, Tennessee, was acquired in June 2006. The property was purchased below replacement cost with an opportunity to increase revenue through leasing vacant space.

### **3 Northborough**

This 157,000-square-foot, Class B office building located in Houston, Texas, was purchased in an off-market transaction in October 2006. The property is currently at stabilized occupancy and provides an opportunity to participate in a tightening Houston office market.

### **1001 West Loop South**

### **2425 West Loop South**

These two assets were also purchased in an off-market transaction in October 2006, and represent a combined 503,000-square-foot of Class A and Class A-/B+ office space in Houston, Texas. The properties provide an opportunity to increase rents through capital repositioning and the lease-up of vacant space in the recovering and popular Galleria submarket.

## Dispositions

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### **Interstate Northwest Business Center**

In late 2004, we acquired a 60% interest in this 286,000-square-foot business park in a premier Atlanta, Georgia, location. The investment provided current cash yields and capital appreciation through leasing vacant space in a recovering market. The property was sold in September 2006.

### **Meridian Crescent Condo Development**

Construction began in January 2004 on this 29-unit, luxury condominium development located in Washington, D.C.'s Meridian Hill area. The investment allowed participation in the growing demand for housing in the D.C. market. The sale of the condominiums was completed in 2006.

### **Morgan Falls Office Park**

In 2006, we implemented a disposition strategy through individual building sales of this five-building office park in Atlanta, Georgia. We completed the disposition of the largest building in November 2006, and still own the remaining buildings.

### **West Volusia Shopping Center**

This 268,000-square-foot, Class B subregional shopping center located in DeLand, Florida, was sold in late 2006.

# Harbert Domestic Real Estate Investments

Investment portfolio as of December 31, 2006

*The portfolio also includes the 2006 acquisitions listed on page 12.*

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*One Bank of America Plaza*

## **One Bank of America Plaza**

This 366,000-square-foot, Class A office property in downtown Raleigh, North Carolina, was acquired in July 2005. We purchased the property below replacement cost and believed the property had significant upside opportunity through the leasing of vacant space. Through successful execution of our strategy, the asset is near stabilization occupancy. The property is located at the center of a \$1 billion downtown Raleigh revitalization effort.

## **Interstate Business Park**

We acquired this 118,000-square-foot office/flex park in Tampa, Florida, in October 2005. The property presented the opportunity to purchase a stabilized asset with immediate, strong cash-on-cash returns. The park is leased to a diverse tenant base with a staggered rent roll and allows for appreciation through bringing below-market rents up to market.

## **North Dallas Office Portfolio**

We acquired this three-building, 455,000-square-foot, Class B office portfolio in Dallas, Texas, in December 2005. The property was purchased below replacement cost, with an opportunity to add value through the lease of vacant space in a recovering market.

## **Vista Centre Shoppes**

In late 2004, we acquired a 60% interest in this 94,400-square-foot, Class B specialty center, adjacent to Walt Disney World in Orlando, Florida. This property provides current cash flow and a repositioning opportunity through increasing below-market rents and achieving an improved tenant mix.

## **Morgan Falls Office Park**

We acquired this 257,000-square-foot office park in the Sandy Springs submarket of Atlanta, Georgia, in mid-2004, at a significant discount-to-replacement cost. The investment provides a value-add opportunity through capital improvements and leasing vacant space in a recovering market. One of the five buildings was sold in November 2006.

# european real estate

In Europe, our real estate team targets acquisition and development opportunities in which we can add value through proactive management. We target opportunities in the office, retail, warehouse/distribution, hospitality and residential sectors ranging from \$10 million to \$100 million in size. In many cases, opportunities of this size are too small for the larger funds to pursue effectively and yet too large or complex for some of the local and smaller regional investors. There are more of these smaller transactions than larger transactions from which to select. Further, these smaller transactions are not typically sold through fully transparent, widely marketed auctions. Thus, by pursuing

*Europe has attracted a significant number of larger foreign and domestic real estate investment firms, but considerable opportunities exist in the more fragmented and less efficient small and mid cap sectors.*

these opportunities, we increase the probability of successful acquisition and the potential to achieve superior risk-adjusted returns.

Other key elements of our investment philosophy include a disciplined focus on underlying real estate fundamentals, diversification, exit strategies and local knowledge. We are real estate investors with operating expertise; we evaluate each transaction on the underlying returns generated by the properties themselves. Although we will capitalize our transactions to enhance returns, we will not use leverage to justify our investment decisions. In order to reduce the overall risk within the portfolio, we believe in diversifying across property types, geography and investment risk.

Our strategy is to maximize value by active, hands-on asset management. This includes asset-specific business plans to improve leasing rates and management strategies designed to enhance the competitive position of each asset and, ultimately, its value as an investment.

We recognize that while capital is global, real estate is a local business. We seek to join with local partners in each investment, partners who have an established track record in both the relevant market and product type, and whose investment interests are aligned with our own.

*“Harbert puts great faith in talent. We consistently hire gifted people and provide them with the resources they need to perform well.”*

*Scott O'Donnell / Vice President & Managing Director / European Real Estate*



THOROUGH

Scott D. O'Donnell  
*VP & Managing Director*

Peter J. A. Land  
*Principal & Director of Investments*

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IN REVIEW

- Acquired a site in Munich, Germany, for a build-to-suit warehouse.
- Successfully launched HEREF II and received commitments for over 85% of the Fund's targeted capital.
- Acquired two properties suitable for low-density, golf-oriented master planned communities in southern Spain.
- Added Asset Manager Huw Davies and Roque Rotaache to the team.
- Sold adjacent office buildings in the city of London.

# 2006 European Real Estate Transactions

## Acquisitions

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*Arcos Gardens*

### **Munich Warehouse**

We acquired a 75% controlling interest in a joint venture that purchased a site to develop a 35,000-square-foot warehouse facility on a build-to-suit basis for a financially strong tenant. The tenant has entered into a 20-year triple net lease agreement. We believe this investment provides a quality asset with current cash flow to mitigate the risk of other, more opportunistic investments.

