InteleK
CORPORATE FINANCE

# Sanitised APES225 Valuation Report – 4 x Pizza Restaurants

## Key Case Facts About This Report For Reviewing Purposes

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|---|---|
| **Standards & Report Type** | This report is a Valuation Engagement and complies with the requirements of the Accounting Professional & Ethical Standards 225 ("APES225") Board who are an independent, national body that sets the code of ethics and professional standards with which members from CPA Australia, Chartered Accountants Australia and New Zealand (CA ANZ) and the Institute of Public Accountants (IPA) must comply. Although this report does not state compliance with the International Valuation Standards ("IVS"), InteleK always follows IVS guidance and best practise, while we also produce reports in compliance with IVS as needed. |
| **End Client Case Information** | We valued 80% of the equity/shares for tax planning purposes. Valuation Date: 30 June 2020. Report Date: 25 August 2020. |
| **InteleK's Clients** | InteleK was engaged by the majority shareholder of the subject company (the "Client"). We were referred the subject company through our network of financial intermediaries of accountants, lawyers, valuation firms and brokers. In this case by a tax focused accounting firm, where we then worked through the valuation directly with the Client. |
| **Process** | This project was typical in nature and followed a fairly standard process with InteleK.<br>1. InteleK was referred the Client via email from our accounting contact. We then gathered some basic information via email and organised an introductory 20 minute call with the Client.<br>2. We gathered further information on that call and explained the valuation process to the Client, educating them about valuation documentation, to logistics and how we produce the final number.<br>3. An engagement letter (contract) was issued to the Client detailing the project information clarified on the call.<br>4. Once the engagement letter was signed and paid, InteleK commenced the valuation. The Client emailed InteleK the necessary valuation documentation, from financials to our questionnaire in the days that followed.<br>5. Upon initial documentation analysis, InteleK then had follow up questions via email, with a 15 minute call that followed with company management.<br>6. Once an initial draft valuation number was developed, we sent the Client the draft numbers and had a 15 minute call to explain. Once they were content, we then delivered the draft report three business days later.<br>7. The Client then signed off on the report and the final report was issued.<br>8. You can expect a 7-10 business day turnaround for our average valuation engagement, from when InteleK receives all the necessary information. |
| **Pricing** | InteleK's valuation reports generally start at $2,500, up to $10,000. For further detail on what drives price within that range and a specific price for this example report, please speak with me directly. |

Re: Valuation of 80% of the Equity of Pizza Company Pty Ltd

Dear Mr Smith,

Pizza Company Pty Ltd

At your request and pursuant to your authorisation, we have conducted a valuation of 80% of the equity of Pizza Company Pty Ltd (hereinafter referred to as "Pizza Company" or "the Company"), as at 30 June 2020, which is detailed in this Valuation Report. It is our understanding that this valuation may be relied upon for tax planning purposes.

We have performed a Valuation Engagement (this "Valuation Report"), as defined by the Accounting Professional & Ethical Standards 225 ("APES225") of the Company as of or at the Valuation Date of 30 June 2020. This valuation uses going concern as the premise of value to arrive at an estimate of value, which was formed upon the review of the information listed in Appendix D: Sources of Information. The resulting estimate of value should not be used for any other purpose or by any other party. This valuation engagement was conducted in accordance with APES225.

This Valuation Report expresses its estimate of value as a conclusion of value and has been performed under the basic/standard of value of "Market Value", as defined by the Australian Taxation Office used herein, defined ordinarily as *"the price that would be negotiated in an open and unrestricted market between a knowledgeable, willing but not anxious buyer and a knowledgeable, willing but not anxious seller acting at arm's length."*

We have appraised a majority, controlling and privately marketable ownership interest in the assets of the subject company. Our Valuation Report consists of:

- This letter which identifies the subject and scope of this valuation and summarises our opinion of value.
- A report containing (i) descriptive data on the Company (ii) a discussion of the appropriate valuation Methodologies and the application of those Methodologies to the valuation of the Company and (iii) the conclusions attained throughout this analysis.

We are of the opinion that, subject to the qualifications made within the body of this report, the Market Value of 80% of the equity (shares) of the Company is:

| Conclusion of Value ($000's) | Value |
|---|---|
| 100% Controlling Privately Marketable Equity Value | $ 2,764 |
| Ownership Interest | 80.0% |
| 80% Pro Rata Equity Value Prior to Shareholder Level Discounts | $ 2,211 |
| Discount for Lack of Control (DLOC) | 0.0% |
| Discount for Lack of Marketability (DLOM) | 10.0% |
| Total Shareholder Level Discount Impact | 10.0% |
| **80% Controlling Equity Value Rounded** | $ 2,000 |

Therefore, based on the above, I conclude the **Market Value of 80% of the equity (shares) of the Company on a going concern basis is $2,000,000 (rounded) as at the Valuation Date of 30 June 2020.**

To arrive at our conclusion of equity (share) value before any secondary discounts, we defined and considered the following:

(i) **Operating Asset Value:** All operating assets such as furniture, fixtures & equipment ("FFE" or PPE) plus (+) all intangible assets, including business goodwill. Note: If any other short-term assets were to be included in an asset sale, these would be added (+) to the Operating Asset Value.

(ii) **Enterprise Value:** *Operating Asset Value* plus (+) normal net working capital (normal levels of short-term assets minus short term liabilities).

(iii) **Equity Value:** *Enterprise Value* minus (-) the value of all interest-bearing debt (long- and short-term component of debt) plus (+) other non-operating/surplus assets and liabilities (excess cash or working capital, non-core assets such as financial investments & real estate, etc.).

The above definition follows the accepted practices to arrive to a conclusion of value. We have made no investigation of, and assume no responsibility for, the title to or any encumbrances against Pizza Company Pty Ltd or its assets. Neither InteleK Corporate Finance, nor any of its employees have any financial interest in Pizza Company Pty Ltd, or its assets. We certify that the compensation received by InteleK Corporate Finance for this study is not in any manner contingent upon the conclusions stated. This report is subject to the limiting factors and assumptions which appear at the end of the report. We have no obligation to update this Valuation Report or our Conclusion of Value for information that comes to our attention after the date of this report.

*Andrew Mackson, CFA, ABV*

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## Executive Summary

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|---|---|
| Valuation Date | 30 June 2020 |
| Report Type | Valuation Report |
| Standard of Value | Market Value |
| Premise of Value | Going concern |
| Intended Use | Taxation and planning purposes |
| Client(s) | Mark Smith |
| Intended User(s) | Mark Smith & Pizza Company Pty Ltd |
| Subject Company | Pizza Company Pty Ltd |
| Level of Value | Majority, controlling, privately marketable ownership interest in 80% of the equity of the subject company. |
| Extraordinary Assumptions or Hypothetical Conditions | None |
| Valuation Currency | Australian dollar |
| Certifying Valuer | Andrew Mackson, CFA, ABV |

## Purpose and Scope of the Valuation

The valuation described in this Valuation Report "Report" was made for the purpose of expressing our conclusion of the Market Value of 80% of the equity of Pizza Company Pty Ltd (hereinafter referred to as "Pizza Company" or "the Company"), at the request of Mark Smith. The Valuation Date ("Valuation Date") is 30 June 2020 and it is our understanding that this valuation may be relied upon to for tax planning purposes.

In forming our conclusion of value, we have relied upon the information provided to us as detailed in Appendix D. We have not conducted a site review of the subject Company's premises, nor have we audited the Company's financial statements, which have been provided by the Company's Management and/or its financial advisors. We have no reason to believe that the provided financial statements and management accounts are not true or accurate.

We have not been advised of any changes during the valuation that will impact the business in the future. It's important to note that to arrive at a premise a value is a process that contains subjectivity and if provided with various information or exogenous events could change the conclusion of value, which we have not been advised as of the Valuation Date. This valuation process uses the standards defined by Accounting Professional & Ethical Standards 225 ("APES225") and different methodologies accepted to perform a valuation.

## Report Type

The scope of work is a Valuation Engagement written as a "Valuation Report", defined as:

(i) Its conclusion of value is expressed as either a single dollar amount or a range, with the currency being the Australian dollar;
(ii) It considers all relevant information as of the Valuation Date available to the valuer at the time of performance of the valuation;
(iii) The valuer conducts appropriate procedures to collect and analyse all information expected to be relevant to the valuation; and
(iv) The valuation considers all conceptual approaches deemed to be relevant by the valuer.

## Standard and Premise of Value

The International Valuation Standards ("IVS") Section 104 Bases of Value is based on the key concept that it is a valuer's sole responsibility to choose the relevant basis (or bases) of value according to the terms and purpose of the valuation assignment.

The standard of value selected for the valuation of Pizza Company is “Market Value” which is defined by the Australian Taxation Office as *“the price that would be negotiated in an open and unrestricted market between a knowledgeable, willing but not anxious buyer and a knowledgeable, willing but not anxious seller acting at arm's length.”*

There are two primary Premises of Value for valuing a company:

1. **Going-Concern:** Going-concern value refers to a company that has the resources to continue the operation indefinitely; and
2. **Liquidation:** A liquidation premise of value refers to the value of a company if operations are ceased and the assets are sold off separately. Within liquidation value, assets may be valued under an orderly liquidation value where assets are assumed to be sold over a reasonable period of time to maximise the proceeds received, or under forced liquidation where they are sold under quick or forced terms, often resulting in lower values than under an orderly liquidation.

The appraisal was performed under the premise of value of going concern.

**Valuation Date:** This valuation is made as of 30 June 2020.

**Report Date:** This report is prepared as of 25 August 2020.

**Assets Appraised:** The scope of this valuation is limited to the 80% of the equity/shares of Pizza Company Pty Ltd.

**We note that some of the numbers in this Report have been modified from the original valuation for sanitisation purposes.**

## Business Description

***Details removed for sanitisation purposes.***

Pizza Company claimed signature dishes are as follows:

- Pizza
- Pastas
- Risotto
- Calzones
- Caprese Salads
- Lasagne

Due to Pizza Company's continued expansion during the last eight years growing to the now fourth locations, the Company's revenue has grown at a compound annual growth rate ("CAGR") of 10.65% over the last 4 years. Despite the expansionary plan in the past 8 years by Pizza Company, at the Valuation Date, they do not have any plans to open new locations in the foreseeable future.

## Economic & Industry Analysis

Where possible to quantify, we have considered both the economic and industry factors in our financial projections for Company. Other factors have been accounted for in our estimation of the required rate of return for the Company, as discussed in more detail further within this report.

### Australian Economy[1]

**Gross Domestic Product**

The economy contracted by 0.3% in the March quarter, leaving annual GDP growth at 1.4%, the weakest annual rate since 2009. This is the result of the bushfires and the early impacts of COVID-19. In per capita terms the economy contracted by 0.7% in the March quarter.

**Consumer Spending**

Household consumption contracted in the first quarter of 2020, falling by 1.1% over the quarter, and 0.2% over the year. Consumption doesn't contract very often – largely because of first needs goods, like food and utilities – and the decline to activity in the March quarter was the largest since 1986.

**Government Spending**

Government spending rose by 1.2% Quarter on Quarter ("q/q") and contributed 0.3 ppt to quarterly growth. The vast majority of the growth is in Government consumption; growth in Government consumption was already strong and has been boosted by the bushfire and COVID-19 response. In the March quarter, Government consumption grew by 1.8% q/q and contributed 0.3 ppt to growth over the quarter.

**Investment**

Private business investment saw mixed fortunes in Q1, leaving it as a neutral force on quarterly GDP. However, indicators suggest investment will drag on growth in the period ahead.

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[1] Quarterly Economic Update: Q1-FY20. EY Australia. June 2020.

Non-mining private business investment contracted by 1.7% in Q1, which was offset by mining investment and continued its expansion growing by 3.6% q/q and 10.3% through the year.

Purchases of machinery and equipment fell by 1.6% in Q1 detracting 0.1 ppt from growth, reflecting firms scaling back their expansion plans. However, non-residential construction rose slightly, by 0.3% q/q.

**Unemployment**

The labour market was steady in Q1, with unemployment averaging 5.2% over the quarter, unchanged from the Q4 average. However, spare capacity rose with under-employment rising to average 8.7% over the quarter, compared with 8.4% over Q4 2019.

**Consumer Prices and Inflation**

Inflation undershot the RBA's 2-3% target band for the 17th consecutive quarter, with underlying inflation as measured by the trimmed mean at 1.8% y/y in Q1. Headline inflation nudged higher, to an annual rate of 2.2%.

