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PACIFIC STAR NETWORK LTD

PROPOSED ACQUISITION OF CROCMEDIA PTY LTD

INDEPENDENT EXPERT'S REPORT AND FINANCIAL SERVICES GUIDE
1 FEBRUARY 2018

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1 February 2018

The Independent Directors
Pacific Star Network Ltd
472 Swan Street
Richmond VIC 3121

Dear Directors,

Independent Expert's Report for Pacific Star Network Ltd

1. Introduction

Pacific Star Network Ltd ("**PNW**") is a media company based in Richmond, Australia and is listed on the ASX. PNW operates in the radio broadcasting, publishing and digital media industry serving niche audiences. PNW operates three digital only radio stations, two radio broadcast channels and is also a publisher of lifestyle and sports magazines.

Crocmedia Pty Ltd ("**Crocmedia**") is a content and entertainment business which connects brands to metropolitan and regional audiences through various media platforms. Crocmedia is Australia's only independent syndicator of sports content, with the core of its business in radio syndication since its first program, Off the Bench, which went to air in February 2008.

On 5 January 2018, PNW and Crocmedia entered into a Share Sale and Purchase Agreement whereby PNW agreed to acquire 100% of the shares outstanding in Crocmedia and the outstanding minority interest in Crocmedia's subsidiary, Thread, for a total consideration of 91.6 million PNW shares. Approximately 4.1 million of these shares have been structured as performance rights as described in Section 10.3 of the notice of meeting. In addition, PNW will issue Crocmedia's key employees with a number of long-term incentive performance rights as described in Section 1.1.

In conjunction with the acquisition of Crocmedia, PNW is undertaking an equity raising of $10 million through the issue of 40 million ordinary shares at $0.25 per share ("**Planned Capital Raising**"). Three vendors of Crocmedia (or their associates) have agreed to participate in the Planned Capital Raising. Viburnum Funds Pty Ltd ("**Viburnum**"), a current shareholder of PNW with a 19.5% shareholding, has committed to funding $8.25 million of the Planned Capital Raising. In this report, we have defined the acquisition of Crocmedia and the outstanding minority interest in Thread, Planned Capital Raising and other associated transactions as the ("**Proposed Transaction**"). We have also defined the combined PNW and Crocmedia after the Proposed Transaction as the ("**Proposed Merged Entity**").

Further information regarding the Proposed Transaction is set out in Section 1 of our detailed report.

2. Purpose of the report

If the Proposed Transaction is approved, the vendors of Crocmedia will acquire a 47.2% interest in PNW. This percentage will increase if the long-term incentive performance rights vest as a result of the Proposed Merged Entity achieving certain EBITDA hurdles as described in Section 1 of our detailed report. As Viburnum has committed to funding $8.25 million of the Planned Capital Raising, it will therefore increase its holding in PNW to above 20%. Approval for the Proposed Transaction is therefore being sought at a general meeting of PNW's shareholders.

In order to assist PNW shareholders not associated with the vendors of Crocmedia or Viburnum ("**Shareholders**") evaluate the Proposed Transaction, the independent directors of PNW have engaged Leadenhall Corporate Advisory Pty Ltd ("**Leadenhall**") to prepare an independent expert's report assessing whether the Proposed Transaction is fair and reasonable. This report is to be included in the notice of meeting that will be sent to Shareholders regarding the Proposed Transaction.

Further information regarding the purpose of this report is provided in Section 2 of our detailed report.

3. Basis of evaluation

In order to assess whether the Proposed Transaction is fair and reasonable we have:

- Assessed it as fair if the value of a PNW share after the Proposed Transaction is greater than or equal to the value of a PNW share before the Proposed Transaction.
- Assessed it as reasonable if it is fair, or despite not being fair, the advantages to Shareholders outweigh the disadvantages.

Further details of the basis of evaluation are provided in Section 2 of our detailed report.

4. The Proposed Transaction is fair

4.1 Value of PNW before the Proposed Transaction

We have assessed the fair market value of a share in PNW using the capitalisation of future maintainable earnings ("**CFME**") method. This assessment has been made on a control basis (i.e. including a control premium) consistent with the requirement of *Regulatory Guide 111: Content of Expert Reports* ("**RG111**") that the comparison for takeover must be made assuming a 100% interest in the target company.

Table 1: Valuation of PNW

($'000)	EBIT	
	Low	High
Maintainable earnings	2,400	2,600
Multiple (control)	9.0x	10.0x
Enterprise value	**21,600**	**26,000**
Surplus assets	62	62
Net debt	(3,803)	(3,803)
Equity value on a control basis	**17,859**	**22,259**
Total number of shares ('000)	72,118	72,118
Assessed value per share ($)	**0.25**	**0.31**

Source: Leadenhall analysis

In applying the CFME approach for PNW, we have selected a maintainable EBIT of $2.4 million to $2.6 million and an EBIT multiple of 9.0 times to 10.0 times.

Further details of our valuation of PNW are provided in Section 8 of our detailed report.

4.2 Value of Proposed Merged Entity

We have determined the fair market value of a share in the Proposed Merged Entity using the CFME method. This assessment has been made on a minority interest basis (i.e. excluding a control premium) as PNW's existing shareholders will become minority shareholders in the Proposed Merged Entity.

Table 2: Valuation of Proposed Merged Entity

($'000)	EBIT	
	Low	High
Maintainable earnings	8,800	9,200
Multiple (minority basis)	8.5x	9.5x
Enterprise value	**74,800**	**87,400**
Surplus assets	62	62
Non-operating liabilities	(2,900)	(3,200)
Net cash	6,738	6,738
Equity value on a minority basis	**78,700**	**91,000**
Allocation to options and performance rights	(2,127)	(2,491)
Value allocated to ordinary shares	**76,573**	**88,509**
Total number of shares ('000)	202,691	202,691
Assessed value per share ($)	**0.38**	**0.44**

Source: Leadenhall analysis

In applying the CFME approach for the Proposed Merged Entity, we have selected a maintainable EBIT (inclusive of synergies) of $8.8 million to $9.2 million and an EBIT multiple of 8.5 times to 9.5 times.

Further details of our valuation of the Proposed Merged Entity are provided in Section 9 of our detailed report.

Conclusion

The Proposed Transaction is fair because the value of a share in the Proposed Merged Entity (i.e. PNW plus Crocmedia and synergies after the Proposed Transaction) is greater than the value of a PNW share before the Proposed Transaction, as set out in the table below:

Table 3: Assessment of fairness

	Section	Low ($)	High ($)
Fair market value of a PNW share (before Proposed Transaction)	8.2.5	0.25	0.31
Fair market value of a Proposed Merged Entity share	9.2.6	0.38	0.44

Source: Leadenhall analysis

5. The Proposed Transaction is reasonable

We have defined the Proposed Transaction as being reasonable if it is fair, or if despite not being fair, the overall advantages of the proposal outweigh its disadvantages to Shareholders. We have therefore considered the advantages and disadvantages to Shareholders of the Proposed Transaction.

Advantages

We have identified the following significant advantages to Shareholders of the Proposed Transaction:

- ***Limited alternatives available:*** Should PNW not successfully complete the Planned Capital Raising there is uncertainty as to whether it will be able to refinance its debt obligations hence continue to trade as a going concern. Since the Planned Capital Raising is dependent on the Proposed Transaction proceeding, the Proposed Transaction will facilitate the Planned Capital Raising and therefore mitigate the refinancing risk for the company.
- ***Potential to realise cost and revenue synergies:*** As set out in Section 6.3, in the longer term, there is the potential to realise significant cost and revenue synergies. An initial synergies assessment performed by management has identified at least $3.0 million of cost synergies to be achieved by the Proposed Transaction. This is equivalent to approximately 50% of the maintainable earnings for PNW and Crocmedia combined. Further potential revenue synergies associated with initiatives such as cross-selling have not yet been quantified.
- ***Complementary activities:*** As PNW and Crocmedia operate in similar parts of the sports media and advertising industry, the Proposed Transaction would not only provide an opportunity for both businesses to consolidate, but may reduce competition in some areas.

Disadvantages

We have identified the following significant disadvantages to Shareholders of the Proposed Transaction:

- ***Selective treatment of certain investors:*** The Planned Capital Raising was negotiated at the same time as the Proposed Transaction, both of which are interdependent. The Planned Capital Raising and the Proposed Transaction are both based on a price of $0.25 per share, being the market price of PNW shares prior to the announcement of the Proposed Transaction. The Planned Capital Raising is priced at a substantial discount to both our assessed value of a share in the Proposed Merged Entity and the current market price of PNW shares, which has increased following the announcement of the Proposed Transaction. The market response since the deal was announced is consistent with our assessed value of shares in the Proposed Merged Entity, which includes the expected synergy benefits arising from the Proposed Transaction. We understand that Shareholders are not invited to participate in the Planned Capital Raising due to PNW's requirement for speed and certainty in raising the funds, thus this represents selective treatment for one of PNW's major shareholders, Viburnum and the other participants in the Planned Capital Raising.

- ***Loss of control:*** If the Proposed Transaction is approved the vendors of Crocmedia would acquire practical control of PNW with a holding slightly below 50% and the possibility of a greater than 50% holding subject to the vesting of the long-term incentive performance rights. This would include the ability to control the assets, the strategic direction of the company, and the decision of when to pay dividends. The vendors of Crocmedia may not always act in the best interest of PNW's current shareholders, subject to compliance with relevant laws and regulations.
- ***Crocmedia's unaudited financial statements:*** Crocmedia has not had their financial statements audited despite the commission of extensive due diligence on Crocmedia. Therefore, financial information of the Proposed Merged Entity has a risk of error. We note that we have allowed for this risk in the selected multiple used to value the Proposed Merged Entity.
- ***Change in investment risk profile:*** While both PNW and Crocmedia are involved in the sports media and advertising industry, investors who acquired PNW shares for exposure to certain characteristics, investment focus and scale of the current PNW may not wish to hold an investment in the Proposed Merged Entity. Whilst the Proposed Merged Entity would likely provide the potential for increased returns on investment, this exposure may not be desirable for some investors due to individual investment preferences.

Conclusion on reasonableness

As the Proposed Transaction is fair it is also reasonable.

6. Opinion

In our opinion, the Proposed Transaction is fair and reasonable to Shareholders. This opinion should be read in conjunction with our detailed report which sets out our scope, analysis and findings in more detail.

Yours faithfully

Richard Norris
Director

Shaun Bettman
Director

Note: All amounts stated in this report are in Australian dollars unless otherwise stated.
Tables in this report may not add due to rounding.

LEADENHALL CORPORATE ADVISORY PTY LTD

ABN 11 114 534 619

Australian Financial Services Licence No: 293586

FINANCIAL SERVICES GUIDE

Leadenhall Corporate Advisory Pty Ltd ("**Leadenhall**" or "**we**" or "**us**" or "**our**" as appropriate) has been engaged to issue general financial product advice in the form of a report to be provided to you.

Financial Services Guide

In providing this report, we are required to issue this Financial Services Guide ("**FSG**") to retail clients. This FSG is designed to help you to make a decision as to how you might use this general financial product advice and to ensure that we comply with our obligations as a financial services licensee.

Financial Services We are Licensed to Provide

We hold Australian Financial Services Licence 293586 which authorises us to provide financial product advice in relation to securities (such as shares and debentures), managed investment schemes and derivatives.

We provide financial product advice by virtue of an engagement to issue a report in connection with a financial product. Our report will include a description of the circumstances of our engagement and the party who has engaged us. You will not have engaged us directly but will be provided with a copy of the report because of your connection to the matters in respect of which we have been engaged to report.

Any report we provide is provided on our own behalf as a financial service licensee authorised to provide the financial product advice contained in that report.

General Financial Product Advice

The advice produced in our report is general financial product advice, not personal financial product advice, because it has been prepared without taking into account your personal objectives, financial situation or needs. You should consider the appropriateness of this general advice having regard to your own objectives, financial situation and needs before you act on the advice. Where the advice relates to the acquisition or possible acquisition of a financial product, you should also obtain a product disclosure statement relating to the product and consider that statement before making any decision about whether to acquire the product.

Benefits that We May Receive

We charge fees for providing reports. These fees will be agreed with the person who engages us to provide the report. Fees will be agreed on either a fixed fee or time cost basis. Leadenhall is entitled to receive a fixed fee of $60,000 (excl. GST) for preparing this report. This fee is not contingent upon the outcome of the Proposed Transaction.

Except for the fees referred to above, neither Leadenhall, nor any of its directors, consultants, employees or related entities, receive any pecuniary or other benefit, directly or indirectly, for or in connection with the provision of this report.

Remuneration or Other Benefits Received by our Employees, Directors and Consultants

All our employees receive a salary. Our employees are eligible for bonuses which are not based on the outcomes of any specific engagement or directly linked to the provision of this report. Our directors and consultants receive remuneration based on time spent on matters.

Referrals

We do not pay commissions or provide any other benefits to any person for referring clients to us in connection with the reports that we are licensed to provide.

Complaints Resolution

As the holder of an Australian Financial Services Licence, we are required to have a system in place for handling complaints from persons to whom we have provided reports. All complaints must be in writing, to the following address:

Leadenhall Corporate Advisory Pty Ltd
GPO Box 1572
Adelaide SA 5001

Email: office@leadenhall.com.au

We will try to resolve your complaint quickly and fairly and will endeavour to settle the matter within 14 days from the time the matter is brought to our attention.

If you do not get a satisfactory outcome, you have the option of contacting the Financial Ombudsman Service ("**FOS**"). The FOS will then be able to advise you as to whether or not they can assist in this matter. The FOS can be contacted at the following address:

Financial Ombudsman Service
GPO Box 3
Melbourne VIC 3001

Telephone: 1300 780 808
Email: info@fos.org.au

Compensation Arrangements

Leadenhall holds professional indemnity insurance in relation to the services we provide. The insurance cover satisfies the compensation requirements of the Corporations Act 2001.

1 February 2018

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CONTENTS

1 THE PROPOSED TRANSACTION

1.1 Acquisition of Crocmedia

PNW is an ASX listed publishing and broadcasting company with a market capitalisation of approximately $27 million. PNW owns two AM commercial radio stations, three digital stations and four publishing titles. Further details of PNW's operations are provided in Section 4 of this report.

Crocmedia is a privately-owned sports media company. Crocmedia provides a number of syndicated radio and television programs including AFL Nation, Football Nation and Sportsday. Further details of Crocmedia's business are provided in Section 5 of this report.

On 5 January 2018, PNW and Crocmedia entered into a Share Sale and Purchase Agreement whereby PNW agreed to acquire 100% of the shares outstanding in Crocmedia and the outstanding minority interest in Crocmedia's subsidiary, Thread, for a total consideration of 91.6 million PNW shares. Approximately 4.1 million of these shares have been structured as performance rights as described in Section 10.3 of the notice of meeting. This has no practical implications for our analysis. The vendors of Crocmedia and the executives receiving the relevant performance rights have agreed to place 100% of the 91.6 million consideration shares in escrow for 18 months and 75% in escrow for 24 months.

As part of the Proposed Transaction PNW will also issue Crocmedia's key employees with a number of long-term incentive performance rights as follows:

- **Tranche 1** - rights will be granted for employees to be issued 2.9 million PNW shares. The rights will vest over 12 months, subject to the Proposed Merged Entity achieving a minimum EBITDA of $10.4 million over the 12-month period to 30 June 2019. If these rights do not vest as a result of the Proposed Merged Entity failing to achieve the EBITDA hurdle, 50% of the rights will roll into Tranche 2 and re-tested based on the hurdle for Tranche 2. The other 50% of the rights will be re-tested against an EBITDA hurdle of $15.5 million for any consecutive 12-month period up to 30 June 2020.
- **Tranche 2** - rights will be granted for employees to be issued 2.9 million PNW shares. The rights will vest over 24 months, subject to the Proposed Merged Entity achieving a minimum EBITDA of $12.6 million over the 12-month period to 30 June 2020. If these rights do not vest as a result of the Proposed Merged Entity failing to achieve the EBITDA hurdle, 50% of the rights (excluding those rolled from Tranche 1) will roll into Tranche 3 and re-tested based on the hurdle for Tranche 3. The other 50% of the rights will be re-tested against an EBITDA hurdle of $17.0 million over the 12-month period to 30 June 2021.
- **Tranche 3** - rights will be granted for employees to be issued 2.9 million PNW shares. The rights will vest over 36 months, subject to the Proposed Merged Entity achieving a minimum EBITDA of $15.5 million over the 12-month period to 30 June 2021. Rights that do not vest as a result of the Proposed Merged Entity not achieving the minimum EBITDA hurdle will expire.

Rights will also be granted for employees to be issued 0.2 million PNW shares under a special purpose performance rights plan, vesting on 29 January 2020, subject to the relevant employee remaining employed by PNW on that date.

1.2 Planned Capital Raising

In conjunction with the acquisition of Crocmedia, PNW is undertaking an equity raising of $10 million through the issue of 40 million ordinary shares at $0.25 per share. Three vendors of Crocmedia (or their associates) have agreed to participate in the Planned Capital Raising. All participants in the equity raising will be required to enter into 12 months voluntary escrow agreements. Viburnum has committed to funding $8.25 million of the Planned Capital Raising.

1.3 Board and management

If the Proposed Transaction is approved, Craig Hutchison, the founder of Crocmedia, will be appointed to the PNW board as a director and will be appointed as the chief executive officer and managing director of PNW. Chris Giannopoulos will also be appointed to the PNW board as an executive director.

1.4 Conditions

The Proposed Transaction is subject to a number of conditions including:

- Approval by Shareholders.
- Receipt of approval from the ASX that PNW has met the requirements of Chapters 1 and 2 of the Listing Rules for re-instatement on the ASX.
- Completion of the $10 million Planned Capital Raising which has already been committed.
- Consent to the Proposed Transaction received from counterparties to material contracts.