### **Spanish Residential**

We acquired approximately 1,350 acres in two parcels comprising a 50/50 joint

venture with a Spanish partner. The properties are both located in southern Spain and are former olive groves. Our objective is to create well-designed master plans for low-density, golf-oriented communities and then to sell the parcels to a third party for implementation of the master plans. There is a growing demand among Northern Europeans for low-density developments centered around recreational facilities and in close proximity to international airports and cultural areas. The master plans for these properties are designed to meet those growing needs.

## Dispositions

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### **Leadenhall/Mitre Street**

These adjacent buildings, formerly the London headquarters of Swiss Re, contain approximately 40,000-square-feet. We acquired the vacant properties in 2004,

refurbished them and re-let the space to various tenants. Once leasing was complete, we marketed and sold the buildings at a price in excess of the original underwriting.

# Harbert European Real Estate Investments

## Investment portfolio as of December 31, 2006

*The portfolio also includes the 2006 acquisitions listed on page 16.*

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### **Arcos Gardens**

This investment is a 404-acre, low-density, second-home golf course community in southern Spain that is being developed in a joint venture with a Spanish developer and a U.S. family trust. The development serves as the official training facility for the golf teams sponsored by the Swedish Golf Federation. Marketing of the residential units began in the first quarter of the year and both potential buyers and the press, who have published numerous positive articles on the development, have received the project favorably.

### **Cadogan Hotel**

In early 2004, we acquired through a joint venture, the Cadogan, a 65-room hotel in Knightsbridge, London. In conjunction with our venture partners, we completed a planned renovation of all common areas and the first two floors of guest rooms; a new restaurant, Langtry's, was opened, and the hotel was rebranded as a Leading Small Hotel of the World. The Cadogan is currently being repositioned as a luxury hotel that targets affluent business and leisure travelers.

### **Clemenceau**

This 70,000-square-foot office building is located in Nanterre, a suburb of Paris. With renovated common areas (lobby, bathrooms, elevators), the team continues to manage the building's rent roll to maximize potential income.

### **Dublin and Leeds Warehouses**

Through two separate joint ventures in which we have a 75% interest, we acquired sites in Dublin, Ireland, and Leeds, England, on



*Cadogan Hotel*

which we developed, respectively, a 37,000-square-foot warehouse/distribution center and a 70,000-square-foot vacant warehouse. At the time of acquisition, a financially strong tenant signed triple net leases with terms of 25 years for both properties. These investments provide quality assets, leased on a long-term basis to a tenant that continues to grow throughout Europe.

### **Paris Warehouse**

We acquired a 75% interest in a joint venture that purchased a vacant 140,000-square-foot warehouse/distribution center in suburban Paris, while simultaneously leasing the facility to a financially strong tenant for a fixed period of 12 years. We believe this investment provides a quality asset, a quality tenant, and mitigates the risk of our other more opportunistic investments.



private capital

# private equity

Our private equity team identifies businesses that have strong management teams in place and are positioned to grow. We traditionally look for opportunities in less competitive sectors of the market, pursuing what we consider attractive investments at a significant discount to valuations in the broader private equity markets. Our investment opportunities are often developed by directly contacting companies in targeted industries, bypassing intermediaries.

The private equity team looks for investments in leveraged buyouts, recapitalizations, expansion projects and select distressed opportunities. We target middle-market companies with valuations of \$10 to \$100 million,

*We attempt to invest in companies with quality management and superior competitive positions.*

with an emphasis on \$20 to \$50 million transactions. We attempt to invest in companies with quality management and superior competitive positions. Our goal is always long-term capital appreciation.

With every investment, we take an active role, using our experience to create value. We give our portfolio companies access to more than capital; we also bring to the table management experience, as well as legal, accounting, treasury and other support services when such services are needed.

We have a disciplined and conservative approach for evaluating potential acquisitions and investments. Our goal in due diligence is to avoid surprises and identify ways in which we can contribute to the long-term success of the company after the acquisition closes. We believe strongly that there is no single road to success and we are willing to work with the management team of each company in which we invest to develop and support a strategy that fits the company and the current situation.

*"Few other private equity firms can match the breadth of expertise Harbert offers its portfolio companies. From management experience to legal, accounting and treasury services, Harbert is far more than a ready source of capital."*

*Michael Rowland / Vice President & Director of Investments / Private Equity*



CAPITAL

Michael A. Rowland  
VP & Director of Investments

Donald R. Beard  
VP & Director of Investments

## 20 06 IN REVIEW

- Completed seven new platform acquisitions and one add-on acquisition to an existing platform company, investing a total of \$58 million.
- At year-end, held positions in nine separate platform companies in various industries including specialty finance, health care, media transportation and logistics and manufacturing.
- Completed the disposition of Community Hospices of America, Inc.
- Completed the disposition of the South Carolina operations of ECA Holdings, LLC, in a transaction that eliminated nearly all of ECA's debt and positioned the company for continued growth in its remaining markets.
- Added one new Director of Investments with significant middle-market investment banking experience. Added two experienced analysts and one junior analyst to the team.

# Private Equity Investments

Investment Portfolio as of December 31, 2006

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## Express Check Advance, LLC

Consumer finance company that operates payday advance lending branches in eight states. Based in Chattanooga, Tennessee.

## Presidential Financial Corporation

Commercial finance company that provides working capital financing to small businesses in the form of asset-based loans. Based in Atlanta, Georgia.

## Winnercomm Holdings, Inc.

Diversified media company that provides television production, remote event production

and aerial camera systems as well as website management, advertising sales and advertising agency services. Based in Tulsa, Oklahoma.

## PWI Holdings, Inc.

Underwrites and administers vehicle extended services agreements and offers sales finance contracts to sub-prime credit consumers through select independent automotive dealers. Based in Orwigsburg, Pennsylvania.

## CF Holding Company Inc.

The nation's largest less-than-truckload ("LTL") carrier and logistics manager exclusively



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serving furniture manufacturers, importers and retailers. Based in Lenoir, North Carolina.

**Child Health Systems, Inc.**

Operates day care and respite care facilities for children with acute medical conditions. Based in Tampa, Florida.