**Interest Rates**

In March, the Reserve Bank of Australia board decided the following: reduce the cash rate target to 0.25 per cent; a target for the yield on 3-year Australian Government bonds of around 0.25 per cent; a term funding facility for the banking system, with particular support for credit to small and medium-sized businesses; and exchange settlement balances at the Reserve Bank will be remunerated at 10 basis points, rather than zero as would have been the case under the previous arrangements. These decisions were maintained throughout the second quarter of 2020.[2]

**Small Business Confidence**

In March business confidence plummeted to an all-time low as businesses grappled with the early fall out from the pandemic, supply chain disruptions, and social distancing policy. The profit environment is weak, overall profits in the March quarter rose by just 1.1%, but for small businesses, they fell by 10%.

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[2] Reserve Bank of Australia Statements by Philip Lowe: Monetary Policies Decision. https://www.rba.gov.au/media-releases/2020/

Faced with these challenges, the focus for many businesses is on survival, not expansion. Forced hibernation, restrained cash flow and the possibility of a recession are all working against the intended boost of low interest rates, and capex plans reflect that.

**Economic Outlook**

The economic outlook remains one of recessionary conditions and a very weak labour market. The economy is likely to begin recovering in Q3, but it will be a long bumpy road, and government support is going to be required for some time to come. Boosting consumer and business confidence is critical to generating a sustainable recovery.

Note that Q1 GDP results don't tell us much about the full impact of COVID-19 nor the effectiveness of the policy response to date, however, understanding the dynamics at play before the onset of the pandemic is important.

**Economic Impact on Company Value**

The current conditions of the overall economy will continue to have repercussions on the discretionary income of households, which will impact the sales of Pizza Company. On the other hand, due to lockdown restrictions promoting delivery services, this is a net positive to the Company. Accordingly, during the recovery stage and whilst the economy idles below full capacity in anticipation of a COVID-19 vaccine, we expect the economic backdrop to have a net neutral impact on the valuation.



## Industry Analysis[3]

The Company is part of the Pizza Restaurants and Takeaways industry. Below we outline a brief summary of the industry.

**Pizza Restaurants and Takeaways**

Company's within the industry of Pizza Restaurants and Takeaways primarily prepare and serve traditional and gourmet pizzas, sides, beverages and desserts. Industry players take customer orders either over the phone, online or in person. Pizzas can be served either on the premises, taken away by the customer or delivered. The major firms in Australia who offered these services are Domino's Pizza and Out of the Box Group.

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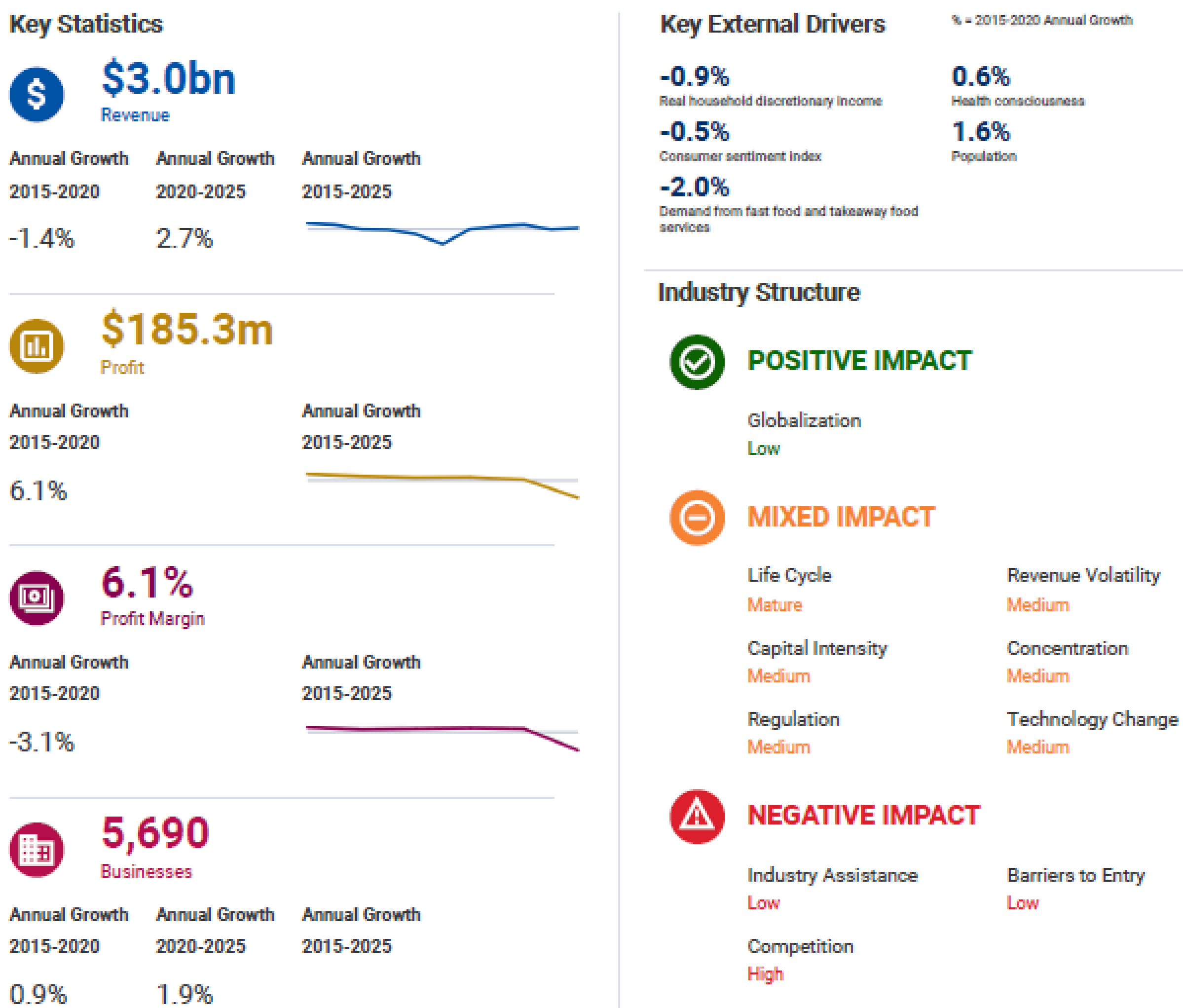
[3] IBISWorld Report ID: OD4025, Pizza Restaurants and Takeaway in Australia Industry Report. June 2020.

Although traditional pizzas have remained popular with Australians, consumer preferences have shifted as consumers have embraced gourmet and healthier options. The effects of COVID-19 are anticipated to negatively affect the industry as social distancing measures restrict dining in options and reduce foot traffic. The ability for industry operators to offer home delivery is likely to somewhat offset this decline. Industry revenue is expected to fall at an annualised 1.4% over the five years through 2019-20, to $3.0 billion.




### Competitive Landscape

The Pizza Restaurants and Takeaway industry faces a high level of competition, with this trend intensifying over the past five years; however, competition is expected to ease in the latter half of 2019-20, due to many cafes and restaurants closing due to social distancing measures. Industry participants compete based on price, product range, marketing, size of operations and reputation. Retailers have also been affected internally by changing consumer tastes and preferences and growing consumer awareness about the fat content of fast food. Externally, the industry is subject to competition from other fast-food services and restaurant operators.

According to IBISWorld, the key success factor of the industry are as follows:

- *Prompt delivery to market:* Pizza delivery establishments must offer prompt and reliable services while still being wary of the costs involved.
- *Ability to quickly adopt new technology:* New technology and the growing prevalence of online communication have changed the way industry operators take orders and engage with customers. Industry firms that adopt new software and cloud computing platforms can further increase revenue.
- *Proximity to key markets:* Industry firms that are located close to key markets can provide added convenience, drive impulse sales and deliver products faster.

**Industry Outlook**

Over the next five years, industry participants will likely continue adopting new technology and systems to improve customer experiences and operational efficiencies. As Australian cities expand, system requirements are anticipated to increase, and franchise owners will be best positioned to tap into these new markets. However, independent operators that can successfully differentiate themselves from large chains are also likely to access these new markets.

Economic recovery from COVID-19 over the next five years is also forecast to benefit industry operators, as consumer sentiment is projected to rebound. Nevertheless, this recovery is expected to begin in the latter half of 2020-21, as social distancing restrictions are likely to continue affecting industry operators throughout 2020. Overall, industry revenue is forecast to increase at an annualised 2.7% over the five years through 2024-25, to $3.5 billion.

## Financial Review

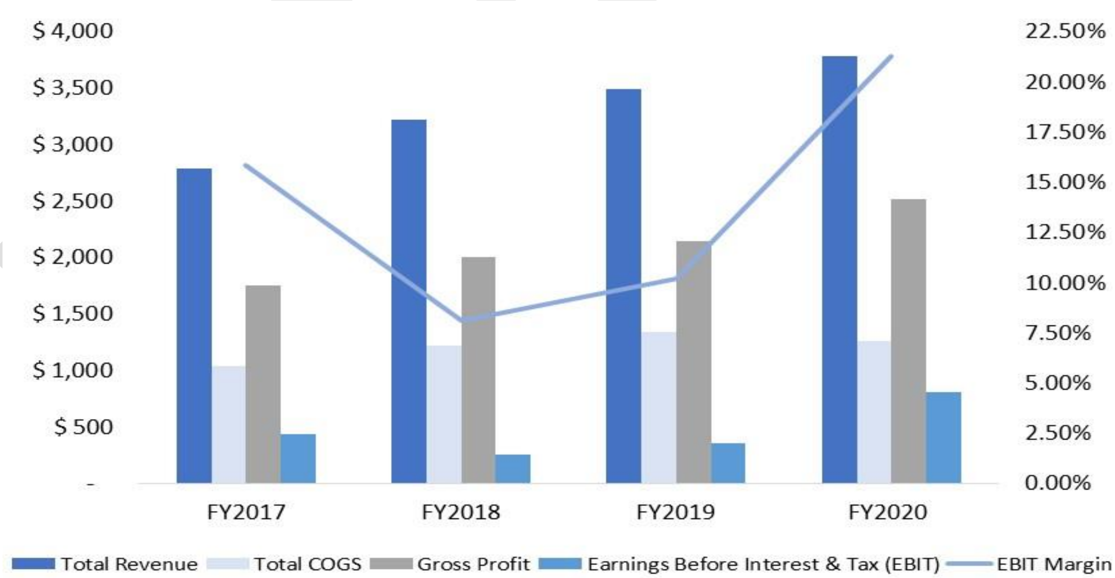
In forming our conclusion of value of the Company, we have analysed the Company's financial performance and position over the Financial Years from 2016 to 2020 inclusive ("the Period"). The Financial Year ("FY") for Pizza Company is a twelve month period ending 30 June. In doing so, we have reviewed the Company's profit and loss statements and balance sheets (statements of position). Refer to appendixes E, F, and G for further details.

### Income Statement

| ($000's) | FY2017 | % | FY2018 | % | FY2019 | % | FY2020 | % |
|---|---|---|---|---|---|---|---|---|
| Total Revenue | $ 2,795 | 100% | $ 3,224 | 100% | $ 3,490 | 100% | $ 3,786 | 100% |
| Total COGS | $ 1,041 | 37.25% | $ 1,219 | 37.81% | $ 1,344 | 38.51% | $ 1,267 | 33.47% |
| Gross Profit | $ 1,754 | 62.75% | $ 2,005 | 62.19% | $ 2,146 | 61.49% | $ 2,519 | 66.53% |
| Total Operating Expenses | $ 1,311 | 46.89% | $ 1,743 | 54.07% | $ 1,789 | 51.25% | $ 1,862 | 49.18% |
| EBIT | $ 443 | 15.86% | $ 262 | 8.12% | $ 357 | 10.24% | $ 807 | 21.32% |
| EBT | $ 429 | 15.34% | $ 248 | 7.70% | $ 345 | 9.89% | $ 796 | 21.02% |
| NPAT | $ 311 | 11.12% | $ 180 | 5.58% | $ 250 | 7.17% | $ 577 | 15.24% |

Note: (1) Information from Company Financial Statements. (2) EBIT = Earnings before interest and taxes. (3) EBT = Earnings before taxes. (4) NPAT = Net profits after taxes.

**Financial Performance FY2017-2020**




Note: Information from Company Financial Statements.

