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FANTASTIC HOLDINGS LIMITED

Takeover offer from Steinhoff Asia Pacific Holdings Pty Ltd by Scheme of Arrangement

INDEPENDENT EXPERT'S REPORT
AND FINANCIAL SERVICES GUIDE

13 OCTOBER 2016

13 October 2016

The Directors
Fantastic Holdings Limited
62 Hume Highway
Chullora NSW 2190

Dear Directors,

Independent Expert's Report for Fantastic Holdings Limited

1. Introduction

Fantastic Holdings Limited ("**Fantastic**") is a public company listed on the Australian Securities Exchange ("**ASX**") that is engaged in the manufacture and retail of furniture. As at 7 October 2016 Fantastic had a market capitalisation of approximately $240.6 million.

Steinhoff Asia Pacific Holdings Pty Ltd ("**Steinhoff**") is also engaged in the manufacture and retail of furniture, with brands including Freedom and Snooze. Steinhoff is a subsidiary of Steinhoff International Holdings NV, a company listed on the Frankfurt Stock Exchange.

On 13 October 2016 Fantastic and Steinhoff entered into a scheme implementation deed for Steinhoff to acquire 100% of the shares in Fantastic, by way of a scheme of arrangement ("**Proposed Transaction**"). Steinhoff has offered $3.50 in cash for each Fantastic share.

Further details of the Proposed Transaction are set out in Section 1 of our detailed report.

2. Purpose of report

There is no formal requirement for an independent expert's report in relation to the Proposed Transaction. However, the directors of Fantastic have requested Leadenhall Corporate Advisory Pty Ltd ("**Leadenhall**") to prepare an independent expert's report to assess whether the Proposed Transaction is in the best interests of Fantastic's shareholders ("**Shareholders**"). This report will be included in the scheme booklet in relation to the Proposed Transaction ("**Scheme Booklet**") to assist Shareholders to evaluate the Proposed Transaction.

Further details of the purpose of this report are set out in Section 2 of our detailed report.

3. Basis of evaluation

In order to assess whether the Proposed Transaction is in Shareholders' best interests we have considered whether it is fair and reasonable to Shareholders. In order to assess whether the Proposed Transaction is fair and reasonable we have:

- Assessed it as fair if the consideration offered by Steinhoff is greater than or equal to the value of a Fantastic share on a control basis
- Assessed it as reasonable if it is fair, or if despite not being fair the advantages to Shareholders outweigh the disadvantages

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

4. Analysis of fairness

We have assessed the fair market value of a Fantastic share to be in the range of $3.42 to $3.77, using the capitalisation of earnings approach as follows:

Table 1: Valuation summary

	EBITDA		EBIT	
	Low	High	Low	High
Selected maintainable earnings	43.5	45.0	36.0	37.5
Selected multiple	7.5	8.0	9.0	9.5
Enterprise value	**326.3**	**360.0**	**324.0**	**356.3**
Surplus assets	1.0	1.0	1.0	1.0
Net cash	29.7	29.7	29.7	29.7
Non-operating liabilities	(1.5)	(1.5)	(1.5)	(1.5)
Equity value	**355.4**	**389.2**	**353.2**	**385.4**
Number of share on issue	103.3	103.3	103.3	103.3
Value per share	**$3.44**	**$3.77**	**$3.42**	**$3.73**

Source: Leadenhall analysis

In applying the capitalisation of earnings approach we have:

- Determined a maintainable level of EBIT of $36.0 million to $37.5 million. This equates to a maintainable level of EBITDA of $43.5 million to $45.0 million after adjusting for depreciation and amortisation. This level of earnings was assessed after consideration of historical earnings (normalised to remove non-recurring items), management forecasts, year to date earnings and brokers' forecasts
- Applied an EBIT multiple of 9.0 to 9.5 times and an EBITDA multiple of 7.5 times to 8.0 times. These are control multiples, derived from analysis of takeover transactions and share market trading prices of companies with similar businesses to Fantastic
- Added surplus assets of $1.0 million in relation to surplus land held by Fantastic
- Added surplus cash of $29.7 million
- Deducted a non-operating liability in relation to closure costs for one store which is due to be closed

The result from this methodology was cross-checked using an analysis of share market trading prior to the announcement of the Proposed Transaction. Further details of the valuation of Fantastic are set out in Section 6 of our detailed report.

We have assessed whether the Proposed Transaction is fair by comparing our assessed fair market value of a Fantastic share on a control basis with the consideration offered. This comparison is set out in the table below.

Table 2: Assessment of fairness

	Low	High
Fair market value of a Fantastic share	$3.42	$3.77
Consideration	$3.50	$3.50

Source: Leadenhall analysis

Since the consideration offered is within the assessed range of values of a Fantastic share the Proposed Transaction is fair to Shareholders.

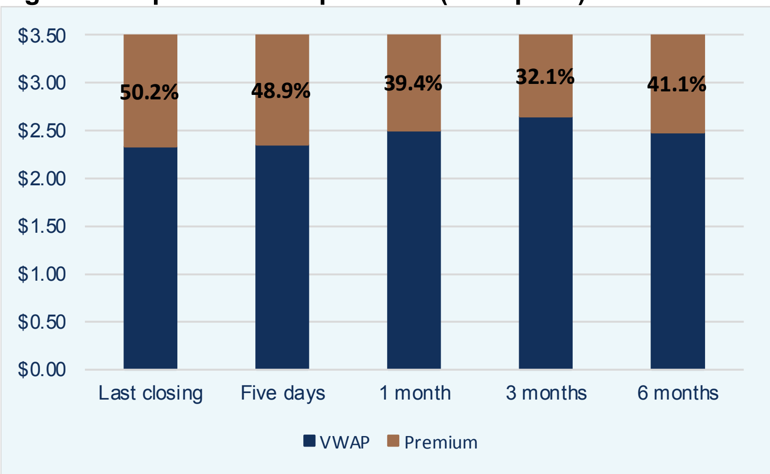
5. Analysis of reasonableness

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. We have therefore considered the following advantages and disadvantages of the Proposed Transaction to Shareholders.

Advantages

- **Premium to market price -** The offer price reflects a meaningful premium to the Fantastic share price immediately prior to the announcement as set out in the figure below:

Figure 1: Implied control premium (offer price)



Source: FactSet and Leadenhall analysis
Note: Last closing is as at 9 October 2016

- **Share price in the absence of an alternative offer -** In the absence of any alternative takeover offer, the only alternative to dispose of Fantastic shares would be to sell them on the market at a price which does not include a premium for control and would incur transaction costs (e.g. brokerage). If the Proposed Transaction is not approved, it is likely that Fantastic shares would trade at a price below the offer price, at least in the short term.
- **No superior alternative offer -** We are not aware of any competing proposals to acquire Fantastic by any third party. However, we note that there would be an opportunity for any other interested party to put forward a competing offer prior to the scheme meeting being held. In these circumstances Shareholders would need to consider the competing offer before concluding on the Proposed Transaction.

Disadvantages

- **Loss of exposure to Fantastic business -** If the Proposed Transaction is completed Shareholders would lose their exposure to the future performance of Fantastic. We note that the Fantastic management team has set out a medium term plan for the business including material growth in store numbers and profitability. If this plan is achieved, it is possible that Fantastic shares may trade at prices higher than the consideration under the Proposed Transaction in the medium term. By accepting the Proposed Transaction, Shareholders will not be able to participate in this potential upside.
- **Synergy benefits -** Given the complementary nature of Steinhoff's business with Fantastic, it is likely that Steinhoff will be able to realise some synergy benefits from acquiring Fantastic. Based on our analysis, the offer price does not appear to include a material amount related to potential synergies as the selected multiples are towards the lower end of the comparable ranges and no synergies have been allowed for in the selected earnings. However, in the absence of a competing proposal, it is common for an acquirer not to pay for potential synergies they may obtain in a business combination.
- **Tax implications -** The acceptance of the offer by the purchaser may have varying tax implications for individual investors which may impact the net cash consideration received. Shareholders should seek their own independent advice as to any potential tax implications upon acceptance of the offer.

Since the Proposed Transaction is fair it is also reasonable.

6. Opinion

In our opinion the Proposed Transaction is fair and reasonable to Shareholders. The Proposed Transaction is therefore in the best interests of 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	Dave Pearson
Director	**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.

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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.

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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 $55,000 (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.

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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.

13 October 2016

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1 TERMS OF THE PROPOSED TRANSACTION

1.1 Overview

Fantastic is listed on the ASX and has a market capitalisation of approximately $240 million as at 7 October 2016. Fantastic is engaged in the manufacture and retail of furniture.

Steinhoff is also engaged in the manufacture and retail of furniture, with brands including Freedom and Snooze. Steinhoff is a subsidiary of Steinhoff International Holdings NV, a company listed on the Frankfurt Stock Exchange with a market capitalisation of approximately €18.3 billion (A$26.9 billion) as at 7 October 2016.

On 13 October 2016 Fantastic and Steinhoff entered into a scheme implementation deed for Steinhoff to acquire 100% of the shares in Fantastic via a scheme of arrangement. The agreed consideration is $3.50 in cash per share, or $361 million in total.

Steinhoff also acquired an option to acquire a 19.9% interest in the shares of Fantastic from a major shareholder. The option is exerciseable in the event that a competing proposal is announced and Steinhoff increases its offer to be equal to or greater than that competing offer.

1.2 Approval

For the Proposed Transaction to become effective it will need to be approved at a meeting of Shareholders. Approval requires both of:

- A majority in number (i.e. more than 50%) of Shareholders present and voting (either in person or by proxy) at the meeting due to be held on 7 December 2016 to vote in favour of the Proposed Transaction
- At least 75% of the votes in respect of the resolution to be cast in favour of the Proposed Transaction

If approved by Shareholders, the scheme will then require approval by the Federal Court of Australia (NSW Registry).

1.3 Conditions

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

- Steinhoff receiving the necessary regulatory approvals, including approval from the Foreign Investment Review Board
- No material adverse events occurring in respect of Fantastic

2 SCOPE

2.1 Purpose of the Report

The Proposed Transaction is to be implemented by a scheme of arrangement under Section 411 of the Corporations Act 2001 ("Section 411"). Under Section 411, the scheme must be approved by Shareholders as described in Section 1.2 above.

Part 3 of Schedule 8 of the Corporations Regulations 2001 (Cwlth) ("Part 3") prescribes the information to be provided to shareholders in relation to schemes of arrangement. Part 3 requires an independent expert's report stating whether a proposed scheme is in the best interests of shareholders of the company subject to the scheme if either:

- The other party to the scheme is entitled to more than 30% of the voting shares in the company which is the subject of the scheme
- A director of the corporation that is the other party to the scheme is also a director of the company that is the subject of the scheme

As Steinhoff does not have any directors in common with Fantastic and does not hold greater than 30% of its shares, there is no formal requirement for an independent expert's report in relation to the Proposed Transaction. However, the directors of Fantastic have requested Leadenhall to prepare an independent expert's report in relation to the Proposed Transaction, as if it was required under Part 3, to assist Shareholders evaluate the Proposed Transaction.

2.2 Basis of Evaluation

Best Interests

There is no legal definition of the expression '*in the best interests*'. However, Regulatory Guide 111: Content of Expert Reports ("RG111") issued by the Australian Securities and Investments Commission ("ASIC") provides guidance on its meaning. RG111.19 requires an expert to assess whether a scheme of arrangement involving a change of control is '*fair and reasonable*'. A transaction would be '*in the best interests*' of shareholders if it is either '*fair and reasonable*' or '*not fair but reasonable*'.

As the Proposed Transaction is a control transaction, we have assessed whether it is fair and reasonable to Shareholders. Neither the ASX Listing Rules nor the Corporations Act 2001 define the term '*fair and reasonable*' and both contain no guidance on what should be considered when assessing whether a proposed transaction is fair and reasonable. However, guidance on what an independent expert should consider and how '*fair and reasonable*' should be defined is contained in RG 111 which states that there should be separate assessments of whether a transaction is '*fair*' and whether it is '*reasonable*'. We have therefore considered the concepts of '*fairness*' and '*reasonableness*' separately as discussed below.

Fairness

RG 111.11 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 Fantastic share with the consideration offered to Shareholders.

The value of a Fantastic share has been determined on a control basis (i.e. including a control premium). This is consistent with the requirement of RG 111.11 that the comparison for a takeover must be made assuming a 100% interest in the target company.

We have assessed the value of Fantastic using the concept of 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 the basis of value described at RG 111.11 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. Our assessed value of Fantastic does not include any special value in accordance with RG111.

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 in favour of 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:

- Any pre-existing interest of Steinhoff in Fantastic
- Existing shareholder composition of Fantastic shares
- The liquidity of the market in Fantastic's shares
- Taxation losses, cash flow or other benefits through achieving 100% ownership of Fantastic
- Any special value of Fantastic to Steinhoff
- The likely market price of Fantastic shares if the Proposed Transaction is unsuccessful
- The value of Fantastic to an alternative bidder and the likelihood of an alternative offer

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

2.3 Individual Circumstances

We have evaluated the Proposed Transaction for the 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 FURNITURE RETAILING INDUSTRY

3.1 Summary

Fantastic operates in the furniture retailing industry which involves procurement and sales of household furniture (such as lounge, dining, bedroom and outdoor furniture), blinds, awnings and mattresses.

The industry has weathered a challenging period over the last four years and is expected to post annualised growth of only 1.3% over the five years to June 2017, according to IBISWorld. This moderate growth was largely driven by a rise in discretionary income and demand from the residential property construction sector but moderated to some extent by negative consumer sentiment attributable to instability in global financial markets and uncertainty around the domestic economy.