2 SCOPE

2.1 Purpose of the report

If the Proposed Transaction is approved the vendors of Crocmedia will acquire an approximate 47.2% interest in PNW as a result of the sale of Crocmedia. This percentage will increase if the long-term incentive performance rights vest as a result of the Proposed Merged Entity achieving certain EBITDA hurdles as described in Section 1 of our report. Three of the vendors (or their associates) have also agreed to participate in the Planned Capital Raising which will further increase their holding in PNW shares. Viburnum, a current shareholder of PNW with a 19.5% shareholding, has committed to funding $8.25 million of the $10.0 million Planned Capital Raising which will therefore increase its interest in PNW to 23.1% post the Proposed Transaction.

An acquisition of securities that enables a securityholder to increase its relevant interests in a listed company from below 20% to above 20% is prohibited under Section 606 of the Corporations Act 2001 ("**s606**"), except in certain circumstances.

One of the exceptions to s606 is where the acquisition of securities is approved at a general meeting of the target company (in this case PNW) in accordance with item 7 of Section 611 of the Corporations Act 2001 ("**s611**"). Approval for the Proposed Transaction is therefore being sought at a general meeting of PNW's shareholders in accordance with item 7 of s611.

Item 7 of s611 requires shareholders to be provided with all of the information known to the company and to the potential acquirer that is material to the shareholders' decision. *Regulatory Guide 74: Acquisitions Approved by Members* ("**RG74**") issued by the Australian Securities and Investment Commission ("**ASIC**") provides additional guidance on the information to be provided to shareholders. RG74 states that the directors of the target company should provide shareholders with an independent expert's report or a detailed directors' report on the Proposed Transaction.

RG111 issued by ASIC requires an independent expert assessing a transaction that has a similar effect to a takeover bid to assess whether the transaction is fair and reasonable.

The directors of PNW have therefore requested Leadenhall to prepare an independent expert's report assessing whether each of the following transactions is fair and reasonable to Shareholders in accordance with s611:

- The issue of shares to the vendors of Crocmedia in relation to the acquisition of Crocmedia.
- The participation in the Planned Capital Raising by the vendors of Crocmedia.
- The acquisition of shares by Viburnum as a result of the Planned Capital Raising.
- The potential acquisition of shares by Craig Hutchison as a result of the vesting of performance rights.
- The acquisition of a relevant interest in its own shares by PNW as a result of the escrow arrangements.

As each of these items are related, we have undertaken a single analysis of whether the Proposed Transaction as a whole (including each of the components listed above) is fair and reasonable. This approach is consistent with the guidance at RG111.54, albeit in relation to a different type of transaction to that contemplated at this section of the regulatory guide. This report is to be included in the notice of meeting in relation to the Proposed Transaction and has been prepared for the exclusive purpose of assisting Shareholders in their consideration of the Proposed Transaction.

2.2 Basis of evaluation

Introduction

As the vendors of Crocmedia will collectively hold a significant stake in PNW should the Proposed Transaction be approved, we have assessed the Proposed Transaction as a control transaction. RG111 requires a separate assessment of whether a control transaction under s611 is '*fair*' and whether it is '*reasonable*'. We have therefore considered the concepts of '*fairness*' and '*reasonableness*' separately. The basis of assessment selected and the reasons for that basis are discussed below.

Fairness

RG111.25 requires an independent expert to evaluate an issue of securities under s611 that has a similar effect to a takeover offer as if it was a takeover offer. RG111.11 defines a takeover offer as being fair if the value of the consideration is equal to, or greater than, the value of the securities subject to the offer.

Accordingly, we have assessed whether the Proposed Transaction is fair by comparing the value of a PNW share before the Proposed Transaction with the consideration offered to Shareholders. As Shareholders would retain their PNW shares if the Proposed Transaction proceeds (as opposed to exchanging them for cash or the acquirer's scrip as in a takeover offer) the effective consideration is the continued ownership of a PNW share, which will become a share in the Proposed Merged Entity.

The value of a PNW share before the Proposed Transaction has been determined on a control basis (i.e. including a control premium). This is consistent with the requirement of RG111.11 that the comparison for a takeover must be made assuming a 100% interest in the target company.

After the Proposed Transaction, a PNW share will effectively be a share in the Proposed Merged Entity (i.e. PNW and Crocmedia combined). This has been assessed on a minority interest basis (i.e. excluding a control premium) as Shareholders would own a minority stake in the Proposed Merged Entity should the Proposed Transaction occur.

We have assessed the values of a PNW share and a Proposed Merged Entity share at fair market value, which is defined by the International Glossary of Business Valuation Terms as:

> *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.*

While there is no explicit definition of value in RG111, this definition of fair market value is consistent with basis of value described at RG111.11 and common market practice.

Special value is defined as the amount a specific purchaser is willing to pay in excess of fair market value. A specific purchaser may be willing to pay a premium over fair market value as a result of potential economies of scale, reduction in competition or other synergies they may enjoy arising from the acquisition of the asset. However, to the extent a pool of hypothetical purchasers could all achieve the same level of synergies the value of those synergies may be included in fair market value. Special value is typically not considered in forming an opinion on the fair market value of an asset. Our valuations of PNW and the Proposed Merged Entity do not include any special value.

Reasonableness

In accordance with RG111, we have defined the Proposed Transaction as being reasonable if it is fair, or if, despite not being fair, Leadenhall believes that there are sufficient reasons for Shareholders to vote for the proposal. We have therefore considered whether the advantages to Shareholders of the Proposed Transaction outweigh the disadvantages. To assess the reasonableness of the Proposed Transaction we have considered the following significant factors recommended by RG111.13:

- The size of existing shareholding blocks in PNW
- The liquidity of the market in PNW's shares
- Any special value of PNW to Crocmedia
- The likely market price of PNW shares if the Proposed Transaction is rejected
- The value of PNW to an alternative bidder and the likelihood of an alternative offer

We have also considered other significant advantages and disadvantages to Shareholders of the Proposed Transaction.

2.3 Individual circumstances

We have evaluated the Proposed Transaction for Shareholders as a whole. We have not considered its effect on the particular circumstances of individual investors. Due to their personal circumstances, individual investors may place a different emphasis on various aspects of the Proposed Transaction from the one adopted in this report. Accordingly, individuals may reach a different conclusion to ours on whether the Proposed Transaction is fair and reasonable. If in doubt investors should consult an independent financial adviser about the impact of this Proposed Transaction on their specific financial circumstances.

3 INDUSTRY ANALYSIS

3.1 Introduction

Both PNW and Crocmedia predominantly generate revenues from advertising via the radio broadcasting industry, with broadcasting accounting for 70% of the FY17 total revenue for PNW and 81% for Crocmedia. We have therefore focussed our analysis on the radio broadcasting industry in Australia, with a brief analysis of the magazine publishing industry in Australia.

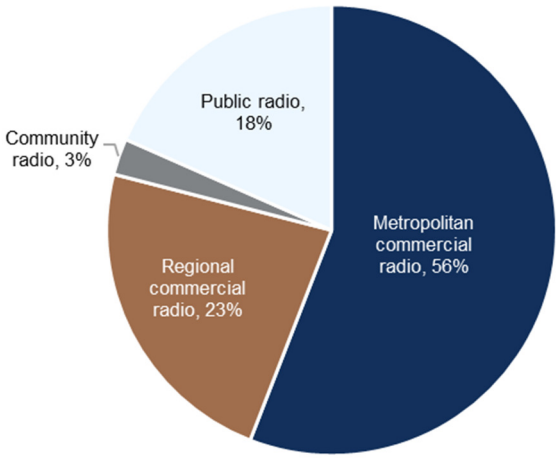
3.2 Radio broadcasting in Australia

3.2.1 Overview and trends

Radio is a unique platform providing listeners with an interactive relationship with the broadcaster which is not easily replicated in other media platforms. According to the IBISWorld industry report, industry players in Australia have increasingly focused on talkback and live sports over the past five years as popular talkback hosts can often generate high ratings and boost advertising revenue for radio networks.

Advertisers are the largest market in the industry, where media buying agencies seek to advertise their own and client's products and services by purchasing air-time during radio programs. Australia's radio broadcasting industry has consistently generated approximately $1.7 billion per year in revenue over the past decade, split among the following segments (described in further detail below):

Figure 1: Industry segmentation



Source: IBISWorld

Metropolitan commercial radio

These radio stations have programs that are typically aimed at providing entertainment, such as popular music targeting specific demographics, talkback programs discussing current news topics and live sports broadcasts. These programs are broadcast in metropolitan areas and therefore tend to generate more advertising revenue as they generally reach larger audiences, hence accounting for the largest share of industry revenue. Furthermore, due to rising migration and people moving from regional to metropolitan areas for work opportunities, this has resulted in the increase in their market share over the past five years. According to figures released by Commercial Radio Australia, as sourced by Deloitte, radio revenue for metropolitan markets was flat in FY17. Total advertising revenue in FY17 for the five metropolitan markets in Australia decreased by 0.21% to approximately $774 million, which was the first contraction since 2012. However, the Melbourne metropolitan market bucked the trend, increasing slightly by 0.27%.

Regional commercial radio

This segment provides similar content to metropolitan commercial radio broadcasters to regional areas. As regional areas are less populous than metropolitan regions, their markets are significantly smaller, and this results in lower revenue from advertisers and market share over the period.

Public radio

Public radio broadcasters include the Australian Broadcasting Corporation ("**ABC**") and Special Broadcasting Service. As these radio stations primarily receive government funding, revenue from advertising is small. As a result of budget cuts imposed by the Federal Government in recent years, the segment's market share of industry revenue has declined.

Community radio

Community radio stations generally broadcast to small local populations, catering to specific communities or social groups. The market share of industry revenue has decreased over recent years as niche community broadcasting services have become increasingly accessible online.

3.2.2 Level of competition

The radio broadcasting industry is highly competitive, with radio broadcasters facing strong competition. Radio stations compete with rival broadcasters for a share of the total listening audience as media buying agencies typically prefer to advertise on stations and in timeslots that reach the largest number of consumers. Radio broadcasters therefore tend to monitor changes in consumer preferences in order to change their mix of programming and personalities to maintain their market share.

According to the IBISWorld industry report, the four largest players (by market share), Southern Cross Media (26.9%), the ABC (18.2%), Here, There & Everywhere (13.8%) and Nova Entertainment (12.4%) are expected to account for over 70% of industry revenue in FY18. The high level of concentration is similar to other traditional media industries within Australia. The level of concentration is limited by the *Broadcasting Services Act 1992* which prevents radio networks from owning more than two radio stations in a defined licence area, promoting media diversity.

Media buying agencies often seek to advertise on other media platforms thus providing additional competition for radio broadcasters' advertising revenue. The rising prevalence of online media platforms and subsequent growth in online advertising has contributed to the industry's rising level of competition in recent years. For instance, the dominance of online platforms such as Facebook and Google have made advertising space cheaper for media buying agencies. Nonetheless, advertising on the radio is still a relatively cheap way of reaching out to people, particularly during morning and afternoon traffic peak hours.

3.3 Key drivers of the radio broadcasting industry

The performance of the radio broadcasting industry is mainly driven by the demand from media buying agencies. As radio broadcasting services are provided to listeners free of charge, advertising spend is crucial to the industry's survival. According to the IBISWorld industry report, demand is expected to increase in FY18, providing more opportunities for the industry.

As many consumers listen to the radio while driving, especially during morning and afternoon peak hours, an increase in the number of motor vehicles on the road usually increases the number of radio listeners. This subsequently boosts advertising revenue, as advertisers seek to reach the largest possible audiences. The number of motor vehicles is similarly expected to rise in FY18 to the benefit of radio broadcasters.

The range of alternative media platforms, such as streaming websites and applications like YouTube, Facebook and Spotify, has increased throughout Australia as the number of mobile phones increases. Therefore, the density of mobile telecommunications poses a threat to the radio broadcasting industry since they are alternatives for listeners.

Within the industry itself, radio broadcasters with a loyal customer base can generate consistent ratings and leverage more revenue from advertisers. In addition, radio programs that dominate ratings in the competitive morning and afternoon traffic peak hours timeslots generally increase revenue due to the larger volume of listeners. Therefore, in order to capture loyalty and appeal to radio listeners, it is necessary for radio broadcasters to understand consumer demographics.

3.4 Magazine publishing in Australia

Magazines earn revenue from multiple sources, such as printed copy sales, subscriptions and advertising. Due to Australia's relatively small population, most magazines have traditionally relied on advertising revenue rather than copy sales for profits. Most magazines focus on a specific topic that appeals to certain demographics, allowing advertisers to market products towards their target audiences.

The magazine publishing industry has struggled in recent years to adapt to a rapidly changing and increasingly diverse media landscape. Online platforms, such as Google, Facebook and Instagram, allow advertisers to reach their target audience more efficiently and often at a lower cost. This trend, in addition to falling readership numbers in mainstream media, has compounded the industry's troubles, contributing to a decline in revenue and profitability over the past five years.

Magazine publishers have responded by introducing a multi-platform business model where many mastheads can now be accessed on digital devices, allowing them to be consumed via different media platforms. Therefore, most magazine publishers have invested in their online platforms, employing teams of graphic designers and software engineers. As a result, wages have increased as a share of revenue, putting further downward pressure on profitability.

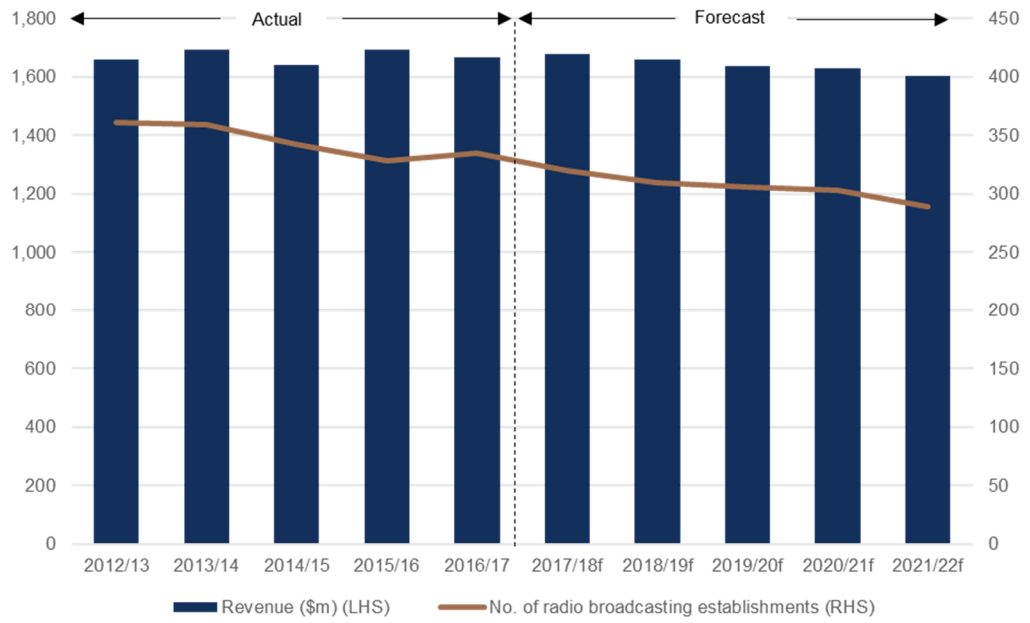
The most popular magazines in Australia have traditionally been magazines aimed at women, such as Cleo and Vogue Australia. However, in recent years, women's magazine readership has fallen as younger readers migrate towards online platforms to keep up-to-date with the latest fashion trends. On the other hand, magazines that publish niche content have not suffered as badly. Smaller publications, such as design focussed frankie Magazine, have risen in popularity and have expanded their customer bases overseas. The ability of these publications to provide content that fills a niche and is not easily replicated has slightly mitigated the industry's recent poor performance.

3.5 Outlook

According to PwC's 16th annual Australian Entertainment & Media Outlook report, Australian traditional media and entertainment companies should collaborate and partner with rivals to achieve growth in the face of strong headwinds. There has been a continuing divergence in traditional and digital media spend across Australia's media and entertainment industry, with the switch of consumer and advertising spending from traditional media to digital set to continue over the next five years. Notwithstanding the trend for traditional media, terrestrial radio revenue is expected to show a compound annual growth of 1.6% to FY21. However, print magazines continue to face strong headwinds, with revenue from both advertising and circulation forecast to decline by approximately 10.0% annually to FY21.

Contrary to the PwC report, IBISWorld estimates that radio broadcasting revenue will decline at an annualised 1.2% over the five years to FY22. Figure 2 below shows the historical and projected movements in industry revenue.

Figure 2: Revenue and number of radio broadcasting establishments



Source: IBISWorld

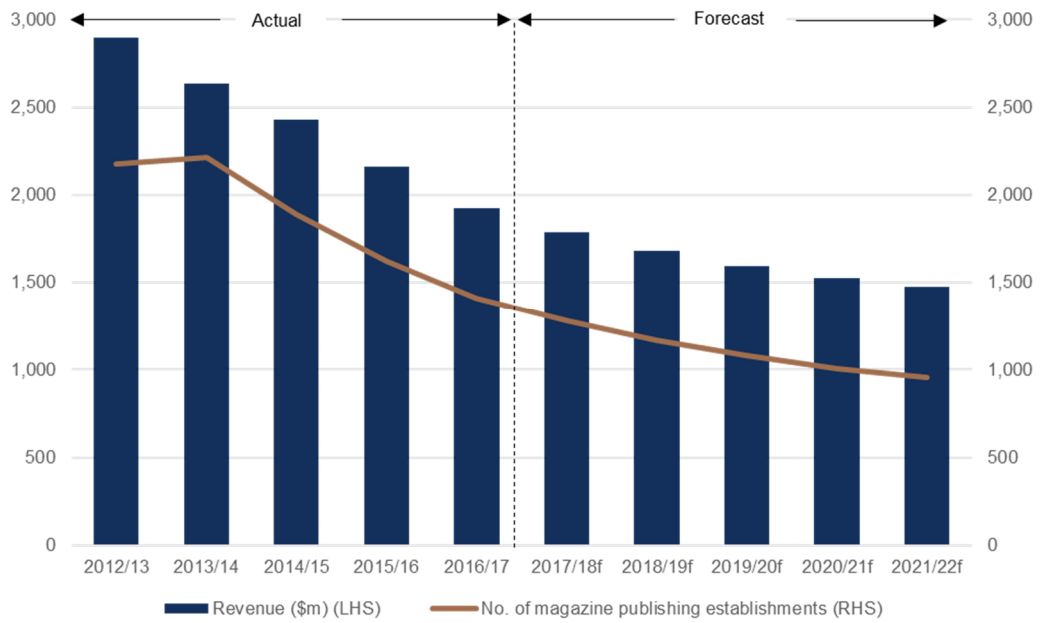
Overall demand from media buying agencies is projected to rise steadily over the next five years, but an increasing share of this advertising revenue is expected to be diverted towards alternative media platforms, particularly websites and other online platforms. Rising competition among rival radio broadcasters and other media platforms will further aggravate the challenges ahead. Further, wage costs are expected to rise as a share of revenue as radio broadcasters compete to attract and retain popular on-air personalities, putting pressure on profitability.