**Aerosol Packaging, LLC**

Packages private-label aerosol products for a wide range of end users. Based in Canton, Georgia.

**TSF Holdings, Inc.**

Manufacturer of polystyrene foam products used in the packaging and construction materials markets. Based in Martinsville, Virginia.

**Dent-A-Med, Inc.**

Consumer finance company that funds retail purchases for consumers with less than perfect credit. Based in Springdale, Arkansas.



# venture capital

Our Venture Capital strategy invests in early stage information technology and health care companies. We seek to invest in the first or second institutional round of financing for companies with experienced management, a defensible strategy and unique technologies that address large and growing markets. A member of the Venture Capital team usually takes a seat on the board of each portfolio company, providing strategic value and perspective to the company's management team.

Our team's target region, stretching from Maryland to Florida, encompasses the fifth largest economy in the world and the fastest



*The Venture Capital team's target region, stretching from Maryland to Florida, encompasses the fifth largest economy in the world.*

growing economic region of the nation. Although this dynamic area is home to numerous research universities, government and corporate research facilities, public companies and an active entrepreneurial community, it has suffered historically from a lack of local venture capital. This produces significant opportunities for quality investments at reasonable valuations.

Our senior management team has more than 60 years' combined experience in venture capital and related markets. They bring together backgrounds in finance, law, business operations, information technology and life sciences, to produce a valuable and coherent perspective on venture investing. Members of the Venture Capital team have participated in more than 30 venture capital investments since 1999, which have, to date, produced four initial public offerings and several M&A transactions.

*“Harbert has done a remarkable job of bringing together talented people who understand the ever-changing nature of the venture capital market.”*

*Will Brooke / Executive Vice President & Managing Partner / Venture Capital*



INSIGHTFUL

Wayne L. Hunter  
Managing Partner

William W. Brooke  
EVP & Managing Partner

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06

IN REVIEW

- Initial investments were made in Optimal Readings, Inc., ION Healthcare, Inc. and Aldagen, Inc. during the year, adding these companies to the Fund's portfolio. The team led or co-led all three investments.
- Portfolio company Airimba Wireless merged with North Carolina-based Windchannel Communications, broadening its internal resources, customer base and market reach.
- Follow-on investments were made in each of MaxCyte, Innovative BioSensors and Unitrends, with new investors joining the Innovative BioSensors' syndicate.
- Tom Roberts was made a Partner in the Fund, and on January 1, 2007, Jeff Harris joined the Fund full-time as Principal.

# Harbert Venture Partners Portfolio

Investment portfolio as of December 31, 2006

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## **Airimba Wireless, Inc.**

Provider of wireless broadband service, offering wireless connectivity and Internet access to targeted multi-family communities and surrounding businesses. Airimba has offices in Raleigh, North Carolina, and Dallas, Texas.

## **Aldagen, Inc.**

Clinical-stage regenerative medicine company developing products related to the transplant of adult human stem cells for tissue regeneration and to treat blood diseases, cancer and genetic diseases, based in Durham, North Carolina.

## **BroadSource, Inc.**

Provider of telecommunications management software serving businesses with the ability to automate service order processing, track assets and inventory, consolidate and reconcile invoices and manage information flow, from network planning and engineering to operations, based in Atlanta, Georgia.

## **Innovative BioSensors, Inc.**

Involved in commercializing novel technology for the rapid detection of pathogens for military and homeland defense markets, food-safety testing and human diagnostics, based in College Park, Maryland.

## **MaxCyte, Inc.**

Clinical-stage company developing both proprietary and partnered therapeutics taking advantage of advanced capabilities for development and manufacturing of cell-based therapies, based in Rockville, Maryland.

## **Optimal Reading, Inc.**

Coordinates gathering and management of diagnostic images from hospitals and clinics in a digital format and delivers them to independent radiologists for reads and diagnosis, based in Birmingham, Alabama.

## **Privaris, Inc.**

Develops wireless biometric authentication devices using fingerprint recognition technology that can overlay onto existing security systems. Offices in Charlottesville and Fairfax, Virginia.

## **TapRoot Systems, Inc.**

Provider of software and services for mobile phone manufacturers and wireless operators worldwide specializing in developing off-the-shelf software subsystems that support a suite of communications protocols for smartphone operating systems, based in Research Triangle Park, North Carolina.

## **Unitrends Software Corporation**

Provides Business System Continuity solutions to small and medium-sized businesses that enable them to get back in business fast when their systems and servers fail, and provides disk-to-disk, high-speed data backup and recovery capabilities in a neatly packaged and cost effective appliance-based solution, headquartered in Columbia, South Carolina.

## **ION Healthcare, Inc.**

Provides respiratory disease management services to patients suffering from sleep apnea

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through proprietary portable testing technologies as well as gold standard in-lab polysomnograms, and provides therapeutic and

compliance services to identified sufferers of OSA. Based in Richmond, Virginia.



# mezzanine capital



Our Mezzanine Capital team invests in small to medium-sized businesses that have reached the lending limits of their commercial banks or have limited ability to borrow from traditional senior lenders. We

*Through leverage, we pursue long-term returns competitive with those of venture capital and private equity transactions.*

typically provide between \$3 to \$10 million in subordinated debt to companies with revenues between \$10 and \$100 million, management with significant ownership and a demonstrated track record. We also look for operating profitability, sufficient cash flow to service debt, growth potential and a viable exit strategy. While we focus on the service sector in compelling markets, we will consider opportunities in any market.

Several market conditions combine to create opportunities for our Mezzanine Capital team, including a lack of liquidity in the small capitalization public equity market, the conservative nature of senior credit markets and the larger bite-size of bigger mezzanine funds.

Our investments are typically structured as five-year interest-only loans that provide a layer of long-term capital to growing businesses. We concentrate on opportunities where we believe the risk of principal is limited and the prospects for equity appreciation is high. We pursue long-term returns competitive with those of venture capital and private equity transactions. Our returns are driven by a combination of leverage, current coupon interest, paid-in-kind interest and warrants with a nominal strike price.