**Performance Commentary**

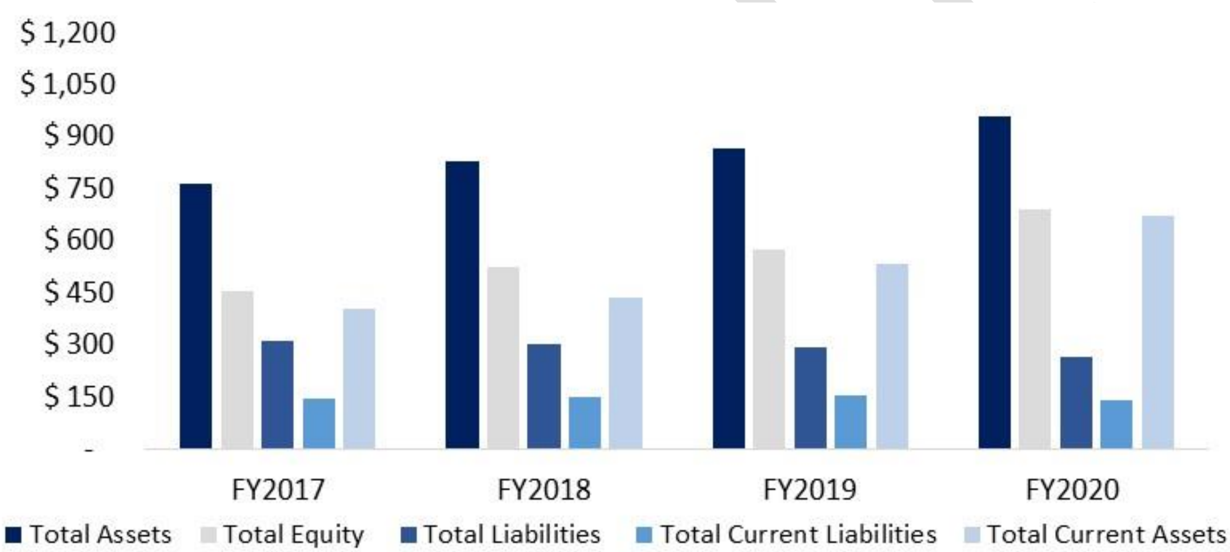
- **Revenue:** Revenue grew fairly consistently over the analysed Period, from FY2017 to FY2018 it grew 15.35% mostly explained due to the opening of their new location. In FY2020 revenue grew from a base of $3,490,480 in FY2019 to $3,786,311 (an 8.48% growth). Growth in FY2020 was positively impacted by an increase in demand for delivery services due to the COVID-19 lockdowns, which attributed to 5% growth of Pizza Company's sales in FY2020.
- **Total COGS:** COGS increased slightly as a percentage of sales from 37.2% to 38.5% between FY2017 and FY2019. In contrast, in FY2020 the total COGS reduced to 33.5% due to a change in suppliers.
- **Total Operating Expenses:** Operating expenses were $1,310,583 (46.9% of sales) in FY2017, before increasing in FY2018 as a percentage of sales to 54.1% due to the new location opening. However, the total operating expenses fell progressively in FY2019 and FY2020, falling to 49.2% of sales.
- **EBIT Margin:** EBIT margins experienced some volatility due to the increased operating expenses in FY2018. In FY2017 the margin was 15.9% before declining in FY2018 to 8.1%. During the following years, the margin continuously improved, surpassing FY2017 with a 17.4% margin in FY2020.

## Historical Balance Sheet

| ($000's) | FY2017 | % | FY2018 | % | FY2019 | % | FY2020 | % |
|---|---|---|---|---|---|---|---|---|
| Total Current Assets | $ 405 | 53.0% | $ 437 | 52.7% | $ 534 | 61.6% | $ 671 | 70.1% |
| Total Assets | $ 765 | 100% | $ 829 | 100% | $ 868 | 100% | $ 958 | 100% |
| Total Current Liabilities | $ 143 | 18.7% | $ 149 | 18.0% | $ 152 | 17.5% | $ 141 | 14.7% |
| Total Liabilities | $ 311 | 40.7% | $ 303 | 36.6% | $ 292 | 33.7% | $ 267 | 27.8% |
| Total Equity | $ 454 | 59.3% | $ 526 | 63.4% | $ 576 | 66.3% | $ 691 | 72.2% |

Note: Information from Company Financial Statements.

### Balance Sheet & Financial Position




Note: Information from Company Financial Statements.

### Financial Position Commentary

- **Total Current Assets:** Current assets were primarily cash and were consistently higher than the current liabilities in each year of the analysed period, whilst they made up the majority of total assets in all years.
- **Total Liabilities:** Total liabilities have been decreasing progressively each year as the Company decided to continue to pay down debt from free cash flow. Total liabilities were $311,300 in FY2017 and had decreased to $266,791 by FY2020.
- **Total Equity:** Total equity continued to grow year on year driven by positive operational cash flow from the income statement to retained earnings. In FY2017 the total equity of the Company was $453,736 and by FY2020, had increase by $237,477 to $691,213.

## Valuation Approaches and Methodologies

Business valuation is guided by two fundamental economic principles:

1. **Principle of 'Future Benefits':** A rational buyer will not buy an asset at a price that exceeds the cash flows that the asset is expected to generate in the future, adjusted for risks associated with achieving those streams of cash flows and time value of money.
2. **Principle of 'Substitution':** A rational buyer will not buy an asset at a price that exceeds the cost to acquire or recreate a similar asset, with similar or greater economic utility.

Generally accepted valuation principles require reliance on three basic approaches:

1. The Income Approach;
2. The Market Approach; and
3. The Asset Based (Cost) Approach.

These Approaches are generally based upon the capitalisation/discount of income, the market/stock exchanges for comparable assets and the cost to reproduce the assets. The Income, Market and Cost Approaches are briefly summarised below.

### Income Approach

The Income Approach is a valuation technique that capitalises or discounts the anticipated income from an appraised asset. This approach is predicated on developing either cash flow or income projections which are then discounted for time and risk.

The main business valuation Methods for SMEs under the Income Approach are:

1. Discounted Cash Flows ("DCF"); and
2. Capitalisation of Future Maintainable Earnings ("FME").

*Discounted Cash Flows:* The Methods such as DCF that utilise a 'stream of earnings' is known as the discounting Methods. The discounting Methods directly account for the time value of money and determine the value of the business enterprise as the present value of the projected earnings/income stream. The risk is quantified by means of the discount rate.

*Capitalisation of Future Maintainable Earnings:* The Methods such as the Capitalisation of FME which rely upon a single value of business earnings are referred to in general as direct capitalisation Methods. A 'single measure of earnings' is an identified earnings number based on historical figures, which are believed to be the most probable representation of maintainable earnings into the future. The risk is then quantified by means of the capitalisation rate.

The selection of these methods depends on the historical performance and the ability to forecast the future, of the company under valuation.

## Market Approach

The Market Approach is another approach that provides an indication of value by comparing the asset under valuation with identical or comparable (that is similar) assets for which price information is available. This comparison measure is the estimated market value based on market prices in actual transactions that have recently been established in the market. After studying the selling prices, value adjustments are made for comparability differences.

The main business valuation Methods for SMEs under the Market Approach are:

1. Comparative Private Company Method;
2. Comparative Public Company Method; and
3. Comparative Prior Transactions Method.

*Comparative Private Company Method:* The Comparative Private Company Transaction Method uses historical transactional data of private companies that provide a reasonable basis for comparison to the relevant investment characteristics of the company being valued. Guideline companies are used as a basis to develop valuation conclusions with respect to the subject company under the presumption that a similar market exists for the subject company as exists for the guideline private companies.

*Comparative Public Company Method:* The Comparative Public Company Method uses historical transactional and trading data of public companies that provide a reasonable basis for comparison to the relevant investment characteristics of the company being valued. Guideline public companies are used as a basis to develop valuation conclusions with respect to the subject company under the presumption that a similar market exists for the subject company as exists for the guideline publicly traded companies.

*Comparative Prior Transactions Method:* The Comparative Prior Transaction Method uses recent transactions involving the Company's stock. The principle of substitution is used to determine the value. This simply means that if one arm's length fair market value transaction occurred at a given price then if nothing has substantially changed, another arm's length fair market value transaction would occur at the same price.

The selection of these Methods depends on the comparative transactional data available.

## Asset Based (Cost) Approach

The Asset Based Approach (or the Cost Approach) provides an indication of value using the economic principle that a buyer will pay no more for an asset than the cost to obtain an asset of equal utility (benefit).

The main business valuation Methods for SMEs under the Asset Based Approach are:

1. Book Value Method;
2. Adjusted Net Assets Method; and
3. Orderly Liquidation Method.

*Book Value:* The book value Method simply calculates the book value, which is an accounting-based value that is calculated by subtracting the book value of total liabilities from the book value of total assets. This method takes as fact that the underlying assets are the driving factor in the valuation of the company and that the fair market value is approximated by the book value.

*Adjusted Net Asset Value:* Determination of asset value begins with the company's reported financial statements. Adjustments are made, as necessary or appropriate, to reflect the market values of the corporation's assets and liabilities, as opposed to their book values. The objective is to arrive at a net asset value, which is defined as the difference between the adjusted valuation of all assets and liabilities. Net asset value should reflect the valuation of assets and liabilities in the context of a going concern. Therefore, net asset value is not the company's liquidation value (Orderly or otherwise) because liquidation value assumes that the business is not a going concern.

*Orderly Liquidation Value:* The Orderly Liquidation Value of the company's assets is another method that is generally not considered appropriate for valuing operating entities. If the company is being valued as a going concern, it will not be able to liquidate its assets and continue operations. However, if the company is being liquidated or the ownership interest being valued has the ability to liquidate the company and would receive a higher return on investment from the liquidation, the liquidation value may be the company's best indication of value.

The Orderly Liquidation Value method develops a value by adjusting the reported book values of a subject company's individual assets to their actual or estimated fair market values as if they were to be sold in an orderly, piecemeal manner and subtracting the associated liabilities adjusted to their actual or estimated fair market liquidation value.

The selection of these Methods often are heavily influenced by the structure of the balance sheet and premise of value.

## Approaches Used

Under ideal circumstances, all three Approaches may be applicable to the valuation of an asset. For certain types of assets, one or more valuation Approaches may be inappropriate. In certain instances, results indicated by one Approach may vary widely from the other two Approaches. When this situation exists, the valuer must discern the reasons for this difference and select the Methods that best represent the considerations of both a willing and knowledgeable buyer and seller.

In valuing Pizza Company, we have formed our conclusion of value using the Income Approach. We decided the Capitalisation of FME would be the best method since the Company has reached a relatively stable revenue level following the opening of its fourth store/location. Additionally, we have not been provided with any financial projections nor expansion plans for the Company for the coming years.

In the following section of this report, we describe the valuation Methods utilised in estimating the value of the Company as a going concern.

### Income Approach – Capitalisation of FME

To determine the Company's value using this Approach, we use the FME as the basic measure of the Company's earning power. To establish what is the FME of the Company, we have used the metric of "normalised earnings", defined as the normalised debt-free pre-tax income available to both debt and equity investors.

We note that most businesses receive revenue and incur costs from time to time that could be considered to be:

(i) Non-recurring in nature, that is an expense that is considered a "once off" expense, not being repeated in the various financial periods;

(ii) Non-cash in nature, that is an expense or income is recorded but no cash is paid out or received); and/or

(iii) Non-commercial in nature, that is they are not required for or derived from the Company's usual activities, not at arms-length or market rates.

Based on the above, this normalisation of the Company's Income Statement has been performed to arrive at a FME measure. The differences between the operating and normalised profits for the Period are as follows:

| ($000's) | FY2017 | FY2018 | FY2019 | FY2020 |
|---|---|---|---|---|
| **Adjusted Income Statement** | | | | |
| Total Revenue | $ 2,795 | $ 3,224 | $ 3,490 | $ 3,786 |
| Earnings Before Tax (EBT) | $ 429 | $ 248 | $ 345 | $ 796 |
| **Total Adjustments to EBT** | $ (18) | $ (28) | $ 2 | $ (127) |
| **Adjusted Debt-free Pre Tax Income** | **$ 410** | **$ 221** | **$ 347** | **$ 669** |

Note: Derived from adding and adjusting non-recurring, non-cash, and non-business related expenses from financial statements. Please see appendix F for further details.

In establishing the FME, we have analysed the last four historical financial years (2017-2020) to build a picture of what we believe will be the future maintainable earnings of the Company, moving forward. We have selected the normalised earnings as the most appropriate earnings metric for FME, as management decisions can impact and potentially skew interest and taxes, impacting the "usability" of other earnings metrics (such as net profit).

Given we made a range of adjustments in establishing the normalised earnings of the Company that could only be made by a controlling shareholder ("Controlling Adjustments"), this will ultimately then yield a value that is on a controlling interest basis, making no further enterprise level discounts or premiums applicable to arrive at a controlling valuation.

