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THE PAS GROUP LIMITED

(Subject to deed of company arrangement)

VALUE OF SHARES ON A LIQUIDATION BASIS

INDEPENDENT EXPERT'S REPORT AND FINANCIAL SERVICES GUIDE
1 DECEMBER 2020

1 December 2020

The Solicitors for the Deed Administrators
The PAS Group Limited (subject to Deed of Company Arrangement)
c/- Ben Mahoney – Partner
Arnold Bloch Leibler
Level 21, 333 Collins Street
Melbourne VIC 3000

Dear Sirs,

Independent Expert's Report for The PAS Group Limited

1. Introduction

The PAS Group Limited (Subject to Deed of Company Arrangement) ("**PAS**") and its 18 Australian subsidiaries (together the "**PAS Group Companies**") went into voluntary administration on 29 May 2020 at which time Martin Ford, Stephen Longley and David McEvoy of PricewaterhouseCoopers ("**PwC**"), were appointed joint and several voluntary administrators of each of the PAS Group Companies. At the second concurrent meetings of creditors of the PAS Group Companies on 17 August 2020, the creditors resolved that 18 of the PAS Group Companies, including PAS, enter identical "Transaction Support" Deeds of Company Arrangement (to facilitate a sale transaction) and that one PAS Group Company execute a "Distribution" Deed of Company Arrangement (to distribute proceeds of realisations to creditors via a distribution fund established under the deed) ("**DOCAs**"). The DOCAs came into effect on 4 September 2020. Martin Ford, Stephen Longley and David McEvoy were appointed the deed administrators of each DOCA ("**Deed Administrators**").

After an extensive, independent and competitive sales process undertaken by the Deed Administrators, the Deed Administrators entered into binding agreements with entities and persons associated with Queens Lane Capital Pty Ltd ("**QLC**"), for the acquisition of PAS' wholesale Designworks business and predominantly wholesale Yarra Trail business and the potential acquisition of the remainder of the PAS Group Companies as a whole, involving the transfer of PAS shares for a purchase price of $1.

The Deed Administrators intend to apply to the Federal Court of Australia ("**Court**") for leave to transfer all the shares in PAS to PAS Group International Pty Ltd (an entity associated with QLC) under section 444GA of the Corporations Act 2001 (Cth) ("**Act**") ("**Section 444GA Application**"). PAS Group International Pty Ltd will also apply to the Australian Securities and Investments Commission ("**ASIC**") for relief from the takeover provisions in Chapter 6 of the Act. Prior to the hearing of the Section 444GA Application, the Deed Administrators will provide an Explanatory Statement to shareholders of PAS.

Leadenhall Corporate Advisory Pty Ltd ("**Leadenhall**") has been engaged to prepare an Independent Expert's Report ("**IER**") assessing the value of a PAS share on a liquidation basis, in accordance with ASIC Regulatory Guide 111 ("**RG 111**").

The subject of the IER is the value of the PAS shares to be transferred to QLC which includes the retail operations of Review and Black Pepper as well as the other residual assets and liabilities in the corporate structure, including the Fiorelli brand (the "**Remaining Operations**" of PAS). This IER does not consider the JETS Swimwear business, which was sold prior to entry into the DOCAs, or the Designworks and Yarra Trail businesses which are to be acquired by entities associated with QLC under separate asset sale agreements.

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

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2. Purpose of the report

We understand that the IER will be used for the following purposes:

- to assist the Court in determining whether to grant leave to the Deed Administrators under section 444GA of the Act to transfer the shares in PAS to PAS Group International Pty Ltd. This requires the Court to consider whether the proposed transfer of shares will unfairly prejudice the interest of PAS' shareholders.
- to assist PAS Group International Pty Ltd with the making of an application to ASIC under section 655(1)(a) of the Act for relief from the operation of section 606 of the Act; and
- to be provided in an Explanatory Statement to be sent to PAS shareholders in relation to the Section 444GA Application.

Further information regarding our scope and purpose is set out in Section 2 of our detailed report.

3. Assessed value

RG 111 requires an assessment of the value of PAS shares on a liquidation basis, where this is the most likely consequence of the transfer of shares not being approved.