The past five years have also seen intensifying price-based competition within the industry as well as competition from external sources, such as department stores and pure-play online retailers, resulting in a contraction in industry profit margins. This has forced the exit of smaller, unprofitable retailers and increased the market share of the larger industry participants.

Over the next five years, the industry is expected to grow at an annualised rate of 1.9% in response to continuing growth in discretionary incomes and increasing residential property construction activity. However, industry growth is expected to be constrained by high levels of competition and the continuation of weak consumer sentiment.

3.2 Products

Table 3 below segments the industry products into five broad categories with a description of each category and its share of industry revenue.

Table 3: Product descriptions and share of industry revenue

Product	Revenue share	Description
Lounge and dining room	48.6%	Includes some of the most expensive types of furniture. This segment has experienced a decline (as a share of total industry revenue) over the past five years attributable to a shift in consumer preference to outdoor furniture and more casual living.
Bedroom	34.0%	Similar to lounge and dining room furniture, this category has also experienced a decline as a share of industry revenue over the past five years. Declining housing affordability is thought to have had a significant impact on bedroom furniture sales.
Blinds and awnings	8.7%	Experienced an increase in share of revenue driven by the growing popularity of outdoor rooms and an increase in the usage of blinds as an alternative to curtains.
Outdoor and garden	6.5%	Includes outdoor dining and lounge settings. Strong growth has been observed in this segment over the past five years in line with increasing popularity of outdoor entertaining and garden design.
Other furniture	2.2%	Includes office furniture and antique-reproduction furniture. Demand in this product segment is driven by a typically older demographic or consumers with higher discretionary income. Its share of revenue has remained stable.

Source: IBISWorld

3.3 Key External Drivers

Table 4 below describes the key external drivers for the industry:

Table 4: Key external drivers

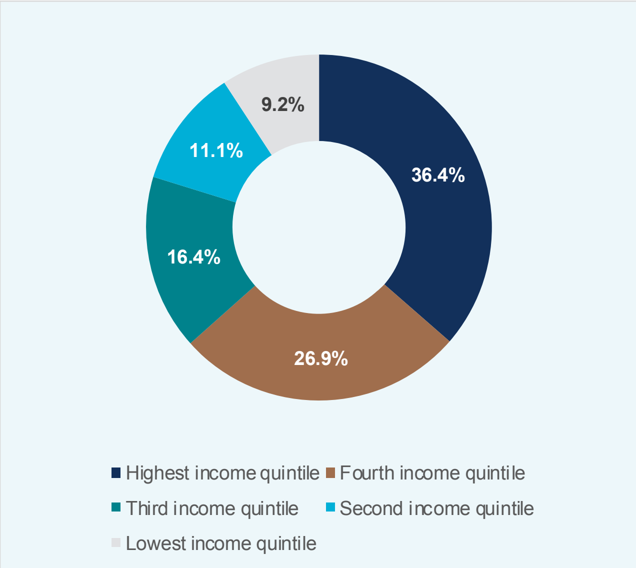
Driver	Description
Real household discretionary income	Refers to the amount of money available to households after deducting essential expenses such as food and housing. Upward trends in discretionary income broaden the type, quality and range of furniture that consumers can afford. The past five years has seen growth in discretionary income driving demand for furniture.
Consumer sentiment	Represents consumer evaluations of their individual financial situations as well as their attitude towards the overall economy. Negative consumer sentiment generally translates to reduced expenditure and curtailed demand for household furniture. In the last few years, unstable global financial markets and poor domestic employment numbers have made consumers pessimistic about the domestic economy resulting in reduced retail spending.
Demand from residential building construction	Housing growth has a strong effect on demand for furniture as new properties are often furnished with new furniture. Residential construction activity has fluctuated significantly over the past five years and is expected to decline in FY17 due to a scale back in multi-unit apartment construction.
Interest rates	Mortgage interest rates influence the amount of discretionary income available to consumers. Falling interest rates result in reduced household debt repayments; freeing up discretionary income. With current interest rates at extremely low levels, limited room exists for further rate reductions.
Exchange rates	A weakening Australian dollar will push up the price of imported furniture products and result in increased prices to consumers (reducing demand) or have a negative effect on the profitability of retailers. The trade-weighted index has fallen by approximately 16% over the past four years and the Australian dollar is now close to what many observers believe to be its fair value.

Source: IBISWorld

3.4 Major Markets

Households are the major market for furniture products. Demand is driven by both discretionary income and individual consumer needs / preferences. As such, the market can be segmented by household income quintiles. The highest income quintile comprises consumers with the highest average annual disposable income. Average income decreases from the highest quintile to the lowest quintile.

Figure 2: Proportion of industry revenue by income quintile (FY17)



Source: IBISWorld

The highest income quintile represents the most significant contributor to industry revenue while the lowest income quintile has contributed the least to industry revenue. This is intuitive given the higher a consumer's average income, the higher their level of discretionary income.

Contribution from the highest income segment has trended upward over the past five years due to rising discretionary income.

The second highest income quintile has remained static which is attributable to a growing trend of bargain hunting and increased competition from online retailers.

The three lowest quintiles have been experiencing a decrease in contribution to revenue marked by low wage growth and the increasing popularity of online marketplaces.

Going forward, the global trend of increasing income inequality will likely translate to further growth of the highest income quintile and consequently, increased industry demand from that group.

3.5 Competitive Environment

The industry experiences a moderate level of competition. Sources of competition are both internal and external to the industry. Internally, price-based competition remains the predominant form of competition between operators. Heavy discounting strategies over the past five years have caused industry profit margins to contract. While price is the main basis of internal competition, range and quality of products has a significant influence on consumer shopping patterns and ultimately on customer loyalty.

In respect of price, retailers range from those seeking to offer a value for money proposition to those offering premium products with matching price points. In respect of range, retailers vary between those offering a specialist range (i.e. only bedroom or sofas) to those covering a large and diversified product range such as department stores that stock a furniture range as well as a variety of other consumer products.

The figure below categorises Australian furniture retailers based on their strategies in respect of price and product range.

Figure 3: Competitive landscape

Source: Leadenhall Analysis

Of the Australian furniture retailers set out in the chart above, Super Amart is the most similar to Fantastic, in particular the Fantastic Furniture brand, in terms of value proposition and range (details of Fantastic's range of retail brands are included in Section 4.3). Super Amart offers a large range of home furnishing solutions, similar to the range offered by Fantastic Furniture, however their range tends to be less targeted towards current trends and more traditional in style, targeting an older demographic. Super Amart operates 50 stores across Australia which represents a smaller national footprint compared to Fantastic Furniture and the Fantastic group as a whole.

Ikea offers products at a similar price point to Fantastic Furniture, but has a much wider range which spans value for money towards mid-range in price and includes a wide range of homewares as well as kitchen and bathroom design offerings. Ikea also operates using a different business model based on large big box stores in a relatively small number of locations. Ikea, like Fantastic Furniture, targets the first homeowner market and those consumers looking for a large fashionable value for money range.

Most of the other retailers above tend towards the mid-range to premium market, targeting one off significant purchases rather than whole room purchases in a single transaction.

A brief description of the top five players in the industry, by market share, is set out in the table below:

Table 5: Major companies in the furniture retailing industry in Australia

Product	Market share	Description
Harvey Norman Holdings Ltd	17.4%	An Australian publicly listed company with furniture retailing operations including Harvey Norman, Domayne and Joyce Mayne. Harvey Norman has maintained market dominance due to its large network of stores and strong branding.
IKEA Pty Limited	9.6%	Owned by Ingka Holding Overseas BV (based in the Netherlands). IKEA will operate ten stores Australia-wide by the end of 2016 with plans to introduce 22 smaller-format stores and online pick-up points supported by a new multipurpose distribution centre slated for completion in March or April 2017.
BBQSAM Holdings Pty Ltd	9.2%	A privately held holding company formed through the merger of Super Amart and Barbeques Galore in 2012. BBQSAM operates over 50 stores in Australia with strong growth in market share over the past five years (albeit from a low base) following the launch of new stores in Western Australia, Queensland and South Australia from 2008 to 2010.
Fantastic Holdings Limited	4.6%	Fantastic's trading businesses include Fantastic Furniture, Plush, Le Cornu (only two stores, one of which is in the process of being closed), and Original Mattress Factory.
Steinhoff Asia Pacific Holdings Pty Ltd	4.1%	Commonly known as Freedom Group and part of the Steinhoff International Group. Steinhoff's brands include Freedom Australia, Freedom New Zealand and Snooze.

Source: IBISWorld

The sector exhibits a moderate level of market share concentration with the four largest players making up over 40% of total industry revenue according to IBISWorld. The remainder of the industry is characterised by low market share concentration and a large number of smaller operators.

The past five years has seen the rationalisation of smaller players as shrinking profit margins forced the exit of less profitable players from the industry and increased merger and acquisition activity as the competition for market share intensified.

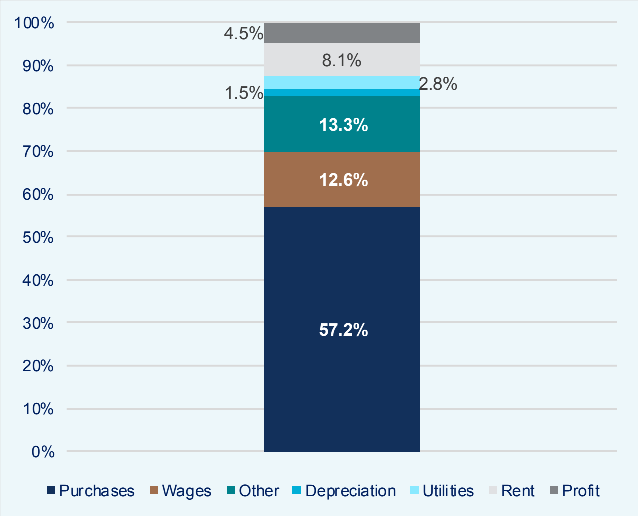
Furniture retailers have also been experiencing increased external competition from department stores and online retailers which has contributed to further price deflation in the industry. Department stores have been making forays into the furniture market by offering a growing range of furniture products. Pure-play online retailers, on the other hand, tend to be more of a threat to industry players at the lower end of the market as mid-range and premium operators generally offer products which have some degree of luxury or customisation associated with them.

The industry is considered to have low barriers to entry, particularly at the lower end, given the low level of capital investment required and the low rate of technology change. However, barriers are expected to increase over the next five years due to the increasingly competitive nature of the industry and its well-established players.

3.6 Industry Cost Structure

Figure 4 below analyses the benchmark cost structure of the industry.

Figure 4: Cost structure (FY17)



Source: IBISWorld

Purchases make up the largest component of industry expenses. Retailers typically purchase their stock from wholesalers or manufacturers.

Over the past five years, purchase costs have decreased as a percentage of industry revenue with a higher proportion of stock being sourced from low-cost countries. This was further supported by a strong Australian dollar between 2011 and 2013.

With the majority of industry imports being sourced from China, purchase costs are expected to decrease further in the short term following continued devaluation of the renminbi over the past two years.

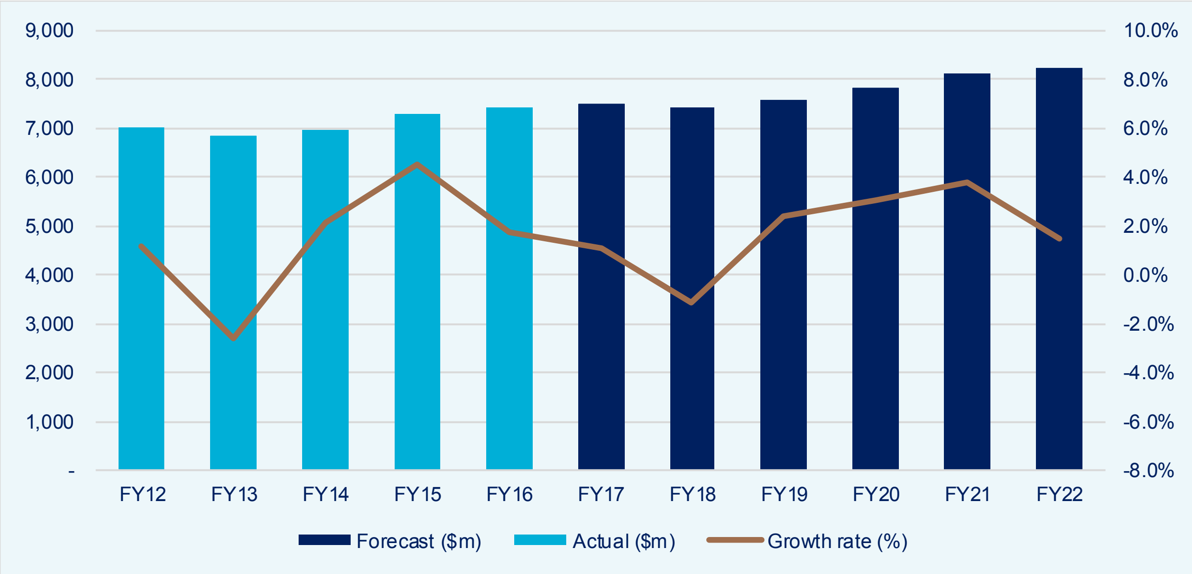
Other key items to note about the cost structure of the industry over the past five years include:

- A general decline in wages as a percentage of industry revenue due to decreasing levels of employment in the industry. This decline was partly offset by a rise in average wages attributable to the introduction of the General Retail Industry Award in 2010
- An increase in IT wage and IT outsourcing costs incurred by industry operators in order to establish and expand their online presence
- Additional advertising / marketing expenditure due to the increased role of advertising in reaching consumers and maintaining competitiveness

3.7 Industry Outlook

Figure 5 below illustrates historical and forecast industry revenue and growth from FY12 to FY22.