In order to arrive at an FME figure, we weighted each year considering the historic growth driven by the opening of new stores/locations, making FY2017 and FY2018 in our opinion following consultation with management, not reflective of the future performance of the Company with all four locations fully operational. Whilst we have also considered the impact of COVID-19 on both historic sales in FY2020 and the impact on future performance, which we believe to be broadly neutral moving forward for the Company. Accordingly, in deriving the FME of the Company, we have weighted FY2019 and FY2020 equally 50% each as we see an equal probability of those year's financial performance moving forward.

The weighted average FME calculation is summarised below:

### Future Maintainable Earnings (FME)

| Financial Year | Normalised Earnings | Weighting | Weighted Value |
|---|---|---|---|
| 2017 | $ 410 | 0% | - |
| 2018 | $ 221 | 0% | - |
| 2019 | $ 347 | 50% | $ 173 |
| 2020 | $ 669 | 50% | $ 334 |
| **Weighted Average Adjusted = FME** | | **100%** | **$ 508** |

Note: Information from Company's adjusted normalised earnings of Financial Statements. Normalised earnings and weighted value are expressed in thousands ($000's).

**The estimated FME is $508,000.**

### Adjusted Net Cash Flow available to Total Invested Capital ("TIC")

With the estimated FME, which is the weighted average of the normalised earnings shown above, we then need to adjust this to find the net cash flow available to total invested capital (both debt and equity financing sources). The procedure is as follows:

| Metric ($000's) | | Amount |
|---|---|---|
| Normalised Earnings | | $ 508 |
| Less: Tax | 25.00% | $ 127 |
| Adjusted Debt-free Net Income (earnings available to TIC) | | $ 381 |
| Plus: Depreciation on Expansionary CAPEX (annually going forward) | | - |
| Less: Expansionary CAPEX (annually going forward) | | - |
| Less: Net Working Capital (annually going forward) | | $ (0.38) |
| **Adjusted Net Cash Flow available to Total Invested Capital (TIC)** | | **$ 380** |

Note: Deriving normalised earnings to Total Invested Capital.

### Assumptions

- **Taxes:** The income tax rate is estimated at 25% considering the expected changes to the small business company tax rates set by the Australia taxation office ("ATO"), where it is expected that the corporate tax rate for small businesses will be lowered from 26% in FY2021 to 25% in FY2022 and beyond[4].
- **Capital Expenditures & Depreciation:** Management did not communicate any estimated expansionary Capital Expenditure ("CAPEX"); thus, no expansionary CAPEX nor associated depreciation were included in the calculation of total adjusted net cash flow

[4] Australian Taxation Office. https://www.ato.gov.au/rates/changes-to-company-tax-rates/.

available to TIC. We note that adjusted depreciation has been included in calculating the normalised earnings used to derive the FME of the Company. This depreciation amount is an estimation of the required annual maintenance or replacement CAPEX to sustain (not expand) the existing capital assets of the Company.

- **Working Capital Needs:** based on the historical net working capital of Pizza Company, we have estimated an immaterial change of $384 into perpetuity for the Company. In forming our opinion of the required incremental "normal" net working capital moving forward, we have excluded any surplus assets and identified excess cash for the estimation of the working capital needs.

**Adjusted Net Cash Flow available to TIC**

The adjusted net cash flow available to TIC is then increased by the long-term sustainable growth rate of the Company, that in the long-term, tends to converge to the natural growth rate of the economy. As the Company communicated that they believe their new stores from FY2019 onwards have reached maximum production capacity and they have no further growth/expansionary plans at the Valuation Date; we believe it reasonable to expect the Company to grow in line with the broader economy moving forward. We have selected a sustainable growth rate of 2.58% for the Company taking into consideration the annual growth of Australian nominal GDP over the last 15 years. The 2.58% growth rate is assumed to be a reasonable reflection of the future and the long-term macroeconomic trends of the Australian economy.

The adjusted net cash flow available to the Company is then increased by the long-term sustainable growth rate of the Company, to find next year's adjusted net cash flow available to the Company which is then discounted using an appropriate discount rate to identify the value of the total invested capital as of the Valuation Date.

**Discount rate**

To calculate the discount rate or weighted average cost of capital (WACC) we have used the Company's expected capital structure in the long run, as well as discussions with management. As previously mentioned, it results in a 100% equity-funded capital structure. Accordingly, the calculated weighted average cost of capital (WACC) is equal to the cost of equity of 18.39%. Refer to Appendix H for the full breakdown of the discount rate.

**Midyear Convention**

In the normal discounting process, it is assumed that the benefit stream is available to the hypothetical buyer at the end of the period. This is not always the case since sales and expenses occur over the course of a period. The benefit stream is then available during the period and not only at the end. To implement this logic, a midyear convention is used. The midyear convention calculates the present value of a benefit stream using arithmetic that presumes half is available before the midyear point and half is available after the midyear point. We have applied the midyear convention because it more closely represents the cash flows received by the subject entity.

**Capitalisation of FME Method**

With all the necessary inputs thus determined, discounting the net cash flow to TIC with the capitalisation rate of 15.81% (where the difference between the cost of capital/discount rate and the capitalisation rate is the long-term expected growth rate), and the application of the midyear convention, the final total invested capital is as follows:

| Variable ($000's) | Amount |
|---|---|
| Adjusted Net Cash Flow available to TIC (1) | $ 380 |
| Long Term Sustainable Growth Rate (2) | 2.58% |
| Next Year's Adjusted Net Cash Flow available to TIC (3) = (1)*[1+(2)] | $ 390 |
| Discount Rate (4) | 18.39% |
| (5) TIC = (3)/[(4)-(2)] | $ 2,468 |
| Midyear Convention Adjustment (6) | 1.09 |
| **Final Total Invested Capital (7) = (5)*(6)** | **$ 2,686** |

Note: Determination of Fair Market Value of Total Invested Capital.

**Indicated Income Approach Value**

To arrive at the indicated equity value, all the interest-bearing debt must be subtracted from the enterprise value and any surplus assets must be added, as illustrated in Appendix G.

| Valuation Calculations ($000's) | Value |
|---|---|
| **TIC (growth model with midyear convention)** | **$ 2,686** |
| Plus: Surplus Assets | $ 258 |
| Less: Interest-bearing debt | $ 180 |
| **100% Controlling Majority Privately Marketable Value Rounded** | **$ 2,764** |

Note: Information from our capitalisation of FME model and Company financials.

**Concluded Equity Value**

Our Conclusion of Value using the Income Approach is that a one hundred percent (100%) controlling interest is **$2,764,000 rounded** prior to any shareholder level discounts**.**

## Asset Based (Cost) Approach

**Book Value Method**

The Book Value Method simply calculates the book value, which is an accounting-based value that is calculated by subtracting the book value of total liabilities from the book value of total assets, resulting in the book value of net assets. This method takes as fact that the underlying assets are the driving factor in the valuation of the company and that the Fair Market Value is approximated by the book value.

While no inspection of the fixed assets of the business has taken place, having reviewed the Company's balance sheet in consultation with Company Management, we have made the assumption that the book values of assets and liabilities are an estimation of Fair Market Value. We are assuming this is the Fair Market Value under the premise of value as going concern. While other short-term assets and liabilities are assumed reasonably liquid and to approximate their Fair Market Values.

| Book Value as at 30 June 2020 ($000's) | |
|---|---|
| **Total Assets** | $ 958 |
| **Total Liabilities** | $ 267 |
| **Book Value of Equity** | **$ 691** |

The book value methodology from the Company's balance sheet identifies the equity value as **$691,000 rounded** prior to any shareholder level discounts. See Appendix G for the Company's Balance Sheet and the identification of surplus assets and liabilities.

## Approaches Considered and Rejected

While there are a range of Methods under the following Approaches that could be used to determine the Fair Market Value of a company, the specific facts of Pizza Company dictates that the following Approaches and any Methods within, were not appropriate. The following lists those Approaches and some of the Methods potentially applicable and the reasons why they were not used.

### Income Approach

**DCF Method:** The Discounted Cash Flows (DCF) method utilises a 'stream of earnings' to account for the time value of money directly and determine the value of the business enterprise as the present value of the projected earnings/income stream.

The DCF Methodology requires forecasting the 'stream of earnings' and having reasonable confidence in those forecasts. Given no forecasts were provided by management and they communicated that they do not have any reason to expect growth to differ from the historical linear trajectory, the DCF method was rejected.

### Asset Based (Cost) Approach

**Adjusted Net Assets Method:** The Adjusted Net Assets Method develops a valuation indication by adjusting the reported book value of a subject company's assets to their actual or estimated fair market values and subtracting its liabilities (adjusted to fair market value, if appropriate).

We were not provided with the adjusted fair market values nor did we conduct a physical inspection of the Company's assets. Accordingly, this method was rejected.

### Market Approach

A market-based company valuation relies upon the comparison of the subject company to similar guideline or comparable companies.

**Comparative Private Company Transaction Method:** The Comparative Private Company Transaction Method uses historical transactional data of companies that provide a reasonable basis for comparison to the relevant investment characteristics of the company being valued. Guideline companies are used as a basis to develop valuation conclusions with respect to the subject company under the presumption that a similar market exists for the subject company as exists for the guideline private companies.

This Method was rejected as insufficient private company comparable transaction data was available.

**Comparative Publicly Traded Company Transaction Method:** The Comparative Public Company Transaction Method uses historical transactional data of public companies that provide a reasonable basis for comparison to the relevant investment characteristics of the company being valued. Guideline companies are used as a basis to develop valuation conclusions with respect to the subject company under the presumption that a similar market exists for the subject company as exists for the guideline publicly traded companies.

This Method was rejected as insufficient public company comparable transaction or trading data was available.

**Comparative Prior Transactions Method:** The Comparative Prior Transaction Method uses recent transactions involving the Company’s stock. The principle of substitution is used to determine the value. This simply means that if one arm’s length fair market value transaction occurred at a given price then if nothing has substantially changed, another arm’s length fair market value transaction would occur at the same price.

This Method was rejected as no information was provided about prior transactions in the Company.

## Reconciliation of 100% Equity Value

We utilised the Capitalisation Method to calculate the value of one hundred percent (100%) of the equity of the Company under a control basis prior to any secondary discounts. We concluded that the value of one hundred percent (100%) of the equity of the Company on a control basis is as follows.

**Pizza Company, Pty Ltd Equity Values Under the Different Valuation Methodologies**

| Valuation Methodology ($000's) | 100% Equity Value | Methodology Weighting | Weighted Value |
|---|---|---|---|
| **Asset Based Approach** | | | |
| Book Value of Equity | $ 691 | 0% | CONSIDERED |
| **Market Approach** | | | |
| Comp. Private Comp. Trans. Revenue Multiple | REJECTED | N/A | N/A |
| Comparative Public Company Transaction | REJECTED | N/A | N/A |
| Comparative Prior Transaction | REJECTED | N/A | N/A |
| **Income Approach** | | | |
| Discounted Cash Flow | REJECTED | N/A | N/A |
| Capitalization of Income | $ 2,764 | 100% | $ 2,764 |
| **Conclusion of 100% Controlling, Privately Marketable Equity Value** | | **100%** | **$ 2,764** |

Note: Derived from capitalisation of future maintainable earnings and book value of equity.

In the sections to follow, we then calculate the value of the eighty percent (80%) shareholding under valuation.

## Shareholder Level Discounts and Other Considerations

Other important characteristics of an investment that need to be considered are:

1) **Lack of control:** the degree of lack of control versus a control position represented by the investment; and
2) **Lack of marketability/liquidity:** the degree of ready marketability or lack of marketability.

**Lack of Control:** A Discount for Lack Of Control ("DLOC") may be applied to the value of a non-controlling interest in a company. Conversely, a premium may be applied to the valuation of a company, or paid in a transaction for control, in which the ownership interest is a controlling position. If the equity holder has a control position, he or she can accelerate the receipt of the future benefits of the company and via management and operational initiatives, take direct steps to enhance the future benefits, or at least the probability that they will be generated. On the other hand, a non-controlling position in a privately held company is generally held at varying degrees of risk of being subject to the judgment, ethics and management skills of the controlling shareholder(s). Depending on a number of items, the impairment of value can be significant. The value of control is dependent on the shareholder's ability to exercise any or all of a variety of rights typically associated with control, that will affect those future benefits. Listed below are several common prerogatives of control:

- Elect directors and appoint management;
- Determine management compensation and perquisites;
- Set policy and change the course of business;
- Acquire or liquidate assets;
- Select people with whom to do business and award contracts;
- Make acquisitions of other companies;
- Liquidate, dissolve, sell out or recapitalise the company;
- Sell or acquire treasury shares;
- Register the company's stock for public offering;
- Declare and pay dividends;
- Change the articles of incorporation or bylaws;
- Block any of the above actions.