Common between the two reports is the trend of radio broadcasters consolidating to rein falling profit margins as many of the costs associated with broadcasting radio programs are fixed. For example, the merger of Macquarie Radio Network and Fairfax Radio Network in 2015. In addition, some players have rationalised their brands across their regional and metropolitan license areas. For example, in 2016, Southern Cross Media announced that it would rebrand 25 of its regional LocalWorks networks to the Triple M brand, allowing the network to increase brand recognition and streamline the sale of advertising.

In September 2017, the Federal Government passed several media reforms impacting the radio broadcasting industry. The two-out-of-three rule, which previously prevented a firm from owning a television network, radio station and newspaper in the same market, was abolished. This move may increase mergers and acquisition activity across the media sector over the next five years, especially as firms seek to cut their cost base to compete with digital media. However, the two-to-a-market rule, preventing radio networks from owning more than two radio stations within the same city or region, was retained under the media reforms. This may therefore curb the effects of abolishing the two-out-of-three rule over the same period.

In agreement with the PwC report on the outlook for magazine publishing, IBISWorld estimates that magazine publishing revenue will fall by an annualised 5.2% through FY22. Figure 3 below shows the historical and projected movements in industry revenue.

Figure 3: Revenue and number of magazine publishing establishments



Source: IBISWorld

The decline of the magazine publishing industry is expected to slow as publishers further adapt to the technological revolution and the shift towards online publications. This is supported by the latest results from the Roy Morgan Australian Magazine Readership report for the 12 months to September 2017, as over 3-in-4 Australians consume magazines across print and online. In addition, six of Australia's top 15 magazines have increased their print readership over the period. While food and entertainment continue to be Australians most popular magazine category, women's fashion magazines had the largest year-on-year readership growth with PNW's frankie Magazine increasing readership by 21% to 398,000 readers over the 12-month period.

Nonetheless, according to IBISWorld, the number of publishing establishments are projected to fall over the next five years as publishing facilities close in the wake of online migration. Consolidation is also expected to occur as the major players aim to improve their economies of scale and increase revenue and market share.

4 PROFILE OF PNW

4.1 Background

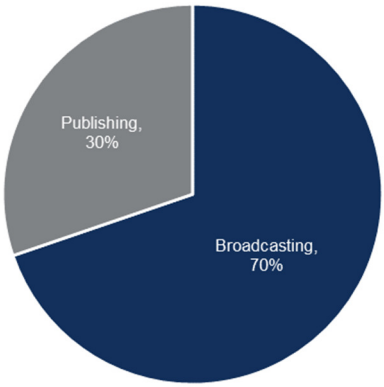
PNW is a media company based in Richmond, Australia and is listed on the ASX. PNW operates in the radio broadcasting, publishing and digital media industry serving niche audiences. PNW operates three digital only radio stations, two radio broadcast channels and is also a publisher of lifestyle and sports magazines.

PNW employs the strategy of designing and monetising shareable content that is unique to target markets which can be distributed through multiple channels. As a result of this strategy, PNW has a strong sustainable digital capability and develops complementary partnerships to leverage their expertise and resources in areas such as video gaming, podcasting and social media.

4.2 Overview of operations

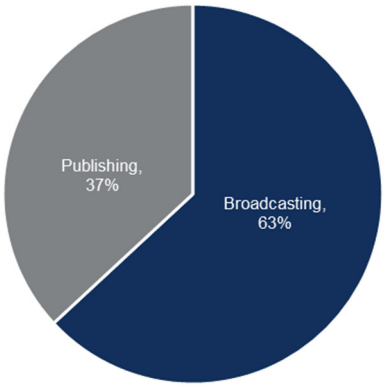
PNW operates through two segments, Broadcasting and Publishing. The FY17 revenue and underlying EBITDA split between the two segments (excluding head office) was as follows:

Figure 4: PNW FY17 revenue split



Source: PNW

Figure 5: PNW FY17 underlying EBITDA split



Source: PNW

Further information of the respective segments is provided below.

4.2.1 Broadcasting

PNW owns two Melbourne AM commercial broadcasting licenses, broadcasting 24/7 on:

- **1116 Sports Entertainment Network** ("**SEN**") – a sports radio station throughout the Melbourne metropolitan area, including live broadcast of the AFL covering six games each week, along with A-League, horse racing, NBL, tennis and other major sporting events. During the financial year ("**FY**") ended 30 June 2017, 1116 SEN was successful in securing another six years of AFL broadcast rights, which is an important part of the station's 24/7 sports programming.
- **Classic Rock Radio** – plays classic rock music from the 1960s to 1980s on digital audio plus, 1377AM in Melbourne and online at classicrock1377.com.au.

The three digital radio stations which PNW operates cover the following genres:

- **AUSSIE** – an all-Australian radio station
- **KOOL** – plays songs from the 1970s and 1980s
- **Rythmos** – an ethnic radio station

The Broadcasting segment mainly generates revenue through advertising, derived from the sale of advertising time. SEN is the key brand of the business which delivers 90% of broadcast revenue and is therefore an integral part of the segment's future plans. The vision for SEN is to deliver first-class sports content, having it widely-distributed on multiple platforms and becoming the number one sports content provider in Australia.

4.2.2 Publishing

The Publishing segment was created as a result of PNW acquiring Morrison Media Services Pty Ltd ("**Morrison Media**") in December 2014 for approximately $10.9 million. This acquisition was part of PNW's strategy to diversify their portfolio beyond broadcasting and sports. Morrison Media is the publisher of frankie Magazine, which has been a strong performer for print magazines in Australia, covering art, fashion and music. According to the latest Roy Morgan Research of Australian Magazine Readership for the twelve months to 30 September 2017, frankie Magazine readership was up 21% to 398,000 readers and is continually rated as Australia's number one women's fashion magazine. Other magazines published under this segment include:

- **SPACES** – exploring homes, studios, shops and cafes of graphic designers, photographers, vintage collectors and shop owners
- **Smith Journal** – quarterly men's publication featuring history, photography, science, design, arts
- **SEN Inside Football** – monthly issue covering the AFL

The Publishing segment mainly derives revenue from placement of advertising in magazines, sales of magazines and subscriptions.

4.3 Competitive position

The table below sets out the strengths, weaknesses, opportunities and threats analysis ("**SWOT**") for PNW.

Table 4: SWOT analysis of PNW

Strengths	Weaknesses
♦ Experienced management team with industry-specific and organisation knowledge. ♦ Equipped with two high-performing assets and brands, SEN and frankie Magazine. ♦ Engaged and loyal audience. ♦ Strong growth in the number of podcast and mobile application downloads. ♦ Strong engagement with audiences through PNW's ability to be adaptable, scalable and innovative.	♦ The need to further develop video capabilities such as content strategy, filming and editing, may lead to the loss of customers to competitors who already have strong content. ♦ Strong reliance on SEN as the primary source of broadcasting revenue. Therefore, AFL off-seasons generally represent little to no monthly revenue growth. ♦ Relatively poor performance from the Publishing segment with the discontinuation of a number of publications in recent years.
Opportunities	**Threats**
♦ Digital growth opportunities through mobile and video content creation, digital partnerships and data and analytics capabilities. ♦ Expand audience base nationally, beyond Melbourne and Victoria. ♦ Refocus of the sales structure to ensure all platforms have adequate sales representation and constant training to upskill teams on the latest digital trends in advertising. ♦ Additional partnerships and alliances with other sports, media and entertainment networks and stations.	♦ Emerging competition in the sports entertainment market with the issue of additional licenses and rights. ♦ Media technology is constantly evolving which brings about a threat of new entrants with superior technology to PNW. ♦ Risk of renewal of AFL rights when the contract expires in 2022. ♦ Refinance of loan facility in March 2018. ♦ Loss of key clients will impact the ability to generate profits, particularly for the Classic Rock Radio station.

Source: PNW and Leadenhall analysis

4.4 Key personnel

The current directors and senior management team of PNW comprise:

Table 5: PNW Key Personnel

Name and title	Experience
Craig Coleman Non-Executive Chairman	Mr Coleman is an experienced senior executive and director with a 30-year career incorporating banking and finance, corporate advisory and investment and funds management. He has previously held positions as managing director of Home Building Society Ltd and senior executive positions with ANZ Banking Group Ltd. He is the co-founder and executive chairman of Viburnum Funds Pty Ltd, an investment fund managing public and private equities which has a 19.5% shareholding in PNW. He is also currently the non-executive chairman of Universal Biosensors Inc and a non-executive director of Bell Financial Group Ltd.
Andrew Moffat Non-Executive Director	Mr Moffat has over 20 years' experience in corporate and investment banking and is currently the sole principal of Cowoso Pty Ltd, a company providing corporate advisory services. He is also a non-executive director of 360 Capital Group Ltd and previously served as the chairman of PNW.
Colm O'Brien Independent Non-Executive Director	Mr O'Brien has over 20 years' experience at executive level, including nine years as CEO with media company Aspermont Limited. He is a director at Carrington Partners, a specialised management consultancy business focused on board and executive level practical advice. He is currently a non-executive director of Kabuni Limited, a non-executive director of Aspermont Limited and a non-executive director of Magyar Mining PLC.
Stephen Sweeney CFO and Company Secretary	Mr Sweeney was appointed to the position of company secretary on 24 January 2007. He is also the company's CFO and has 25 years' experience in senior financial management positions with listed, financial services and government entities.

Source: PNW

4.5 Financial performance

The audited consolidated statements of financial performance for FY16, FY17 and unaudited consolidated statement of financial performance for the twelve months to 31 October 2017 are set out below.

Table 6: Statement of Financial Performance of PNW

$'000	FY16	FY17	LTM Oct'17
Revenue			
Broadcast revenue	14,449	15,293	15,494
Publishing revenue	9,322	6,626	5,968
Other revenue	188	163	49
Total revenue	**23,959**	**22,082**	**21,511**
Sales and marketing expenses	(4,068)	(4,331)	(3,393)
Administration and occupancy expenses	(3,727)	(3,342)	(3,680)
Technical expenses	(7,112)	(6,952)	(7,067)
Production expenses	(4,759)	(3,594)	(3,083)
Corporate expenses	(856)	(790)	(1,018)
Impairment expenses	-	(8,239)	(8,239)
Restructuring expenses	(611)	(262)	(202)
EBITDA	**2,826**	**(5,428)**	**(5,171)**
Depreciation	(469)	(404)	(404)
Amortisation	(634)	(636)	(642)
EBIT	**1,723**	**(6,468)**	**(6,217)**
Interest income	24	11	8
Interest expense	(333)	(314)	(332)
Share of profit of associates	15	39	35
Profit/(loss) before income tax	**1,429**	**(6,732)**	**(6,506)**
Income tax expense	(336)	(609)	(645)
Net profit/(loss) after income tax	**1,093**	**(7,341)**	**(7,151)**
Revenue growth %	*n/a*	*-8%*	*n/a*
EBITDA margin[1] %	*14%*	*14%*	*15%*
EBIT margin[1] %	*10%*	*9%*	*10%*
Earnings/(loss) per share[2] ($)	*0.02*	*(0.10)*	*(0.10)*

Source: PNW
Notes:
1. Adjusted EBITDA and EBIT margins exclude one-off impairment and restructuring expenses.
2. Calculated on an undiluted basis.

In relation to the financial performance of PNW set out above, we note the following:

- Revenue from the Broadcasting segment has increased by 6% in FY17 mainly as a result of the launch of a new breakfast show. Revenue from the Publishing segment was down approximately 29% due to the discontinuation of some loss-making publications. The significant decrease in publishing revenue has resulted in an 8% fall in total revenue in FY17.
- Impairment expenses are comprised of a $7.4 million write-off of goodwill arising from the acquisition of Morrison Media in FY15 and $0.8 million relating to the impairment of mastheads in Publishing.
- Excluding the impairment charges, operating expenses have remained relatively consistent in the past two years. Approximately 70% of the total operating expenses pertain to the Broadcasting segment.
- Restructuring expenses pertain to the restructuring of PNW which include payments for redundancies.
- Adjusted EBITDA and EBIT margins for the past two years have been consistent at around 14% and 9% respectively.
- A normalisation of earnings has been performed in Section 8.

4.6 Financial position

The audited consolidated statements of financial position as at 30 June 2016, 30 June 2017 and unaudited consolidated statement of financial position as at 31 October 2017 are set out in the table below.

Table 7: Statement of Financial Position of PNW

$'000	30-Jun-16	30-Jun-17	31-Oct-17
Current assets			
Cash and cash equivalents	1,908	1,663	1,647
Trade receivables and prepayments	4,704	4,533	5,091
Total current assets	**6,612**	**6,196**	**6,738**
Non-current assets			
Intangible assets	19,935	11,192	10,784
Property, plant and equipment	1,382	1,197	1,382
Investments and receivables from associate	266	293	277
Deferred tax asset	769	648	680
Total non-current assets	**22,352**	**13,330**	**13,123**
Total assets	**28,964**	**19,526**	**19,861**
Current liabilities			
Trade and other payables	(3,358)	(2,493)	(2,223)
Borrowings	-	(5,750)	(5,750)
Employee entitlements	(740)	(607)	(673)
Income tax	(325)	(363)	(352)
Total current liabilities	**(4,423)**	**(9,213)**	**(8,998)**
Non-current liabilities			
Borrowings	(5,750)	-	-
Employee entitlements	(53)	(7)	-
Deferred tax liability	(766)	(649)	(656)
Total non-current liabilities	**(6,569)**	**(656)**	**(656)**
Total liabilities	**(10,992)**	**(9,869)**	**(9,654)**
Net assets	**17,972**	**9,657**	**10,207**
Net tangible liabilities per share[1] ($)	*(0.03)*	*(0.02)*	*(0.01)*

Source: PNW
Note 1: Calculated by deducting the balance of intangible assets from net assets and on an undiluted basis.

In relation to the historical financial position of PNW set out above, we note the following:

- Cash decreased by $0.2 million during FY17 as a result of cashflow from operations ($1.4 million) being used to fund dividends ($1.0 million), restructuring costs ($0.2 million) and the purchase of property, plant and equipment ($0.4 million). Cashflow from operations was approximately 31% lower than FY16.
- Intangible assets decreased significantly in FY17 due to an impairment of the goodwill on the acquisition of Morrison Media, as well as the impairment of the Inside Football masthead.
- PNW has a $7.35m loan facility with the Commonwealth Bank of Australia ("**CBA**") which was due to mature on 17 December 2017. However, a three-month extension to 30 March 2018 was announced by PNW on 8 December 2017. The facility has a variable interest rate which is based on the bank bill swap rate plus a margin. A significant portion of this facility is an interest-only bank loan of $5.75 million which was fully drawn down for the acquisition of Morrison Media. In accordance with RG111.15, we have assumed that the loan will be refinanced and hence our valuations have been prepared on a going concern basis.

4.7 Capital structure and shareholders

As at 12 January 2018, PNW had a total of 71.1 million ordinary shares on issue. In addition, there are currently a total of 1.03 million share options on issue, where approximately 1.0 million share options are vested and exercisable at $0.30 per share, expiring on 1 September 2018.

The following table sets out details of PNW's substantial shareholders as at 12 January 2018:

Table 8: PNW's substantial shareholders

Shareholder	Shares held	% total shares
Ron Hall	20,109,998	28.3%
Viburnum Funds	13,851,198	19.5%
Myer Herszberg	9,610,136	13.5%
Radio 3AW Melbourne	7,932,357	11.2%
Peter Quattro	3,847,171	5.4%
Other shareholders	15,742,410	22.1%
Total	**71,093,270**	**100.0%**

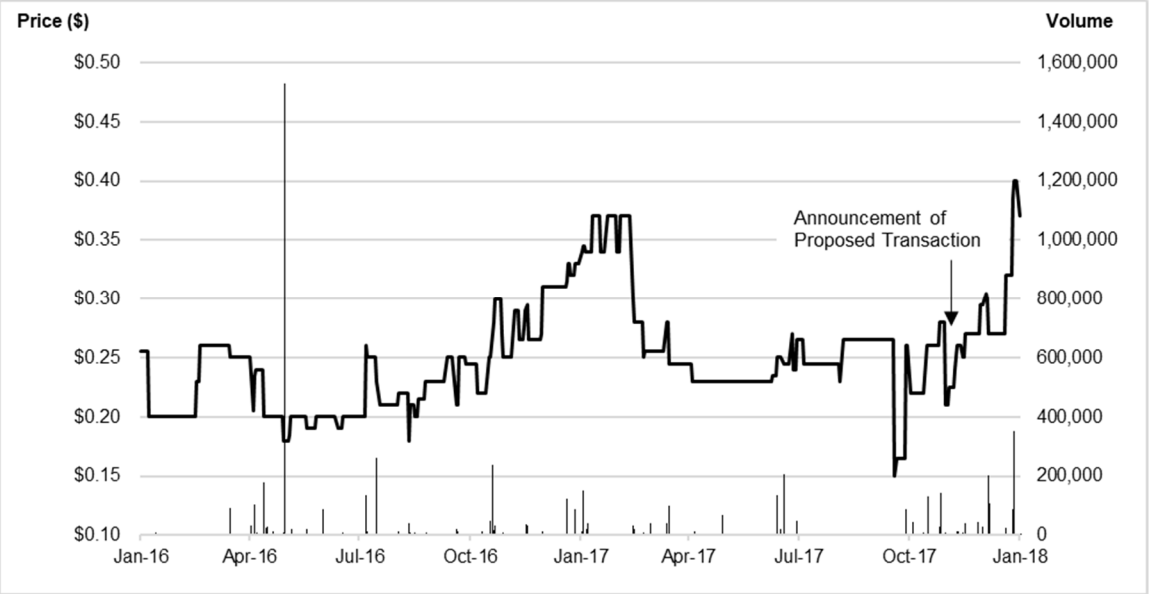
Source: PNW and ASX announcements

We note that there are no controlling shareholders, although the top four shareholders hold approximately 73% and Mr Ron Hall is able to block a special resolution as a result of his shareholding exceeding 25%.