Liquidation value is defined as:

> *"The amount that would be realised when an asset or group of assets are sold on a piecemeal basis. Liquidation Value should take into account the costs of getting the assets into saleable condition as well as those of the disposal activity. Liquidation Value can be determined under two different premises of value:*
>
> *(a) an orderly transaction with a typical marketing period, or*
>
> *(b) a forced transaction with a shortened marketing period."*

In assessing the liquidation value of PAS shares we take account of the financial difficulties faced by the company. As the Remaining Operations of PAS are operating at a loss, have little prospect of becoming profitable in the short term and have already been through an extensive sales campaign, our approach has been to assume a forced sale of the main assets and allow for lease termination costs and redundancy costs. We have assumed the retail stores are closed in an orderly process while attempting to maximise the sale proceeds from the existing inventory.

The following table sets out our assessment of the liquidation value of PAS Shares.

Table 1: Liquidation value of PAS shares

$'000	Consolidated Group	Liquidation Values Low	Liquidation Values High
Current assets			
Cash and cash equivalents	21,743	21,743	21,743
Trade and other receivables	24,201	19,361	19,361
Inventories	12,381	2,476	6,191
Other current assets	613	-	-
Total current assets	**58,938**	**43,580**	**47,294**
Non-current assets			
Trade and other receivables	17	-	-
Property, plant and equipment	4,233	-	423
Right of use asset	9,073	-	-
Deferred tax assets	15,983	-	-
Intangible assets	47,306	-	473
Total non-current assets	**76,613**	**-**	**896**
Total assets	**135,551**	**43,580**	**48,191**
Current liabilities			
Trade and other payables	(28,724)	(28,724)	(28,724)
Borrowings	(5,309)	(5,309)	(5,309)
Provisions	(6,096)	(17,720)	(15,525)
Financial liabilities	(254)	(254)	(254)
Lease liabilities	(5,874)	(5,874)	(5,874)
Tax liabilities	(194)	(194)	(194)
Other liabilities	(856)	(856)	(856)
Total current liabilities	**(47,307)**	**(58,930)**	**(56,736)**
Non-current liabilities			
Provisions	(741)	(741)	(741)
Other non-current liabilities	0	0	0
Lease liability	(5,358)	(5,358)	(3,751)
Deferred tax liability	(10,362)	-	-
Total non-current liabilities	**(16,461)**	**(6,099)**	**(4,492)**
Total liabilities	**(63,768)**	**(65,030)**	**(61,227)**
Net assets	**71,784**	**(21,450)**	**(13,037)**

Source: Leadenhall analysis

This analysis has been cross-checked with reference to the Deed Administrators Estimated Outcome Statement which is broadly consistent with our conclusions.

Further details of our valuation of a PAS share are provided in Section 6 of our detailed report.

4. Opinion

In our opinion, the fair market value of the shares in PAS is nil on a liquidation basis.

This opinion should be read in conjunction with our detailed report which sets out our scope, analysis and findings in more detail.

Yours faithfully

Simon Dalgarno	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.

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

General Financial Product Advice

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

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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 $50,000 (excl. GST) for preparing this report. This fee is not contingent upon the outcome of the Proposed Transaction.

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

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

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

Referrals

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

Complaints Resolution

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

Leadenhall Corporate Advisory Pty Ltd
GPO Box 1572
Adelaide SA 5001

Email: office@leadenhall.com.au

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

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

Australian Financial Complaints Authority
GPO Box 3
Melbourne VIC 3001

Website: www.afca.org.au
Email: info@afca.org.au
Telephone: 1800 931 678 (free call)

Leadenhall's AFCA membership number is 12224

Compensation Arrangements

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

1 December 2020

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1 THE PROPOSED TRANSACTION

1.1 Background

In the year ended 30 June 2019, PAS reported a "*particularly challenging year*" and that "*intensifying macro-economic pressures and industry headwinds continue to challenge the operating environment*". At this time PAS reported it was "*executing on strategic priorities to drive sustainable profitable growth and shareholder value*."

Prior to December 2019, management had been in the process of implementing a turnaround strategy, which in addition to focussing on delivering efficiencies across support functions, focussed on rationalising the retail and brand portfolio and enhancing the online presence.

In PAS' December 2019 half year report:

- Net profit for the half year from continued operations after tax decreased from $1.3 million in the previous corresponding period to a loss of $1.0 million.
- Underlying EBIT for the half year from continuing operations decreased by $3.0 million on the previous corresponding period from $6.7 million to $3.7 million.
- It was disclosed as a subsequent event that:

  "*PAS sources a large component of its apparel from factories in China and the spread of coronavirus has resulted in extensions to the traditional Chinese New Year factory and port closures whilst quarantine restrictions have been implemented. The prolonged slowdown in industrial activity has resulted in delays to the resumption of production and shipping which we expect to have a negative impact on the industry as a whole and in particular on the delivery of orders to our wholesale and retail businesses.*
  We have also observed further reductions to foot traffic in some key shopping precincts and until the potential shipping backlog is cleared from China and the local market response stabilizes, it is not possible to accurately forecast the impact the coronavirus may have on the full year financial results.