Obviously, many factors can impact the degree of control a shareholder has over the operations of a corporation or limited liability company. When any of the control elements are not available to the ownership interest being considered, the value attributable to a valuation developed under a controlling assumption must be reduced accordingly. Quantifying this amount is challenging and requires analysis of both the market driven observations/studies and the specific valuation case facts by experienced analysts. In our experience, we generally observe DLOCs in a range of up to 15%.

Importantly in the valuation of the Company, we have analysed the Company bylaws which give equal voting rights (among other rights) for each share held (i.e. all shares have equal voting rights). Accordingly, the eighty percent (80%) shareholding thus has 80% of the voting rights, more than sufficient for the simple majority terms of the Bylaws to have full control of the Company. Considering this and the other aforementioned factors, academic studies which analyse historical average DLOCs observed via transactions in the market, the shareholder splits of the Members of the Company and other factors, we believe that no DLOC should be applied to the eighty percent (80%) of the shares of the Company under valuation.

| Conclusion of Value ($000's) | Value |
|---|---|
| 100% Controlling Privately Marketable Equity Value | $ 2,764 |
| Ownership Interest | 80% |
| 80% Pro Rata Equity Value Prior to Shareholder Level Discounts | $ 2,211 |
| Discount for Lack of Control (DLOC) | 0.0% |

Note: Derived from our capitalisation FME model and Company's financial information; plus, conclusion of controlling interest.

**Lack of Marketability/Liquidity:** A discount for lack of marketability ("DLOM") reflects the fact that, unlike publicly traded companies, there is not a quick source of liquidity for owners of a closely-held business. This applies to both controlling and minority interests, however it is often significantly higher for minority and/or non-controlling interests as this makes the investment even more illiquid, given the lack of decision-making ability around when and how to "market" or "liquidate" the assets of the company. Practically speaking, if we had the same 30% shareholding of two smaller companies that were identical, however one was a public listed company (and thus given the 30% shareholding could be liquidated in a short time frame e.g. T+3) and the other was a private unlisted company, the enhanced liquidity available to the former has value and thus should be valued at a premium, under Fair Market Value.

There have been many studies undertaken over the years in the United States of America ("USA") in an attempt to understand the impact of marketability as a characteristic of equity ownership. Unfortunately, a similar level of academic literature is not available specific to DLOM in the Australian market to our knowledge, given our research. Accordingly, below and in our DLOM conclusions we analyse the studies and data developed in the USA, conscious of both the similarities and differences between these two developed markets. The USA based studies themselves are varied and complex and discounts remain an area of opinion and discretion. However, they can be generally classified into four general categories.

- Restricted Stock Studies, Private Placements, and Private Investment in Public Equity ("PIPEs");
- Pre-IPO Studies;
- Other Minority Public Stock Evidence such as Event Studies & Bid-Ask Spread Analysis; and
- Volatility & Other Quantitative Model.

The above methods and their findings are detailed within the USA based BVR's 'Guide to Discounts for Lack of Marketability', written by John Stockdale, Sr. The most recent and fifth edition details across 644 pages the theories, evidence, and techniques for determining DLOMs which we consider in our assessment of an applicable DLOM for the Company. Quantifying this amount is challenging and requires analysis of both the market driven observations/studies and the specific valuation case facts by experienced analysts. In our experience, generally we observe that DLOMs fall in a range of up to 40%, with the median lying between 20-30%. However, there are circumstances where the appropriate discount could be significantly larger than 40%.

Given we are valuing an eighty percent (80%) shareholding in the Company, with the remaining twenty percent (20%) of the shares held by another individual shareholder, we see the eighty percent (80%) shareholding as being less marketable than a one hundred percent (100%) shareholding. With a minority shareholder present, the eighty percent (80%) shareholding is a less attractive prospect as even with control, there is still another shareholder to be conscious of when making decisions that affect all shareholders. Whilst the eighty percent (80%) shareholder does not receive 100% of the profitability from their controlling position and potential time investment in the Company. Considering the above factors and academic studies which analyse historical average DLOMs observed via transactions in the market, we believe that a DLOM of 10% should be applied to the eighty percent (80%) of the shares of the Company under valuation.

| Conclusion of Value ($000's) | Value |
|---|---|
| 100% Controlling Privately Marketable Equity Value | $ 2,764 |
| Ownership Interest | 80.0% |
| 80% Pro Rata Equity Value Prior to Shareholder Level Discounts | $ 2,211 |
| Discount for Lack of Marketability (DLOM) | 10.0% |

Note: Derived from our capitalisation FME model and Company's financial information; plus, conclusion of marketability.

### Discounts Conclusion

We have applied the applicable shareholder level discounts to 80% of the value determined from 100% of the company, established under "Reconciliation of Value". Below is the breakdown of the discounts applied to the 80% shareholding.

| Conclusion of Value ($000's) | Value |
|---|---|
| 100% Controlling Privately Marketable Equity Value | $ 2,764 |
| Ownership Interest | 80.0% |
| 80% Pro Rata Equity Value Prior to Shareholder Level Discounts | $ 2,211 |
| Discount for Lack of Control (DLOC) | 0.0% |
| Discount for Lack of Marketability (DLOM) | 10.0% |
| Total Shareholder Level Discount Impact % | 10.0% |
| Total Shareholder Level Discount | $ 221 |
| **80% Controlling Equity Value Rounded** | $ 2,000 |

Note: Derived from our capitalisation FME model and Company's financial information; plus, conclusion of marketability and controlling interest.

## Conclusion of Value

We relied upon the Income approach in our Conclusion of Value of the Company. A full breakdown of these conclusions can be seen below:

| Conclusion of Value ($000's) | Value |
|---|---|
| 100% Controlling Privately Marketable Equity Value | $ 2,764 |
| Ownership Interest | 80.0% |
| 80% Pro Rata Equity Value Prior to Shareholder Level Discounts | $ 2,211 |
| Total Shareholder Level Discount Impact % | 10.0% |
| Total Shareholder Level Discount | $ 221 |
| **80% Controlling Equity Value Rounded** | $ 2,000 |

Note: Derived from our capitalisation FME model and Company's financial information; plus, conclusion of shareholder level discounts.

**The final conclusion of the Equity Value of the 80% shareholding of Pizza Company is $2,000,000 (rounded).**

Andrew Mackson, CFA, ABV

Head Business Valuer

InteleK Corporate Finance

25 August 2020.

## Appendix A: Valuation Analyst's Representations & Qualifications

**Andrew Mackson, CFA, ABV (White labelled, insert your credentials and company specifics)**

Andrew is one of the Co-founders of InteleK Corporate Finance and has broad experience across valuations, wealth management and ECM & DCM. Andrew is the Head of Business Appraisals and has performed over 150 business valuations primarily in the United States & Australia. Andrew is sector agnostic however only performs valuations that can be done remotely, via video calls with management, access to documentation online and where an on-site visit is not necessary. Andrew's experience has been valuing businesses with revenue between USD 1-20 million, up to as high as USD 120 million.

**Valuation Purposes**

- Internal purposes such as shareholder transactions, disputes & strategic planning;
- Gift and estate tax for the IRS/ATO;
- Buy/sell-side transaction support;
- Complex company structure/reversing related parties for fair market value;
- Mergers and acquisitions; and
- Financing purposes including SBA loans.

**Education & Qualifications**

- CFA (Chartered Financial Analyst) Charterholder since September 2017;
- Associate of the American Institute of Certified Public Accountants (AICPA);
- Accredited in Business Valuation (ABV) Holder since May 2020; and
- Duel Bachelors of Commerce and Economics from the University of Queensland, Australia.

**Other Professional Experience**

Corporate: Prior to co-founding InteleK, Andrew worked for Swiss Bank UBS (Sydney, Australia). Andrew commenced in Equity Research before moving to Wealth Management where he had broad experience facilitating and selling ECM & DCM transactions to the 100+ UBS Wealth Management client advisor base. Andrew was involved in over 70 transactions, across both DCM (listed hybrids and OTC debt for transactions raising $20.2bn) and ECM (block trades, placements, entitlements & IPOs for transactions raising $30.9bn).

Personal Private Equity: Andrew purchased a tourism business in January 2018 before exiting and executing its sale in September 2020 in a challenging COVID-19 impacted industry.

## Appendix B: Statement of Assumptions and Limiting Conditions

1. The conclusion of value arrived at herein is valid only for the stated purpose as of the date of the valuation.

2. Financial statements and other related information provided by the Company or its representatives, in the course of this engagement, have been accepted without any verification as fully and correctly reflecting the enterprise's business conditions and operating results for the respective periods, except as specifically noted herein. InteleK Corporate Finance has not audited, reviewed, or compiled the financial information provided to us and, accordingly, we express no audit opinion or any other form of assurance on this information.

3. Public information and industry and statistical information have been obtained from sources we believe to be reliable. However, we make no representation as to the accuracy or completeness of such information and have performed no procedures to corroborate the information.

4. We do not provide assurance on the achievability of the results forecasted by the Company because events and circumstances frequently do not occur as expected; differences between actual and expected results may be material; and achievement of the forecasted results is dependent on actions, plans, and assumptions of management.

5. The conclusion of value arrived at herein is based on the assumption that the current level of management expertise and effectiveness would continue to be maintained, and that the character and integrity of the enterprise through any sale, reorganisation, exchange, or diminution of the owners' participation would not be materially or significantly changed.

6. This report and the conclusion of value arrived at herein are for the exclusive use of our client for the sole and specific purposes as noted herein. They may not be used for any other purpose or by any other party for any purpose. Furthermore, the report and conclusion of value are not intended by the author and should not be construed by the reader to be investment advice in any manner whatsoever. The conclusion of value represents the considered opinion of InteleK Corporate Finance, based on information furnished to them by the Company and other sources.

7. Neither all nor any part of the contents of this report (especially the conclusion of value, the identity of any valuation specialist(s), or the firm with which such valuation specialists are connected or any reference to any of their professional designations) should be disseminated to the public through advertising media, public relations, news media, sales media, mail, direct transmittal, or any other means of communication without the prior written consent and approval of InteleK Corporate Finance.

8. Future services regarding the subject matter of this report, including, but not limited to testimony or attendance in court, shall not be required of InteleK Corporate Finance unless previous arrangements have been made in writing.

9. InteleK Corporate Finance is not an environmental consultant or auditor, and it takes no responsibility for any actual or potential environmental liabilities. Any person entitled to rely on this report, wishing to know whether such liabilities exist, or the scope and their effect on the value of the property, is encouraged to obtain a professional environmental assessment. YOUR COMPANY does not conduct or provide environmental assessments and has not performed one for the subject property.

10. InteleK Corporate Finance has not determined independently whether the Company is subject to any present or future liability relating to environmental matters (including, but not limited to CERCLA/Superfund liability) nor the scope of any such liabilities. YOUR COMPANY appraisal takes no such liabilities into account, except as they have been reported to YOUR COMPANY by the Company or by an environmental consultant working for the Company, and then only to the extent that the liability was reported to us in an actual or estimated dollar amount. Such matters, if any, are noted in the report. To the extent such information has been reported to us, YOUR COMPANY has relied on it without verification and offers no warranty or representation as to its accuracy or completeness.

11. InteleK Corporate Finance has not made a specific compliance survey or analysis of the subject property to determine whether it is subject to, or in compliance with, the American Disabilities Act of 1990, and this valuation does not consider the effect, if any, of noncompliance.

12. No change of any item in this appraisal report shall be made by anyone other than InteleK Corporate Finance, and we shall have no responsibility for any such unauthorised change.

13. Unless otherwise stated, no effort has been made to determine the possible effect, if any, on the subject business due to future Federal, state, or local legislation, including any environmental or ecological matters or interpretations thereof.

14. If prospective financial information approved by management has been used in our work, we have not examined or compiled the prospective financial information and therefore, do not express an audit opinion or any other form of assurance on the prospective financial information or the related assumptions. Events and circumstances frequently do not occur as expected and there will usually be differences between prospective financial information and actual results, and those differences may be material.

15. We have conducted interviews with the current management of the Company concerning the past, present, and prospective operating results of the Company.

16. Except as noted, we have relied on the representations of the owners, management, and other third parties concerning the value and useful condition of all equipment, real estate, investments used in the business, and any other assets or liabilities, except as specifically stated to the contrary in this report. We have not attempted to confirm whether all assets of the business are free and clear of liens and encumbrances or that the entity has good title to all assets.