Figure 5: Industry revenue and growth



Source: IBISWorld

The following factors are expected to affect industry growth and profitability over the next five years:

- Continuing growth of household discretionary income and increasing housing demand will contribute to industry revenue
- Current historic low interest rates and a recovering economy are both likely to support increased consumer spending in the medium term
- Price is expected to continue to be the main aspect of competition and existing levels of price-based competition will continue to hinder industry profitability
- External competition from department stores and online-only retailers will continue placing downward pressure on industry profit margins
- Retailers in the lower end of the market are expected to be increasingly vulnerable to online retailers and used furniture sales through online marketplaces such as eBay and Gumtree
- Bricks-and-mortar retailers are expected to implement online business models to supplement their existing businesses in order to prevent further erosion of their customer base
- Product design in line with industry trends and store layout will remain crucial along with quality and range of products
- The mature nature of the industry suggests that further consolidation is likely with smaller enterprises being acquired by larger operators

Based on the above factors, in the medium term, the industry is likely to favour larger operators who exhibit greater capacity to control costs and maintain profit margins. However, these retailers, particularly those operating in the value for money segment, will need to focus on developing a clear online strategy as well as easy to use e-commerce offerings in order to address the growing threat of pure online furniture retailers.

4 PROFILE OF FANTASTIC

4.1 Introduction

Fantastic is a leading Australian furniture retailer and manufacturer. Fantastic operates more than 125 stores across the four brands of Fantastic Furniture, Plush, Original Mattress Factory and Le Cornu.

Fantastic is also Australia's largest lounge manufacturer, with its factory able to produce 160,000 lounges each year. In addition, Royal Comfort Bedding, Fantastic's mattress manufacturing operation, has the capacity to produce over 125,000 mattresses each year. Fantastic also operates a manufacturing plant in Vietnam and has a 60% interest in a sofa manufacturing joint venture in China.

4.2 History

A brief history of Fantastic is set out in the table below:

Table 6: History of Fantastic

Year	Event
1989	Business established by Paul Harding and Jonathan De Jong selling plastic garden furniture at Sydney's Parklea Markets.
1991	The first Fantastic Furniture store was opened at Birkenhead Point, NSW.
1992	The Fantastic Lounge Factory was opened and commenced production of lounges for the Fantastic Furniture stores.
1995	The Fantastic Metal Factory was opened and it began producing sturdy metal furniture at competitive prices.
1996	Due to pressures created by rapid growth, the business was placed into Administration. The business was subsequently acquired by Peter Brennan, Peter Draper and Julian Tertini. Over the next few years, the company embarked on a sustainable growth plan.
1999	Fantastic Furniture distributed its first retail catalogue to over 1 million households. Fantastic Holdings Limited listed on the ASX.
2000	Fantastic launched Plush, a lounge specialist retail brand, offering high quality lounges at affordable prices. Fantastic Furniture expanded into Victoria.
2006	Fantastic launched Original Mattress Factory, a mattress specialist offering factory direct prices on a large range of mattresses. In the same year, Fantastic expanded its manufacturing capabilities by acquiring Royal Comfort Bedding, a NSW mattress manufacturer.
2008	Fantastic acquired Dare Gallery, a retail chain offering a range of home furnishings and LeCornu, a South Australian furniture retailer. Fantastic becomes Australia's largest vertically integrated furniture company.
2012	Fantastic Manufacturing, a purpose built manufacturing facility in Vietnam, was established. Fantastic Manufacturing can produce more than 200,000 units per year.
2015	The Dare Gallery business was sold and manufacturing commenced in the Chinese joint venture facility.
2016	Announced the closure of the Le Cornu store and conversion of the Ashley store in South Australia.

Source: Fantastic

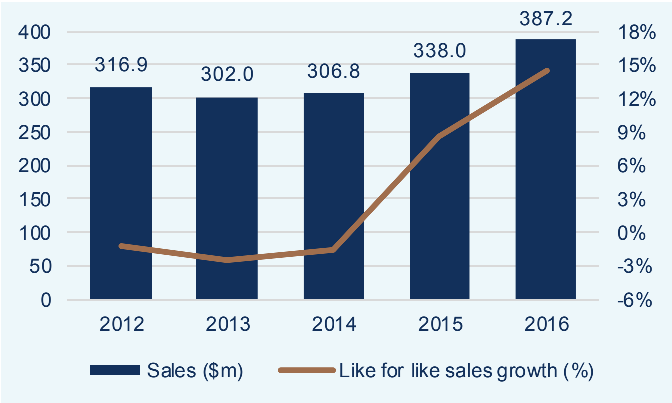
4.3 Retail Brands

Fantastic Furniture

Fantastic Furniture operates over 70 stores, plus two franchised stores, throughout Australia and employs approximately 700 people in their retail operations. Fantastic Furniture focuses on value for money by providing stylish affordable furniture to the Australian market. Fantastic Furniture has a large product range that spans all aspects of household furniture and includes a range of package deals tailored to consumers who are looking to fill a room at an affordable price without compromising quality. First home owners are therefore a key target segment for the business.

Fantastic Furniture has experienced strong sales growth over the last two years as set out in the graph below:

Figure 6: Fantastic Furniture sales ($m) 2012 to 2016



Sales dipped in 2013, with little growth in 2014, predominantly due to an adverse macroeconomic environment (economic weakness and low consumer confidence), increasing competition and a lower exchange rate placing pressure on pricing.

Sales increased in 2015 and 2016 due to strategic initiatives aimed at enhancing the product offering, improving customer service, engaging the workforce and investing in more effective marketing solutions.

Source: Fantastic

Longer term, management expect that there is potential to grow the Fantastic Furniture network to 100 stores in Australia. In FY17 four to six new stores are planned and an additional 14 existing stores will be refurbished. In addition, Fantastic Furniture now has a fully operational e-commerce platform and has experienced strong growth in online sales (the online channel is now the largest store in the network). Further innovation is anticipated to continue to grow the online sales channel.

Beyond FY17 additional growth is expected to be underpinned by:

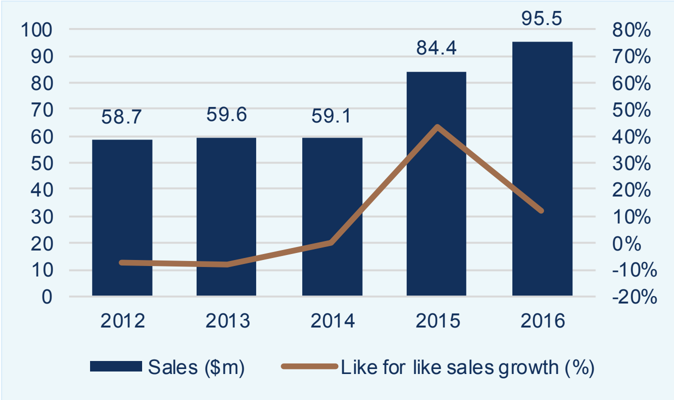
- Improved margins through new product innovations and supply chain efficiency and productivity
- Refurbishment of stores to improve the customer experience and like for like sales
- Further investment in e-commerce to drive sales growth
- New store growth in potential new territories and markets

Plush

Plush is a specialist sofa retailer which operates 35 stores across the east coast of Australia and South Australia. In 2000 Plush opened its first store in Victoria which specialised in affordable designer leather sofas imported from Italy and Asia. In 2004 Plush expanded its range to include fabric sofa options. Plush strives to create high quality, hand-crafted sofas that are designed for comfort and built to last. The Plush sofa range includes over 100,000 sofa combinations and each sofa comes with a ten year warranty.

Although smaller than Fantastic Furniture, Plush generates significant revenue as illustrated in the graph below:

Figure 7: Plush sales ($m) 2012 to 2016



Sales were static between 2012 and 2014 predominantly due to an adverse macroeconomic environment (economic weakness and low consumer confidence), increasing competition, a lower exchange rate and discounting required to clear excess inventory.

Sales increased in 2015 and 2016 due to strategic initiatives aimed at enhancing the product offering, improving customer service, engaging the workforce and investing in more effective marketing solutions.

Source: Fantastic

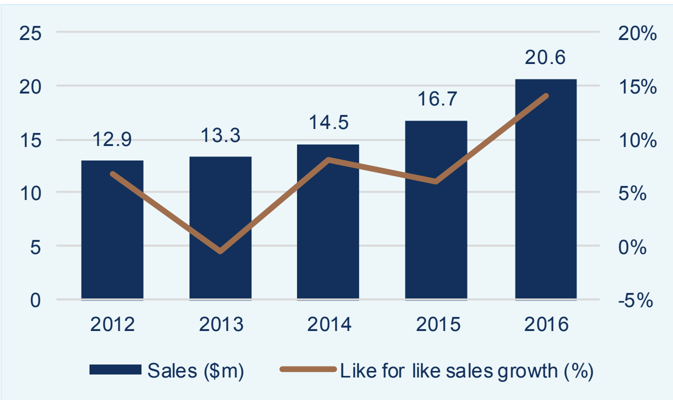
Longer term, management expect that there is potential to grow the Plush network to 60 stores in Australia, with four new showrooms planned for FY17. Sales will also benefit from the Plush e-commerce platform which was launched in August 2016. Other growth initiatives include trialling two new concept showrooms and a continued focus on improving the product offering and customer experience.

Original Mattress Factory

Original Mattress Factory was established in 2006 and operates 18 stores across NSW and the ACT. It is a specialist mattress retailer and unlike other retailers does not sell other bedroom furniture and accessories. Original Mattress Factory delivers a large range of mattresses at low prices and provides consumers with a five to ten year workmanship guarantee and a 100 night comfort guarantee.

Original Mattress Factory is a small but growing business in the Fantastic group as demonstrated in the graph below:

Figure 8: Original Mattress Factory sales ($m) 2012 to 2016



Sales were fairly flat between 2012 and 2014 predominantly due to an adverse macroeconomic environment (economic weakness and low consumer confidence), increasing competition and a lower exchange rate placing pressure on pricing.

Sales improved between 2014 and 2016 due to strategies targeting improved marketing messages, development of product mix and team engagement and training.

Source: Fantastic

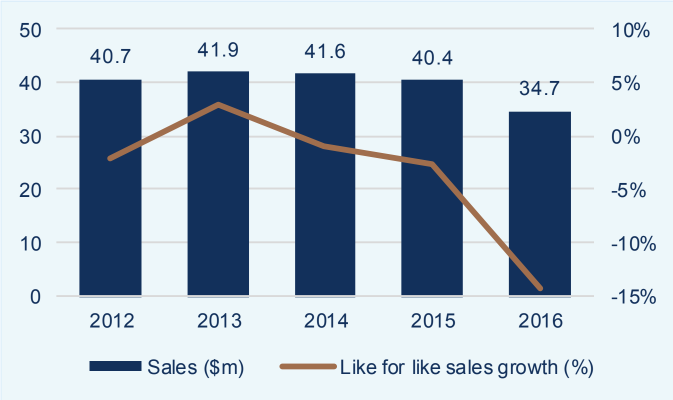
Longer term, management expect that there is potential to grow the Original Mattress Factory network to 90 stores, with rapid expansion planned for NSW and QLD in the medium term, with 6 new stores expected to open in FY17. In order to achieve this growth, management are focussing on:

- Continued product development with both local and overseas suppliers to deliver innovation and value
- Driving growth through e-commerce platforms
- Increased brand recognition in the market

Le Cornu

The Le Cornu brand and two stores (Adelaide and Darwin) were acquired by Fantastic in 2008. Le Cornu has a long history in South Australia with its origins dating back to 1861. The Le Cornu stores offer a large range of furniture options across the living, dining, bedroom, outdoor and office segments. Sales have been relatively flat since 2012 with a significant decline in 2016 as set out in the graph below.

Figure 9: Le Cornu sales ($m) 2012 to 2016



Source: Fantastic

Sales over the period have been negatively impacted by increased competition, including from Fantastic Furniture.

Despite the adoption of a recovery plan in the first half of FY16, sales continued to decline. This decline was mostly attributable to the Adelaide store which traded at a loss of approximately $4 million in FY16.

As a result of the poor trading performance of the Adelaide store and the proposed sale of the existing leased premises, Fantastic have decided to undertake an orderly wind down of this store over the first half of FY17. This will result in some one off costs, including redundancies. The Darwin store will continue to operate under the Le Cornu name with a hybrid product offering, by introducing Fantastic Furniture product lines to the Northern Territory for the first time.

Ashley Furniture Homestore

Fantastic opened an Ashley Furniture Homestore in Gepps Crossing South Australia in FY15 as a trial of their new partnership arrangement with Ashley Homestores Ltd, an American furniture and homewares company. The Ashley store has been loss making since inception and as such management have decided to transition the Ashley Furniture Homestore to a Fantastic Furniture store in the second half of 2016.