4.8 Share price performance

The following chart shows the share market trading of PNW shares for the past two years:

Figure 6: Share price performance of PNW shares



Source: S&P Capital IQ

In relation to the trading of PNW shares over the last two years we note the following:

- PNW shares have traded infrequently over the period with an average daily volume of approximately 11,000 shares. There were also a number of periods of several days in which there were no trades while daily market trading of PNW shares is often under $10,000. In addition, the total volume of shares traded over the past six months, up to the date of announcement of the Proposed Transaction, was approximately 1% of the total number of shares outstanding. The illiquidity is possibly a result of a large proportion of the shares on issue being held by long-term holders including management and directors.
- The trading price has ranged between 15 cents to 40 cents per share with a volume-weighted average price ("**VWAP**") over the period of approximately 25 cents, which is lower than the current share price of 39 cents.

- The spike in volume and slight fall in price in May 2016 followed changes made in the executive team of PNW, with the resignation of the former Group CEO.
- There were two occurrences of a significant fall in share price. The first of which happened in February 2017 on the announcement of PNW's half yearly results, with the share price falling from 37 cents to 30 cents. The second occurrence was in September 2017, where the share price fell from 26.5 cents to 15 cents, similarly around the period of announcing their full year results.
- Since the announcement of the Proposed Transaction on 22 November 2017, the share price has increased from the previous closing price of 22.5 cents to a high of 40 cents over a two-month period.

4.9 Outlook

PNW anticipates revenue growth opportunities to occur predominantly from the Broadcasting segment via an increase in both agency and direct customer radio sales in the Melbourne market. In addition, digital sales are expected to increase marginally as PNW continues to build on its digital capabilities. EBITDA margins from the Broadcasting segment are also projected to increase steadily in the near future as a result of the projected increase in revenue.

The Publishing segment is expected to generate lower revenue in FY18 due to the closure of an underperforming magazine title. Increases in sales of the popular frankie Magazine and Smith Journal are expected to cushion the impact of the loss in revenue from the discontinued publications. Despite a lower revenue, EBITDA is projected to increase from cost savings attributable to the closure of loss making publications, in addition to cost efficiency initiatives in the frankie Magazine and Smith Journal publications.

5 PROFILE OF CROCMEDIA

5.1 Background

Crocmedia is a content and entertainment business which connects brands to metropolitan and regional audiences through various media platforms. Crocmedia is Australia's only independent syndicator of sports content, with the core of its business in radio syndication since its first program, Off the Bench, which went to air in February 2008.

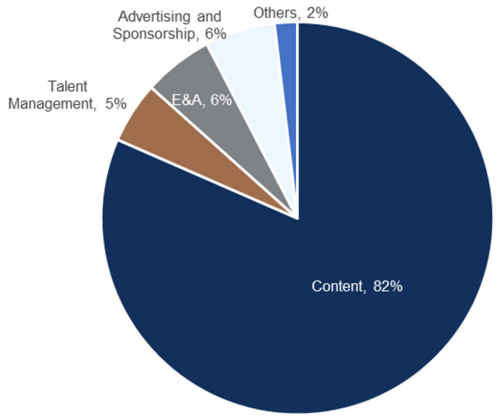
Crocmedia's vision is to build an asset base across Australia which includes:

- Owned radio, digital and social media
- Syndicated radio and television content
- Sales agency opportunities across (but not limited to) RSN, Macquarie Radio Network and Radio TAB and high-profile talents through Bravo Talent Management ("**Bravo**")
- Stadium assets, including corporate hospitality, and the possibility to facilitate the sale of big screen and LED advertising in the major sporting stadiums across Australia
- Rights to major events, such as AFL Country Game and Spring Racing
- Exclusive live sports broadcasting rights

5.2 Overview of operations

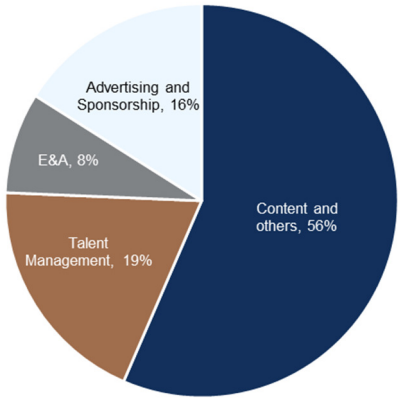
Crocmedia mainly operates through four segments, Content, Talent Management, Events and Brand Activation ("**E&A**") and Advertising and Sponsorship. The FY17 revenue and EBITDA split was as follows:

Figure 7: Crocmedia FY17 revenue split



Source: Crocmedia

Figure 8: Crocmedia FY17 EBITDA split



Source: Crocmedia

Further information of the respective segments is provided below.

5.2.1 Content

Crocmedia specialises in creating a range of radio, television and digital content for brands across a wide array of sports, producing 130-140 hours of radio per week and broadcasting to over 200 stations around Australia and New Zealand through syndication. Current major programs include:

- **AFL Nation** – in 2016, Crocmedia secured a six-years deal with the AFL to broadcast to over 200 markets Australia-wide and has an estimated audience size of 785,000.
- **Off the Bench** – is an entertainment based sporting program which is now one of the largest sports programs across Australia. A corresponding television show is also produced which focuses on local and country football.
- **Sportsday** – commenced in 2009 across regional Victoria before expanding to the other states. Multiple versions of the show are now produced daily, broadcast across the various states. It has expanded its footprint into metropolitan Melbourne, Adelaide and Perth with programs currently on-air in these markets.

Revenue is derived from advertising, mainly through brand integration, by national brands such as McDonald's, Red Energy and Kia. Crocmedia covers all costs of production, such as talent and producers, as well as payments to radio and TV stations to deliver programming on their platforms in return for three to five minutes of advertising per hour within the programs. Content sales represent approximately 82% of Crocmedia's total revenue for FY17.

5.2.2 Talent Management

Bravo is a boutique talent management agency that specialises in and offers exclusive representation of media professionals including presenters, broadcasters and entertainers across TV, radio, sports and entertainment. Bravo represents some of the most recognisable names in Australian television and radio, such as Scott Cam, Shaynna Blaze, Ross Greenwood, Merv Hughes, Jennifer Adams and AFL Hall of Fame members, Wayne Carey and Dermott Brereton.

Bravo also offers a unique booking service for their clients and are able to source and secure talents for brands and events including:

- PR and advertising campaigns
- Corporate business and charity events
- Product endorsements
- Red carpet events
- Personal appearances
- Speaking engagements

Bravo generates revenue mainly from the sale of their talents' services, contributing approximately 5% of Crocmedia's total revenue for FY17, net of payments to talents.

5.2.3 E&A

The E&A division provides brand activation services and creative solutions for brands wanting to activate or leverage their sponsorships and media partnerships and/or to reach consumers through non-traditional means and social media. The division also develops touring events, such as Road to Origin, and is responsible for delivering a number of promotional events for the other divisions of Crocmedia.

BallPark was fully acquired by Crocmedia in May 2017 and has since been incorporated within this division. BallPark provides customers with exclusive access to events. Since its inception in 2014, BallPark has developed a reputation for organising fun, once-in-a-lifetime sports, entertainment and travel tours for individuals and corporate groups, which include the Super Bowl.

The E&A division, together with the recently acquired and incorporated BallPark, derives revenue through the sales of brand activation advice and exclusive access to events, contributing approximately 6% of Crocmedia's total revenue for FY17.

5.2.4 Advertising and Sponsorship

In February 2017, Crocmedia acquired an 87% interest in Thread, which is a boutique creative agency specialising in:

- Brand strategy
- Campaign planning
- Concept development
- Sponsorship strategy and management
- Events
- Social media

With the acquisition, Thread now manages key sponsorship agreements with major clients and the AFL for major brands. Thread contributed approximately 6% of Crocmedia's total revenue for FY17.

5.3 Competitive position

The table below sets out the SWOT for Crocmedia.

Table 9: SWOT analysis of Crocmedia

Strengths	Weaknesses
♦ Experienced management team with industry-specific and organisation knowledge. ♦ Recently awarded exclusive rights, such as the FFA commercial radio rights for six years and to sell RSN 927 programming, which is a sports racing radio station based in Melbourne. ♦ Secured a six-year deal in 2016 with the AFL to broadcast to over 200 markets Australia-wide. ♦ Strong and stable revenue growth in recent years, particularly from content sales which represent its popularity. ♦ Healthy and growing sales pipeline, with an increased level of committed sales in FY18.	♦ Crocmedia currently has limited access to capital which may inhibit its growth.
Opportunities	**Threats**
♦ Crocmedia's recent investment in the Coventry Street TV studio presents an opportunity to produce visual content across television, web and social media to cater to young demographics. Crocmedia's television division currently only generates about 30% of total content income. ♦ Crocmedia has recently agreed in principle to become the regional syndication arm of a national radio network. ♦ Opportunities exist to expand Crocmedia's digital products with the appointment of a national digital sales director.	♦ Heavy reliance on key personnel. Loss could cause material disruption to the business' activities and operations in the short to medium term. ♦ Inability to retain existing media rights contracts as a significant proportion of revenue is dependent on securing these rights. ♦ Emerging competition in the sports entertainment market with the issue of additional licenses and rights. ♦ Media technology is constantly evolving which brings about a threat of new entrants with superior technology to Crocmedia. ♦ Risk of renewal of radio and distribution rights when the contracts expire.

Source: Crocmedia and Leadenhall analysis

5.4 Key personnel

The current directors and senior management team of Crocmedia comprises:

Table 10: Crocmedia directors and senior management team

Name and title	Experience
Craig Hutchison Founder and CEO	Mr Craig Hutchison is a household name and multi award winning journalist in sport. He has a vast network and has assisted with completing deals and providing advice on alternative ways to structure negotiations.
Jodie Simm General Manager	Ms Jodie Simm has had 10 years of experience working with Deloitte Growth Solutions as a Client Director consulting to SME's regarding all tax, business, and accounting issues before working with Crocmedia and has now been with the business for over 10 years.
Chris Giannopoulos Executive Director	Mr Chris Giannopoulos was Director of Client Management and New Business Development at IMG for 14 years before he joined Crocmedia in March 2011. He has extensive media contacts and strong negotiation skills and is focusing on building its distribution platforms along with managing Bravo Talent Management.
Sam Bingley Chief Commercial Officer	Mr Sam Bingley has over 17 years of experience in the Sporting and Radio Industry, including Austereo, the AFL & Melbourne Racing Club. He brings exceptional managerial experience to Crocmedia's sales team of 24 personnel. He has extensive networks across the Corporate Media Industry and through media agencies Australia-wide.
Mark Rothfield Non-Executive Director	Mr Mark Rothfield is a managing director of the Chase Properties and Development Group, which is a substantial shareholder of Crocmedia. He was also a director of a ladies-fashion importing company for over 30 years.

Source: Crocmedia

5.5 Financial performance

The unaudited consolidated statements of financial performance for FY16, FY17 and twelve months to 31 October 2017 are set out below.

Table 11: Unaudited Statement of Financial Performance of Crocmedia

$'000	FY16	FY17	LTM Oct'17
Revenue			
Content sales	13,944	17,805	20,796
Non-content sales	2,135	4,275	4,863
Total revenue	**16,079**	**22,080**	**25,659**
Cost of sales	(6,166)	(8,600)	(10,800)
Gross profit	**9,913**	**13,480**	**14,859**
Salaries	(5,478)	(6,526)	(7,941)
Other operating expenses	(2,821)	(4,404)	(3,218)
EBITDA	**1,614**	**2,550**	**3,700**
Depreciation & amortisation expenses	(161)	(202)	(215)
EBIT	**1,454**	**2,348**	**3,485**
Interest income	3	4	49
Interest expense	(100)	(46)	(75)
Profit before tax	**1,357**	**2,305**	**3,459**
Income tax expense	(444)	(595)	(428)
Net profit after income tax	**913**	**1,710**	**3,031**
Revenue growth	*n/a*	*37%*	*n/a*
Gross profit margin %	*62%*	*61%*	*58%*
EBITDA margin %	*10%*	*12%*	*14%*
EBIT margin%	*9%*	*11%*	*14%*
Earnings per share ($)	*88*	*165*	*293*

Source: Crocmedia

In relation to the historical financial performance of Crocmedia set out above, we note the following:

- The figures presented above are unaudited. The reliability of the financial information is therefore lower than if they had been audited or independently reviewed.
- Revenue increased significantly in FY17 due to increased syndication and advertising sales in the content business, as well as the full acquisition of BallPark (tours) and the acquisition of an 82% interest in Thread (creative agency) which contributed approximately $1.5 million in non-content sales. The increase in revenue in the twelve months to October 2017 was mainly contributed by strong revenue growth in content sales as a result of the AFL rights.
- The increase in cost of sales is largely in line with the movement in revenue and as a result, gross profit margins have remained fairly consistent, fluctuating between 61% and 62%.
- Employee expenses have increased consistently, in line with the growth in the number of full-time employees from a total of 46 employees as at 30 June 2016 to a total of 76 employees as at 31 October 2017.
- EBITDA and EBIT margins have both increased marginally by approximately 2% and 5% in FY17 and twelve months to 31 October 2017 respectively.
- A normalisation of earnings has been performed in Section 9.

5.6 Financial position

The unaudited consolidated statements of financial position[1] as at 30 June 2016, 30 June 2017 and 31 October 2017 are set out in the table below.

Table 12: Unaudited Statement of Financial Position[1] of Crocmedia

$'000	FY16	FY17	31-Oct-17
Current assets			
Cash	82	838	1,429
Trade and other receivables	4,190	5,698	7,542
Prepayments	138	1,210	1,701
Other current assets	112	119	1
Total current assets	**4,523**	**7,865**	**10,673**
Non-current assets			
Plant and equipment	599	1,517	2,151
Intangible assets	1,125	1,440	1,494
Investments	53	237	355
Other non-current assets	13	83	218
Total non-current assets	**1,789**	**3,277**	**4,218**
Total assets	**6,312**	**11,141**	**14,891**
Current liabilities			
Trade and other payables	(1,915)	(2,935)	(4,764)
Hire purchase current	(56)	(57)	(537)
Employee entitlements current	(221)	(361)	(1,111)
Deferred income	(554)	(1,894)	(824)
Income tax	(156)	(359)	(141)
Total current liabilities	**(2,902)**	**(5,606)**	**(7,377)**
Non-current liabilities			
Borrowings	-	(727)	(48)
Employee entitlements non-current	-	(24)	(24)
Hire purchase non-current	(103)	(45)	(45)
Loans related parties	(132)	(132)	(132)
Total non-current liabilities	**(235)**	**(928)**	**(249)**
Total liabilities	**(3,136)**	**(6,534)**	**(7,627)**
Net assets	**3,175**	**4,607**	**7,264**
Net tangible assets per share[2] ($)	*198*	*306*	*557*

Source: Crocmedia
Notes:
1. We have reclassified (i) NAB loan account from cash to debt, (ii) director loan from current liabilities to non-current assets and (iii) grouped similar accounts (such as employee payables and provisions).
2. Calculated by deducting the balance of intangible assets from net assets.

In relation to the historical financial position of Crocmedia set out above, we note the following:

- The figures presented above are unaudited. The reliability of the financial information is therefore lower than if they had been audited or independently reviewed.
- In particular, with the acquisition of Thread, there was neither the recognition of a pre-acquisition profit reserve for the calculation of goodwill acquired, nor was there a recognition of goodwill. As a result, the value of non-controlling interest is indeterminable. This therefore compounds the potential lack of reliability due to the absence of an audit.
- The trade and other receivables balance, predominantly consisting of trade receivables, forms the bulk of Crocmedia's working capital. Approximately 83% of the trade receivables balance are current and up to 60 days outstanding. The increase in trade receivables is in line with the increase in sales.

- The significant increase in property, plant and equipment since FY16 is mainly attributable to the acquisition of plant and equipment as part of Crocmedia's expansion plans beyond Melbourne.
- The bulk of the intangible assets balance pertains to goodwill arising from the acquisition of Crocmedia's own shares from its minority shareholder.
- Deferred income relates to fees received in advance for content sales and the provision of services. Approximately half of the deferred income pertains to customers from the parent entity and Bravo, while the bulk of the remaining is in relation to customers from BallPark.
- The borrowings predominantly relate to equipment loans utilised under their existing loan facilities with the National Australia Bank ("**NAB**"). Crocmedia has a limit of approximately $3.5 million from the NAB, with expiry dates between July and November 2018 and at interest rates of approximately 2.16% above the minimum lending rate. Other facilities include a revolving lease limit of $150,000 to cater for the general leasing requirements for the group, bank guarantees of approximately $330,000 as security deposits for rentals and business credit card with a limit of $50,000 for business purchases and expenses.

5.7 Capital structure and shareholders

As at 23 November 2017 Crocmedia had a total of 10,358 ordinary shares on issue. There were no options, convertible notes or other convertible securities or rights to receive shares. The following table sets out details of Crocmedia's substantial shareholders as at that date:

Table 13: Substantial shareholders

Shareholder	Shares held	% total shares
Craig Hutchison	6,008	58.0%
Rothfield family and associates	3,279	31.7%
Leisa Giannopoulos	904	8.7%
Other shareholders	167	1.6%
Total	**10,358**	**100.0%**

Source: Crocmedia

We note that Mr Craig Hutchison is the controlling shareholder and there are only two other shareholders with holdings over 5%.