*“Freedom and accountability. As a strategy manager at Harbert, you are given plenty of both, which is why many of us choose to work here.”*

*John Harrison / Vice President & Director of Investments / Mezzanine Capital*



John C. Harrison  
VP & Director of Investments

John S. Scott  
Director of Investments

Robert A. Bourquin  
Director of Investments

Brent G. Ray  
Director of Investments

## 2006 IN REVIEW

- Closed 12 new investments and five add-on investments for a total of approximately \$70 million invested.
- Held final closing for Harbert Mezzanine Partners II, LP (HMP II) in January 2006. A total of \$109 million was committed to HMP II.
- HMP II completed the small business investment company licensing process with the SBA and received its SBIC license in January 2006.
- Exited eight portfolio companies through sales to strategic and financial buyers or recapitalizations. Six of these loans were repaid with warrant gains and/or paid-in-kind interest realized.
- Added Associate Andy Tatman, formerly of Morgan Keegan in Nashville, Tennessee, to the investment team in March 2006.

# Harbert Mezzanine Partners

## New Investments in 2006

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### Atlantic Coast Media Group, LLC

Developer and marketer of consumer products based in Hoboken, New Jersey.

### Controlled Contamination Services Holdings, Inc.

Provider of cleanroom services based in San Clemente, California.

### Cambridge Advisory Group, Inc.

Employee benefits plan consultant and actuarial services provider based in King of Prussia, Pennsylvania.

### Cory Packaging, Inc.

*(dba Master Packaging, Inc.)*

Manufacturer of flexible packaging products based in Tampa, Florida.

### COCAT Holdings, LLC

Provider of property restoration, reconstruction and renovation services based in Denver, Colorado.

### Highwinds Capital, Inc.

Provider of Usenet software based in Orlando, Florida.



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**Holdaway Medical Services, LLC**

Provider of respiratory therapy, home medical equipment and home infusion services based in Louisville, Kentucky.

**Intersearch Group, Inc.**

Provider of Internet search services based in San Francisco, California.

**Narcote, LLC**

Provider of coated and laminated composite fabrics based in Piney Flats, Tennessee.

**PML Exploration Services, LLC**

Provider of mud logging services to the exploration and production sector of the energy industry based in Oklahoma City, Oklahoma.

**Turning Technologies, LLC**

Provider of interactive group response systems based in Youngstown, Ohio.

**Wyndlam Jade, LLC**

Provider of planning and management services for conventions, incentives and travel based in Plano, Texas.



# independent power

In the 1980s, Harbert Corporation began taking advantage of emerging opportunities in the power generation market, opportunities driven by deregulation of the industry. It developed and built 10 power plants, most of which it continues to own and operate today. When the power management team joined Harbert Management Corporation in 1993, the power industry was one of the first asset classes targeted for investment. We believe independent power remains an excellent opportunity for us because of our experience and the industry's attractive risk/reward profile.

*From the beginning, our strategy has been to invest in power assets that have power sales contracts.*

From the beginning, our strategy has been to invest in power assets that have power sales contracts. Contract revenues provide us and our investment partners with predictable cash flow streams. At the end of a contract, the project should have significant remaining value that can enhance investor returns.

Over time, the independent power industry has matured. Other investors have also recognized the benefits of equity-like returns often combined with bond-like risk. Therefore, competition for power assets has increased, which has driven returns down. We have reacted to these changes by pursuing earlier-stage projects that have a higher risk profile but that also provide opportunity for a higher return. Our team's history of developing and building power projects gives us skills that many of our competitors do not possess and allows us to compete effectively for earlier-stage projects. This strategy has proven successful and we expect to continue pursuing similar project development opportunities in selected markets. We expect that our future investments will include a combination of development and acquisition of existing power plants.

*"Few investment funds can match our experience in Independent Power. As this business continues to evolve, that experience is one of our greatest assets."*

*Wayne Nelson / President & CEO / Independent Power*



LONGEVITY

Wayne B. Nelson, III  
*President & CEO*  
*Harbert Power, LLC*

Patrick E. Molony  
*Executive Vice President & COO*  
*Harbert Power, LLC*

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06

**IN REVIEW**

- Sold our interest in 225 MW power plant in Paris, Texas.
- Developed first investment for Fund III - Mackenzie Green Energy, British Columbia.
- First closing for Fund III; \$220 million committed.
- Funds I and II continued to meet or exceed our expectations.

# Harbert Power

Portfolio as of December 31, 2006

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## INVESTMENTS

### **Kalaeloa** (50% ownership)

209 MW oil-fired plant

Oahu, Hawaii

### **Lockport** (24.3% ownership)

200 MW gas-fired plant

Lockport, New York

### **Paris** (18% ownership)

225 MW gas-fired plant

Paris, Texas

### **Soda Lake** (50% ownership)

14 MW geothermal plant

Fallon, Nevada

### **GWF Energy** (40% ownership)

#### • **Phase I**

95 MW gas-fired plant

Hanford, California

#### • **Phase II**

97 MW gas-fired plant

Henrietta, California

#### • **Phase III**

170 MW gas-fired plant

Tracy, California

### **Fluvanna** (30% ownership)

885 MW gas-fired plant

Fluvanna County, Virginia

### **Freeport** (90% ownership)

50 MW gas-fired plant

Long Island, New York

### **Pinelawn** (90% ownership)

80 MW gas-fired plant

Long Island, New York

### **Mackenzie Green Energy** (50% ownership)

55 MW wood-fired plant

British Columbia (in development)

## MANAGED ASSETS

### **Bridgewater** (40% ownership)

16 MW wood-fired plant

Bridgewater, New Hampshire

### **Tracy** (34.5% ownership)

20 MW wood-waste plant

Tracy, California

### **GWF Power Systems** (50% ownership)

#### • **Site I - Site II - Site V**

20 MW petroleum coke plants

Pittsburg, California

#### • **Site III - Site IV**

20 MW petroleum coke plants

Antioch, California

#### • **Hanford** (50% ownership)

27 MW petroleum coke plant

Hanford, California



*GWF Power Systems - Site I*

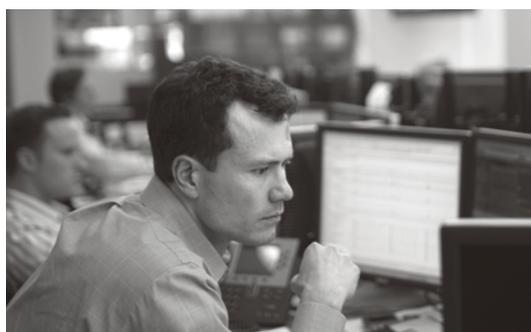


# absolute return strategies

# distressed/event

Our Distressed/Event team uses a disciplined long/short approach in managing its investment portfolio. Our predominant strategy is to purchase distressed or stressed assets at a discount and to short high-dollar priced, heavily leveraged issues, which we anticipate will capitulate. Over the past several years, our team has extended their approach to include activist/special situation investing throughout the entire capital structure.