4.4 Manufacturing Operations

Fantastic owns three manufacturing facilities (two in Australia and one in Vietnam) and also has a 60% interest in a Chinese joint venture manufacturing facility. Most of the manufacturing output is sold directly through Fantastic's retail brands with an additional $2 million of sales, largely to two franchised stores, in FY15 and FY16. In FY16, the manufacturing operations focussed on adopting world's best practice, introducing Lean Six Sigma approaches with internal teams in all factories, examining every point of the manufacturing process to improve efficiencies. A brief overview of each of the manufacturing facilities is provided below.

Fantastic Lounge Factory

Fantastic Lounge Factory is Australia's largest lounge manufacturer with over 150 employees and the capacity to produce over 155,000 lounges each year. In FY16 over 130,000 sofas were manufactured by the Fantastic Lounge Factory and it has the ability to rapidly increase production to meet Fantastic's growth plans. The Fantastic Lounge Factory provides Fantastic Furniture customers with the ability to customise their furniture sofa and bedhead choices with over 100 fabric choices on offer. Products are manufactured exclusively for Fantastic Furniture and the factory currently produces over 40 different models in its 15,000m^2 purpose built facility at Fairfield East in NSW. The factory dispatches over 4,000 trucks per year to Fantastic Furniture stores all over Australia.

Royal Comfort Bedding

Royal Comfort Bedding was acquired by Fantastic in 2006 and produces an exclusive range of Australian made mattresses for Fantastic Furniture. Since acquisition, Royal Comfort Bedding has grown significantly from producing 200 mattresses per day in 2006 to manufacturing 11 different mattress models with a capacity of 500 mattresses per day currently. Royal Comfort Bedding supplies Fantastic Furniture with 100% of their mattress range. The Royal Comfort Bedding factory will be relocating to a new state of the art factory in Sydney's Western suburbs late in 2017. This factory is expected to provide future efficiency benefits and a reduced environmental footprint.

Fantastic Manufacturing Vietnam

Fantastic opened its first purpose built manufacturing facility in Vietnam in 2012. In 2016 a new 10,000 m^2 manufacturing facility was built and is now fully operational. The Vietnam factory produces steel beds and metal components for the Australian manufacturing facilities. Fantastic Manufacturing Vietnam employs over 70 people and can produce more than 200,000 units per year. The new factory has the ability to produce a complete range of metal furniture for the global market and recently displayed products at a trade show in Vietnam. In the future it is expected that Fantastic Manufacturing Vietnam will continue to supply the Australian Fantastic brands as well as other global customers.

China Joint Venture

Fantastic has a 60% interest in Fantastic International Manufacturing – FIM Limited, a company domiciled in Hong Kong which owns Fantastic International Manufacturing Jiangsu Co. Ltd, domiciled in China. The joint venture is located in Changzhou, China and is involved in the manufacture of household furniture. The joint venture manufacturing facility was completed in FY14 (production commencing FY15) and supplies sofas and upholstered beds direct to Fantastic retail stores and is also pursuing opportunities to sell to external retailers. The 40,000 m^2 facility is focused on manufacturing entry level sofa products and is currently producing around 400 sofas a day with a capacity to produce around 1,000 sofas per day with incremental cost as minimal additional capital expenditure would be required.

4.5 Property

Fantastic owns the sites for two of its retail stores, as set out below:

- 978 Hunter Street, Newcastle West, NSW
- 143 Gladstone Road, Allenstown, QLD

The Newcastle store site holds development potential for the future with significant development activity currently occurring in the area. The Rockhampton store currently only occupies half of the land area. Based on negotiations with prospective purchasers, the other half of the land is expected to be realised for approximately $1 million net of tax.

In addition, Fantastic previously owned a property in Dandenong, Victoria which was sold in 2015 for $26 million. The gain on the sale was approximately $0.6 million.

4.6 Directors and Senior Management

The key management personnel of Fantastic include:

Table 7: Senior management

Key Personnel	Experience
Debra Singh **Group CEO Retail**	Prior to appointment as Group CEO in March 2016, Ms Singh held roles as the CEO of Fantastic Furniture and Chief Operating Officer of Fantastic. Ms Singh has over 30 years of experience in retail operations, organisational design, human resources and change management.
Brian Cassell **CFO and Company Secretary**	Mr Cassell was appointed interim CFO of Fantastic in February 2016. Subsequently in August 2016, Mr Cassell accepted a permanent role as CFO of Fantastic. Mr Cassell has more than 20 years' experience as a public company CFO, having previously held this position with Rural Press Limited and Fairfax Media Limited. He was previously an Audit Partner at KPMG.
Jason Newman **CEO Manufacturing**	Mr Newman has over 20 years of furniture manufacturing and leadership experience with particular emphasis in bedding, upholstery and metal manufacturing. Mr Newman started with Fantastic in 2007 as General Manager Royal Comfort Bedding. He was appointed CEO Fantastic Manufacturing in 2016 and currently oversees the operation of Fantastic's furniture factories.
Bill Keighran **General Manager Original Mattress Factory**	Mr Keighran has been a senior executive with Fantastic for 15 years, involved in the development and growth of both the Fantastic Furniture and Plush retail brands. Previously Mr Keighran was retail CEO of The Galore group and a founding Director of the Freedom Furniture group. Mr Keighran has over 30 years' of retail experience with a focus on business start-ups and retail brand development, along with extensive business experience in South East Asia.
Chris Burke **General Manager Plush**	Mr Burke has over 25 years' experience in retail, property management and fashion, holding CEO, Country Manager and General Manager positions. After joining Marks & Spencer as a graduate, he worked in Habitat for over 10 years during which time he established profitable businesses in Europe and Asia. He joined the Fantastic, leading the turnaround of Dare Gallery and moving to Plush Sofas in 2013.
Melissa Blackley **Group Chief People Officer**	Ms Blackley joined Fantastic in May 2016 and has an extensive background in leading human resources for large companies in a diverse range of industries. She has headed global HR functions for a number of ASX listed organisations and worked in Asia, New Zealand and the United States.

Source: Fantastic

The Board of Directors of Fantastic comprises:

Table 8: Directors

Directors	Experience
Julian Tertini **Non-executive Director**	Mr Tertini has over 30 years' experience in the retail industry and was a founding shareholder and Executive Director responsible for retail operations and product development for Freedom Furniture. Mr Tertini has served on a number of private company boards in the retail, hospitality and broadcasting industries.
Peter Brennan **Non-executive Director**	Mr Brennan is a Fellow of the Institute of Chartered Accountants in Ireland and an Associate of the Institute of Chartered Accountants in Australia with over 35 years' experience in accountancy. He spent ten years in the banking and finance sector and held a number of senior management positions with St George Bank Limited.
Geoffrey Squires **Independent Non-executive Director**	Mr Squires has over 40 years' experience in the building and construction industry. He spent 24 years with Monier Limited and was the General Manager – Roofing division from 1986 to 1994. Mr Squires currently serves on a number of private company boards in the building and shipping industries.
John Hughes **Independent Non-executive Director**	Mr Hughes has over 40 years' business experience. An experienced Senior Executive and Director, Mr Hughes led Thorn Group Limited as CEO/MD through a significant business expansion and profit growth following its IPO in 2006 before retiring from Thorn in 2014. Previously, he was CEO/MD of Ruralco Limited and led the company through ten years of growth and diversification.
Robyn Watts **Independent Non-executive Director**	Ms Watts has over 27 years' experience as CEO of various businesses, most recently as CEO of ABC Enterprises and was previously CEO of Southern Star Sales. Ms Watts brings specialist skills and knowledge in the areas of business strategy and marketing. Ms Watts is currently a director of publicly listed The Vita Group and is also a director of private company Geyer as well as the Australian School of the Performing Arts.

Source: Fantastic

4.7 Financial Performance

The audited statements of financial performance for the three years ended 30 June 2014, 2015 and 2016 are set out in the table below.

Table 9: Financial performance

$'000	FY14	FY15	FY16
Sales	447,772	496,921	543,700
Cost of sales	(245,352)	(274,624)	(305,822)
Gross profit	**202,420**	**222,297**	**237,878**
Other income	4,812	3,961	2,634
Expenses			
Employment expenses	(76,614)	(87,062)	(91,436)
Property expenses	(57,719)	(58,600)	(58,411)
Marketing expenses	(33,299)	(34,885)	(36,534)
Sales related expenses	(5,581)	(5,908)	(8,715)
Other expenses	(14,145)	(12,877)	(21,895)
Share of loss of joint venture	-	(865)	(371)
Total expenses	**(187,358)**	**(200,197)**	**(217,362)**
EBITDA	**19,874**	**26,061**	**23,150**
Depreciation	(9,423)	(5,775)	(5,552)
EBITA	**10,451**	**20,286**	**17,598**
Amortisation	(1,777)	(1,250)	(1,364)
EBIT	**8,674**	**19,036**	**16,234**
Financial income	120	364	584
Financial expense	(434)	(124)	(153)
Net profit before tax	**8,360**	**19,276**	**16,665**
Income tax expense	(2,572)	(6,072)	(5,228)
Net profit after tax	**5,788**	**13,204**	**11,437**
Other comprehensive income	(330)	2,374	(1,526)
Total comprehensive income net of tax	**5,458**	**15,578**	**9,911**
Margins			
Gross margin %	*45.2%*	*44.7%*	*43.8%*
EBITDA margin %	*4.4%*	*5.2%*	*4.3%*
EBITA margin %	*2.3%*	*4.1%*	*3.2%*
EBIT margin %	*1.9%*	*3.8%*	*3.0%*
Expenses / sales	*41.8%*	*40.3%*	*40.0%*

Source: Fantastic

Note: the audited financial statements include some depreciation which is allocated to cost of sales and other income. We have grossed up these items for the allocated depreciation and included all depreciation as a single line item

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

- There has been strong sales growth across the three years, despite the sale of the Dare Gallery business in FY15. This growth is due to delivering on key initiatives including creating a stronger customer value proposition, developing e-commerce solutions, strengthening of product mix and improved workforce engagement
- Gross margin contracted by approximately 1% in FY16 due to the sale of the higher margin Dare business, the decline in the Le Cornu and Ashley businesses and the weakening Australia dollar

- Other income predominantly relates to franchise fees and property income. FY15 also includes $1.2 million in relation to the gain on the sale of the Dare business. In the statutory accounts other income is presented net of applicable depreciation. In order to determine an accurate EBITDA figure, we have grossed up other income for depreciation
- Total expenses as a percentage of sales declined over the period reflecting productivity gains and efficiency on utilisation of fixed costs. This overhead efficiency has also resulted in an increasing EBITDA margin over the period
- Depreciation was higher in FY14 because of the full year impact of Dare (sold in FY15) and non-recurring asset write offs of $3.8 million
- Other comprehensive income predominantly relates to exchange differences on translation of foreign operations and gains/losses on cash flow hedges net of any income tax effect

4.8 Financial Position

The audited statements of financial position as at 30 June 2014, 2015 and 2016 are set out in the table below.

Table 10: Financial position

$'000	FY14	FY15	FY16
Current assets			
Cash and cash equivalents	21,127	36,721	31,863
Trade and other receivables	9,304	4,630	5,796
Other financial assets	-	2,011	-
Inventories	81,278	90,544	93,326
Total current assets	**111,709**	**133,906**	**130,985**
Non-current assets			
Investments	24,423	3,712	-
Property, plant & equipment	30,275	27,115	28,833
Investment in joint venture	-	5,644	5,463
Intangible assets	8,069	7,772	6,760
Deferred tax assets	7,564	8,984	12,527
Other non-current assets	49	-	3
Total non-current assets	**70,380**	**53,227**	**53,586**
Total assets	**182,089**	**187,133**	**184,571**
Current liabilities			
Trade and other payables	(35,726)	(38,415)	(39,737)
Interest bearing loans	-	(5,000)	-
Current tax payable	-	(4,000)	(3,196)
Employee benefits	(13,499)	(20,263)	(19,171)
Provisions	(1,454)	(1,688)	(7,736)
Total current liabilities	**(50,679)**	**(69,366)**	**(69,840)**
Non-current liabilities			
Interest bearing loans	(15,000)	-	-
Employee benefits	(1,581)	(1,952)	(2,225)
Provisions	(2,518)	(3,564)	(3,165)
Deferred tax liabilities	(1,742)	(2,335)	(1,905)
Total non-current liabilities	**(20,841)**	**(7,851)**	**(7,295)**
Total liabilities	**(71,520)**	**(77,217)**	**(77,135)**
Net assets	**110,569**	**109,916**	**107,436**

Source: Fantastic

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

- The increase in cash in FY15 was due to the sale of the Dare business and the Dandenong property
- Trade and other receivables relate to external and related party (franchisees) trade receivables of approximately $1.4 million in FY16 and other receivables predominantly comprising of various prepayments relating to workers compensation premiums, deposits placed with suppliers and marketing prepayments
- Other financial assets in FY15 relate to forward exchange contracts for the purposes of cash flow hedging

- Inventory increased in FY15 and FY16 due to the implementation of the 'Always in store' position and the impact of the decline in the Australian dollar against the US dollar
- In FY14 and FY15, investments relate to two properties owned by Fantastic (Dandenong and Rockhampton Store). The decline in FY15 was due to the sale of the Dandenong property. In FY16 the remaining property, the Rockhampton Store, was reclassified to property, plant and equipment. The Newcastle Store has always been included in property plant and equipment
- Property, plant & equipment predominantly relates to store fit outs as well as fit-outs and machinery in the distribution centres and factories
- The investment in joint venture balance relates to the investment in the Chinese production facility. The movement between FY15 and FY16 relates to Fantastic's share of the joint venture loss which is offset to some extent by currency gains
- Intangible assets relate to goodwill, $2.6 million as at 30 June 2016, and software, $4.1 million as at 30 June 2016
- $10 million of borrowings was repaid in FY15 from the proceeds of the sale of the Dandenong property. The remaining $5 million was repaid in FY16 from surplus cash
- The increase in provisions in FY16 predominantly related to $4.1 million provided for the closure of the Le Cornu store in South Australia and an increase in the product warranty provision of $1.4 million due to an internal management decision to make provisions in light of extended warranties being offered on product sales

4.9 Cash Flow

The audited statements of cash flows for the three years ended 30 June 2014, 2015 and 2016 are set out in the table below.