6 PROFILE OF PROPOSED MERGED ENTITY

6.1 Introduction

The Proposed Merged Entity will consist of the integrated PNW and Crocmedia following the Proposed Transaction and will remain listed on the ASX. A significant amount of cost synergies, which represent a key part of the strategic rationale for the transaction, are expected to be realised through the merger. These synergies originate from streamlining management functions, live sports broadcasting and programming costs and economies of scale from maximising PNW's broadcasting and distribution capabilities.

6.2 Overview of operations

The Proposed Transaction would create a sports content and entertainment business capable of delivering brand stories and exclusive content via multiple media platforms. The Proposed Merged Entity will have a radio broadcast footprint comprising two Melbourne-based owned broadcast licenses and syndication agreements with 200 frequencies in 88 radio markets across metropolitan and regional Australia.

6.3 Rationale for Proposed Transaction

The Proposed Transaction is supported by compelling strategic rationale due to the highly complementary nature of PNW and Crocmedia. The strategic rationale includes:

- Scale and complementary service offerings across multiple media platforms which provide a point of differentiation and a platform for future growth.
- Becoming better placed to service brand partners by offering an expanded solution across multiple media platforms including owned and supplied radio, television, online, in-stadium, events and print.
- The ability to leverage the combined platform and operational expertise with other potential sports rights.
- Potential cross-sell opportunities of content created by both PNW and Crocmedia.
- Potential cost and revenue synergies associated with sharing service functions, centralising talent management, consolidating broadcast operations and the marketing of a broader set of services to a wider set of brand partners.

6.4 Key personnel

The proposed directors and senior management team of the Proposed Merged Entity comprises:

Table 14: Proposed Merged Entity directors and senior management team

Name and title	Experience
Craig Coleman Non-Executive Chairman	Current Non-Executive Chairman of PNW
Andrew Moffat Non-Executive Director	Current Non-Executive Director of PNW
Colm O'Brien Independent Non-Executive Director	Current Independent Non-Executive Director of PNW
Craig Hutchison Managing Director	Current Managing Director and Founder of Crocmedia
Chris Giannopoulos Executive Director	Current Executive Director of Crocmedia

Source: PNW and Crocmedia

6.5 Post-merger capital structure

The following table summarises the major shareholdings in the Proposed Merged Entity after the acquisition:

Table 15: Proposed Merged Entity substantial shareholders

Shareholder	Shares held	% total shares
Craig Hutchison	49,410,736	24.4%
Viburnum Funds	46,851,198	23.1%
Rothfield family and associates	26,969,619	13.3%
Ron Hall	20,109,998	9.9%
Other shareholders	59,349,918	29.3%
Total[1]	**202,691,469**	**100.0%**

Source: PNW and Crocmedia
Note 1: This is inclusive of the shares issued as part of the Planned Capital Raising, which is a condition of the Proposed Transaction. However, this is not inclusive of the long-term incentive performance rights to be issued as part of the Proposed Transaction.

6.6 Proforma financial performance

The historical statements of financial performance for PNW and Crocmedia for the twelve months to 31 October 2017 have been presented on a proforma, combined basis as set out below:

Table 16: Proforma Statement of Financial Performance of the Proposed Merged Entity

$'000	PNW[1]	Crocmedia	Proforma adjustments	Proposed Merged Entity
Revenue	**21,511**	**25,659**	**-**	**47,170**
Adjusted EBIT	**2,439**	**3,685**	**3,000**	**9,124**
Interest expense	(324)	(26)	-	(350)
Share of profit of associates	35	-	-	35
Profit before tax	**2,150**	**3,659**	**3,000**	**8,774**
Income tax expense	(645)	(428)	(900)	(1,973)
Net profit after income tax	**1,505**	**3,231**	**2,100**	**6,801**
EBIT margin %				*19%*
Earnings per share[2] ($)				*0.03*

Source: PNW and Crocmedia
Notes:
1. PNW's figures have been adjusted by PNW management to be consistent with the classification in the annual report. Therefore, there exists a slight difference from the management figures presented in the notice of meeting.
2. Calculated on an undiluted basis and excludes amortisation of intangible assets as a result of the Proposed Transaction.

The above proforma adjustments relate to cost synergies expected to arise from the Proposed Transaction, net of 30% corporate tax. One-off costs of achieving these synergies are not included.

Synergy analysis

PNW and Crocmedia have estimated annual synergies from the Proposed Transaction to be approximately $3.0 million per annum, on a conservative basis, should the Proposed Transaction proceed. The estimates were based on a detailed line-by-line analysis of costs to identify overlapping areas which can be consolidated or considered to be synergistic in nature. Broadly, the five main areas identified are occupancy, broadcasting, talent, employment and board of directors' costs. While the breakdown of cost savings is not presented due to it being commercially sensitive, we note the following:

- Occupancy relates to the marginal cost savings derived from the amalgamation of corporate head offices. The estimates were based on PNW relocating to Crocmedia's premises based on Crocmedia's current rent per square metre and at the same time, property outgoings would be reduced similarly based on Crocmedia's current outgoings.

- Cost savings from broadcasting predominantly relate to the opportunity to remove duplication of the live AFL broadcasts, in which currently both PNW and Crocmedia call some of the same games each round. Estimates were based on the assumption that only one broadcast would be required per game. In addition, it is noted that in merging the broadcasting of AFL games, there would be additional games which would not be covered by the Proposed Merged Entity. Costs associated with covering the additional games have also been taken into account based on Crocmedia's current costs. Other broadcasting duplication mainly pertains to A-league games which can be broadcast on SEN rather than Macquarie should the Proposed Transaction complete.
- Talent cost savings relate to the reduction of talent personnel due to the consolidation of programming. Other employee cost savings are derived from the removal of duplicated roles at the corporate level.
- Cost savings from the board of directors' fees are in relation to the resignation of three directors. Two of them will be replaced by executive directors who will not receive additional director fees outside of their remuneration packages.

In addition, Crocmedia management has made an estimate from the potential additional revenue available to the Proposed Merged Entity through cross-selling between the two businesses. Further work and analysis needs to be undertaken on the level and extent of the revenue synergies. Therefore, we have not included estimates of the revenue synergies in our analysis.

Based on the consideration discussed above, conservative estimates to account for other costs which may not be identified during the process and the ability and timing of implementation, we have included the cost savings of $3.0 million in our analysis.

6.7 Proforma financial position

The historical statements of financial position for PNW and Crocmedia as at 31 October 2017 have been presented on a proforma, combined basis as set out below:

Table 17: Proforma Statement of Financial Position of the Proposed Merged Entity

$'000	PNW	Crocmedia	Proforma adjustments	Proposed Merged Entity
Current assets				
Cash and cash equivalents	1,647	1,429	7,771	10,847
Trade and other receivables	4,798	7,542	-	12,340
Prepayments and other current assets	293	1,702	-	1,995
Total current assets	**6,738**	**10,673**	**7,771**	**25,182**
Non-current assets				
Property, plant and equipment	1,382	2,151	-	3,533
Deferred tax asset	680	-	-	680
Goodwill	-	1,172	15,260	16,432
Intangible assets	10,784	322	-	11,106
Investments and receivables from associates	277	355	-	632
Other non-current assets	-	218	-	218
Total non-current assets	**13,123**	**4,218**	**15,260**	**32,601**
Total assets	**19,861**	**14,891**	**23,031**	**57,783**
Current liabilities				
Short-term borrowings	(5,750)	(540)	-	(6,290)
Trade and other payables	(2,223)	(4,764)	-	(6,987)
Income tax	(352)	-	-	(352)
Current provisions	(673)	(389)	-	(1,062)
Other current liabilities	-	(1,526)	-	(1,526)
Total current liabilities	**(8,998)**	**(7,219)**	**-**	**(16,217)**
Non-current liabilities				
Long-term borrowings	-	(48)	-	(48)
Deferred tax liabilities	(656)	-	-	(656)
Other non-current liabilities	-	(358)	-	(358)
Total non-current liabilities	**(656)**	**(406)**	**-**	**(1,062)**
Total liabilities	**(9,654)**	**(7,625)**	**-**	**(17,279)**
Net assets	**10,207**	**7,266**	**23,031**	**40,504**
Net tangible assets per share[1] ($)				*0.06*

Source: PNW and Crocmedia
Note 1: Calculated by deducting the balance of intangible assets from net assets and on an undiluted basis.

The above proforma adjustments relate to:

- Cash proceeds of the Planned Capital Raising of $10.0 million less transaction costs of approximately $2.2 million, which have both been respectively included as part of net cash and non-operating liabilities of the Proposed Merged Entity in Section 9.2.3.
- Provisional accounting entries in relation to the goodwill acquired as part of the Proposed Transaction.

7 VALUATION METHODOLOGY

7.1 Available valuation methodologies

To estimate the fair market value of PNW and the Proposed Merged Entity (inclusive of Crocmedia) we have considered common market practice and the valuation methodologies recommended in RG 111. There are a number of methods that can be used to value a business including:

- The discounted cash flow method ("**DCF**")
- The CFME method
- Asset based methods
- Analysis of share market trading
- Industry specific rules of thumb

Each of these methods is appropriate in certain circumstances and often more than one approach are applied. The choice of methods depends on several factors such as the nature of the business being valued, the return on the assets employed in the business, the valuation methodologies usually applied to value such businesses and the availability of the required information. A detailed description of these methods and when they are appropriate is provided in Appendix 2.

7.2 Selected methodology – PNW

In selecting an appropriate valuation methodology to value PNW, we have considered the following factors:

- PNW is neither an asset based business nor an investment holding company. It is also considered to be a going concern, thus an asset approach is not appropriate.
- No longer-term financial projections beyond FY18 exist for PNW. Therefore, a DCF approach is no more reliable than the CFME approach.
- There are some listed companies engaged in somewhat similar businesses to PNW as well as companies operating in comparable industries with similar profit drivers. We are also aware of a number of comparable transactions involving similar companies. Therefore, we consider the CFME approach to be appropriate.
- Share market trading in PNW shares has been relatively illiquid, with periods where no shares have been traded. This means that an analysis of share market trading is not a reliable measure of the intrinsic value of a PNW share.
- We are not aware of any industry specific valuation methodologies appropriate to PNW.

Accordingly, we are of the opinion that the most appropriate methodology to value PNW is the CFME method. We have also considered an analysis of recent share market trading in PNW shares, up to the date of the announcement of the Proposed Transaction, as a broad cross-check.

7.3 Selection of valuation methodology – Proposed Merged Entity

In selecting an appropriate valuation methodology to value the Proposed Merged Entity (including Crocmedia) we have considered the following factors:

- While it would be possible to assess the value of the Proposed Merged Entity by aggregating an assessed value for PNW with our assessed value for Crocmedia, this approach would not reliably capture estimated synergies, transaction costs, diversification and scale benefits of the merged business. Thus, we believe it is appropriate to value the Proposed Merged Entity as a single, combined business.
- The Proposed Merged Entity would neither be an asset based business nor an investment holding company. It is also considered to be a going concern, thus an asset based approach is not appropriate.
- There are some listed companies and comparable transactions with similar business exposure and near-term growth prospects to the Proposed Merged Entity as well as companies operating in comparable industries with similar profit drivers. Thus, we consider the CFME approach to be appropriate.

- Proposed Merged Entity shares do not currently exist, thus market trading cannot be directly observed. However, to the extent that the market expects the Proposed Transaction to complete, market trading in PNW after the Proposed Transaction was announced may give an indication of the market's assessment of the value per share of the Proposed Merged Entity.
- Crocmedia has experienced significant growth and is expecting strong growth to continue over the medium term. A DCF approach can capture this expected earnings growth and the associated costs. This can be aggregated with the cash flow model for PNW, with adjustments made for expected synergies and transaction costs, to derive a cash flow model for the Proposed Merged Entity. However, similar to PNW, no longer-term financial projections beyond FY18 exist for Crocmedia. Therefore, a DCF approach is no more reliable than the CFME approach.
- We are not aware of any industry specific valuation methodologies appropriate to the Proposed Merged Entity.

Accordingly, we are of the opinion that the most appropriate methodology to value the Proposed Merged Entity is the CFME method based on the estimated combined earnings, taking into account synergies, transaction costs, diversification and scale benefits of the merged entity. We have also considered an analysis of share market trading in PNW shares post announcement of the Proposed Transaction as a broad cross-check.

8 VALUATION OF PNW

8.1 Background

We have assessed the fair market value of PNW using the CFME method, with a broad cross-check to an analysis of recent share market trading in PNW shares. This assessment has been made on a control basis as required by RG111.

8.2 Capitalisation of future maintainable earnings

Determining the fair market value of PNW using the CFME method requires consideration of the following factors:

- An appropriate level of maintainable earnings
- An appropriate earnings multiple
- The value of any non-operating assets and liabilities

These considerations are discussed in more detail below.

8.2.1 Maintainable earnings

The first step in the valuation process is to determine the measure of earnings to be capitalised for valuation purposes. The following measures of earnings are often used for business valuations:

- **Revenue**: mostly used for companies that do not make a positive EBITDA or as a cross-check of a valuation conclusion derived using another method.
- **EBITDA**: most appropriate where depreciation distorts earnings, for example in a company that has a significant level of depreciating assets but little ongoing capital expenditure requirement.
- **EBITA**: in most cases EBITA will be more reliable than EBITDA as it takes account of the capital intensity of the business.
- **EBIT**: while commonly used in practice, multiples of EBITA are usually more reliable as they remove the impact of amortisation which is a non-cash accounting entry that does not reflect a need for future capital investment (unlike depreciation).
- **NPAT**: relevant in valuing businesses where interest is a major part of the overall earnings of the group (e.g. financial services businesses such as banks).

Multiples of EBITDA, EBITA and EBIT are commonly used to value the whole business for acquisition purposes where gearing is in the control of the acquirer. In contrast, NPAT (or P/E) multiples are often used for valuing a minority interest in a company as the investor has no control over the level of debt.

We have selected to analyse multiples of EBIT because:

- Earnings multiples based on EBITDA and EBIT are not affected by different financing structures which impact multiples of net profit after tax.
- The varying capital intensity of the comparable companies means that an analysis of EBIT is a more reliable measure than the multiples of EBITDA.
- Third party forecasts of EBITA for comparable companies are not readily available making EBITA multiples difficult to calculate without making assumptions about ongoing levels of depreciation and amortisation (i.e. most brokers do not separately forecast depreciation and amortisation).

When considering an appropriate level of future maintainable earnings, it is important to base the analysis on a maintainable level of earnings which includes adjustment for any non-recurring items as these items will not impact the ongoing earnings of the business. The following table sets out normalised EBIT for PNW for FY16, FY17 and twelve months to October 2017.

Table 18: PNW's normalised earnings

Description ($'000)	FY16	FY17	LTM Oct'17
Unadjusted EBIT	**1,723**	**(6,468)**	**(6,217)**
Impairment expenses	-	8,239	8,239
Restructuring expenses	611	262	201
Discontinued publications' trading losses[1]	247	143	132
Legal levies and costs	-	128	128
Salaries from the discontinuation of roles	-	168	148
Rent savings and adjustments	-	29	42
Miscellaneous adjustments	-	(110)	(234)
Adjusted EBIT	**2,581**	**2,391**	**2,439**
Adjusted EBIT margin %	*11%*	*11%*	*11%*

Source: PNW and Leadenhall analysis
Note 1: No depreciation and amortisation were attributed to these publications.

The 'Adjusted EBIT' for FY16, FY17 and twelve months to October 2017 include the following adjustments to reported EBIT:

- Non-recurring impairment expenses in relation to the write-off of goodwill arising from the acquisition of Morrison Media in FY15 and impairment of mastheads in the publication business.
- Non-recurring restructuring expenses pertaining to payments for redundancies.
- Operating loss from the publications which were recently discontinued.
- Various non-recurring legal levies and costs incurred, such as for the defence of a legal claim for royalties and reviewing legal documents in relation to a six-year AFL broadcast rights agreement.
- Non-recurring salaries from the discontinuation of roles, which include the Head of Technology.
- Rent savings and adjustment from the writing back of the provision for additional rent payable and the closure of the Gold Coast office.
- Miscellaneous adjustments such as non-recurring income from the refund of payroll tax and reversal of licence fee accruals which were abolished by the Australian Communications and Media Authority.

In addition to the above, we have been provided with the PNW board approved budget for FY18 and strategic plan to FY20. We have not disclosed these forecasts due to the commercially sensitive nature of the information contained.

After considering the historical earnings, forecast earnings and margins of comparable companies, we have selected the following maintainable earnings.

Table 19: Selected maintainable earnings of PNW

Description ($'000)	EBIT Low	EBIT High
Maintainable earnings	2,400	2,600

Source: PNW and Leadenhall analysis

8.2.2 Earnings multiple

The multiples selected to apply to maintainable earnings implicitly reflect expectations about future growth, risk and the time value of money. Multiples can be derived from three main sources:

- The trading prices of companies that are engaged in the same or similar lines of business and that are actively traded on a public stock market. We have set out our analysis of the trading multiples below.
- From transactions of significant interests in companies engaged in the same or similar lines of business.
- It is also possible to build a multiple from first principles based on an appropriate discount rate and growth expectations. This approach is generally used when the first two are not possible. We have not taken this approach in valuing PNW.

In respect of public company trading multiples, we note that there are limited companies which operate in the same segments as PNW listed on the ASX. However, there are a number of listed Australian companies that operate in the broader media and broadcasting sector that have similar growth and risk factors to PNW.

The following table sets out the historical and forecast trading EBIT multiples for the selected comparable companies.