## Appendix C: Certification of the Valuation Analyst

1. The statements of fact contained in this report are true and correct.
2. The analyses, opinions, and conclusion of value included in the valuation report are subject to the specified assumptions and limiting conditions, and they are the personal analyses, opinions, and conclusion of value of the valuation analyst.
3. I have no present or prospective interest of the property that is the subject of this report, and I have no personal interest with respect to the parties involved.
4. I have performed no services, as an valuer or in any other capacity, regarding the property that is the subject of this report within the three-year period immediately preceding acceptance of this assignment.
5. I have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.
6. My engagement in this assignment was not contingent upon developing or reporting predetermined results.
7. My compensation for completing this assignment is not contingent upon the development or reporting of a predetermined value or direction in value that favours the cause of the client, the amount of the value opinion, the attainment of the stipulated result, or the occurrence of a subsequent event directly related to the intended use of this appraisal.
8. My analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with APES225 and following guidance from the International Valuation Standards.
9. Cameron Braid, MBA assisted in the preparation of this report.
10. I have not made a personal inspection of the property that is the subject of this report.
11. No one provided significant real property appraisal assistance to the person signing this certification.



**Andrew Mackson, CFA, ABV**

Head Business Valuer

InteleK Corporate Finance

## Appendix D: Sources of Information

Source of Information Disclaimer:

Information in this report was obtained from management, including the owner Mr. Smith, public records and other sources considered to be informed and reliable. Therefore, I have relied upon the referenced information without independent verification.

Company Information:

- Pizza Company Financial Statements for the financial years 2017, 2018, 2019 & 2020;
- Pizza Company Partner Responsible Fees;
- Memo response to request for information;
- The Company's shareholder agreements;
- Additional information of client contracts and recurring clients; and
- Other Sources of Information:
    - IBIS World (Industry Report OD4025, Pizza Restaurants and Takeaway. June 2020);
    - Industry Betas, Salvidio & Partners;
    - Duff & Phelps Valuation Handbook, Guide to Cost of Capital; and
    - Australian Bureau of Statistics.

## Appendix E: Income Statement

| | FY2017 | FY2018 | FY2019 | FY2020 |
|---|---|---|---|---|
| **Income** | | | | |
| Net Revenues | $2,794,830 | $3,223,948 | $3,490,480 | $3,786,311 |
| *Revenue Growth Rate* | | 15.4% | 8.3% | 8.5% |
| **Total Revenue** | **$2,794,830** | **$3,223,948** | **$3,490,480** | **$3,786,311** |
| **COGS** | | | | |
| Cost of Goods Sold | $1,040,976 | $1,218,886 | $1,344,303 | $1,267,153 |
| **Other Costs** | $0 | $0 | $0 | $0 |
| **Total COGS** | $1,040,976 | $1,218,886 | $1,344,303 | $1,267,153 |
| **Gross Profit** | **$1,753,854** | **$2,005,062** | **$2,146,177** | **$2,519,157** |
| **Operating Expenses** | | | | |
| **Total Operating Expenses** | **$1,310,583** | **$1,743,296** | **$1,788,743** | **$1,861,949** |
| **Operating Income** | **$443,271** | **$261,765** | **$357,434** | **$657,209** |
| Cashflow boost ATO | | | | $50,000 |
| Jobkeeper Subsidy | | | | $100,000 |
| **Total Other Income** | | | | **$150,000** |
| **Earnings Before Interest & Tax (EBIT)** | **$443,271** | **$261,765** | **$357,434** | **$807,209** |
| Interest Expense | $14,560 | $13,440 | $12,320 | $11,200 |
| **Earnings Before Tax (EBT)** | **$428,711** | **$248,325** | **$345,114** | **$796,009** |
| Provision (Benefit) for Taxes | | | | |
| *Effective Tax Rate* | *27.5%* | *27.5%* | *27.5%* | *27.5%* |
| **Net Income** | **$310,816** | **$180,036** | **$250,207** | **$577,106** |

Appendix: Information from Company Financial Statements.

**Income Statement Continued – Operating expenses in full.**

| | FY2017 | FY2018 | FY2019 | FY2020 |
|---|---|---|---|---|
| **Operating Expenses** | | | | |
| Acounting fees | $23,043 | $32,856 | $33,049 | $32,654 |
| Advertising | $45,304 | $70,237 | $54,968 | $63,958 |
| Alarm Monitoring Service | $1,437 | $2,394 | $1,803 | $2,039 |
| Bank Charges | $27,948 | $36,219 | $41,412 | $45,572 |
| Consultancy fees | $35,869 | $36,945 | $38,053 | $75,069 |
| Depreciation | $89,957 | $97,965 | $83,372 | $71,698 |
| Penalty fees | $4,958 | $1,293 | $1,938 | $2,039 |
| Filing Fee | $465 | $564 | $349 | $465 |
| Insurance - General | $19,145 | $16,226 | $37,357 | $49,765 |
| Kitchen Supplies | $3,467 | $5,432 | $4,239 | $4,728 |
| Legal Costs | $8,596 | $12,943 | $15,394 | $22,934 |
| Licences & Fees | $2,403 | $3,204 | $2,803 | $3,104 |
| Meals & Entertainment | $12,958 | $23,958 | $2,234 | $5,039 |
| Miscellaneous Expense | $9,049 | $1,396 | $21,086 | $12,345 |
| Motor Vehicle expenses | $7,594 | $12,049 | $33,405 | $22,034 |
| Office Expense | $5,628 | $22,938 | $10,293 | $6,274 |
| Other Supplies | $14,382 | $14,905 | $17,708 | $22,467 |
| Pest control | $8,094 | $1,395 | $1,593 | $4,857 |
| Postage | $0 | $322 | $0 | $506 |
| Printing and stationery | $123 | $498 | $142 | $80 |
| Rent | $174,303 | $250,498 | $258,013 | $265,753 |
| Repairs & Maintenance | $24,592 | $35,847 | $58,308 | $54,307 |
| Salaries & Wages | $624,092 | $819,678 | $830,436 | $839,154 |
| Staff training | $1,203 | $3,294 | $1,890 | $1,123 |
| Superanuuation Contribution | $59,289 | $77,869 | $78,891 | $79,720 |
| Telephone | $9,049 | $15,948 | $7,584 | $8,495 |
| Travel Expense | $61,748 | $95,244 | $105,692 | $112,054 |
| Uniforms | $5,646 | $13,081 | $2,748 | $15,228 |
| Utilities | $9,847 | $13,049 | $15,049 | $8,094 |
| Workers Comp Insurance | $20,394 | $25,049 | $28,934 | $30,394 |
| **Total Operating Expenses** | **$1,310,583** | **$1,743,296** | **$1,788,743** | **$1,861,949** |

Appendix: Information from Company Financial Statements.

## Appendix F: Adjusted Income Statement

| | FY2017 | FY2018 | FY2019 | FY2020 |
|---|---|---|---|---|
| **Adjusted Income Statement** | | | | |
| Total Revenue | $ 2,794,830 | $ 3,223,948 | $ 3,490,480 | $ 3,786,311 |
| Earnings Before Tax (EBT) | $ 428,711 | $ 248,325 | $ 345,114 | $ 796,009 |
| **Adjustments & Addbacks** | | | | |
| *+ Non-Cash Expenses* | | | | |
| Depreciation | $ 89,957 | $ 97,965 | $ 83,372 | $ 71,698 |
| Less: Depreciation Normalised | $ (88,438) | $ (97,556) | $ (78,691) | $ (69,291) |
| *+Cash Expenses* | | | | |
| Consultancy fees | - | - | - | $ 37,535 |
| Penalty fees | $ 4,958 | $ 1,293 | $ 1,938 | $ 2,039 |
| Miscellaneous Expense | $ 9,049 | $ 1,396 | $ 21,086 | $ 12,345 |
| Motor Vehicle expenses | $ 7,594 | $ 2,049 | $ 23,405 | $ 12,034 |
| Office Expense | - | $ 15,540 | - | - |
| Other Supplies | - | - | - | $ 6,802 |
| Pest control | $ 5,479 | - | - | - |
| Travel Expense | $ 15,000 | $ 15,000 | $ 15,000 | $ 15,000 |
| Interest | $ 14,560 | $ 13,440 | $ 12,320 | $ 11,200 |
| Less: Owner's wage, Normalised | $ (70,000) | $ (70,000) | $ (70,000) | $ (70,000) |
| Superannuation contribution | $ (6,650) | $ (6,650) | $ (6,650) | $ (6,650) |
| Cashflow boost ATO | - | - | - | $ (50,000) |
| Jobkeeper Subsidy | - | - | - | $ (100,000) |
| **Total Adjustments to EBT** | $ (18,491) | $ (27,523) | $ 1,780 | $ (127,289) |
| **Adjusted Debt-free Pre Tax Income** | **$ 410,220** | **$ 220,803** | **$ 346,893** | **$ 668,720** |

Notes:

1. Information from Company Financial Statements.
2. **Depreciation:** Non-cash in nature and has been added back.
3. **Interest**: Non-business related in nature (that is, they are not required for or derived from the company's usual activities). Additionally, by definition, EBITDA does not include interest incomes or expenses.
4. **Consultancy Fees:** consisted of a once-off expense in FY2020 and has been added back.
5. **Penalty Fees:** were non-business related and have been added back.

6. **Miscellaneous Expenses:** were non-business related and have been added back.
7. **Motor Vehicle Expenses:** consisted of non-business related expenses and have been added back.
8. **Office Expenses:** consisted of a once-off expense in FY2018 and has been adjusted to normalise profits.
9. **Other Supplies:** consisted of a once-off expense in FY2020 and has been adjusted to normalise profits.
10. **Pest Control:** consisted of a once-off expense in FY2017 and has been added back.
11. **Travel Expense:** consisted of non-business related expenses and have been adjusted to normalise profits.
12. **Owner's Wage:** was below fair market value and was adjusted to arrive at the fair market value compensation.
13. **Superannuation Contribution:** was adjusted to reflect the fair market compensation of the owner.
14. **Cashflow Boost ATO:** was considered once off and has been added back.
15. **Jobkeeper Subsidy:** was considered once off and has been added back.

## Appendix G: Balance Sheet

| | FY2017 | FY2018 | FY2019 | FY2020 |
|---|---|---|---|---|
| **Assets** | | | | |
| **Current Assets** | | | | |
| Cash | $327,150 | $310,365 | $364,503 | $488,742 |
| Accounts Receivable | $15,314 | $17,665 | $19,126 | $20,747 |
| Inventory | $62,744 | $73,467 | $81,026 | $76,376 |
| Loans to Shareholders | $0 | $15,831 | $6,782 | $13,782 |
| Other Investments | $0 | $0 | $56,831 | $68,831 |
| Other Current Assets | $0 | $20,045 | $6,109 | $2,734 |
| **Total Current Assets** | $405,208 | $437,374 | $534,378 | $671,213 |
| **Fixed Assets** | | | | |
| Total Property & Equipment | $449,784 | $489,827 | $416,862 | $358,489 |
| Less: Accumulated Depreciation | ($89,957) | ($97,965) | ($83,372) | ($71,698) |
| Net Fixed Assets | $359,827 | $391,862 | $333,489 | $286,792 |
| **Total Fixed Assets** | $359,827 | $391,862 | $333,489 | $286,792 |
| **Total Assets** | **$765,036** | **$829,236** | **$867,867** | **$958,004** |
| **Liabilities** | | | | |
| **Current Liabilities** | | | | |
| Accounts Payable | $71,300 | $83,485 | $92,076 | $86,791 |
| Short-Term Debt | $72,000 | $66,000 | $60,000 | $54,000 |
| **Total Current Liabilities** | $143,300 | $149,485 | $152,076 | $140,791 |
| **Long term Liabilities** | | | | |
| Long-Term Debt | $168,000 | $154,000 | $140,000 | $126,000 |
| **Total Long Term Liabilities** | $168,000 | $154,000 | $140,000 | $126,000 |
| **Total Liabilities** | **$311,300** | **$303,485** | **$292,076** | **$266,791** |
| **Net Assets** | **$453,736** | **$525,750** | **$575,792** | **$691,213** |

Note: Information from the Company's financial information.

In the table below we have split out the balance sheet for information purposes by what we determine in consultation with Management to be business related or operational assets and liabilities, non-business related or surplus assets and liabilities and interest-bearing debt.