Table 11: Cash flow

$'000	FY14	FY15	FY16
Cash flows from operating activities			
Receipts from customers	504,683	552,464	600,888
Payments to suppliers and employees	(484,978)	(527,850)	(571,851)
Interest received	120	364	584
Interest paid	(434)	(124)	(83)
Income tax paid	(7,667)	(541)	(9,329)
Net cash from operating activities	**11,724**	**24,313**	**20,209**
Cash flows from investing activities			
Acquisition of property, plant and equipment	(7,490)	(4,950)	(6,152)
Sale of property, plant and equipment	12,056	-	106
Sale of investments	-	26,811	-
Payment for investments	(487)	(1,712)	-
Payment for intangibles	(310)	(1,328)	(1,682)
Deconsolidation of China subsidiary	-	(4,142)	-
Net cash from investing activities	**3,769**	**14,679**	**(7,728)**
Cash flows from financing activities			
Repayment of external borrowings	(10,324)	(10,000)	(5,000)
Proceeds from issuance of shares	3,150	-	-
Dividends paid	(6,184)	(13,418)	(12,391)
Net cash from financing activities	**(13,358)**	**(23,418)**	**(17,391)**
Opening cash	**18,993**	**21,127**	**36,721**
Net cash flows	2,135	15,574	(4,910)
Foreign exchange difference	(1)	20	52
Closing cash	**21,127**	**36,721**	**31,863**

Source: Fantastic

In relation to the historical cash flows of Fantastic we note the following:

- The increase in receipts from customers and payments to suppliers and employees is consistent with the growth in sales across FY15 and FY16
- Income tax paid in FY15 was low due to the receipt of a tax refund relating to FY14 and a $4 million increase in the balance of current tax payable in FY15
- The $12 million inflow from sale of property, plant and equipment in FY14 reflects the sale of the Campbelltown property
- The $26 million inflow from sale of investments in FY15 reflect the sale of the Dandenong property
- Proceeds from the sale of properties have been applied toward reducing external borrowings

4.10 Outlook for Fantastic

We have reviewed detailed FY17 budgets for each of the Fantastic brands. We are unable to disclose the details of these budgets due to their commercially sensitive nature. However, we have discussed the budgets with management to obtain an understanding of the budgeting process and the strategies in place to facilitate the achievement of FY17 budgets. The key strategies driving growth expectations are:

- Store network expansion and continued investment in refurbishment of existing store network
- Continued focus on supply chain efficiency and overhead recovery through increasing output for manufacturing facilities for both internal and external sales
- Further investment in e-commerce to drive sales growth
- Investment in staff training to maximise conversion rates and revenue per customer
- Closure of the underperforming Le Cornu in Adelaide and transition of the Ashley store to Fantastic Furniture

Year to date actual performance for the months of July and August at a group level has been in line with budget. At an individual brand level, the following events have impacted performance:

- A key supplier of mattresses for the Original Mattress Factory went into liquidation. This affected availability of supply and subsequently sales. Normal supply levels are now being restored and there is not expected to be any long lasting effect on sales
- Plush has experienced a strong start to the year which has resulted in a large order book that is expected to be converted to sales in the coming months as revenue is recognised on delivery
- New store growth is on target with several potential new sites having been identified and lease negotiations underway
- External sales from the factories in Vietnam and China are gaining momentum

4.11 Capital Structure

As at 5 October 2016, Fantastic had a total of 103,257,398 ordinary shares on issue. The top 10 beneficial owners accounted for around 90.3% of the ordinary shares on issues. A summary of the top 10 shareholders and their holdings is set out in the table below:

Table 12: Top 10 shareholders

Rank	Investor	Number of shares	% of issued capital
1	Tertini, Julian[1]	41,776,211	40.5%
2	RBC Investor Services Australia	11,828,985	11.5%
3	HSBC Custody Nominees	11,100,757	10.8%
4	Brennan, Peter[2]	10,698,016	10.4%
5	J P Morgan Nominees Australia	7,032,619	6.8%
6	Citicorp Nominees	3,602,062	3.5%
7	BNP Paribas	2,455,363	2.4%
8	National Nominees	2,078,221	2.0%
9	Trinity Management	1,806,148	1.7%
10	Norman Role	900,000	0.9%
	Total	**93,278,382**	**90.3%**

Source: Fantastic

Note:

1. The total includes 10,000,000 shares held by Yaquina Pty Limited and 934,137 shares held by Lawncat Pty Ltd over which Mr Tertini has voting power.

2. The total includes 3,989,965 shares held by Mrs Patricia Brennan over which Mr Brennan has voting power.

4.12 Share Price Performance

The following chart shows the share market trading of Fantastic shares for the past five years:

Figure 10: Fantastic share price performance

Source: FactSet

We note the following in relation to the share price of Fantastic in the five years to 7 October 2016:

- The share price rose significantly between mid-2012 and February 2013 on the back of solid profit growth under difficult trading conditions, a turnaround in the Dare Gallery business and an increase in the dividend paid compared to the prior year
- On 20 May 2013, Fantastic released an updated profit guidance for FY13 advising that previously reported NPAT targets would not be met. On the back of this announcement, the closing share price fell from $2.74 on 20 May 2013 to $1.87 on 21 May 2013, with 3.4 million shares sold on 21 May 2013
- The share price continued a gradual decline over FY14 due to limited growth and difficult trading conditions
- There was a steady increase in the share price over FY15 as sales growth picked up and a sale was finalised for the underperforming Dare Gallery business
- The share price dropped again in January 2016, from $2.10 on 6 January 2016 to $1.76 on 22 January 2016, after the announcement of the resignation of the CFO on 18 January 2016 and the CEO on 22 January 2016
- Since June 2016, the share price has risen by approximately 50% from around $2.00 to a high of $2.95 on 29 August 2016. This increase is likely due to the announcement of the closure of the underperforming Le Cornu store in Adelaide in July 2016 as well as positive financial results for FY16 which included a largely unexpected special dividend of $0.15 per share announced on 25 August 2016
- Since the ex-dividend date of 2 September 2016, the share price has trended downwards to sit at $2.33 at the end of trading on 7 October 2016

5 VALUATION METHODOLOGY

5.1 Available Valuation Methodologies

To estimate the fair market value of Fantastic 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 ("DCF") method
- The capitalisation of future maintainable earnings ("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 is applied, at least as a secondary cross-check to a primary method. The choice of methods depends on 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.

5.2 Selection of Valuation Methodology

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

- Fantastic is neither 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 likely to be the most appropriate
- There are some listed companies with similar businesses to Fantastic and a wide range of listed companies operating in comparable industries with similar profit drivers. We are also aware of a number of transactions involving similar companies. Thus we are able to apply the CFME approach
- Fantastic is a mature operating business. Given the mature nature of the business the use of the DCF method is unlikely to add value to our analysis
- Fantastic shares are publicly traded on the ASX in an informed and fairly liquid market. This allows an analysis of share market trading to be undertaken
- We are not aware of any industry specific valuation methodologies appropriate to Fantastic

Accordingly, we are of the opinion that the most appropriate methodology to value Fantastic is the CFME method with an analysis of share market trading considered as a cross-check.

6 VALUATION OF FANTASTIC

6.1 Capitalisation of Future Maintainable Earnings

Determining the fair market value of Fantastic using the CFME approach requires consideration of the following factors:

- An appropriate earnings base for assessing maintainable earnings
- An appropriate level of maintainable earnings
- An appropriate earnings multiple
- The value of any net debt and non-operating assets and liabilities

These considerations are discussed in more detail below.

Bases of 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 are not expected to be profitable in the near term 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 typically a non-cash accounting entry that may 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 both EBITDA and 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 both EBITDA and EBIT is useful
- Third party forecasts of EBITA are not readily available making EBITA multiples difficult to calculate without making assumptions about ongoing levels of depreciation (i.e. most brokers do not separately forecast depreciation and amortisation)
- Fantastic has limited amortisation, the majority of which is related to software, which is likely to require ongoing capital expenditure, making EBITA multiples less reliable

Level of maintainable earnings

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 EBITDA and EBIT for Fantastic for FY15 and FY16:

Table 13: Normalised earnings FY15 and FY16

$'m	Notes	FY15	FY16
Unadjusted EBITDA		**26.1**	**23.2**
Dare Gallery trading	1	(1.0)	-
Dare Gallery gain on sale	2	(1.2)	-
Le Cornu trading	3	(0.7)	3.5
Le Cornu impairment	4	-	9.1
Ashley trading	5	0.6	0.8
Gain on sale of property	6	(0.5)	-
Normalisation of incentive scheme expense	7	0.6	(1.9)
One-off provisions	8	-	1.9
Adjusted EBITDA		**23.8**	**36.5**
Depreciation		(5.8)	(5.6)
Amortisation		(1.3)	(1.4)
EBIT		**16.8**	**29.6**
Depreciation and amortisation related to discontinued businesses	9	0.6	0.5
Adjusted EBIT		**17.4**	**30.1**

Source: Fantastic and Leadenhall analysis

Each of the adjustments are explained below:

1. Dare Gallery Trading

The Dare Gallery business was sold during FY15. The contribution from Dare Gallery to FY15 earnings has been removed in order to present the performance of the continuing business only.

2. Dare Gallery Gain on Sale

A gain was recognised in FY15 upon the sale of Dare Gallery. This has also been removed in order to reflect only the continuing businesses.

3. Le Cornu Trading

Fantastic are in the process of closing the Le Cornu store in Adelaide. The earnings or losses from this store have been removed in order to give a true reflection of the earnings generating by the continuing business.

4. Le Cornu impairment

The Le Cornu impairment charge recognised in FY16 related to the closure of the Adelaide store which is considered to be a one-off impairment expense. In order to represent the earnings of the continuing business we have removed the impact of this impairment expense.

5. Ashley Trading

Fantastic intend to transform the current Ashley store into a Fantastic Furniture store. The Fantastic Furniture store is expected to be a better fit for the local market and therefore the losses incurred by the Ashley store are not expected to continue. As such, the losses realised by Ashley have been removed in calculating the earnings of the continuing business.

6. Gain on sale of property

In FY15, Fantastic sold a property they owned in Dandenong Victoria which resulted in a recognition of a gain on the sale. As property sales are not part of Fantastic's core business activities, we have removed this gain when calculating the earnings of the continuing business.

7. Normalisation of incentive scheme expense

Fantastic periodically recognises expenses for non-cash incentives earned by employees under relevant incentive schemes. The valuation of these incentives in FY16 resulted in a reversal of part of the expenses recognised in previous years. As such we have normalised this expense by adjusting earnings in the relevant financial years to reflected the updated FY16 estimate of the total expense.

8. One-off provisions

A total expense of $1.9 million was recognised in FY16 relating to one-off provisions. This was predominantly related to an increased provision for warranty expenses in light of extended warranties being offered on product sales which is not expected to be incurred in the future.

9. Depreciation and amortisation related to discontinued businesses

In order to calculate earnings from the continuing business we have added back the depreciation and amortisation relating to the discontinued businesses of Dare Gallery and Le Cornu.

In addition to the above, we have had access to four broker reports which include forecast EBITDA and EBIT for FY17 and FY18. These broker forecasts are set out in the table below:

Table 14: Broker forecasts for Fantastic

$'m	Forecast date	EBITDA FY17	EBITDA FY18	EBIT FY17	EBIT FY18
Broker 1	25/08/2016	40.9	44.4	32.9	36.2
Broker 2	26/08/2016	36.4	38.6	29.4	31.2
Broker 3	26/08/2016	39.9	45.2	32.9	37.7
Broker 4	29/08/2016	37.0	40.0	30.0	33.0
Average		**38.6**	**42.1**	**31.3**	**34.5**

Source: various broker reports

The average growth expectations for FY17 amongst the brokers was 11.7% for EBITDA (high of 18.6% and low of 5.5%) and 10.2% for EBIT (high of 14% and low of 6%). The majority of the brokers still perceive some risk in the ability of the newly formed management team to continue to deliver on the growth initiatives introduced by the previous management team. These concerns are moderating due to the strong FY16 performance.

To date Fantastic has provided little guidance to the market regarding earnings expectations for FY17 other than their intention to open approximately 15 new stores. As such, the broker forecasts have been estimated with little information regarding Fantastic's earnings expectations for the future.