Table 20: Trading multiples of comparable companies

Company	Market Cap (AUD'm)	EBIT growth[1]	EBITDA multiple		EBITDA margin[1]	EBIT multiple		EBIT margin[1]
			Current	Forecast		Current	Forecast	
Domestic radio broadcasters								
Southern Cross Media Group Ltd	938	1%	7.3x	7.5x	25%	8.8x	9.0x	21%
HT&E Ltd	570	20%	6.4x	6.6x	26%	8.1x	8.2x	21%
Macquarie Media Ltd	222	9%	8.2x	n/a	21%	9.0x	n/a	19%
Pacific Star Network Ltd[2]	16	2%	4.6x	n/a	14%	6.6x	n/a	11%
Average (Domestic radio broadcasters)		***8%***	***6.6x***	***7.0x***	***22%***	***8.1x***	***8.6x***	***18%***
Median (Domestic radio broadcasters)		***6%***	***6.9x***	***7.0x***	***23%***	***8.5x***	***8.6x***	***20%***
Other domestic media companies								
Fairfax Media Ltd	1,748	6%	8.5x	7.8x	14%	9.5x	9.3x	12%
Nine Entertainment Co. Holdings Ltd	1,349	21%	11.8x	7.0x	13%	16.0x	8.3x	11%
Seven West Media Ltd	965	8%	11.2x	6.1x	15%	14.6x	7.3x	13%
APN Outdoor Group Ltd	773	8%	9.4x	9.2x	26%	11.2x	11.1x	22%
oOh!media Ltd	722	24%	9.6x	8.6x	23%	14.3x	12.7x	15%
QMS Media Ltd	319	49%	9.8x	8.3x	23%	14.8x	8.3x	19%
Prime Media Group Ltd	99	-8%	2.2x	2.7x	23%	2.5x	3.4x	20%
Average (Other domestic media)		***15%***	***8.9x***	***7.1x***	***20%***	***11.8x***	***8.6x***	***16%***
Median (Other domestic media)		***8%***	***9.6x***	***7.8x***	***23%***	***14.3x***	***8.3x***	***15%***
Average (Overall)		***13%***	***8.1x***	***7.1x***	***20%***	***10.5x***	***8.6x***	***17%***
Median (Overall)		***8%***	***8.5x***	***7.5x***	***23%***	***9.5x***	***8.3x***	***19%***

Source: S&P Capital IQ and Leadenhall Analysis as at 15 December 2017
Notes:
1. Growth and margins are based on 3-year averages to FY18.
2. PNW market capitalisation is sourced from S&P Capital IQ as at 21 November 2017 (before announcement of the Proposed Transaction). Current EBITDA and EBIT multiples have been calculated based on the normalised earnings in the last twelve months to October 2017.

It should be noted that these multiples are based on trading of minority shareholders. In contrast, we are considering the value of a PNW share on a control basis. Therefore, consideration must be given to observed control premiums in the Australian market and the impact on the minority trading multiples, of the comparable companies, if applied. Further information on control premiums is provided in Appendix 4.

In addition to considering the differences between minority and control multiples, we have also considered the following factors in relation to the comparable company trading multiples in determining an appropriate earnings multiple to apply to the valuation of PNW:

- The average and median forecast EBIT trading multiples are 8.6x and 8.3x with a range of 3.4x to 12.7x.
- There are no media companies listed in Australia which have a similar mix of radio broadcasting and publishing as PNW. Fairfax Media Ltd is predominantly an Australian publisher, with a relatively small exposure to radio broadcasting via its shareholding in Macquarie Media Ltd.
- We have included other domestic media companies (consisting of publishers, television broadcasters and media advertisers) in our basket of comparable companies, even though they are exposed to different risks and structures compared to radio broadcasters, as they are still part of the media industry competing for advertising revenues.
- Pure play radio broadcasting companies generally produce higher margins than publishing (Fairfax Media Ltd) and television broadcasting companies (Nine Entertainment Co. Holdings Ltd and Seven West Media Ltd) and similar margins to media advertising companies. PNW generates margins lower than radio broadcasting companies due to its operations model where approximately 37% of its earnings are derived from the publishing segment. All other things being equal, companies with lower margins tend to trade on lower multiples.
- PNW is smaller than the majority of the comparable listed companies. All other things being equal, smaller companies trade on lower multiples.
- While the level of exposure is different, in terms of operations, margins and historical growth, Fairfax Media Ltd and Macquarie Media Ltd are the most comparable of the companies identified. Fairfax Media Ltd has a current and forecast multiple of 9.5x and 9.3x respectively, while Macquarie Media Ltd has a current multiple of 9.0x. However, PNW is significantly smaller in size and has a lower level of assets backing, thus a lower multiple is therefore appropriate for PNW (before allowing for a control premium).
- As set out in Appendix 4, evidence from studies has indicated that premiums for control on successful takeovers have frequently been in the range of 20% to 40%. Based on the observed trading multiples of comparable companies and in consideration of the factors discussed above, we are of the opinion that an appropriate EBIT multiple for PNW is between 7.0x and 8.0x, which represents an EBIT multiple (on a control basis) of between 8.4x and 11.2x.

In addition to our analysis of trading multiples, we have also reviewed relevant transaction multiples, from Australia and overseas. The table below shows the historical (where available) EBITDA and EBIT multiples from relevant transactions with publicly available data.

Table 21: Transaction multiples

Target	Acquirer	Date	Target Description	Transaction value (A$m)	Implied control premium	EBITDA multiple	EBIT multiple
Domestic broadcasting companies							
Macquarie Radio Network Ltd	Fairfax Radio Network Pty Ltd	Mar-15	Radio broadcasting	121	n/a	11.6x[1]	12.3x[1]
Radio 96FM Perth Pty Ltd	Australian Radio Network Pty Ltd	Jan-15	Radio broadcasting	78	n/a	9.0x[2]	n/a
Sunshine Coast Broadcasters Pty Ltd	Eon Broadcasting Pty Ltd	Mar-13	Radio broadcasting	18	n/a	9.3x[1]	n/a
Consolidated Media Holdings Ltd	News Ltd	Nov-12	Television broadcasting	2,160	9%	24.7x	24.7x
Nova Entertainment Pty Ltd	Illyria Pty Ltd	Aug-12	Radio broadcasting	172	n/a	n/a	34.5x
Seven Media Group Pty Ltd	Seven West Media Ltd	Apr-11	Television broadcasting	4,148	n/a	11.5x	13.1x
Austereo Group Ltd	Southern Cross National Network Pty Ltd	Apr-11	Radio broadcasting	920	15%	10.0x	11.0x
Average					**12%**	**12.7x**	**19.1x**

Source: S&P Capital IQ
Notes:
1. Calculated based on available financial information (from the annual report) as at the date of transaction.
2. Estimates obtained from Radio Today.

The observed multiples from comparable transactions are control multiples and include any premium paid for control. Therefore, no adjustment for a control premium is required.

We have considered the following factors in relation to the above transaction multiples in determining an appropriate earnings multiple to apply to the valuation of PNW:

- Transaction multiples incorporate varying degrees of control premium and possibly an element of special value to the extent this was paid for by the acquirers.
- The most comparable transactions are the acquisitions of Macquarie Radio Network Ltd in March 2015 and Austereo Group Ltd in April 2011. Macquarie Radio Network Ltd owns and operates commercial radio stations across metropolitan and regional Australia, as well as, public relations and marketing communications agency and digital media platforms. Austereo Group operates radio networks, digital radio and comedy channels and provides marketing solutions, campaign implementation to consumers and advertisers. Given the relatively small size of PNW, it would likely attract a smaller multiple than these transactions.

Our key considerations in selecting appropriate earnings multiples to apply to our valuation of PNW are summarised below:

- We have placed more reliance on the transaction multiples as guidance in selecting earnings multiples on a control basis.
- We have considered the potential synergies available to a potential buyer of the business where it is often a component of the control premium paid to acquire control of a business. The transactions we have considered are control transactions and would therefore include a control premium inclusive of any synergies to the extent they were available to the acquirer and that there was sufficient tension in the sales process to compel the acquirer to pay for such synergies.

In addition, the financial forecasts for PNW provided to us anticipate continued growth in revenue as discussed in Section 4.9, primarily due to the expected benefits from increased demand in SEN. However, we perceive a number of risks to achieving the forecast figures including:

- The budget and forecast assume growth opportunities to come predominantly from the Broadcasting segment with increase in sales in the saturated Melbourne market where advertising revenue has only increased marginally or near stagnation in FY17.
- There may be increasing competition in the sports entertainment industry with the granting of new licenses, as well as from alternative media platforms. Therefore, the threat of new entrants could result in the loss of market share and hence appeal to downstream media buying agencies.

Based on the consideration discussed above, we have selected the following earnings multiples to apply to our valuation of PNW (on a control basis).

Table 22: Selected earnings multiples

Description	EBIT	
	Low	High
Selected earnings multiple	9.0x	10.0x

Source: Leadenhall analysis

We note the selection of the multiple, within a fairly broad range, does not impact our conclusion on the Proposed Transaction.

8.2.3 Non-operating assets and liabilities

In order to assess the value of PNW, it is necessary to identify any other assets and liabilities not included in the enterprise value calculated. These can be:

- **Surplus assets**: assets held by the company that are not utilised in its business operation. This could be investments, unused plant and equipment held for resale, or any other assets that is not required to run the operating business. It is necessary to ensure that any income from surplus assets (i.e. rent / dividends) is excluded from the business value.
- **Non-operating liabilities**: liabilities of a company not directly related to its current business operations, although they may relate to previous business activities, for example claims against the entity. We have not identified any material non-operating liabilities owed by PNW.
- **Net debt**: comprising of debt used to fund a business, less surplus cash held by the company.

Each of these factors are considered below.

Surplus assets

As at 31 October 2017, PNW has approximately $0.1 million of surplus assets pertaining to receivables from associates.

Net debt

The net debt position for PNW as at 31 October 2017 is set out in the table below:

Table 23: Net debt summary

($'000)	
Cash	1,647
Borrowings	(5,750)
Cash from exercising options[1]	300
Net debt	**(3,803)**

Source: PNW and Leadenhall analysis
Note 1: For the purpose of our analysis, we have assumed the options outstanding will be exercised.

8.2.4 Shares outstanding

PNW currently has approximately 71.1 million ordinary shares and 1.03 million share options outstanding. As the share options are currently in the money, we have assumed they will be converted into ordinary shares in determining the value of a PNW share (on a control basis). Therefore, the total number of shares included as part of our analysis is approximately 72.1 million.

8.2.5 Valuation summary

Based on the CFME analysis set out above, the value of a PNW share (on a control basis) is as set out in the table below.

Table 24: CFME valuation summary of PNW

($'000)	EBIT	
	Low	High
Maintainable earnings	2,400	2,600
Multiple (control)	9.0x	10.0x
Enterprise value	**21,600**	**26,000**
Surplus assets	62	62
Net debt	(3,803)	(3,803)
Equity value on a control basis	**17,859**	**22,259**
Total number of shares ('000)	72,118	72,118
Assessed value per share ($)	**0.25**	**0.31**

Source: Leadenhall analysis

8.3 Analysis of share trading

Market trading in PNW shares provides an indication of the market's assessment of the current value of PNW on a minority basis. We have presented an analysis of recent trading in PNW's shares in Section 4.8 above and a summary of the share prices over the past six months, up to the date of announcement of the Proposed Transaction, below.

Table 25: Share price performance of PNW shares

$	Low	High	VWAP
6-month	0.15	0.28	0.25
3-month	0.15	0.28	0.26
1-month	0.21	0.28	0.27

Source: S&P Capital IQ

When assessing market trading it is necessary to consider whether the market is informed and liquid. In this regard we note:

- As set out in Section 4.8, the trading volume is below the level at which large institutional investors are able to invest and may therefore be seen as a deterrent for other significant investors.
- PNW is not a constituent of the major indices, hence it receives lesser market attention and is less attractive to institutional investors who are mandated to invest in index equities.
- PNW has continuous disclosure obligations under the ASX Listing Rules, thus the market is informed about its activities.

As a result of these factors, we consider the market trading to be reasonably well informed and moderately liquid. We have therefore undertaken only a high-level analysis of share market trading, taking reference to the trading price range of between $0.15 and $0.28, as well as the respective VWAPs of a PNW share over the various periods within the past six months as shown above. We consider the trading price range over the past month of between $0.21 and $0.28 to be a more reliable market indication of the current value of PNW as it captures the one-month period up to the announcement of the Proposed Transaction. Comparing these trading prices (on a minority basis) with our assessed value per share (on a control basis) implies a control premium of between 11% and 19%. We do not consider this unreasonable considering the synergies that are available to a buyer and limited liquidity in the shares traded.

8.4 Conclusion on value

Based on our CFME analysis and share trading cross-check, we have selected a valuation range for a share in PNW of between $0.25 and $0.31, on a control basis.

9 VALUATION OF PROPOSED MERGED ENTITY

9.1 Introduction

We have determined the fair market value of a share in the Proposed Merged Entity using the CFME method, based on the future maintainable EBIT of the Proposed Merged Entity, inclusive of synergies. We have also considered an analysis of share market trading in PNW shares post announcement of the Proposed Transaction as a broad cross-check. This assessment has been made on a minority interest basis (i.e. excluding a control premium) as PNW's existing shareholders would be minority shareholders in the Proposed Merged Entity.

9.2 Capitalisation of future maintainable earnings

Determining the fair market value of the Proposed Merged Entity using the CFME method requires consideration of the following factors:

- An appropriate level of maintainable earnings
- An appropriate earnings multiple
- The value of any non-operating assets and liabilities

These considerations are discussed in more detail below.

9.2.1 Maintainable earnings

We have utilised the same basis and approach in Section 8.2.1 to determine the measure of earnings to be capitalised. When considering the future maintainable EBIT of the Proposed Merged Entity, we have taken into account the following:

- The future maintainable EBIT for PNW
- The future maintainable EBIT for Crocmedia
- Cost and revenue synergies

These considerations are discussed in more detail below.

Maintainable EBIT for PNW

As discussed in Section 8.2.1, we have assessed the future maintainable EBIT for PNW between $2.4 million and $2.6 million.

Maintainable EBIT for Crocmedia

When considering an appropriate level of future maintainable earnings, it is important to base the analysis on a maintainable level of earnings which includes adjustment for any non-recurring items as these items will not impact the ongoing earnings of the business. The following table sets out normalised EBIT for Crocmedia for FY16, FY17 and twelve months to 31 October 2017.

Table 26: Crocmedia's normalised earnings

Description ($'000)	FY16	FY17	LTM Oct'17
Unadjusted EBIT	**1,454**	**2,348**	**3,485**
Incentive payment	-	(250)	(250)
Loss on disposal of property, plant and equipment	11	277	277
Redundancy and restructuring expenses	-	115	115
Specific provisions for doubtful debts	-	66	66
Thread's pre-acquisition earnings	-	-	81
Thread's non-controlling interests	-	104	104
Miscellaneous adjustments	-	(193)	(193)
Adjusted EBIT	**1,465**	**2,467**	**3,685**
Adjusted EBIT margin %	*9%*	*11%*	*14%*

Source: Crocmedia and Leadenhall analysis

The 'Adjusted EBIT' for FY16 and FY17 include the following adjustments to reported EBIT:

- Non-recurring incentive payment received by Crocmedia from the previous landlord for the early break of the lease which had been included as other revenue in FY17.
- Non-recurring property, plant and equipment write-off from the office relocation.
- Non-recurring redundancy and restructuring expenses pertaining to payments for redundancies and consulting fees in relation to business restructuring.
- Specific provisions for doubtful debts in relation to two debtors who went into liquidation.
- Three months of Thread's pre-acquisition earnings in order to estimate the last twelve months earnings of Thread since Crocmedia had only acquired Thread in February 2017.
- Earnings attributable to the remaining 18% non-controlling interests in Thread, which will be acquired together as part of the acquisition of Crocmedia.
- Miscellaneous adjustments such as relocation expenses, bonuses, annual leave and long service leave provisions and fringe benefits tax liabilities.

In addition to the above, we have been provided with the Crocmedia board approved budget for FY18. We have not disclosed these forecasts due to the commercially sensitive nature of the information contained.

After considering the historical earnings, forecast earnings and margins of comparable companies, we have selected the following maintainable earnings. More emphasis has been placed on the FY18 budget as it accounts for earnings from the recently awarded exclusive commercial radio and programming rights.

Table 27: Selected maintainable earnings of Crocmedia

Description ($'000)	EBIT Low	EBIT High
Maintainable earnings	3,400	3,600

Source: Crocmedia and Leadenhall analysis

Conclusion on the assessment of maintainable EBIT

We have selected the following future maintainable EBIT of the Proposed Merged Entity.

Table 28: Selected maintainable earnings of the Proposed Merged Entity

Description ($'000)	EBIT Low	EBIT High
Maintainable earnings for PNW	2,400	2,600
Maintainable earnings for Crocmedia	3,400	3,600
Synergies	3,000	3,000
Maintainable earnings for Proposed Merged Entity	**8,800**	**9,200**

Source: PNW, Crocmedia and Leadenhall analysis

9.2.2 Earnings multiple

We have referred to the same peer group of listed companies and comparable transactions analysed in Section 8.2.2 and have selected an EBIT multiple of between 8.5x and 9.5x (on a minority basis) to apply to our valuation of the Proposed Merged Entity. This selection is consistent with the multiple (on a control basis) applied to the valuation of PNW, with a 0.5x discount to account for the absence of audited financial information for Crocmedia. Whilst a higher multiple could arguably be selected to reflect the benefits of the Proposed Merged Entity, we note the selection of the multiple, within a fairly broad range, does not impact our conclusion on the Proposed Transaction.

9.2.3 Non-operating assets and liabilities

Similar in the approach for the valuation of PNW in Section 8.2.3, it is necessary to identify any other assets and liabilities not included in the enterprise value calculated in order to assess the value of the Proposed Merged Entity. Each of these factors are considered below.

Surplus assets

As at 31 October 2017, the Proposed Merged Entity has approximately $0.1 million of surplus assets pertaining to receivables from associates.

Non-operating liabilities

For the purpose of our analysis, we have classified the implementation costs in deriving synergies of between $0.7 million and $1.0 million and total expected transaction costs of approximately $2.2 million as non-operating liabilities, set out in the table below.