PAS was in the midst of planning a rights issue when COVID-19 first hit, and the resultant impact on the stock market prevented this from proceeding. At the same time, PAS had been exploring the potential to conduct a placement, which was also abandoned due to the extremely difficult trading environment and the very low share price.

1.2 Administration process

The PAS Group Companies went into voluntary administration on 29 May 2020 at which time Martin Ford, Stephen Longley and David McEvoy of PwC, were appointed joint and several voluntary administrators of each of the PAS Group Companies.

At the second concurrent meetings of creditors of the PAS Group Companies on 17 August 2020, the creditors resolved that 18 of the PAS Group Companies, including PAS, enter identical "Transaction Support" Deeds of Company Arrangement (to facilitate a sale transaction) and that one PAS Group Company execute a "Distribution" Deed of Company Arrangement (to distribute proceeds of realisations to creditors via a distribution fund established under that deed). The DOCAs came into effect on 4 September 2020. Martin Ford, Stephen Longley and David McEvoy were appointed Deed Administrators.

The Deed Administrators continued to trade the various PAS businesses (subject to the various COVID19 restrictions) whilst undertaking a process to sell the businesses. After an extensive and competitive sales process, the Deed Administrators entered into binding agreements on 23 October 2020 with entities and persons associated with QLC for:

- the sale of the assets and undertakings of the wholesale Designworks business and the predominantly wholesale Yarra Trail business ("**Asset Sale Agreements**")
- the potential sale of the remainder of the PAS Group Companies as a whole, including the possible transfer of all shares in PAS Group to the new purchaser ("**Implementation Deed**")

(together, the "**Sale Transactions**").

At the time of writing, the Asset Sale Agreements have not yet completed.

Prior to execution of the DOCAs, on 7 August 2020, the Deed Administrators entered into an agreement for the sale of the assets of the JETS Swimwear business to Seafolly Holdings Pty Ltd ("**Seafolly**"). Seafolly was under voluntary administration at the time of entry into that agreement.

1.3 Sales Process

We understand that following their appointment, the Administrators undertook a comprehensive sales process for PAS which included consideration of offers for the entire business and individual assets/brands. This process included:

- Advertisements calling for expressions of interest being placed in the Australian Financial Review
- 50 parties expressing interest in all, or parts of, PAS
- 45 parties being issued an Information Overview, after signing a Confidentiality Agreement
- 15 parties submitting non-binding indicative offers
- Detailed negotiations with several parties
- The re-testing of market interest and re-engagement in negotiation with several parties.

This process resulted in the sale of JETS Swimwear to Seafolly, and the entry into the Sale Transactions described above.

Based on our discussions with PwC and the information provided by them, in our opinion an extensive, independent and competitive sales process was undertaken by the Deed Administrators.

1.4 Sale Transaction

On 23 October 2020, PAS and the Deed Administrators entered into the Implementation Deed with, amongst other parties, PAS Group International Pty Ltd ("**PAS Purchaser**").

Under the Implementation Deed, the PAS Purchaser takes the economic benefit and burden of the PAS Group Companies' remaining businesses on and from 1 October 2020. The PAS Purchaser has agreed to (amongst other things):

- Acquire all the shares in PAS for a nominal purchase price of $1, payable to the PAS Group Company which is the party to the Distribution DOCA, namely The PAS Group Distribution Company Pty Ltd (Subject to Deed of Company Arrangement) ACN 620 985 864 (formerly Bondi Bather Pty Limited) for distribution to creditors of the PAS Group Companies under the distribution fund, with such acquisition to occur by virtue of a transfer of shares under section 444GA of the Act.
- Reimburse the legal fees incurred by the Deed Administrators and PAS for making the Section 444GA Application up to a maximum of $250,000.
- Accept liability on and from 1 October 2020 for:
  - operating costs of the PAS Group Companies' remaining businesses, including liabilities arising under purchase orders or customer orders and orders for new stock; and
  - certain employee wages and leave entitlements which will accrue in the period from 1 October 2020 until completion of the share sale.