In addition to the broker forecasts we have been provided with the Fantastic Board approved budget for FY17 for the individual brands as well as the consolidated group. Fantastic is targeting earnings growth in excess of the broker forecasts for FY17. The FY17 forecast growth is driven by:

- Like for like store growth in excess of projected industry growth
- Margin improvement through new product innovations and working on efficiencies with suppliers
- Supply chain re-design to improve efficiency and productivity
- Further investment in e-commerce to drive sales growth
- Refurbishment of existing stores to improve customer experience
- The full year impact of new stores opened in FY16 (two Fantastic Furniture and two Plush)
- Opening of 15 new stores across the three brands

We perceive the following risks to achieving the FY17 budget:

- Ability to continue to deliver above market like for like growth
- There has been a history of closing underperforming stores which indicates that not all new stores are successful and that existing stores may become unprofitable in the future
- Increasing competition in the value for money market, particularly from emerging online players like Temple and Webster, may erode any margin gains expected from supply chain and efficiency initiatives
- The new store roll out targets may not be achieved. In particular, sites have not yet been secured for a number of the potential new stores
- The factories in Vietnam and China may continue to underperform, unless new external customers can be found
- A number of key management personnel are new in their roles which may cause some disruption in the short term
- Macroeconomic risks including the potential for a slowdown in residential construction

From discussions with management we understand year to date performance has been in line with budget for most of the business units. Budgeted EBIT at a group level has been negatively impacted by continuing losses from the Le Cornu store as well as supply disruptions at Original Mattress Factory (due to insolvency of a key supplier). The Le Cornu full year impact is expected to be break even after consideration of September and October trading and the write-back of some non-recurring provisions. In addition, the growth planned in the FY17 budget is heavily back ended with most of the new store openings and other strategic initiatives expected to be achieved in the second half of the year.

After considering the broker forecasts and the Fantastic FY17 budget, including conducting a high level sensitivity analysis, we have selected the following maintainable earnings:

Table 15: Selected maintainable earnings

	EBITDA		EBIT	
	Low	High	Low	High
Selected maintainable earnings	43.5	45.0	36.0	37.5

Source: Leadenhall analysis

We note that assuming same store growth of 5%, this implies EBIT growth from the full year impact of stores opened in FY16, new stores opened in FY17 and other FY17 strategic initiatives of $4.3 million to $5.8 million which we do not consider to be unreasonable.

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:

- Using the guideline public company method, market multiples are derived from 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
- The merger and acquisition method uses multiples 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 based on an appropriate discount rate and growth expectations

We have conducted an analysis of both public company trading multiples and transaction multiples in order to determine an appropriate earnings multiple to apply to the valuation of Fantastic.

In respect of public company trading multiples, there are limited companies listed on the ASX that are directly comparable to Fantastic. The most comparable Australian listed companies are:

- Harvey Norman Holdings Limited
- Nick Scali Limited

We note that Fantastic management also consider these to be comparable to Fantastic and monitor their performance.

There are also a number of listed Australian companies that operate retail (consumer discretionary) businesses that have similar profit drivers to Fantastic. From these companies, we have selected those that we consider to be most comparable and/or of a similar size to Fantastic. Although, Australian companies are the most comparable as they operate in the same market as Fantastic, we have also considered listed furniture retailers in other developed markets.

The following table sets out the historical and forecast trading EBITDA and EBIT multiples for the following three subsections of comparable companies:

- **Australian furniture retailers:** Australian companies where a significant portion of revenue is derived from furniture sales
- **Other Australian consumer discretionary retailers:** Australian companies that operate consumer discretionary retail businesses that are of a similar size or have similar drivers to Fantastic
- **Overseas furniture retailers:** Overseas companies where the majority of revenue is derived from furniture sales

We have also presented an adjusted average and median which modifies the calculated average and median to exclude outliers.

Table 16: Trading multiples of comparable companies

Company	Market cap ($m)	EBITDA multiple Historical	EBITDA multiple Current	EBITDA multiple Forecast	EBIT multiple Historical	EBIT multiple Current	EBIT multiple Forecast
Australian furniture retailers							
Harvey Norman	5,685	10.6x	9.7x	9.4x	12.2x	11.2x	10.8x
Nick Scali	465	11.1x	10.2x	9.1x	12.0x	11.0x	9.9x
Fantastic Holdings	279	7.0x	6.3x	5.8x	8.6x	7.7x	7.1x
Average		**9.6x**	**8.7x**	**8.1x**	**11.0x**	**10.0x**	**9.3x**
Median		**10.6x**	**9.7x**	**9.1x**	**12.0x**	**11.0x**	**9.9x**
Other Australian consumer discretionary retailers							
JB Hi-Fi	3,320	11.4x	10.1x	9.5x	13.6x	12.9x	12.2x
Myer	1,055	5.5x	5.4x	5.1x	10.1x	9.4x	8.6x
RCG Corporation	931	13.6x	9.1x	7.7x	16.6x	11.4x	9.4x
Michael Hill	663	10.8x	9.3x	8.4x	15.1x	12.8x	11.5x
Helloworld	487	10.4x	5.3x	4.6x	38.1x	8.6x	6.7x
Kathmandu	382	6.8x	6.4x	5.9x	8.7x	8.2x	7.6x
Adairs	375	9.6x	8.3x	7.3x	10.8x	9.6x	8.5x
Baby Bunting	374	18.7x	14.7x	12.1x	22.5x	17.5x	14.3x
Beacon Lighting	365	12.7x	11.7x	10.5x	13.9x	12.6x	11.2x
Billabong	216	7.1x	6.0x	5.0x	16.0x	10.9x	7.9x
Specialty Fashion	104	4.7x	3.4x	3.1x	33.6x	8.3x	6.5x
Average		**10.1x**	**8.2x**	**7.2x**	**18.1x**	**11.1x**	**9.5x**
Median		**10.4x**	**8.3x**	**7.3x**	**15.1x**	**10.9x**	**8.6x**
Average excluding outliers		**9.8x**	**8.0x**	**7.1x**	**13.1x**	**10.5x**	**9.0x**
Median excluding outliers		**10.4x**	**8.3x**	**7.3x**	**13.7x**	**10.3x**	**8.6x**
Overseas furniture retailers							
DFS Furniture	954	8.0x	7.5x	7.4x	9.8x	9.4x	9.5x
Haverty Furniture Companies	556	5.6x	5.6x	5.3x	8.6x	9.0x	8.3x
Flexsteel Industries	521	8.2x	n/a	n/a	10.0x	n/a	n/a
BMTC Group	493	7.8x	n/a	n/a	9.1x	n/a	n/a
Pier 1 Imports	452	3.3x	4.0x	3.9x	5.5x	9.3x	7.6x
Bassett Furniture Industries	360	6.1x	5.7x	5.1x	8.6x	8.0x	7.0x
Average		**6.5x**	**5.7x**	**5.4x**	**8.6x**	**8.9x**	**8.1x**
Median		**7.0x**	**5.6x**	**5.2x**	**8.9x**	**9.1x**	**7.9x**
Average excluding outliers		**7.1x**	**6.3x**	**5.9x**	**9.2x**	**8.8x**	**8.3x**
Median excluding outliers		**7.8x**	**5.7x**	**5.3x**	**9.1x**	**9.0x**	**8.3x**

Source: FactSet and Leadenhall Analysis
Notes:
1. Data as at 20 September 2016
2. The multiples highlighted in grey are regarded as outliers

It should be noted that these multiples are based on trading of minority shareholdings. In contrast, we are considering the value of Fantastic 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.

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 Fantastic:

- Fantastic's trading multiples are at the lower end of the comparable Australian companies and are the lowest when excluding those comparable companies that have recently experienced a significant decline in performance (Myer, Helloworld, Billabong and Specialty Fashion). We consider that there may be a number of factors contributing to Fantastic's relatively low multiples:
  - Fantastic operates on relatively low margins (EBITDA and EBIT). The companies with the most comparable margins are JB Hi-Fi, Myer and Billabong. All other things being equal, higher margins generally support higher multiples
  - Fantastic is one of the smaller companies in terms of market capitalisation. All other things being equal, smaller companies trade on lower multiples
  - The market appears to have a more conservative view of short term growth potential than management, although forecast growth (EBITDA and EBIT) from FY16 to FY17 is still towards the higher end of the comparable companies
  - Fantastic's largest brand, Fantastic Furniture, is focused on the value for money end of the market which is likely to be more exposed to increasing competition, particularly from online furniture retailers
  - Some of the other comparable companies have a much smaller store footprint than Fantastic (Nick Scali, Baby Bunting, Adairs and Beacon Lighting). As such the market may be of the view that the long term organic growth potential of these companies is higher than Fantastic
  - Given the relatively tightly held register, Fantastic shares trade with lower liquidity than other companies of a similar size, which may also place downward pressure on the share price and therefore trading multiple
- The most comparable overseas companies are DFS Furniture (United Kingdom) and Basset Furniture Industries (United States). DFS Furniture is larger than Fantastic and therefore would be expected to trade on higher multiples. Bassett Furniture is more comparable in size and has similar margins and slightly lower forecast growth. The housing market in Australia is more buoyant than the United States and thus it is likely Fantastic would trade at slightly higher multiples than Bassett Furniture

Ultimately the comparable companies exhibit a fairly wide range of trading multiples, with issues such as underperformance (Myer, Helloworld, Billabong and Specialty Fashion), potential for organic growth through new store roll-outs (Nick Scali, Baby Bunting, Adairs and Beacon Lighting) and growth through acquisition (RCG and JB Hi-Fi) impacting the observed multiples of a number of the comparable Australian companies.

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 and forecast (where available) EBITDA and EBIT multiples from transactions with publicly available data.

Table 17: Comparable transaction multiples

Target	Acquirer	Close date	Target Description	Ent. value (US$'m)	Control premium	EBITDA Hist.	EBITDA Fore.	EBIT Hist.	EBIT Fore.
Australia									
The Good Guys	JB Hi-Fi	n/a	Whitegoods/electronics retailer	633	n/a	n/a	n/a	11.7	n/a
Hype DC	RCG Corporation	Jul-16	Premium shoe and apparel retailer	87	n/a	6.0	n/a	n/a	n/a
Accent Group	RCG Corporation	May-15	Premium shoe and apparel retailer	185	n/a	6.0	4.7	n/a	n/a
David Jones Ltd	Woolworths Holdings	Aug-14	Department store operator	1,957	25%	10.4	n/a	14.4	n/a
Witchery	Country Road	Aug-12	Womens fashion	172	n/a	5.1	n/a	n/a	n/a
Average						**6.9**	**4.7**	**13.1**	**n/a**
Median						**6.0**	**4.7**	**13.1**	**n/a**
Overseas									
Mattress Firm	Steinhoff International	n/a	Mattress and bedding retailer	3,848	nmf	18.4	10.8	28.4	15.9
Online Republic	Webjet Ltd	Jun-16	Online travel	59	n/a	7.1	n/a	n/a	n/a
Galeria Kaufhof	Hudson Bay Co.	Sep-15	Department store operator	3,183	n/a	9.0	n/a	14.6	n/a
Saks, Inc.	Hudson Bay Co.	Nov-13	Luxury departmnt store operator	2,699	5%	10.2	10.1	18.7	20.2
The Brick Ltd	Leon's Furniture	Mar-13	Furniture, appliance and electronics	728	54%	5.8	6.1	8.8	7.9
Cost Plus, Inc.	Bed Bath & Beyond	May-12	Casual home furnishings	631	22%	11.8	8.8	18.1	12.0
Average						**10.4**	**9.0**	**17.7**	**14.0**
Median						**9.6**	**9.5**	**18.1**	**14.0**

Source: FactSet and Leadenhall analysis
Note: control premium is based on the target share price on the day immediately prior to the transaction being announced)

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 appropriate earnings multiple to apply to the valuation of Fantastic:

- The Good Guys are around twice the size of Fantastic and margins on whitegoods are generally higher than the margins achieved by Fantastic. On this basis the multiple paid for the Good Guys would be expected to be higher than for Fantastic
- The RCG acquisitions of Hype DC and Accent Group were both at 6.0x EBITDA (based on the RCG share price at announcement). The footwear and apparel retailing sector is an extremely competitive environment in which changing fashion trends can have significant impacts on business performance. As such it would be expected that businesses in this sector would attract lower multiples. As Fantastic is larger than both Accent and Hype DC, it is expected that a higher multiple would be applicable to Fantastic
- David Jones is significantly larger than Fantastic and would therefore be expected to attract a higher transaction multiple
- The Witchery acquisition multiple (based on historical earning) is likely to be understated due to its loss making subsidiary MIMCO UK. While the consideration paid for the business reflected the losses of MIMCO UK and the estimated cost of the planned closure of the business, the historical earnings is based on normalised earnings which did not reflect the losses and closure costs
- The two international transactions that are most similar in size and industry to Fantastic are the acquisitions of The Brick Ltd and Cost Plus, Inc. Cost Plus is larger than Fantastic with high growth expectations at the time of the transaction (30% EBITDA forecast in FY13) thus indicating that a multiple for Fantastic would be below the multiple implied by the Cost Plus acquisition. The Brick acquisition occurred during a period of weak economic conditions and increasing competition (imminent entry of Target into the Canadian market) for furniture retailers in Canada. These factors resulted in low growth expectations and relatively low implied multiples on the Brick Transaction and as such an appropriate multiple for Fantastic would be expected to be higher

Our key considerations in selecting appropriate earnings multiples to apply to our valuation of Fantastic 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 what the selected control multiples may convert to in terms of minority multiples and compared to this to the observed trading multiples of comparable companies
- Fantastic does not have effective operational control over the Chinese joint venture which could be seen as a risk
- We have allowed for substantial growth in the selected maintainable earnings, particularly at the high end, and have therefore kept this in mind when considering appropriate multiples (i.e. growth potential should not be double counted by including it in both the selected maintainable earning and multiples)

Based on the above, we have selected the following earnings multiples to apply to our valuation of Fantastic:

Table 18: Selected earnings multiples

	EBITDA		EBIT	
	Low	High	Low	High
Selected earnings multiples	7.5	8.0	9.0	9.5

Source: Leadenhall analysis

Non-operating assets and liabilities

The multiplication of maintainable earnings by a selected control multiple results in an enterprise or business value. In order to assess the equity value (value to shareholders) it is necessary to allow for non-operating assets and liabilities. These can be:

- **Surplus assets:** assets held by the company that are not utilised in its business operations
- **Net debt:** comprising of debt used to fund a business, less surplus cash held by the company
- **Non-operating liabilities:** liabilities of a company not directly related to its current business operations

Each of these factors are considered below.