Table 29: Non-operating liabilities

($'000)	Low	High
Implementation costs	(700)	(1,000)
Transaction costs	(2,200)	(2,200)
Total non-operating liabilities	**(2,900)**	**(3,200)**

Source: PNW, Crocmedia and Leadenhall analysis

Net cash

As set out in Section 1.4, one of the conditions which must be satisfied prior to the completion of the Proposed Transaction is the simultaneous completion of the Planned Capital Raising. Therefore, we have included the cash proceeds from the Planned Capital Raising of $10 million together with the net debt position for the Proposed Merged Entity as at 31 October 2017, set out in the table below:

Table 30: Net cash summary

($'000)	
PNW's cash	1,647
PNW's borrowings	(5,750)
Crocmedia's cash	1,429
Crocmedia's borrowings	(588)
Proceeds from capital raising	10,000
Net cash	**6,738**

Source: PNW, Crocmedia and Leadenhall analysis

9.2.4 Value attributable to potential shares and options

The following table provides a summary of the assessed value of the potential shares and options:

Table 31: Proposed Merged Entity options and performance rights

Description	Number	Value range	Low ($'000)	High ($'000)
Existing PNW options				
Options[1]	1,000,000	$0.10 - $0.15	105	154
Options[2]	25,000	$0.23 - $0.26	6	7
New performance rights to be issued				
Special purpose performance rights[3]	200,000	$0.38 - $0.44	76	87
Performance rights related to Proposed Transaction[4]	8,562,709	$0.23 - $0.26	1,941	2,243
Total	**9,787,709**		**2,127**	**2,491**

Source: Leadenhall analysis
Notes:
1. Options with an exercise price of $0.30 expiring on 1 September 2018.
2. Nil price options expiring on 1 October 2018 and with a vesting condition of achieving EBITDA budget and year-on-year circulation growth of frankie Magazine and remaining employed by PNW on the vesting date.
3. Performance rights with a vesting period of approximately 2 years and a vesting condition of remaining employed by PNW.
4. Performance rights with vesting periods and conditions as set out in Section 1.1.

We have analysed the value of the options and special purpose performance rights using the Black-Scholes option pricing model. The key assumptions were a 0% dividend yield, volatility of 50% and for the special purpose performance rights, they were all assumed to meet the required vesting condition.

We have assigned a probability weighting of 60% in meeting the performance hurdle of the long-term incentive performance rights. In selecting this weighting, we have considered the comparable companies analysis, synergies, latest year-to-date results and the growth opportunities of the Proposed Merged Entity. The EBITDA hurdles have been set to grow by approximately 21% annually to FY21. However, a number of risks exist in achieving the required growth which would reduce the likelihood of meeting the performance hurdle. Furthermore, we note the selection of a higher probability weighting would not alter our opinion.

9.2.5 Number of shares in the Proposed Merged Entity

In our consideration of the number of shares in the Proposed Merged Entity we have included:

- 71.1 million PNW shares currently on issue
- 91.6 million shares to be issued as consideration for Crocmedia
- 40.0 million shares to be issued as part of Planned Capital Raising

The number of shares outstanding post-transaction is set out in the table below:

Table 32: Shares outstanding post-transaction

('000)	
PNW shares currently on issue	71,093
Shares to be issued as consideration for Crocmedia	91,598
Shares to be issued as part of planned capital raising	40,000
Total shares	**202,691**

Source: Leadenhall analysis

9.2.6 Valuation summary

Based on the CFME analysis set out above, the value of a share of the Proposed Merged Entity (on a minority basis) is as set out in the table below.

Table 33: CFME valuation summary of the Proposed Merged Entity

($'000)	EBIT	
	Low	High
Maintainable earnings	8,800	9,200
Multiple (minority basis)	8.5x	9.5x
Enterprise value	**74,800**	**87,400**
Surplus assets	62	62
Non-operating liabilities	(2,900)	(3,200)
Net cash	6,738	6,738
Equity value on a minority basis	**78,700**	**91,000**
Allocation to options and performance rights	(2,127)	(2,491)
Value allocated to ordinary shares	**76,573**	**88,509**
Total number of shares ('000)	202,691	202,691
Assessed value per share ($)	**0.38**	**0.44**

Source: Leadenhall analysis

9.3 Analysis of share trading

Similar to Section 8.3, we have analysed PNW's share price post announcement of the Proposed Transaction to capture the market's assessment of the current value of the Proposed Merged Entity on a minority basis. As set out in Section 8.3, we consider the market trading to be reasonably well informed and moderately liquid. We have therefore undertaken only a high-level analysis of share market trading, taking reference to the trading price range of between $0.25 and $0.40, as well as the VWAP of a PNW share of $0.34 over the two-month period since the announcement of the Proposed Transaction. We consider the VWAP of $0.34 to be a more reliable market indication of the current value of PNW as it factors the volume of transactions at a specific price point over the two-month period. This is therefore broadly in line with our CFME values which is not unreasonable given the limited liquidity in share trading and also, the level of access to management and information provided to us than an ordinary investor has.

9.4 Conclusion on value

Based on our CFME analysis and analysis of share trading cross-check, we have selected a valuation range for a share in the Proposed Merged Entity of between $0.38 and $0.44, on a minority basis. We note this is a relatively broad range which reflects the wide range of potential outcomes in relation to near-term revenue growth and synergies.

10 EVALUATION

10.1 Fairness

In order to assess whether the Proposed Transaction is fair we have compared:

- Our assessed fair market value of a PNW share before the Proposed Transaction on a control basis (i.e. including a control premium); with
- Our assessed fair market value of a share in the Proposed Merged Entity (i.e. PNW plus Crocmedia after the Proposed Transaction), on a minority interest basis

This comparison is set out below.

Table 34: Assessment of fairness

	Section	Low ($)	High ($)
Fair market value of a PNW share (before Proposed Transaction)	8.2.5	0.25	0.31
Fair market value of a Proposed Merged Entity share	9.2.6	0.38	0.44

Source: Leadenhall analysis

Since the value of a PNW share before the Proposed Transaction (on a control basis) is below the value of a share in the Proposed Merged Entity (on a minority basis), the Proposed Transaction is fair to Shareholders.

As noted in Section 9.2, whilst the value of the Proposed Merged Entity is sensitive to certain key assumptions in respect of maintainable earnings and earnings multiple, we note that any reasonable changes to these assumptions would not alter the above conclusion.

10.2 Reasonableness

We have defined the Proposed Transaction as reasonable if it is fair, or if despite not being fair, there are sufficient reasons for Shareholders to vote for the proposal. Whilst the Proposed Transaction is fair, we have also considered the following advantages and disadvantages of the Proposed Transaction to Shareholders.

10.2.1 Advantages

Limited alternatives available

Should PNW not successfully complete the Planned Capital Raising there is uncertainty as to whether it will be able to refinance its debt obligations hence continue to trade as a going concern. Since the Planned Capital Raising is dependent on the Proposed Transaction proceeding, the Proposed Transaction will facilitate the Planned Capital Raising and therefore mitigate the refinancing risk for the company.

Potential to realise cost and revenue synergies

As set out in Section 6.3, in the longer term, there is the potential to realise significant cost and revenue synergies. An initial synergies assessment performed by the management has identified at least $3.0 million of cost synergies to be achieved by the Proposed Transaction. This is equivalent to approximately 50% of the maintainable earnings for PNW and Crocmedia combined. Further potential revenue synergies associated with initiatives such as cross-selling have not been quantified.

Complementary activities

As PNW and Crocmedia operate in similar parts of the sports media and advertising industry, the Proposed Transaction would not only provide an opportunity for both businesses to consolidate, but may reduce competition in some areas.

10.2.2 Disadvantages

Selective treatment of certain investors

The Planned Capital Raising was negotiated at the same time as the Proposed Transaction, both of which are interdependent. The Planned Capital Raising and the Proposed Transaction are both based on a price of $0.25 per share, being the 30-day VWAP of PNW shares prior to the announcement of the Proposed Transaction. The Planned Capital Raising is priced at a substantial discount to both our assessed value of a share in the Proposed Merged Entity and the current market price of PNW shares, which has increased following the announcement of the Proposed Transaction. The market response since the deal was announced is consistent with our assessed value of shares in the Proposed Merged Entity, which includes the expected synergy benefits arising from the Proposed Transaction. We understand that Shareholders are not invited to participate in the Planned Capital Raising due to PNW's requirement for speed and certainty in raising the funds, thus this represents selective treatment for one of PNW's major shareholders, Viburnum and the other participants in the Planned Capital Raising.

Loss of control

If the Proposed Transaction is approved the vendors of would acquire practical control of PNW with a holding slightly below 50% and the possibility of a greater than 50% holding subject to the vesting of the long-term incentive performance rights. This would include the ability to control the assets, the strategic direction of the company, and the decision of when to pay dividends. The vendors of Crocmedia may not always act in the best interest of PNW's current shareholders, subject to compliance with relevant laws and regulations.

Crocmedia's unaudited financial statements

Crocmedia has not had their financial statements audited despite the commission of extensive due diligence on Crocmedia. Therefore, financial information of the Proposed Merged Entity has a risk of error.

Change in investment risk profile

While both PNW and Crocmedia are involved in the sports media and advertising industry, investors who acquired PNW shares for exposure to certain characteristics, investment focus and scale of the current PNW may not wish to hold an investment in the Proposed Merged Entity. Whilst the Proposed Merged Entity would likely provide the potential for increased returns on investment, this exposure may not be desirable for some investors due to individual investment preferences.

10.2.3 Conclusion on reasonableness

As the Proposed Transaction is fair it is also reasonable.

10.3 Opinion

The Proposed Transaction is fair and reasonable to Shareholders.

An individual shareholder's decision in relation to the Proposed Transaction may be influenced by their own circumstances. If in doubt, the shareholder should consult an independent financial adviser.

APPENDIX 1: GLOSSARY

Term	Meaning
ABC	Australian Broadcasting Corporation
ASIC	Australian Securities and Investments Commission
ASX	ASX Limited
Bravo	Bravo Talent Management
CAGR	Compound annual growth rate
CBA	The Commonwealth Bank of Australia
CFME	Capitalisation of future maintainable earnings method
Chapter 2E	Chapter 2E of the Corporations Act
Corporations Act	The Corporations Act 2001
Crocmedia	Crocmedia Pty Ltd
DCF	Discounted cash flow method
EBIT	Earnings before interest and tax
EBITDA	Earnings before interest, tax, depreciation and amortisation
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 arms' 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
FOS	Financial Ombudsman Service
FSG	Financial Services Guide
FY	Financial year
Leadenhall	Leadenhall Corporate Advisory Pty Ltd
Morrison Media	Morrison Media Services Pty Ltd
NAB	The National Australia Bank
NPAT	Net profit after tax
PBT	Profit before tax
Planned Capital Raising	$10 million offer of new shares
PNW	Pacific Star Network Ltd
Proposed Merged Entity	Combination of PNW and Crocmedia after the Proposed Transaction
Proposed Transaction	Acquisition of 100% of Crocmedia
RG74	Regulatory Guide 74: Acquisitions Approved by Members
RG76	Regulatory Guide 76: Related Party Transactions
RG111	Regulatory Guide 111: Content of Expert Reports
s606	Section 606 of the Corporations Act 2001
s611	Section 611 of the Corporations Act 2001
SEN	Sports Entertainment Network
Shareholders	PNW's shareholders not associated with the vendors of Crocmedia or Viburnum
SWOT	Strengths, weaknesses, opportunities and threats analysis
Viburnum	Viburnum Funds Pty Ltd
VWAP	Volume-weighted average price

APPENDIX 2: VALUATION METHODOLOGIES

In preparing this report we have considered valuation methods commonly used in practice and those recommended by RG 111. These methods include:

- The discounted cash flow method
- The capitalisation of earnings method
- Asset based methods
- Analysis of share market trading
- Industry specific rules of thumb

The selection of an appropriate valuation method to estimate fair market value should be guided by the actual practices adopted by potential acquirers of the company involved.

Discounted Cash Flow Method

Description

Of the various methods noted above, the discounted cash flow method has the strongest theoretical standing. It is also widely used in practice by corporate acquirers and company analysts. The discounted cash flow method estimates the value of a business by discounting expected future cash flows to a present value using an appropriate discount rate. A discounted cash flow valuation requires:

- A forecast of expected future cash flows
- An appropriate discount rate

It is necessary to project cash flows over a suitable period of time (generally regarded as being at least five years) to arrive at the net cash flow in each period. For a finite life project or asset this would need to be done for the life of the project. This can be a difficult exercise requiring a significant number of assumptions such as revenue growth, future margins, capital expenditure requirements, working capital movements and taxation.

The discount rate used represents the risk of achieving the projected future cash flows and the time value of money. The projected future cash flows are then valued in current day terms using the discount rate selected.

The discounted cash flow method is often sensitive to a number of key assumptions such as revenue growth, future margins, capital investment, terminal growth and the discount rate. All of these assumptions can be highly subjective sometimes leading to a valuation conclusion presented as a range that is too wide to be useful.

Use of the Discounted Cash Flow Method

A discounted cash flow approach is usually preferred when valuing:

- Early stage companies or projects
- Limited life assets such as a mine or toll concession
- Companies where significant growth is expected in future cash flows
- Projects with volatile earnings

It may also be preferred if other methods are not suitable, for example if there is a lack of reliable evidence to support a capitalisation of earnings approach. However, it may not be appropriate if:

- Reliable forecasts of cash flow are not available and cannot be determined
- There is an inadequate return on investment, in which case a higher value may be realised by liquidating the assets than through continuing the business

Capitalisation of Earnings Method

Description

The capitalisation of earnings method is a commonly used valuation methodology that involves determining a future maintainable earnings figure for a business and multiplying that figure by an appropriate capitalisation multiple. This methodology is generally considered a short form of a discounted cash flow, where a single representative earnings figure is capitalised, rather than a stream of individual cash flows being discounted. The capitalisation of earnings methodology involves the determination of:

- A level of future maintainable earnings
- An appropriate capitalisation rate or multiple

A multiple can be applied to any of the following measures of earnings:

Revenue – most commonly used for companies that do not make a positive EBITDA or as a cross-check of a valuation conclusion derived using another method.

EBITDA - most appropriate where depreciation distorts earnings, for example in a company that has a significant level of depreciating assets but little ongoing capital expenditure requirement.

EBITA - in most cases EBITA will be more reliable than EBITDA as it takes account of the capital intensity of the business.

EBIT - whilst commonly used in practice, multiples of EBITA are usually more reliable as they remove the impact of amortisation which is a non-cash accounting entry that does not reflect a need for future capital investment (unlike depreciation).

NPAT - relevant in valuing businesses where interest is a major part of the overall earnings of the group (e.g. financial services businesses such as banks).

Multiples of EBITDA, EBITA and EBIT are commonly used to value whole businesses for acquisition purposes where gearing is in the control of the acquirer. In contrast, NPAT (or P/E) multiples are often used for valuing minority interests in a company.

The multiple selected to apply to maintainable earnings reflects expectations about future growth, risk and the time value of money all wrapped up in a single number. Multiples can be derived from three main sources. Using the guideline public company method, market multiples are derived from the trading 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, such as the ASX. The merger and acquisition method is a method whereby multiples are derived from transactions of significant interests in companies engaged in the same or similar lines of business. It is also possible to build a multiple from first principles.

Use of the Capitalisation of Earnings Method

The capitalisation of earnings method is widely used in practice. It is particularly appropriate for valuing companies with a relatively stable historical earnings pattern which is expected to continue. This method is less appropriate for valuing companies or assets if:

- There are no suitable listed company or transaction benchmarks for comparison
- The asset has a limited life
- Future earnings or cash flows are expected to be volatile
- There are negative earnings or the earnings of a business are insufficient to justify a value exceeding the value of the underlying net assets

Asset Based Methods

Description

Asset based valuation methods estimate the value of a company based on the realisable value of its net assets, less its liabilities. There are a number of asset based methods including:

- Orderly realisation
- Liquidation value
- Net assets on a going concern basis
- Replacement cost
- Reproduction cost

The orderly realisation of assets method estimates fair market value by determining the amount that would be distributed to shareholders, after payment of all liabilities including realisation costs and taxation charges that arise, assuming the company is wound up in an orderly manner. The liquidation method is similar to the orderly realisation of assets method except the liquidation method assumes the assets are sold in a shorter time frame. Since wind up or liquidation of the company may not be contemplated, these methods in their strictest form may not necessarily be appropriate. The net assets on a going concern basis method estimates the market values of the net assets of a company but does not take account of realisation costs.

The asset / cost approach is generally used when the value of the business' assets exceeds the present value of the cash flows expected to be derived from the ongoing business operations, or the nature of the business is to hold or invest in assets. It is important to note that the asset approach may still be the relevant approach even if an asset is making a profit. If an asset is making less than an economic rate of return and there is no realistic prospect of it making an economic return in the foreseeable future, an asset approach would be the most appropriate method.

Use of Asset Based Methods

An asset-based approach is a suitable valuation method when:

- An enterprise is loss making and is not expected to become profitable in the foreseeable future
- Assets are employed profitably but earn less than the cost of capital
- A significant portion of the company's assets are composed of liquid assets or other investments (such as marketable securities and real estate investments)
- It is relatively easy to enter the industry (for example, small machine shops and retail establishments)

Asset based methods are not appropriate if:

- The ownership interest being valued is not a controlling interest, has no ability to cause the sale of the company's assets and the major holders are not planning to sell the company's assets
- A business has (or is expected to have) an adequate return on capital, such that the value of its future income stream exceeds the value of its assets

Analysis of Share Trading

The most recent share trading history provides evidence of the fair market value of the shares in a company where they are publicly traded in an informed and liquid market. There should also be some similarity between the size of the parcel of shares being valued and those being traded. Where a company's shares are publicly traded then an analysis of recent trading prices should be considered, at least as a cross-check to other valuation methods.

Industry Specific Rules of Thumb

Industry specific rules of thumb are used in certain industries. These methods typically involve a multiple of an operating figure such as eyeballs for internet businesses, numbers of beds for hotels etc. These methods are typically fairly crude and are therefore usually only appropriate as a cross-check to a valuation determined using an alternative method.

APPENDIX 3: COMPARABLE COMPANIES

The following company descriptions are extracted from descriptions provided by S&P Capital IQ.