## Categorised Balance Sheet

| ($000's) | FY2020 | Business Related | Non-business related | Debt |
|---|---|---|---|---|
| **Assets** | | | | |
| **Current Assets** | | | | |
| Cash | $ 489 | $ 314 | $ 175 | |
| Accounts Receivable | $ 21 | $ 21 | | |
| Inventory | $ 76 | $ 76 | | |
| Loans to Shareholders | $ 14 | | $ 14 | |
| Other Short-Term Loans | - | | - | |
| Other Investments | $ 69 | | $ 69 | |
| Other Current Assets | $ 3 | $ 3 | | |
| Total Current Assets | $ 671 | $ 413 | $ 258 | - |
| **Fixed Assets** | | | | |
| Total Property & Equipment | $ 358 | $ 358 | | |
| Accumulated Depreciation | $ (72) | $ (72) | | |
| Net Fixed Assets | $ 287 | $ 287 | | |
| Total Fixed Assets | $ 287 | $ 287 | - | - |
| **Total Assets** | **$ 958** | **$ 700** | **$ 258** | **-** |
| | | | | |
| **Liabilities** | | | | |
| **Current Liabilities** | | | | |
| Accounts Payable | $ 87 | $ 87 | | |
| Short-Term Debt | $ 54 | | | $ 54 |
| Total Current Liabilities | $ 141 | $ 87 | - | $ 54 |
| **Long term Liabilities** | | | | |
| Long-Term Debt | $ 126 | | | $ 126 |
| Total Long Term Liabilities | $ 126 | - | - | $ 126 |
| **Total Liabilities** | **$ 267** | **$ 87** | **-** | **$ 180** |
| **Net Assets** | **$ 691** | **$ 613** | **$ 258** | **$ (180)** |

Notes:

- **Surplus assets:** consisted of short-term loans to shareholders, other investments, and excess cash for a total of $257,721 as of the valuation date.
- **Debt:** the total interest-bearing debt consisted of short-term debt of $54,000 and long-term debt of $126,000 as of the valuation date.
- **Net Operating Assets –** NTA: After adding back surplus assets and liabilities, and interest-bearing debt, the NTA was $613,492 in FY2020.

## Appendix H: Discount and/or Capitalisation Rates

**Weighted Average Cost of Capital ("WACC")**

The final discount rate or weighted average cost of capital ("WACC") to be applied to the projected cash flows is calculated using the following formula:

WACC = [(Cost of Equity) * (% Equity)] + [(Cost of Debt) * (1-Tax Rate) * (% Debt)]

The application of the above formula is as follows:

| Cost of Capital | Build-Up |
|---|---|
| **Adjusted CAPM** | |
| **Cost of Equity** | |
| Risk Free Rate | 1.02% |
| Equity Risk Premium | 5.13% |
| Beta | 0.78 |
| Size Risk Premium | 8.39% |
| Company Specific Risk Premium | 5.00% |
| **Indicated Cost of Equity** | **18.39%** |
| **Cost of Debt** | |
| Financing Rate | 6.14% |
| Tax Rate | 27.50% |
| **Indicated Cost of Debt** | **4.45%** |
| **Capital Structure** | |
| Weight of Equity | 100% |
| Weight of Debt | 0% |
| **Indicated Weighted Average Cost of Capital** | **18.39%** |

Appendix: Information from sources and methods explained below.

The calculated weighted average cost of capital (WACC) was determined to be 18.39%. This represents an estimate of the WACC considering the build-up method employed in calculating the cost of equity only, as the Company is expected to move to a debt free capital structure in future.

**WACC & Capital Structure**

To calculate a WACC to apply to the projected free cash flows to invested capital, we have used the Company's capital structure advised by management of 100% equity and 0% debt into perpetuity. Pizza Company has no plans for further expansions; therefore, they will continue to finance their activities with equity only in the foreseeable future.

**Cost of Debt Capital**

The cost of debt is estimated based on the Company's current borrowing rate of approximately 6.14%. Given that interest is tax-deductible, the cost of debt is calculated after-tax, using the estimated income tax rate of 25% as discussed above. As a result, the estimated after tax cost of debt is 4.45%, although with a future expected weighting of 0% to debt, this does not affect the WACC.

**Cost of Equity Capital**

The discount rate or capitalisation rate represents the risk an investor is willing to accept for the potential reward an investment in the subject company will return. Different rates apply to different types of businesses. It is also known as the return that an investor requires from the investment. This risk is not calculated in a vacuum or a sterile environment but rather it is calculated based on the factors that can be contrasted against investing in other vehicles/assets that are available as of the valuation date. The formula is as follows:

$$Ke = R_f + \beta \times IMRP + RP_s + CSPR$$

$Ke = Cost\ of\ Equity\ Capital$
$R_f = Risk\ free\ rate$
$IMRP = Implied\ Market\ Risk\ Premium$
$\beta = Beta$
$RP_s = Size\ risk\ premium$
$CSPR = Company\ specific\ risk\ premium$

The build-up method layers different risk estimates to build up a discount rate. The following sections explain various components used in the build-up method.

**Build-Up Method Risk Elements**

**Risk-Free Rate**

The relevant risk-free rate of return is the return on a risk-free security, typically over a long-term period. In practice, long-dated government bonds are an acceptable benchmark for the risk-free security. We have chosen the nominal Australia 15-year Spot Treasury Yield as a proxy for the risk-free rate.

**Implied Equity Market Risk Premium**

The implied equity market risk premium represents the additional return as an excess above the risk-free rate that investors expect from an investment in a well-diversified portfolio of assets (such as a market index) due to their increased exposure to risk when investing in equity securities. We have used the returns of the Australian equity/stock market and risk-free rate as of June 2020.

**Beta[5]**

The Beta factor is a measure of the risk of an investment or business operation, relative to a well-diversified portfolio of assets. The risks captured by Beta are those unable to be eliminated by an investor through diversification. Such risks are referred to as systematic, undiversifiable or uninsurable risk. In short, the Beta is a measure of the relative riskiness of an asset in comparison to the market as a whole.

**Size Premium**

Empirical evidence shows that the risk reward principle (the greater the risk the greater the reward) holds true in the size or capitalisation of a company. The size premium represents average annual returns for small capitalisation stocks minus average annual returns for large capitalisation stocks. The CRSP size premium data included in the Duff & Phelps Valuation Handbook is broken down into average portfolio sizes and a regression equation based on different size measures.

Due to the size measure of Pizza Company being far below the 25$^{th}$ portfolio average, as recommended, we have used the regression equation based on Duff & Phelps Valuation Handbook.

**Company Specific Risk Premium ("CSRP")**

The CSRP adjusts the cost of equity for company-specific factors not captured by the previous components of the built-up cost of equity. From the Duff & Phelps Size Premium

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[5] Industry Betas. Salvidio & Partners. Q2 2020.

Study, it specifically states that companies that fall within certain parameters are not included; for this reason, we have stated these parameters in the below table. This is, among other factors, a starting point for analysing the additional risk factors specific to the subject company and its potential CSRP, that are not already captured within the built-up cost of equity. Based on these exclusion factors we then drill down further, reviewing several quantitative and qualitative factors such as reliance on key suppliers, customers, legal risks, leverage risk, profitability, etc. to capture this additional risk specific to the subject company, again stressing only those that have not been captured or are above average within/of the other components of the built-up cost of equity. With these factors, we build a company-specific risk profile and find the company-specific risk premium.

**Distinction of types of companies and specific metrics that are excluded from the Duff & Phelps Size Premium Study.**

| | |
|---|---|
| **Companies EXCLUDED from the 25th Portfolio** | 1. Financial services companies;<br>2. American Depository Receipts (ADRs);<br>3. Non-operating holding companies;<br>4. Unseasoned companies;<br>5. High financial-risk companies. |

*Points 4. and 5. listed above are of particular relevance within SME business valuations and hence we have broken them down further below.*

| | |
|---|---|
| **Unseasoned Companies** | 1. Start-up companies;<br>2. Companies lacking 5 years of publicly traded price history;<br>3. Companies with sales below $1 million in any of the previous five fiscal years;<br>4. Companies with a negative average 5-year EBITDA for the previous five fiscal years;<br>5. Companies not listed on one of the major U.S. stock exchanges (NYSE, NYSE MKT or NASDAQ). |
| **High-financial-risk companies** | 1. Companies that Standard & Poor's has identified in the Compustat database as in bankruptcy or in liquidation;<br>2. Companies with an "average 5-year net income available to common equity" less than zero for the previous five years, |

| | |
|---|---|
| | (either in absolute terms or as a percentage of the book value of common equity);<br>3. Companies with “average 5-year operating income” less than zero for the previous five years, (either in absolute terms or as a percentage of net sales);<br>4. Companies with negative book value of equity at any one of the company’s previous five fiscal year-ends;<br>5. Companies with a debt-to-total capital ratio exceeding 80%, (debt is measured in book value terms, and total capital is measured as book value of debt plus market value of equity). |

We have concluded that the Company’s specific risk premium is 5.00% by assessing the aforementioned risk factors.

**Total Cost of Equity**

To develop the cost of equity for the Company, the components discussed above were introduced in the formula of Cost of Equity Capital.

**The calculated equity discount rate using the build-up method for the Company is 18.39%**.

## Appendix I: Glossary

**Adjusted Book Value Method:** A method within the asset approach whereby all assets and liabilities (including off-balance sheet, intangible, and contingent) are adjusted to their fair market values.

**Adjusted Net Asset Method:** Is a business valuation technique that changes the stated values of a company's assets and liabilities to reflect their estimated current fair market values better. By adjusting asset or liability values up or down, the net effect offers values that can be used in going-concern assessments or liquidation scenarios.

**Appraisal:** An appraisal is a valuation of property, such as real estate, a business, collectible, or an antique, by the estimate of an authorised person.

**Appraisal Approach:** The appraisal approach is a procedure for determining an asset's value. The appraisal approach values assets based on a number of factors, such as its cost, the income it generates or its fair market value as compared to similar assets.

**Appraisal Date:** Refers to the date on which the value of an asset is determined. It is also known as valuation date.

**Appraisal Method:** Within approaches, a specific way to determine value.

**Appraisal Procedure:** The act, manner, and technique of performing the steps of an appraisal method.

**Arbitrage Pricing Theory:** A multivariate model for estimating the cost of equity capital, which incorporates several systematic risk factors.

**Asset (Asset – based) approach:** A general way of determining a value indication of a business, business ownership interest, or security using one or more methods based on the value of the assets net of liabilities.

**Assets:** Is any resource owned by the business such as an item, property, investments.

**Accounts receivable:** Is the amount owed to a company resulting from the company providing goods and/or services on credit.

**Amortisation:** Refers to reduction in the cost of intangible assets over its life span.

**Business:** A business is defined as an organisation or enterprising entity engaged in commercial, industrial, or professional activities.

**Business Enterprise:** A commercial, industrial, service, or investment entity (or a combination thereof) pursuing an economic activity.

**Business valuation:** The act or process of determining the value of a business enterprise or ownership interest therein.

**Capital Asset Pricing Model (CAPM):** A model in which the cost of capital for any stock or portfolio of stocks equals a risk-free rate plus a risk premium that is proportionate to the systematic risk of the stock or portfolio.

**Capex:** Capital expenditure is the amount spent to acquire or upgrade productive assets (such as buildings, machinery and equipment, vehicles) in order to increase the capacity or efficiency of a company.

**Capitalisation:** A conversion of a single period of economic benefits into value.

**Capitalisation Factor:** Any multiple or divisor used to convert anticipated economic benefits of a single period into value.

**Capitalisation of Earnings Method:** A method within the income approach whereby economic benefits for a representative single period are converted to value through division by a capitalisation rate.

**Capitalisation rate:** Any divisor (usually expressed as a percentage) used to convert anticipated economic benefits of a single period into value.

**Capital structure:** The composition of the invested capital of a business enterprise; the mix of debt and equity financing.

**Cash flow:** Cash that is generated over a period of time by an asset, group of assets, or business enterprise. It may be used in a general sense to encompass various levels of specifically defined cash flows. When the term is used, it should be supplemented by a qualifier (for example, “free”, “discretionary” or “operating”) and a specific definition in the given valuation context.

**Common Size Statements:** Financial statements in which each line is expressed as a percentage of the total. On the balance sheet, each line item is shown as a percentage of total assets, and on the income statement, each item is expressed as a percentage of sales.

**Control:** The power to direct the management and policies of a business enterprise.

**Control Premium:** An amount or a percentage by which the pro rata value of a controlling interest exceeds the pro rata value of a non-controlling interest in a business enterprise to reflect the power of control.

**Cost Approach:** A general way of determining a value indication of an asset such as a business, business ownership interest, or security by using the economic principle that a buyer will pay no more for an asset than the cost to obtain an asset of equal utility (benefit).

**Cost of capital:** The expected rate of return that the market requires in order to attract funds to a particular investment.

**Company:** Refers to the company under valuation in this Report.

**Discount for lack of control:** An amount or percentage deducted from the pro rata share of value of 100% of an equity interest in a business to reflect the absence of some or all of the powers of control.