Our specialized approach and utmost commitment to fundamental analysis have proven to be a winning combination, particularly in highly volatile periods. The strategy



*...our team has been able to achieve superior investment returns, independent of the broader markets.*

includes a focus on restructuring/bankruptcies, liquidations, event-driven situations, turnarounds, capital structure arbitrage and short sales. The portfolio invests in all levels of the capital structure, selecting the level(s) for investment based upon our perception of the best value. We closely monitor our leverage as well as our exposure to individual issuers and industry sectors. Since we launched this strategy in 2001, it has been effective in a variety of credit environments.

In August 2006, we launched Harbinger Capital Partners Special Situations Fund with approximately \$200 million in capital. Since that initial closing, the Fund, which focuses on long-only investment opportunities, has held subsequent closings, bringing year-end assets to \$500+ million.

As Harbinger Capital Partners Fund I passed its five-year anniversary this past June, we viewed the launch of the Special Situations Fund, with its longer lock-up period, as a natural extension of our investment team's evolving control/activist strategy and an opportunity for investors to leverage the experience we have gained since Fund I's inception. The two funds frequently co-invest, increasing the breadth of opportunities available to all investors.

*"It's impossible to overstate the importance of the legal, compliance and accounting support provided by Harbert's back office professionals. It frees us to devote every minute of every working day to investing and pursuing returns."*

*Philip Falcone / Vice President & Senior Managing Director / Harbinger Capital Partners Funds*



RETURNS

Philip A. Falcone  
VP & Senior Managing Director

Howard P. Kagan  
Managing Director & Director  
of Investments

Lawrence M. Clark  
Managing Director & Director  
of Investments

Kathleen K. Murphy  
Portfolio Strategist

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06

#### IN REVIEW

- The Distressed/Event team added five investment professionals: Jeffrey Kirshner, Esq., formerly of Bingham McCutchen, LLP; David Maura, formerly of First Albany Capital; Joseph Cleverdon, formerly with Houlihan Lokey; Joseph Anto, a recent graduate of Columbia Business School and formerly of ABS Capital Partners; and William Drew, formerly of Deutsche Bank.
- Our profits this year were generated on the long side of the portfolio, as robust technicals in the credit markets proved challenging for many short positions.

# emerging markets

Our Emerging Markets strategy seeks to uncover attractive opportunities for absolute returns in the financial markets in Latin America, Eastern and Central Europe and Asia, excluding Japan, through a hedged (long/short) format. We use a mix of financial instruments, including equity and fixed income securities, as well as derivatives and options of both government and corporate issuers, for our investments.

Our investment team uses a combined macro and bottom-up approach when selecting countries in which to invest, first

***This strategy seeks to uncover attractive opportunities for absolute returns in the financial markets in Latin America, Eastern and Central Europe and Asia, excluding Japan.***

analyzing the global economy, then comparing economic fundamentals and assessing economic and political factors within the countries under consideration. We conduct our own research in-house when selecting countries in which to invest. To select particular equity issues for our investments, we conduct a fundamental, bottom-up company analysis aimed at identifying companies that will benefit from changes in country conditions.

We seek to address risk by managing the portfolio's exposure to macro themes, country, currency and company. We also hedge interest rate and country risk through currency, interest rate and default swap markets. Additionally, we generally do not borrow funds for our long positions, and we emphasize investing in liquid instruments, which give us greater hedging options and enable us to better manage our positions when global and country conditions change.

*“There are opportunities for investment throughout the emerging markets of the world. Finding them takes discipline, resources and connections. All of which Harbert brings to the table every day.”*

*Peter Lannigan / Vice President & Senior Managing Director / Emerging Markets*



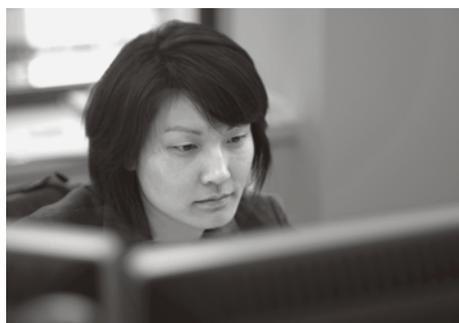
Heather N. Leonard  
VP & Managing Director

Peter S. Lannigan  
VP & Senior Managing Director

## 20 06 IN REVIEW

- Most of our profits this year were generated from our long positions in emerging markets equities where we again maintained the majority of our exposure in equities with a domestically-focused business profile.
- On the fixed income side of the portfolio, our exposure to select local fixed income markets also contributed positively to performance.
- Throughout the year, we hedged our country risk with credit default swaps and we hedged our interest rate risk with interest rate swaps.

# capital structure/convertible arbitrage



Our Capital Structure and Convertible Arbitrage team pursues absolute returns by investing in securities across the capital structure and in related derivative securities, either long or short. We seek to generate returns by capitalizing on volatility in securities pricing and collecting positive

*We use fundamental research to identify and manage opportunities we feel have attractive risk/reward profiles.*

cash flow from interest-bearing securities. In this strategy, we focus on liquid instruments and generally invest in investment-grade, high-yield and convertible debt, credit derivatives, equities and equity derivatives.