Surplus assets

Surplus assets are assets owned by an entity that are not required to generate the earning of its business. This could be investments, unused plant and equipment held for resale, or any other asset of the company that is not required to run its operating business. It is necessary to ensure that any income from surplus assets (e.g. rent / dividends) is excluded from the business value.

We have identified the following surplus asset of Fantastic as at 25 September 2016 (latest financial month end):

Table 19: Surplus assets

Surplus assets	Value $'m
Vacant land (Rockhampton QLD)	1.0
Total	**1.0**

Source: Fantastic

Fantastic owns the land upon which the Rockhampton Fantastic Furniture store is located. There is additional vacant land at this site which is surplus to requirements. Based on negotiations with potential purchasers the surplus land is expected to realise approximately $1 million after deducting the estimated tax payable from the proposed price.

Net cash

The net cash of Fantastic as at 25 September 2016 was as follows:

Table 20: Net cash

Net debt	Value $'m
Cash at bank	16.4
Term deposit	7.0
USD (converted at US$1.00:A$0.767)	6.3
Total	**29.7**

Source: Fantastic and Reserve Bank of Australia

Fantastic have advised that all of the cash held by the company is surplus to their ongoing business operations.

Non-operating liabilities

Non-operating liabilities are liabilities that are not related to the ongoing business operations, although they may relate to previous business activities, for example legal claims against the entity.

We have identified the following non-operating liability of Fantastic as at 25 September 2016:

Table 21: Non-operating liabilities

Non-operating liabilities	Value $'m
Le Cornu closure costs	1.5
Total	**1.5**

Source: Fantastic

Fantastic intends to close the Adelaide Le Cornu store in the second half of 2016. The $1.5 million represents the cash component of provision for closure costs recognised in the FY16 financial statements ($2.2 million net of applicable tax deductions estimated at 30%).

Valuation summary

Based on the selected maintainable earnings and EBITDA and EBIT multiples, the resulting value of a Fantastic share is set out in the table below.

Table 22: Summary of CFME analysis

	EBITDA		EBIT	
	Low	High	Low	High
Selected maintainable earnings	43.5	45.0	36.0	37.5
Selected multiple	7.5	8.0	9.0	9.5
Enterprise value	**326.3**	**360.0**	**324.0**	**356.3**
Surplus assets	1.0	1.0	1.0	1.0
Net cash	29.7	29.7	29.7	29.7
Non-operating liabilities	(1.5)	(1.5)	(1.5)	(1.5)
Equity value	**355.4**	**389.2**	**353.2**	**385.4**
Number of share on issue	103.3	103.3	103.3	103.3
Value per share	**$3.44**	**$3.77**	**$3.42**	**$3.73**

Source: Leadenhall analysis

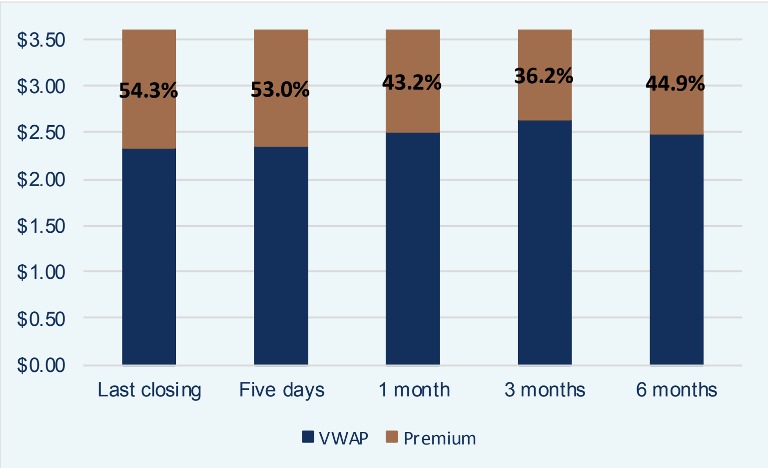
6.2 Analysis of Share Trading

Market trading in Fantastic shares prior to the announcement of the Proposed Transaction provides an indication of the market's assessment of the value of Fantastic on a minority basis. We have presented an analysis of recent trading in Fantastic shares in Section 4.12 above. When assessing market trading it is necessary to consider whether the market is informed and liquid. In this regard we note:

- Fantastic shares are fairly tightly held reducing the number of shares available for market trading. Daily values traded are often under $100,000, This level is below the level at which large institutional investors may wish to trade and may be seen as a deterrent for other significant investors
- Fantastic is a listed company with continuous disclosure obligations under the ASX Listing Rules, thus the market is reasonably informed about its activities. However, we note Fantastic has provided limited commentary regarding its future plans and has not provided earnings guidance

As a result of these factors we consider the market trading to be reasonably informed and moderately liquid. We have therefore undertaken only a high level analysis of share market trading, by assessing the level of control premium implied by our valuation range compared to the volume weighted average price of a Fantastic share over the last six months, as set out in the figure below.

Figure 11: Implied control premiums (mid-point of valuation range)



The control premium implied by the mid-point of our valuation range relative to the share price of Fantastic over the periods set out in the adjacent figure range from 54.3% at the last closing price of $2.33 on 7 October 2016 to 36.2% over the 3 month VWAP of $2.64.

Source: FactSet and Leadenhall analysis
Note: The VWAP's presented above have been adjusted to take account of the $0.15 special dividend for all trading prior to the ex-dividend date

The Fantastic share price has fluctuated significantly over the past three months, rising to a high of close to $3.00 after the announcement of FY16 results and a special dividend of $0.15. Since the ex-dividend date, the share price has fallen significantly (more than amount of the dividend paid) to a close of $2.43 on 20 September 2016. This decline has been in the absence of any market releases by Fantastic. It is likely that in the absence of the Proposed Transaction, or the speculation/announcement of any similar transaction, that the price of Fantastic would continue to trade at current levels, at least in the short term.

The generally observed range for control premiums between 20% to 40%. In addition, the average control premium observed for transactions in the retail trade sector in Australia between 2005 and 2015 was 30% and the average of the available control premiums for the comparable transactions is 27%. On this basis the control premium implied by our assessed value of a Fantastic share appears reasonable. Further information on observed control premiums is included in Appendix 4.

6.3 Conclusion on Value

Based on our CFME and share trading analysis we have selected a valuation range for a share in Fantastic, on a control basis, as set out in the table below.

Table 23: Selected valuation range

	Low	High
Selected valuation range	$3.42	$3.77

Source: Leadenhall analysis

7 EVALUATION

7.1 Fairness

We have assessed whether the Proposed Transaction is fair by comparing our assessed fair market value of a Fantastic share on a control basis with the consideration offered. This comparison is set out in the table below.

Table 24: Assessment of fairness

	Low	High
Fair market value of a Fantastic share	$3.42	$3.77
Consideration	$3.50	$3.50

Source: Leadenhall analysis

Since the consideration offered is within the assessed range of values of a Fantastic share the Proposed Transaction is fair to Shareholders.

7.2 Reasonableness

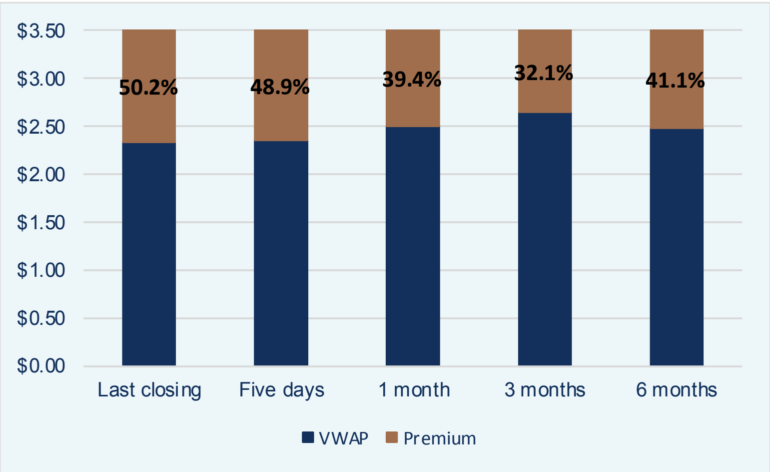
We have defined the Proposed Transaction as reasonable if it is fair, or if despite not being fair, there are sufficient reasons for Shareholders to vote for the proposal. We have therefore considered the following advantages and disadvantages of the Proposed Transaction to Shareholders.

Advantages

Premium to market price

The offer price reflects a meaningful premium to the Fantastic share price immediately prior to the announcement as set out in the figure below:

Figure 12: Implied control premium (offer price)



Source: FactSet and Leadenhall analysis
Note: The VWAP's presented above have been adjusted to take account of the $0.15 special dividend for all trading prior to the ex-dividend date

Share price in the absence of an alternative offer

In the absence of any alternative takeover offer, the only alternative to dispose of Fantastic shares would be to sell them on the market at a price which does not include a premium for control and would incur transaction costs (e.g. brokerage). If the Proposed Transaction is not approved, it is likely that Fantastic shares would trade at a price below the offer price, at least in the short term.

No superior alternative offer

We are not aware of any competing proposals to acquire Fantastic by any third party. However, we note that there would be an opportunity for any other interested party to put forward a competing offer prior to the scheme meeting being held. In these circumstances Shareholders would need to consider the competing offer before concluding on the Proposed Transaction.

Disadvantages

Loss of exposure to Fantastic business

If the Proposed Transaction is completed Shareholders would lose their exposure to the future performance of Fantastic. We note that the Fantastic management team has set out a medium term plan for the business including material growth in store numbers and profitability. If this plan was achieved, it is possible that Fantastic shares may trade at prices higher than the consideration under the Proposed Transaction in the medium term. By accepting the Proposed Transaction, Shareholders will not be able to participate in this potential upside.

Synergy benefits

Given the complementary nature of Steinhoff's business with Fantastic, it is likely that Steinhoff will be able to realise some synergy benefits from acquiring Fantastic. Based on our analysis, the offer price does not appear to include a material amount related to potential synergies as the selected multiples is towards the lower end of the comparable ranges and no synergies have been allowed for in the selected earnings. However, in the absence of a competing proposal, it is common for an acquirer not to pay for potential synergies they may obtain in a business combination.

Tax implications

The acceptance of the offer by the purchaser may have varying tax implications for individual investors which may impact the net cash consideration received. Shareholders should seek their own independent advice as to any potential tax implications upon acceptance of the offer.

Conclusion on reasonableness

As the Proposed Transaction is fair it is also reasonable.

7.3 Opinion

The Proposed Transaction is fair and reasonable to Shareholders. The Proposed Transaction is therefore in the best interests of Shareholders.

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

APPENDIX 1: GLOSSARY

Term	Meaning
ASIC	Australian Securities and Investments Commission
ASX	ASX Limited
CFME	Capitalisation of future maintainable earnings
DCF	Discounted cash flow
EBIT	Earnings before interest and tax
EBITA	Earnings before interest, tax and amortisation
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 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
Fantastic	Fantastic Holdings Limited
FOS	Financial Ombudsman Service
FSG	Financial Services Guide
FY	Financial year
IPO	Initial public offering
Leadenhall	Leadenhall Corporate Advisory Pty Ltd
NPAT	Net profit after tax
P/E	Price to earnings
Part 3	Part 3 of Schedule 8 of the Corporations Regulations 2001 (Cwlth)
Proposed Transaction	Steinhoff's offer to acquire Fantastic
RG111	Regulatory Guide 111: Content of Expert Reports
Scheme Booklet	Scheme Booklet issued by Fantastic in relation to the Proposed Transaction
Section 411	Section 411 of the Corporations Act 2001
Shareholders	Current shareholders of Fantastic
Steinhoff	Steinhoff Asia Pacific Holdings Pty Ltd
US	United States
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 ENTITIES

The following company descriptions are extracted from descriptions provided by FactSet.