**Discount for lack of marketability**: An amount or percentage deducted from the value of an ownership interest to reflect the relative absence of liquidity/marketability.

**Discount for Lack of Voting Rights:** An amount or percentage deducted from the per share value of a minority interest voting share to reflect the absence of voting rights.

**Discount rate:** A rate of return used to convert a future monetary sum into present value.

**Discounted cash flow method (DCF):** A method within the income approach whereby the present value of future expected net cash flows is calculated using a discount rate.

**Discounted Future Earnings Method:** A method within the income approach whereby the present value of future expected economic benefits is calculated using a discount rate.

**Depreciation:** Refers to the reduction in the cost base of a tangible fixed assets over its lifespan. It is calculated using an appropriate accounting method, such as reducing its cost base by an amount equal to the proportionate use of the asset in that specific year.

**EBITDA:** Earnings before interest, taxes, depreciation, and amortisation is a measure of a company's overall financial performance and is used as an alternative to simple earnings or net income in some circumstances.

**Economic life:** The period of time over which an asset may generate economic benefits.

**Economic Benefits:** Inflows such as revenues, net income, net cash flows, etc.

**Economic Life:** The period of time over which property may generate economic benefits.

**Effective Date:** The specific point in time as of which the valuator's conclusion of value applies (also referred to as "Valuation Date" or "Appraisal Date").

**Enterprise:** A commercial, industrial, service, or investment entity (or a combination thereof) pursuing an economic activity.

**Enterprise Value:** Enterprise Value (EV) is a measure of value attributable to all holders of capital in the firm, less any liquid non-operating or surplus assets such as cash, surplus inventory, financial investments or non-core real estate. EV is a measure of the firms total operating assets. All 'long term' providers of capital such as debt holders, equity holders (common and preferred) and minority interests all have claims on the firm's mass of operating assets. We note that in practice, different valuation practitioners will consider some cash as a "normal working" balance and thus include it in EV, as part of working capital (only subtracting any "surplus" cash). Whilst others will subtract all cash balances.

**Equity:** The owner's interest in an asset after deduction of all liabilities.

**Equity Net Cash Flows:** Those cash flows available to pay out to equity holders (in the form of dividends) after funding operations of the business enterprise, making necessary capital investments, and increasing or decreasing debt financing.

**Equity risk premium:** A rate of return added to a risk-free rate to reflect the additional risk of equity instruments over risk free instruments (a component of the cost of equity capital or equity discount rate).

**Excess Earnings:** That amount of anticipated economic benefits that exceeds an appropriate rate of return on the value of a selected asset base (often net tangible assets) used to generate those anticipated economic benefits.

**Excess Earnings Method:** A specific way of determining a value indication of a business, business ownership interest, or security determined as the sum of a) the value of the assets derived by capitalising excess earnings, and b) the value of the selected asset base. Also frequently used to value intangible assets.

**Fair Market Value:** The price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arm's length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts.

**Fairness Opinion:** An opinion as to whether or not the consideration in a transaction is fair from a financial point of view.

**Financial Risk:** The degree of uncertainty of realising expected future returns of the business resulting from financial leverage.

**Forced Liquidation Value:** Liquidation value, at which the asset or assets are sold as quickly as possible, such as at an auction.

**Future Maintainable Earnings (FME):** The expected earnings of a company that is an assumption of the future maintainable earnings of the subject business. FME is represented in a single number and is calculated using a range of factors, not limited to historical adjusted financial earnings and expectations of the financial performance of the business in future.

**Financial risk:** The degree of uncertainty of realising expected future returns of the business resulting from financial leverage.

**Free cash flow to the firm (FCFF):** Represents the amount of available cash flow from operations available to the firm's providers of capital, after all cash expenses and necessary capital investments have been made.

**Going concern:** An ongoing operating business enterprise.

**Goodwill:** The estimated value of intangible assets arising as a result of name, reputation, customer loyalty, location, products, and similar factors not separately identified.

**Goodwill Value:** The value attributable to goodwill.

**Guideline Public Company Method:** A method within the market approach whereby market multiples are derived from market prices of stocks of companies that are engaged in the same or similar lines of business and that are actively traded on a free and open market.

**Income Approach:** A general way of determining a value indication of an asset such as a business, business ownership interest, security, or intangible asset using one or more methods that convert anticipated economic benefits into a present single amount.

**Intangible Assets:** Nonphysical assets such as franchises, trademarks, patents, copyrights, goodwill, equities, mineral rights, securities, and contracts (as distinguished from physical assets) that grant rights and privileges and have value for the owner.

**Internal Rate of Return:** A discount rate at which the present value of the future cash flows of the investment equals the cost of the investment.

**Income stream:** The money a company generates on a regular basis.

**Industry Risk Premium:** The Industry Risk Premium is the additional return an investor expects to receive for investing in a specific industry, than the market as a whole.

**Intrinsic Value:** The value that an investor considers, on the basis of an evaluation or available facts, to be the "true" or "real" value that will become the market value when other investors reach the same conclusion. When the term applies to options, it is the difference between the exercise price or strike price of an option and the market value of the underlying security.

**Invested Capital:** The sum of equity and debt in a business enterprise. Debt is typically a) all interest-bearing debt, or b) long-term interest-bearing debt. When the term is used, it should be supplemented by a specific definition in the given valuation context.

**Invested Capital Net Cash Flows:** Those cash flows available to pay out to equity holders (in the form of dividends) and debt investors (in the form of principal and interest) after funding operations of the business enterprise and making necessary capital investments.

**Investment Risk:** The degree of uncertainty as to the realisation of expected returns.

**Investment Value:** The value to a particular investor based on individual investment requirements and expectations.

**Key Person Discount:** An amount or percentage deducted from the value of an ownership interest to reflect the reduction in value resulting from the actual or potential loss of a key person in a business enterprise.

**Levered Beta:** The beta reflecting a capital structure that includes debt.

**Limited Appraisal:** The act or process of determining the value of a business, business ownership interest, security or intangible asset with limitations in analyses, procedures or scope.

**Liquidity:** The ability to quickly convert property to cash or pay a liability.

**Liquidation Value:** The net amount that would be realised if the business is terminated and the assets are sold piecemeal. Liquidation can be either "orderly" or "forced."

**Liabilities:** Are amounts owed to creditors for a past transaction and describes the obligation of one party to pay a debt owed to another party.

**Majority Control:** The degree of control provided by a majority position.

**Majority Interest:** An ownership interest greater than 50% of the voting interest in a business enterprise.

**Market Capitalisation of Equity:** The share price of a publicly traded stock multiplied by the number of shares outstanding.

**Market Capitalisation of Invested Capital:** The market capitalisation of equity plus the market value of the debt component of invested capital.

**Market Approach:** A general way of determining a value indication of an asset such as a business, business ownership interest, security, or intangible asset by using one or more methods that compare the subject asset to similar businesses, business ownership interests, securities, or intangible assets that have been sold.

**Market multiple:** The market value of a company's equity or invested capital divided by a company measure (such as economic benefits, a measure of earnings, sales etc).

**Marketability:** The ability to quickly convert as asset to cash at minimal cost.

**Merger and Acquisition Method:** A method within the market approach whereby pricing multiples are derived from transactions of significant interests in companies engaged in the same or similar lines of business.

**Mid-Year Discounting:** A convention used in the Discounted Future Earnings Method that reflects economic benefits being generated at midyear, approximating the effect of economic benefits being generated evenly throughout the year.

**Minority Discount:** A discount for lack of control applicable to a minority interest.

**Minority Interest:** An ownership interest less than 50 percent of the voting interest in a business enterprise.

**Multiple:** The inverse of the capitalisation rate.

**Net Book Value:** With respect to a business enterprise, the difference between total assets (net of accumulated depreciation, depletion, and amortisation) and total liabilities as they appear on the balance sheet (synonymous with Shareholder's Equity). With respect to a specific asset, the capitalised cost less accumulated amortisation or depreciation as it appears on the books of account of the business enterprise.

**Net Cash Flow:** Refers to the gain or loss of funds over a period after all debts are paid.

**Net Present Value:** The value, as of a specified date, of future cash inflows less all cash outflows (including the cost of investment) calculated using an appropriate discount rate.

**Net Tangible Asset Value:** The value of the business enterprise's tangible assets (excluding excess assets and non-operating assets) minus the value of its liabilities.

**Non-Operating Assets:** Assets not necessary to ongoing operations of the business enterprise.

**Normalised Earnings:** Economic benefits adjusted for nonrecurring, non-economic or other unusual items to eliminate anomalies and/or facilitate comparisons.

**Normalised Financial Statements:** Financial statements adjusted for non-operating assets and liabilities and/or for non-recurring, non- economic or other unusual items to eliminate anomalies and/or facilitate comparisons.

**Orderly Liquidation Value:** Liquidation value at which the asset or assets are sold over a reasonable period of time to maximise proceeds received.

**Premise of value:** An assumption regarding the most likely set of transactional circumstances that may be applicable to the subject valuation, for example, going concern, liquidation or orderly disposition.

**Present Value:** The value, as of a specified date, of future economic benefits and/or proceeds from sale, calculated using an appropriate discount rate.

**Portfolio Discount:** An amount or percentage deducted from the value of a business enterprise to reflect the fact that it owns dissimilar operations or assets that do not fit well together.

**Price/Earnings Multiple:** The price of a share of stock divided by its earnings per share.

**Rate of Return:** An amount of income (loss) and/or change in value realised or anticipated on an investment, expressed as a percentage of that investment.

**Report:** This document, outlined as either an Appraisal Report, or Valuation Report.

**Report Date:** The date conclusions are transmitted to the client.

**Replacement Cost New:** The current cost of a similar new property having the nearest equivalent utility to the property being valued.

**Reproduction Cost New:** The current cost of an identical new property.

**Required Rate of Return:** The minimum rate of return acceptable by investors before they will commit money to an investment at a given level of risk.

**Residual Value:** The value as of the end of the discrete projection period in a discounted future earnings model.

**Return on Equity:** The amount, expressed as a percentage, earned on a company's common equity for a given period.

**Return on Invested Capital:** The amount, expressed as a percentage, earned on a company's total capital for a given period.

**Risk-Free Rate:** The rate of return available in the market on an investment free of default risk.

**Risk Premium:** A rate of return added to a risk-free rate to reflect risk.

**Rule of Thumb:** A mathematical formula developed from the relationship between price and certain variables based on experience, observation, hearsay or a combination of these; usually industry specific.

**Systematic Risk:** the risk that is common to all risky securities and cannot be eliminated through diversification. The measure of systematic risk in stocks is the beta coefficient.

**Special Interest Purchasers:** Acquirers who believe they can enjoy post-acquisition economies of scale, synergies or strategic advantages by combining the acquired business interest with their own.

**Standard of Value:** The identification of the type of value being used in a specific engagement (e.g., fair market value, fair value, investment value).

**Sustaining Capital Reinvestment:** The periodic capital outlay required to maintain operations at existing levels, net of the tax shield available from such outlays.

**Seller's Discretionary Earnings:** Is an estimate of the total adjusted financial benefit one (1) full time owner operator would derive from the business annually.

**Size Premium:** Size premium is the additional remuneration due to the higher risk and therefore, the higher cost of capital, associated with the smaller size of the company.

**Tangible Assets:** Physical assets such as property, plant and equipment etc.

**Terminal Value:** Is the value of a business or project beyond the forecast period when future cash flows can be estimated.

**Transaction Method:** A method within the market-based approach whereby pricing multiples are derived from transactions of significant interests in companies engaged in the same or similar lines of business.

**The Company:** Refers to the company under valuation in this Report.

**Treasury Bonds:** Treasury bonds are issued by the U.S. Federal Government. They are often used as a proxy for the risk-free rate as they are considered to be the lower risk asset available, as they are backed by the U.S. Government.

**Unsystematic Risk:** The risk specific to an individual security that can be negated through diversification.

**Unlevered Beta:** The beta reflecting a capital structure without debt.

**Valuation:** The act or process of determining the value of a business, business ownership interest, security, or intangible asset.

**Valuation Approach:** A general way of determining a value indication of an asset such as a business, business ownership interest, security, or intangible asset using one or more valuation methods.

**Valuation Method:** Within approaches, a specific way to determine an asset's value.

**Weighted Average Cost of Capital (WACC):** The cost of capital (discount rate) determined by the weighted average, at market value, of the cost of all financing sources in the business enterprise's capital structure.

**Weighted Average Method:** The mean in which each item being averaged is multiplied by a number (weight) based on the item's relative importance. The result is summed and the total is divided by the sum of the weights.