We use fundamental research to identify and manage opportunities we feel have attractive risk/reward profiles. Our securities selection process is based on bottom-up credit and equity analysis, which includes extensive documentation review. Securities may be held long or short, or in combination with other securities, to best express the underlying investment thesis. Quantitative analysis helps refine our assessment of securities pricing and determine optimal trade entry and exit points. Top-down macro analysis guides positioning of the portfolio's aggregate risk exposures.

We seek to control downside risk through diversification and by actively managing our position size. We also use futures, swaps, index and over-the-counter products to hedge unwanted risks.

*“Working for Harbert, I can focus my energies on pursuing promising opportunities knowing that I have the support and expertise in the back office to manage all other aspects of our business.”*

*Eric Wong / VP & Senior Managing Director / Capital Structure*



PREPARED

Eric D. Wong

*VP & Senior Managing Director*

Kara K. W. Byun

*Director of Investments*

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06

#### IN REVIEW

- Began investing on September 1, 2006.
- Kara Byun joined the team as Director of Investments. She previously worked as a trader and analyst for Angelo, Gordon & Co.
- Eric Wong joined Harbert as Senior Managing Director for the Capital Structure and Convertible Arbitrage strategy. He previously held senior positions at Aviator Fund Management, Angelo, Gordon & Co. and Trust Company of the West.

# merger arbitrage/event driven

In December 2006, we launched our Merger Arbitrage and Event Driven strategy in response to the increasing volume of mergers and acquisitions. The Fund seeks to generate superior risk-adjusted returns by realizing the discrepancy between an equity's current price and the value implied by an announced transaction. We do not invest in every proposed merger. We are more selective, believing that every transaction must stand on its own merits.

The Fund also invests in companies undergoing other types of significant change that we believe will lead to materially different valuations. These event driven situations

*At Harbert, we are relentless in our research of opportunities.*

can include restructurings, management changes, regulatory changes, corporate auctions, spin-offs and the involvement of corporate activists.

Our research process combines a rigorous analysis of the fundamental and strategic benefits of a transaction with an intensive review of the regulatory landscape. We further seek to enhance returns and manage risk by optimizing position size at critical points throughout the merger process and, when appropriate, through the creative use of derivatives.

Mergers and acquisitions are again in vogue; there has been a consistent increase in both the total number of transactions proposed and in the value of the average transaction. Looking towards 2007 and beyond, we are very encouraged by the strength of corporate balance sheets, continued low interest rates and the amount of private equity capital yet to be deployed.

*“The M&A market seems poised to have another record year in 2007. The housing market has slowed without causing any collateral damage to economic growth; the consensus is that interest rates are heading lower and the outlook for inflation is benign. This backdrop and the large amounts of cash in both corporate balance sheets and private equity funds should keep M&A activity trading higher.”*

*Neil Kennedy / VP & Senior Managing Director / Merger Arbitrage and Event Driven Fund*



DECISIVE

Neil B. Kennedy  
VP & Senior Managing Director

## 20 06 IN REVIEW

- Neil Kennedy joined the Harbert team as Vice President & Senior Managing Director for the Merger Arbitrage and Event Driven Strategy.
- The strategy launched in December and earned a respectable return during its first month.
- John Frank joined the investment team as a Director. He previously was a Senior Analyst with Charter Management.



support

# investor services and risk management

We have grown considerably since 1993. Today, we have over \$7.5 billion in committed capital and assets under management across 10 asset classes and 22 funds; we have more than 900 investors and more than 400 investing sponsors. To manage our operations, we have created a sophisticated infrastructure that supports our commitment to compliance and transparency to our investors. We think our infrastructure also gives investors confidence and differentiates us from many of our “unregistered” competitors.

We also believe that centralizing all of our non-investment related functions at our corporate headquarters in Birmingham allows us to communicate and operate more effectively. It also gives our back office professionals greater independence and control and frees our investment teams to pursue exceptional risk-adjusted absolute returns.

Our staff of qualified professionals performs all of our accounting, compliance, risk management and marketing/investor relations functions. These same people also assist portfolio companies and the investment professionals where appropriate.

**Financial Controls and Reporting.** This team includes 17 CPAs, as well as other experienced staff members who provide investor reporting, risk management, internal audit and accounting and tax services for Harbert’s funds. This team follows established accounting and legal standards and operates independently of the fund managers to provide an additional layer of protection for Harbert’s investors.

**Private Market Funds.** The investor reporting group handles communications with respect to each investor’s capital account in the private market funds, as well as capital calls and distributions. The group also provides quarterly and annual investment reports to our private market fund investors and independently calculates fund level performance for all of the private market funds. Performance returns in the annual reports are audited annually.

**Absolute Return Strategies.** Hedge Fund Administration provides administrative and operational support functions for our absolute return strategies, including trade capture and settlement monitoring, preparation of daily performance and risk reports for management, acting as liaison to prime brokers, custodians and the funds’ administrator and coordinating investor servicing functions with our administrator.

**Internal Audit.** This team ensures that we comply with policies and procedures adopted by Harbert in various areas. Their responsibilities include audit review of performance returns, third-party marketing and referral arrangements. In addition, this team monitors and assists all due diligence conducted by our private market funds.

**Risk Management.** Every trading day, our risk management team monitors trading for our absolute return strategies. They also review each fund’s portfolio and provide the investment teams with a daily risk analysis. The risk

## Financial Controls and Reporting

*“Harbert, from the launch of its first fund, has believed in a strong, independent back office to support its fund strategies and protect its investments and its investors. That belief never wavers.”*

*David Boutwell / Executive Vice President & Chief Administrative Officer / Financial Controls and Reporting*



*- back row -*

David A. Boutwell      Elizabeth A. Deuel      Darlene A. Hartmann      Christopher N. Jones  
*EVP & Chief Administrative Officer      Director of Internal Audit      Director of Investor Reporting      Director of Information Technology*

*- front row -*

Susan M. Shalhoop      Todd D. Nunnelley      Sonja J. Keeton  
*Director of Hedge Fund Administration      Director of Risk Management      Controller & Director of Corporate Tax*

management team meets regularly with senior management at Harbert to discuss its analysis.