Company	Description
Adairs Ltd.	Adairs Ltd. engages in the retail of Manchester and homewares. Its retail brands include Adairs, Adairs Kids, and Urban Home Republic. The company was founded in 2010 and is headquartered in Melbourne, Australia.
Baby Bunting Group Ltd.	Baby Bunting Group Ltd. is a one stop baby shop, which provides baby products. It offers products of brands, such as mountain buggy, bugaboo, safe-n-sound, phil & teds, babylove, childcare, maclaren, boori, stokke, babybjorn, medela, avent, johnsons, huggies and oricom. Baby Bunting Group was founded by Arnold and Gail Nadelman in 1979 and is headquartered in Dandenong South, Australia.
Bassett Furniture Industries, Inc.	Bassett Furniture Industries, Inc. engages in the manufacture and sale of home furnishings. The company was founded by John David Bassett in 1902 and is headquartered in Bassett, VA.
Beacon Lighting Group Ltd	Beacon Lighting Group Ltd. engages in the retailing of lighting, ceiling fans, and light globes. The company was founded in 1967 and is headquartered in Mulgrave, Australia.
Billabong International Limited	Billabong International Ltd. engages in the marketing, distribution, wholesaling and retailing of apparel, accessories, eyewear, wetsuits and hardgoods in the boardsports sector. Its brands include Billabong, Element, RVCA, VonZipper, Sector 9, Xcel, Tigerlily, Kustom, Honolua and Palmers Surf. Billabong International was founded by Gordon Stanley Merchant and Rena Merchant in 1973 and is headquartered in Gold Coast, Australia.
BMTC Group Inc.	BMTC Group, Inc. is a holding company which manages and operates retail sales networks of furniture and household and electronic appliances in Quebec. It sells its products through a network of stores. The company was founded on September 5, 1989 and is headquartered in Montreal East, Canada.
DFS Furniture PLC	DFS Furniture Plc designs, manufactures, sells, and delivers upholstered furniture products. It sells its products through a retail network of upholstered furniture stores, as well as through online in the United Kingdom and Ireland. Its business roots back to 1969 when Graham Kirkham founded a single DFS store near Doncaster, United Kingdom. The company was founded in 1969 and is headquartered in Doncaster, the United Kingdom.
Fantastic Holdings Limited	Fantastic Holdings Ltd. engages in the manufacturing, retailing, importing of household furniture. It operates through the following business segments: Retail and Property. The Retail segment comprises businesses that retail locally manufactured and imported household furniture under the Fantastic Furniture, Plush, Original Mattress Factory, Le Cornu and Dare Gallery brands in Australia. Fantastic Holdings is headquartered in Sydney, Australia.

Company	Description
Flexsteel Industries, Inc.	Flexsteel Industries, Inc. manufactures, imports, and markets residential and commercial upholstered and wooden furniture products. It offers sofas, loveseats, chairs, reclining and rocker-reclining chairs, swivel rockers, sofa beds, convertible bedding units, occasional tables, desks, dining tables and chairs, and bedroom furniture. Its products are used in home, office, hospitality, health care, and other commercial applications. The company was founded in 1893 and is headquartered in Dubuque, IA.
Harvey Norman Holdings Ltd	Harvey Norman Holdings Ltd. operates and franchises household goods retail stores. The company grants franchises to the independent business operators, as business owners who retail products for the home and office, which include electrical, computers & communications, small appliances, furniture, bedding & manchester, home improvements, lighting and carpet & flooring. The company was founded by Gerald Harvey and Ian John Norman in October 1982 and is headquartered in Sydney, Australia.
Haverty Furniture Companies, Inc.	Haverty Furniture Cos., Inc. operates as a specialty retailer of residential furniture and accessories. The company provides a wide selection of products and styles and various brands carried furniture. It operates its business through home furnishings retailing segment. The company offers the bedding product lines, which include Sealy, Serta, Stearns, Foster and Tempur-Pedic. It also provides financing through an internal revolving charge credit plan, as well as a third party finance company. The company was founded by James Joseph Haverty in 1885 and is headquartered in Atlanta, GA.
Helloworld Limited	Helloworld Ltd. is an integrated travel company, which engages in the selling of international and domestic travel products and services and the operation of a franchised network of travel agents. The company was founded in May 2001 and is headquartered in Sydney, Australia.
JB Hi-Fi Limited	JB Hi-Fi Ltd. engages in the retailing of home consumer products from stand-alone destination sites, shopping centre locations and online stores. It engages in the sale of consumer electronics products and services, which includes televisions, audio equipment, computers, cameras, telecommunications products and services, software, musical instruments, white goods, cooking products, small appliances, digital content and information technology and consulting services. The company was founded by John Barbuto in 1974 and is headquartered in Melbourne, Australia.
Kathmandu Holdings Limited	Kathmandu Holdings Ltd. designs, markets and retails clothing and equipment for travel and adventure. It operates through three geographical segments: New Zealand, Australia and the United Kingdom. Its products include waterproof jackets, down jackets, thermals, fleece jackets, shirts, pants, merino apparel and thermals, footwear, socks, packs, bags, sleeping bags, tents, travel and camping accessories. It's products market under the brand name, Kathmandu. The company was founded in 1987 and is headquartered in Christchurch, New Zealand.
Michael Hill International Ltd.	Michael Hill International Limited manufactures, wholesales, and distributes jewelry. The Company offers rings, pendants, necklaces, bangles, earrings, bracelets, watches, and other accessories. Michael Hill operates stores in New Zealand, Australia, Canada, and the United States. (Source: Bloomberg)

Company	Description
Myer Holdings Limited	Myer Holdings Ltd. operates department stores. Its core product categories include youth fashion, children's wear, intimate apparel, beauty, fragrance and cosmetics, homewares, electrical goods, toys, fashion accessories and general merchandise. The company's brands portfolio includes Basque, Regatta, Reserve, Trent Nathan, Bauhaus and Australian House and Garden, as well as the new categories, such as sass & bide intimates, Jayson Brunsdon Home, and Leona Edmiston Home. The company was founded by Sidney Myer in 1900 and is headquartered in Docklands, Australia.
Nick Scali Limited	Nick Scali Ltd. is a furniture retailer operating primarily on the east coast of Australia. The principal activities of the company are the sourcing and retailing of household furniture and related accessories. Its products include dining chairs, dining tables, regular lounges, modular lounges, recliner lounges, entertainment units, TV units, coffee tables, side tables, occasional chairs, TV recliner chairs and bar stools. The company was founded by Nicodemo Domenico Scali in 1962 and is headquartered in Lidcombe, Australia.
Pier 1 Imports, Inc.	Pier 1 Imports, Inc. engages in the provision of retail sales of decorative home furnishings, furniture, and gifts. Its products include decorative home furnishings, dining, kitchen goods, bath, bedding accessories, and specialty items for the home. The company was founded in 1962 and is headquartered in Fort Worth, TX.
RCG Corporation Limited	RCG Corp. Ltd. operates as an investment holding company, which owns and operates a number of footwear businesses. It operates through its subsidiaries, which include The Athlete's Foot Australia Pty ltd., and RCG Brands Pty Ltd. The Athlete's Foot Australia Pty Ltd. is a retailer of athletic footwear. The RCG Brands Pty Ltd. is a wholesale and distribution company, which distributes the Merrell, Cushe and CAT brands of footwear and apparel. The company was founded on February 23, 2004 and is headquartered in Sydney, Australia.
Specialty Fashion Group Limited	Specialty Fashion Group Ltd. engages in the retailing of women's clothing in Australia, New Zealand, South Africa, and the United States. It offers its products through various brands, such as Millers, Crossroads, Katies, Autograph, Rivers and City Chic. The company was founded by Arnold Ian Miller and Sara Miller in 1993 and is headquartered in Alexandria, 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:

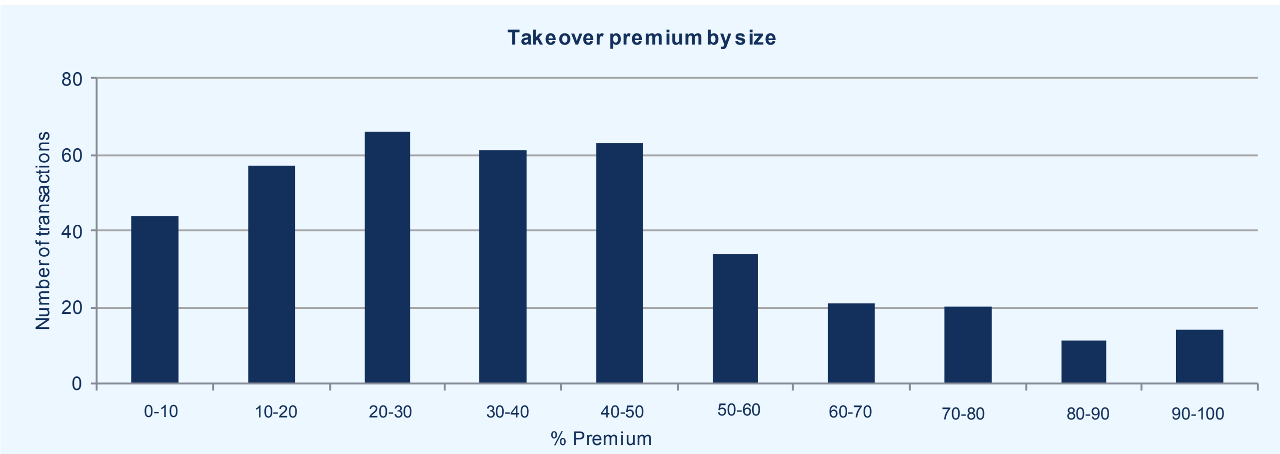
- Appoint or change operational management
- Appoint or change members of the board
- Determine management compensation
- Determine owner's remuneration, including remuneration to related party employees
- Determine the size and timing of dividends
- Control the dissemination of information about the 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.

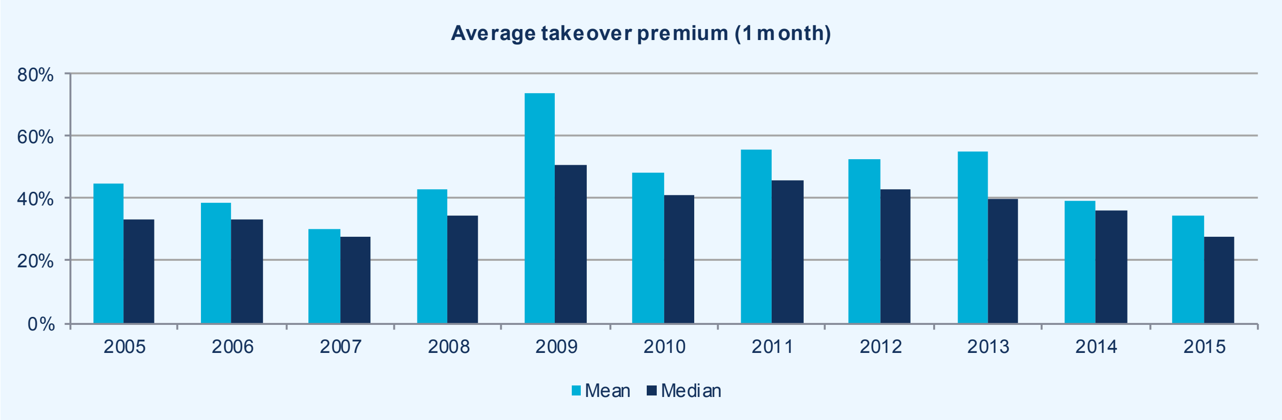


Sources: FactSet, Leadenhall analysis

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.

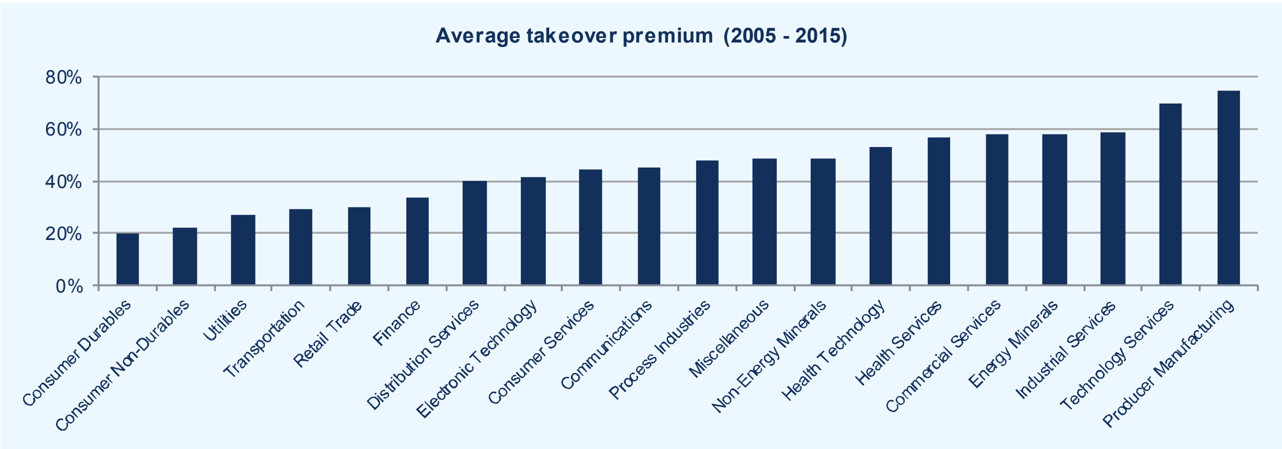


Sources: FactSet, Leadenhall analysis

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 Fantastic'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 Fantastic 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 Fantastic's management for confirmation of factual accuracy.

Prospective information

To the extent that this report refers to prospective financial information, we have considered the prospective financial information and the basis of the underlying assumptions. The procedures involved in Leadenhall's consideration of this information consisted of enquiries of Fantastic's personnel and analytical procedures applied to the financial data. These procedures and enquiries did not include verification work nor constitute an audit or a review engagement in accordance with Australian Auditing Standards, or any other standards. Nothing has come to our attention as a result of these enquiries to suggest that the financial projections for Fantastic, when taken as a whole, are unreasonable for the purpose of this report.

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 of Fantastic 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.

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 Fantastic and their officers, employees, agents or advisors, Fantastic 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 Fantastic and their officers, employees, agents or advisors or the failure by Fantastic 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, Dave Pearson, BCom., CA, CFA, CBV, M.App.Fin, Simon Dalgarno, B.Ec, FCA, F.FINSIA Katy Lawrence, BCom., CA and Chern Fung Yee, BCom., CPA (Aus).

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

Independence

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