Company	Description
APN Outdoor Group Ltd	APN Outdoor Group Limited operates as an outdoor advertising company in Australia and New Zealand.
Fairfax Media Ltd	Fairfax Media Limited operates as a digitally progressive media company in Australia and New Zealand.
HT&E Ltd	HT&E Limited, together with its subsidiaries, operates as a media and entertainment company in Australia, New Zealand, and Hong Kong.
Macquarie Media Ltd	Macquarie Media Limited engages in the radio and associated media activities in Australia.
Nine Entertainment Co. Holdings Ltd	Nine Entertainment Co. Holdings Limited engages in television broadcasting and program production businesses in Australia.
oOh!media Ltd	oOh!media Limited, an out of home media company, provides outdoor media, production, and advertising services in Australia and New Zealand.
Pacific Star Network Ltd	Pacific Star Network Limited operates as a media company in Australia.
Prime Media Group Ltd	Prime Media Group Limited provides commercial television broadcasting services in Australia.
QMS Media Ltd	QMS Media Limited provides out-of-home advertising and media services in Australia and internationally.
Seven West Media Ltd	Seven West Media Limited, together with its subsidiaries, operates as a multi-platform media company in Australia.
Southern Cross Media Group Ltd	Southern Cross Media Group Limited engages in the creation and broadcasting of content on free to air commercial radio, TV, and online media platforms in Australia.

APPENDIX 4: CONTROL PREMIUM

Background

The difference between the control value and the liquid minority value is the control premium. The opposite of a control premium is a minority discount (also known as a discount for lack of control). A control premium is said to exist because the holder of a controlling stake has several rights that a minority holder does not enjoy (subject to shareholders agreements and other legal constraints), including:

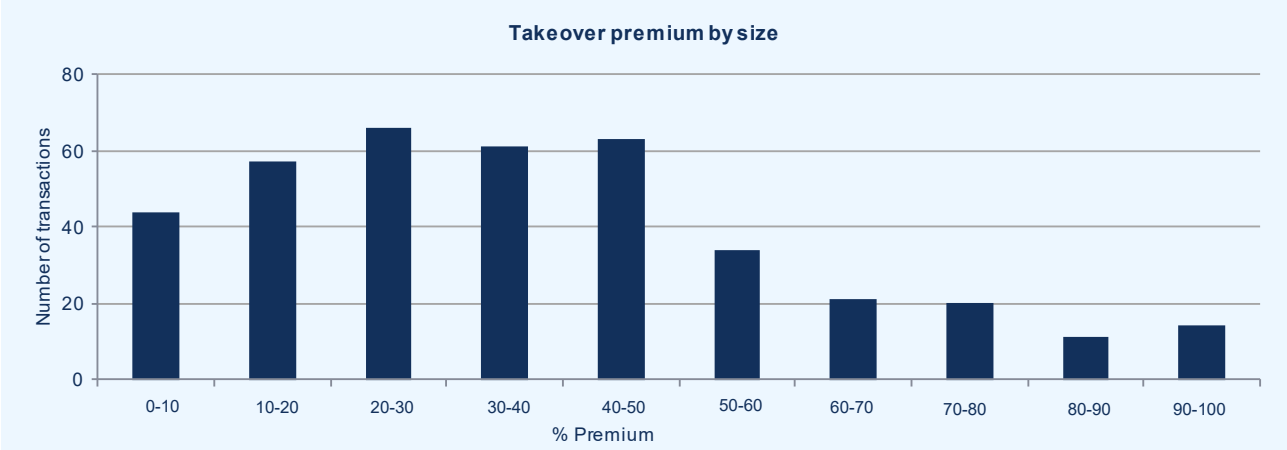
- Appoint or change operational management
- Appoint or change members of the board
- Determine management compensation
- Determine owner's remuneration, including remuneration to related party employees
- Determine the size and timing of dividends
- Control the dissemination of information about the company
- Set strategic focus of the organisation, including acquisitions, divestments and any restructuring
- Set the financial structure of the company (debt / equity mix)
- Block any or all of the above actions

The most common approach to quantifying a control premium is to analyse the size of premiums implied from prices paid in corporate takeovers. Another method is the comparison between prices of voting and non-voting shares in the same company. We note that the size of the control premium should generally be an outcome of a valuation and not an input into one, as there is significant judgement involved.

Takeover Premiums

Dispersion of premiums

The following chart shows the spread of premiums paid in takeovers between 2005 and 2015. We note that these takeover premiums may not be purely control premiums, for example the very high premiums are likely to include synergy benefits, while the very low premiums may be influenced by share prices rising in anticipation of a bid.

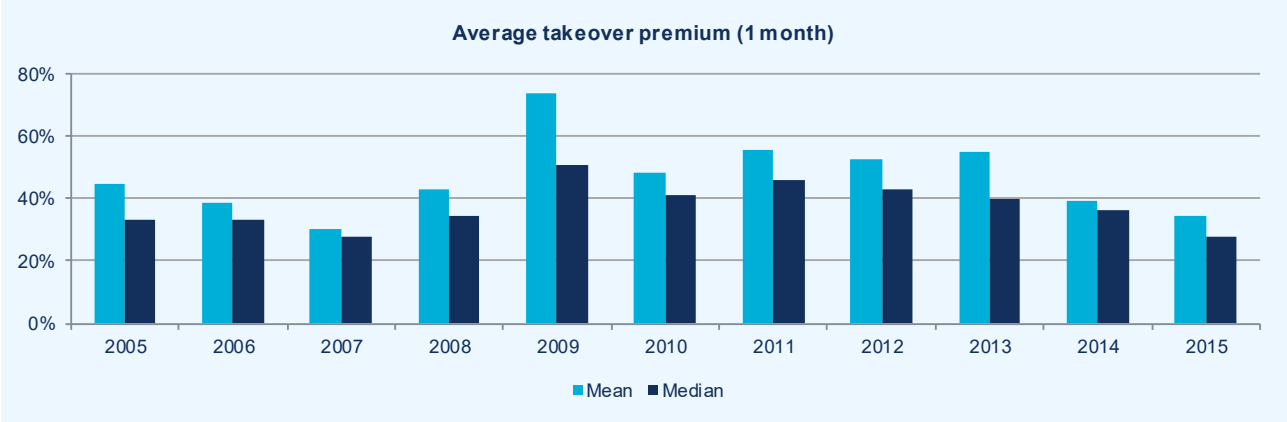


Sources: FactSet, Leadenhall analysis

This chart highlights the dispersion of premiums paid in takeovers. The chart shows a long tail of high premium transactions, although the most common recorded premium is in the range of 20% to 30%, with approximately 60% of all premiums falling in the range of 0% to 40%.

Premiums over time

The following chart shows the average premium paid in completed takeovers compared to the price one month before the initial announcement.

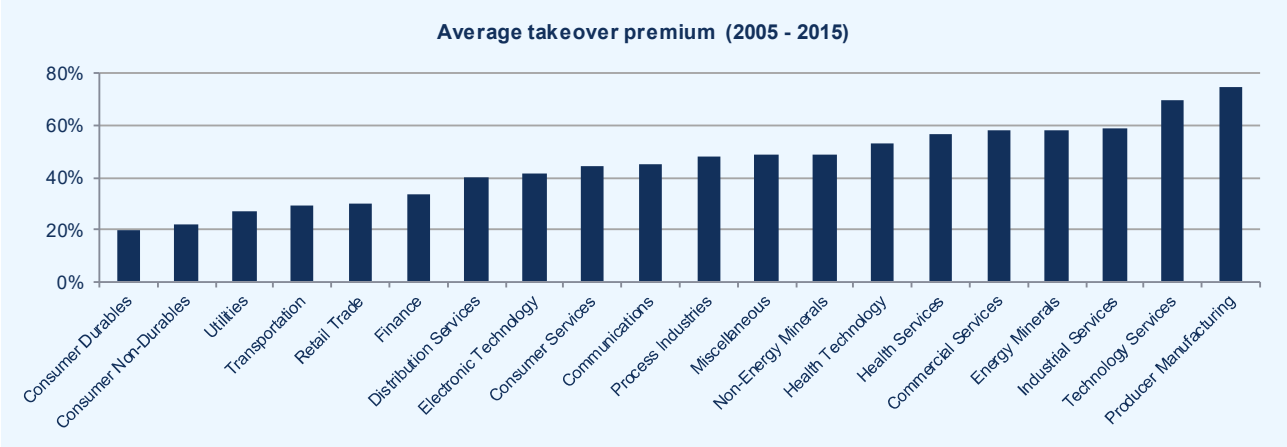


Sources: FactSet, Leadenhall analysis

The chart indicates that while premiums vary over time, there is no clearly discernible pattern. The mean is higher than the median due to a small number of high premiums.

Premiums by industry

The following chart shows the average takeover premium by industry, compared to the share price one month before the takeover was announced. Most industries show an average premium of 20% to 50%.



Sources: FactSet, Leadenhall analysis

A number of industries have fairly high averages which have been impacted by specific transactions as set out below:

- **Producer Manufacturing:** includes two transactions with control premiums over 100%. The average premium is 25% lower when these transactions are excluded.
- **Technology Services:** includes four transactions with control premiums in excess of 100%. The average premium is 30% lower when these transactions are excluded.
- **Industrial Services:** includes two transactions with control premiums in excess of 100%. The average premium is 30% lower when these transactions are excluded.
- **Energy Minerals:** includes six transactions with control premiums in excess of 100%. The average premium is 20% lower when these transactions are excluded.
- **Commercial Services:** includes four transactions with control premiums in excess of 100%. The average premium is 20% lower when these transactions are excluded.
- **Health Services:** includes one transaction with a control premium of 183%. The average premium is 20% lower when this transaction is excluded.

Key factors that generally lead to higher premiums being observed are more than one party presenting a takeover offer, favourable trading conditions in certain industries (e.g. recent mining and tech booms), when the price includes special value and scrip offers where the price of the acquiring entity's shares increases between announcement and completion.

Industry Practice

In Australia, industry practice is to apply a control premium in the range of 20% to 40%, as shown in the following list quoting ranges noted in various independent experts' reports.

- Deloitte - 20% to 40%
- Ernst & Young - 20% to 40%
- Grant Samuel - 20% to 35%
- KPMG - 25% to 40%
- Lonergan Edwards - 30 to 35%
- PwC - 20% to 40%

The range of control premiums shown above is consistent with most academic and professional literature published by leading valuation experts.

Alternative View

Whilst common practice is to accept the existence of a control premium, in the order of 20% to 40%, certain industry practitioners (particularly in the US) disagree with the validity of this conclusion. Those with an alternate view point to the fact that very few listed companies are acquired each year as evidence that 100% of a company is not necessarily worth more than the proportionate value of a small interest. The reason we see some takeovers at a premium is that if a company is not well run, there is a control premium related to the difference in value between a hypothetical well run company and the company being run as it is.

Impact of Methodologies Used

The requirement for an explicit valuation adjustment for a control premium depends on the valuation methodology and approach adopted and the level of value to be examined. It may be necessary to apply a control premium to the value of a liquid minority value to determine the control value. Alternatively, in order to estimate the value of a minority interest, it may be necessary to apply a minority discount to a proportional interest in the control value of the company.

Discounted cash flow

The discounted cash flow methodology generally assumes control of the cash flows generated by the assets being valued. Accordingly, such valuations reflect a premium for control. Where a minority value is sought a minority discount must therefore be applied. The most common exception to this is where a discounted dividend model has been used to directly determine the value of an illiquid minority holding.

Capitalisation of earnings

Depending on the type of multiple selected, the capitalisation of earnings methodology can reflect a control value (transaction multiples) or a liquid minority value (listed company trading multiples).

Asset based methodologies

Asset based methodologies implicitly assume control of the assets being valued. Accordingly, such valuations reflect a control value.

Intermediate Levels of Ownership

There are a number of intermediate levels of ownership between a portfolio interest and 100% ownership. Different levels of ownership/strategic stakes will confer different degrees of control and rights as shown below.

- 90% - can compulsory purchase remaining shares if certain conditions are satisfied
- 75% - power to pass special resolutions
- > 50% - gives control depending on the structure of other interests (but not absolute control)
- > 25% - ability to block a special resolution
- > 20% - power to elect directors, generally gives significant influence, depending on other shareholding blocks
- < 20% generally has only limited influence

Conceptually, the value of each of these interests lies somewhere between the portfolio value (liquid minority value) and the value of a 100% interest (control value). Each of these levels confers different degrees of control and therefore different levels of control premium or minority discount.

50%

For all practical purposes, a 50% interest confers a similar level of control to holdings of greater than 50%, at least where the balance of the shares are listed and widely held. Where there are other significant holders, such as in a 50/50 joint venture, 50% interests involve different considerations depending upon the particular circumstances.

Strategic parcels do not always attract a control premium. In fact, if there is no bidder, the owner may be forced to sell the shares through the share market, usually at a discount to the prevailing market price. This reflects the fact that the sale of a parcel of shares significantly larger than the average number of shares traded on an average day in a particular stock generally causes a stock overhang, therefore there is more stock available for sale than there are buyers for the stock and in order to clear the level of stock available, the share price is usually reduced by what is referred to as a blockage discount.

20% to 50%

Holdings of less than 50% but more than 20% can confer a significant degree of influence on the owner. If the balance of shareholders is widely spread, a holding of less than 50% can still convey effective control of the business. However, it may not provide direct ownership of assets or access to cash flow. This level of holding has a strategic value because it may allow the holder significant influence over the company's management, possibly additional access to information and a board seat.

<20%

Holdings of less than 20% are rarely considered strategic and would normally be valued in the same way as a portfolio interest given the stake would not be able to pass any ordinary or special resolution on their own if they were against the interests of the other shareholders. Depending on the circumstances, a blockage discount may also apply.

As explained above, the amount of control premium or minority discount that would apply in specific circumstances is highly subjective. In relation to the appropriate level of control premium, Aswath Damodaran[1] notes "the value of controlling a firm has to lie in being able to run it differently (and better)". A controlling shareholder will be able to implement their desired changes. However, it is not certain that a non-controlling shareholder would be able to implement changes they desired. Thus, following the logic of Damodaran and the fact that the strategic value of the holding typically diminishes as the level of holding decreases, the appropriate control premium for a non-controlling shareholder should be lower than that control premium for a controlling stake.

[1] *Aswath Damodaran is a Professor of Finance at the Stern School of Business at New York University, where he teaches corporate finance and equity valuation. He has written several books on equity valuation, as well as corporate finance and investment. He is also widely published in leading finance journals.*

Key Factors in Determining a Reasonable Control Premium

Key factors to consider in determining a reasonable control premium include:

- **Size of holding** – Generally, larger stakes attract a higher control premium
- **Other holdings** – The dispersion of other shareholders is highly relevant to the ability for a major shareholder to exert control. The wider dispersed other holdings are, the higher the control premium
- **Industry premiums** – Evidence of premiums recently paid in a given industry can indicate the level of premium that may be appropriate
- **Size** – medium sized businesses in a consolidating industry are likely to be acquired at a larger premium than other businesses
- **Dividends** – a high dividend payout generally leads to a low premium for control
- **Gearing** – a company that is not optimally geared may attract a higher premium than otherwise, as the incoming shareholder has the opportunity to adjust the financing structure
- **Board** – the ability to appoint directors would increase the control premium attaching to a given parcel of shares. The existence of independent directors would tend to decrease the level of premium as this may serve to reduce any oppression of minority interests and therefore support the level of the illiquid minority value
- **Shareholders' agreement** - the existence and contents of a shareholders agreement, with any protection such as tag along and drag along rights offered to minority shareholders lowers the appropriate control premium

APPENDIX 5: QUALIFICATIONS, DECLARATIONS AND CONSENTS

Responsibility and purpose

This report has been prepared for PNW's shareholders for the purpose of assessing the fairness and reasonableness of the Proposed Transaction. Leadenhall expressly disclaims any liability to any shareholder, or anyone else, whether for our negligence or otherwise, if the report is used for any other purpose or by any other person.

Reliance on information

In preparing this report we relied on the information provided to us by PNW and Crocmedia being complete and accurate and we have assumed it has been prepared in accordance with applicable Accounting Standards and relevant national and state legislation. We have not performed an audit, review or financial due diligence on the information provided. Drafts of our report were issued to PNW's management and Crocmedia's management for confirmation of factual accuracy.

Prospective information

To the extent that this report refers to prospective financial information, we note that the forecasts and projections supplied to us are, by definition, based upon assumptions about events and circumstances that have not yet transpired. Actual results in the future may be different from the prospective financial information referred to in this report and the variation may be material, since anticipated events frequently do not occur as expected. Accordingly, we give no assurance that any forecast results will be achieved. Any future variation between the actual results and the prospective financial information utilised in this report may affect the conclusions included in this report.

Market conditions

Leadenhall's opinion is based on prevailing market, economic and other conditions as at the date of this report. Conditions can change over relatively short periods of time. Any subsequent changes in these conditions could impact upon the conclusion reached in this report.

As a valuation is based upon expectations of future results it involves significant judgement. Although we consider the assumptions used and the conclusions reached in this report are reasonable, other parties may have alternative expectations of the future, which may result in different valuation conclusions. The conclusions reached by other parties may be outside Leadenhall's preferred range

Indemnities

In recognition that Leadenhall may rely on information provided by PNW and Crocmedia and their officers, employees, agents or advisors, PNW has agreed that it will not make any claim against Leadenhall to recover any loss or damage which it may suffer as a result of that reliance and that it will indemnify Leadenhall against any liability that arises out of Leadenhall's reliance on the information provided by PNW and Crocmedia and their officers, employees, agents or advisors or the failure by PNW and Crocmedia and their officers, employees, agents or advisors to provide Leadenhall with any material information relating to this report.

Qualifications

The personnel of Leadenhall principally involved in the preparation of this report were Richard Norris, BA (Hons), FCA, M.App.Fin, F.Fin, Shaun Bettman, BCom, CA, GradDipAppFin, Gary Cornelius, B.Ec (Hons), FFTP, FAICD Dip and Bruce Li, BCom, CA.

This report has been prepared in accordance with "APES 225 – Valuation Services" issued by the Accounting Professional & Ethical Standards Board and is a valuation engagement in accordance with that standard.

Independence

Leadenhall has acted independently of PNW. Compensation payable to Leadenhall is not contingent on the conclusion, content or future use of this report.