**Investment Committees.** Each of Harbert’s private market funds is overseen by an investment committee. Before any fund can make an investment or a divestiture, it must receive unanimous approval from the members of its investment committee. Each committee includes at least one member of the Harbert board who is not engaged in the day-to-day operation of the fund the committee oversees.

**Regulatory Oversight.** Our affiliates, Harbert Fund Advisors, Inc., and HMC Investments, Inc., serve as investment advisors and domestic placement agents, respectively, for each of our funds. Harbert Fund Advisors is registered as an investment advisor with the SEC. HMC Investments is a member of the NASD and SIPC. Harbert European Fund Advisors, Ltd., is authorized by the Financial Services Authority of the United Kingdom and provides advisory services by agreement with Harbert Fund Advisors to the Harbert European Real Estate Funds and engages in certain marketing activities in Europe on behalf of the Harbert sponsored funds.

## Legal and Compliance

*“Our goal is to serve the Harbert organization by helping investment and management teams accomplish their objectives in full compliance with applicable legal requirements and Harbert’s fiduciary duty to its investors.”*

*Bill Lucas / Executive Vice President & General Counsel / Legal and Compliance*



INVOLVED

William R. Lucas, Jr.  
*EVP & General Counsel*

Joel B. Piassick  
*EVP*

Mike C. Bauder  
*VP & Director of Compliance*

There are 15 professional and support staff personnel in the legal and compliance group, including eight attorneys. This team provides legal, compliance and risk management support to Harbert, its affiliates and fund portfolio companies. Harbert’s legal staff also manages the Harbert Funds’ relationships with outside legal counsel.

Our compliance group includes our chief compliance officer, two assistant directors of compliance and support staff. The compliance group is responsible for implementing policies and procedures to ensure Harbert, its employees and its Funds comply fully with all applicable laws and regulations, as well as Harbert’s Code of Ethics.

## Investor Relations

*“Over the last 12 months we have added Institutional Investors from around the world which has increased the breadth and diversity of our investor base.”*

*Charles Miller / Executive Vice President & CFO / Investor Relations*



*- back row -*

Michael J. Larsen  
*Managing Director*

Lynette P. Horton  
*Managing Director*

Carlton M. Forrester  
*Managing Director*

*- front row -*

Charles D. Miller  
*EVP & Chief Financial Officer*

Rest B. Heppenstall  
*Managing Director*

Our Investor Relations group is structured to serve as the interface between our investors and the entire Harbert organization. All of our Investor Relations professionals are knowledgeable about the full array of the firm's products and work with existing and prospective investors in understanding and defining their investment needs. Each of the Investment Relations professionals is a licensed Registered Representative with the NASD and, where appropriate, the FSA. The group is headquartered in Birmingham but has offices in New York and London to serve those vibrant markets.

Within investor relations, our communications group produces and manages all of our marketing and investor relations material, including the Harbert Web site ([www.harbert.net](http://www.harbert.net)) and this annual report. In addition, the communications department maintains the firm's intranet, produces a quarterly internal newsletter, manages certain investor communications and coordinates special communication needs for all of our offices, such as press releases.

# harbert realty services, inc.

Harbert Realty Services, Inc., a subsidiary of Harbert Management Corporation, is a full-service, commercial real estate company. Actively involved in all areas of commercial brokerage, the company's firsthand experience in development, leasing, market analysis, property management and finance increases the value it provides to real estate investors.

Harbert Realty Services also provides support to broader Harbert activities, including due diligence services, local market expertise and consulting support for strategic real estate needs and financial consolidation. The company provides real estate management and leasing services for selected Harbert properties and for the properties of other major corporate clients.

*...the company's firsthand experience in development, leasing, market analysis, property management and finance increases the value it provides to real estate investors.*

Harbert Realty Services' Corporate Services Group (CSG) is a commercial real estate service provider with transactional and advisory capabilities. CSG's various offices provide assistance nationwide to maximize the total portfolios of CSG's partners, rather than focusing on the singular transactions approach of traditional brokerages.

## COMMERCIAL SERVICES GROUP 2006 IN REVIEW

- Represented Amedisys, Inc., a national home healthcare provider, in acquiring 44 new locations in 16 states.
- Completed 35 branch bank site acquisitions over a seven-state region for AmSouth Bank (now Regions Bank).
- Opened new offices in Atlanta and South Florida to manage expanding client needs and new business opportunities.
- Selected to provide Lease Administration and Real Estate Accounting Services for VF Corporation (NYSE: VFC)—a Fortune 500 company. VF is the nation's second largest apparel company and the number one manufacturer of jeans in the U.S.
- Added the territories of Georgia (Atlanta), North and South Carolina and South Florida to its Corporate Real Estate Partnership with Regions Bank. Covering this additional territory will significantly increase transaction business and brokerage opportunities in these markets and, with new offices in Atlanta and South Florida, will provide a foundation for further development opportunities and other corporate services opportunities.

*“Our experience in the real estate business goes back decades. We approach every aspect of our business as an owner/manager. It’s how we entered the business and how we’ve managed to be successful over the years.”*

*Harry Lynch / President & Chief Executive Officer / Harbert Realty Services, Inc.*



Ken B. Findley  
*EVP-Marketing*

Mary C. Echols  
*EVP-Financial Services*

David R. Williams  
*EVP & COO*

Harry M. Lynch  
*President & CEO*

## Harbert Realty Services, Inc.

### 2006 IN REVIEW

- Completed the sale of The Shops at Market Square retail center in Ft. Myers, Florida. This high-end retail property was developed, fully leased and sold within an 18-month period.
- Acquired City Center office building in Altamonte Springs, Florida. This office property was acquired below replacement cost with an opportunity to add value through repositioning and development of a retail component on the site.
- Acquired a retail site in Oviedo (Orlando), Florida, to develop a high-end retail and

specialty office building. This site represents one of the last developable parcels in a growing market with solid fundamentals.

### COMMERCIAL BROKERAGE SERVICES

#### 2006 IN REVIEW

Broker of record for the land sale of 180 acres to be developed as The Grove, an \$80 million mixed-use development centered in Hoover, Alabama.

# HERO

*Imagine yourself a young single mother of five. Your 10-year-old son's kidneys fail suddenly and his only hope for survival is you. Willingly, happily, you give up one of your own kidneys to help him live. But the act costs you valuable time at work and the necessities of living continue whether you can pay for them or not. Such was the plight of a young single mother in Birmingham. And such is the opportunity for the HERO Foundation to reach out and help when other options are unavailable. For this particular mother, the Foundation provided help with rent, food and bills for the months when the mother could not work.*

## Harbert Employees Reaching Out (HERO) Foundation

It is not enough to live, work and thrive in this world. Because we can, we have an obligation to help people in need in our community. It's an obligation our employees fully embrace. That's why we founded the HERO Foundation, to give our employees the means to reach out and affect the communities in which we live.

The HERO Foundation provides direct financial assistance to help people who have been affected by natural disasters, medical conditions or temporary financial hardships to regain their independence and self-sufficiency. We established HERO in 1998 after a tragic spring tornado season left dozens of people in Alabama without shelter, clothes or food. Since 1998, the Foundation has helped many individuals

and families in need of temporary assistance because of hardships, when no other safety net was available.

The committees that manage the Foundation are made up of employees from across the company. The Foundation's resources come from Harbert's employees, its affiliates and from contributions raised from the community during annual fundraisers. We learn of people in need from employee referrals and from several partners in the community, including Children's Hospital, Alabama Children's Rehabilitation Services and the Alabama Head Injury Foundation to name a few.

Each year, as Harbert celebrates its successes, few match the pride created by the actions of our employees through the HERO Foundation.

*"In reflecting over the past nine years of existence for the Harbert Employees Reaching Out Foundation, I feel our greatest accomplishment is that we have touched the lives of so many individuals and families. The fact that we have surpassed \$1 million in approved grants is the testament of our employees' belief and commitment that we have the ability to help those in need."*

*Margaret Russo / Manager-Hedge Fund Investor Reporting / Harbert Management Corporation*



*This past year, we had a unique opportunity to help a Birmingham family in need. The family recently adopted a young girl, a victim of Katrina and an abusive family life. We were able to donate an SUV to help make their lives just a little easier.*



*Harbert hosts a variety of events to raise money for the HERO Foundation. And while our offices do not typically resemble Santa's workshop, every year our employees collect hundreds of presents to make the holidays more cheerful for families in need.*

# management

## CORPORATE OFFICERS

Raymond J. Harbert\*\*  
Chairman & Chief Executive Officer

Michael D. Luce\*\*  
President & Chief Operating Officer

David A. Boutwell\*\*  
Executive Vice President & Chief  
Administrative Officer

William W. Brooke\*  
Executive Vice President & Managing Partner  
Venture Capital

William R. Lucas, Jr.\*  
Executive Vice President, General Counsel  
& Secretary

Charles D. Miller\*  
Executive Vice President & Chief  
Financial Officer

Joel B. Piassick  
Executive Vice President &  
Assistant Secretary

## INVESTMENT PROFESSIONALS

**ABSOLUTE RETURN STRATEGIES**  
Distressed/Event  
Philip A. Falcone\*  
Vice President & Senior Managing Director

Lawrence M. Clark  
Managing Director & Director of Investments

Howard P. Kagan  
Managing Director & Director of Investments

Emerging Markets  
Peter S. Lannigan  
Vice President & Senior Managing Director

Heather N. Leonard  
Vice President & Managing Director

Capital Structure/Convertible Arbitrage  
Eric D. Wong  
Vice President & Senior Managing Director

Merger Arbitrage/Event Driven  
Neil Kennedy  
Vice President & Senior Managing Director

## REAL ESTATE

Domestic Real Estate  
Michael P. White  
Vice President & Director of Investments

Alan C. Fuller  
Vice President & Director of Investments

European Real Estate  
Scott D. O'Donnell  
Vice President & Managing Director

Peter J. A. Land  
Principal & Director of Investments

## PRIVATE CAPITAL

Private Equity  
Donald R. Beard  
Vice President & Director of Investments

Michael A. Rowland  
Vice President & Director of Investments

Venture Capital  
William W. Brooke\*  
Executive Vice President & Managing Partner

Wayne L. Hunter  
Managing Partner

Mezzanine Capital  
John C. Harrison\*  
Vice President & Director of Investments

Independent Power  
Wayne B. Nelson, III  
President & Chief Executive Officer  
Harbert Power, LLC

Patrick E. Molony  
Executive Vice President & COO  
Harbert Power, LLC

## HARBERT REALTY SERVICES

Harry M. Lynch  
President & Chief Executive Officer  
Harbert Realty Services, Inc.

\* Board of Directors Member

\*\* Board of Directors and Executive Committee Member

# locations

Harbert Management Corporation  
Corporate Headquarters  
Birmingham Office  
[www.harbert.net](http://www.harbert.net)

Harbert Investor Relations  
[irelations@harbert.net](mailto:irelations@harbert.net)

## **BIRMINGHAM**

One Riverchase Parkway South  
Birmingham, Alabama 35244  
205 987 5500 tel  
205 987 5568 fax

## **NEW YORK**

555 Madison Avenue, 16th Floor  
New York, New York 10022  
212 521 6970 tel  
212 521 6971 fax

## **NASHVILLE**

618 Church Street, Suite 500  
Nashville, Tennessee 37219  
615 301 6400 tel  
615 301 6401 fax

## **RICHMOND**

1210 East Cary Street, Suite 400  
Richmond, Virginia 23219  
804 782 3800 tel  
804 782 3810 fax

## **LONDON**

34 Brook Street  
London W1K 5DN  
United Kingdom  
+44 (20) 7408 4120 tel  
+44 (20) 7408 4121 fax

## **HARBERT REALTY SERVICES**

1901 6th Avenue North, Suite 2001  
Birmingham, Alabama 35203  
205 323 2020 tel  
205 323 2026 fax  
[www.harbertrealty.com](http://www.harbertrealty.com)



## Harbert® Management Corporation

One Riverchase Parkway South  
Birmingham, Alabama 35244

205 987 5500 tel  
205 987 5568 fax  
[www.harbert.net](http://www.harbert.net)

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