Upon completion of the transfer of PAS shares pursuant to the Implementation Deed (by way of section 444GA of the Act) PAS and its remaining businesses will cease to be subject to the Transaction Support DOCAs and the PAS Purchaser will be the owner of PAS.

In the event the share sale does not proceed the PAS Purchaser may either:

- Instruct the Deed Administrators to commence a managed wind down of the PAS Group Companies' remaining businesses.
- Enter into an asset sale agreement for all or part of the assets of the remaining PAS Group Companies under which the PAS Purchaser:
    - may elect to acquire some or all assets which relate to or are used in connection with the PAS Group Companies' remaining businesses for a purchase price of $2; and
    - will bear the costs of the managed wind down of the parts of the PAS Group Companies' remaining businesses it opts not to acquire.

The share sale is conditional upon, amongst other matters:

- The Court granting approval for the transfer of PAS shares to the PAS Purchaser under section 444GA of the Act.
- The PAS Purchaser applying for and obtaining from ASIC such exemptions or modifications from the takeover provisions in Chapter 6 of the Act as are necessary to enable the transfer of PAS shares to the PAS Purchaser in the Section 444GA Application ("**ASIC Relief**").

Further details concerning the Implementation Deed, the Section 444GA Application and the application for ASIC Relief, are included in the Deed Administrators' Explanatory Statement.

2 SCOPE

2.1 Purpose of the report

Court Approval of the Section 444GA Application

Pursuant to Section 444GA(3) of the Act, the Court may only approve a transfer of shares by the administrator of a deed of company arrangement if it is satisfied that the proposed share transfer will not '*unfairly prejudice the interests of members of the company*'. The transfer of shares contemplated by the Implementation Deed will not unfairly prejudice PAS' shareholders if PAS shares have no value. We understand that the Deed Administrators therefore intend to tender this report to the Court as evidence in support of the Section 444GA Application.

We have read the Federal Court of Australia's *Expert Evidence Practice Note (GPN-EXPT)*, which contains a copy of the Harmonised Expert Witness Code of Conduct and agree to be bound by it. The opinions stated in this report are based wholly, or substantially on specialised knowledge arising from training, study and experience in the field of business valuation. We have made all inquiries which we believe are appropriate and no relevant matters of significance have, to our knowledge, been withheld from the Court.

ASIC Relief

A transfer of shares that will result in a person's voting power in a public company increasing from 20% or below to more than 20%, or from a starting point that is above 20% and below 90%, is prohibited by Chapter 6 of the Act ("**Chapter 6**"), except in certain circumstances.

Pursuant to the share sale the PAS Purchaser will acquire 100% control of PAS. Accordingly, to enable the transfer of PAS shares to the PAS Purchaser under section 444GA of the Act, the purchaser needs to obtain relief from ASIC from the operation of the takeover's provisions contained in Chapter 6. We understand the PAS Purchaser intends to provide this report to ASIC in support of its application for ASIC Relief.

Information to Shareholders

We understand this report is also to be included in the Explanatory Statement to be sent to Shareholders advising them about the Section 444GA Application.

2.2 Basis of evaluation

For the purposes of the share valuation, we have been instructed to assume that the Asset Sale Agreements for the Designworks and Yarra Trail businesses are complete and therefore the valuation of shares is based on the assets and undertakings of the remaining PAS Group Companies' which are proposed to be sold via the Implementation Deed (including proceeds from the Asset Sale Agreements).

RG111 provides guidance on the preparation of experts' reports. RG111 requires experts to assess the value of a business that is subject to a DOCA based on the higher of the sum of the liquidation value of underlying assets or the value of the business as a whole. We consider this to be consistent with the definition of a liquidation basis of value, which is defined by the International Valuation Standard 104: Bases of Value as:

> *"The amount that would be realised when an asset or group of assets are sold on a piecemeal basis. Liquidation Value should take into account the costs of getting the assets into saleable condition as well as those of the disposal activity.*

The International Valuation Standard 104 notes that a liquidation can be either "orderly" or "forced". For the reasons discussed in Section 5, we have assumed a forced liquidation as that is the likely consequence of the transfer of shares not being approved by the court.

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

3 INDUSTRY ANALYSIS

3.1 Overview of the clothing retailing industry

The Australian clothing retailing industry consists of over 10,000 businesses that collectively generated an annual revenue of $15.73 billion in FY2020. Between 2015 and 2020, the industry experienced a compound annual growth rate ("**CAGR**") of 0.2%, compared to a CAGR of 1.4% over the preceding 5 years. A decline of 8.5% is anticipated for FY21 due to the impact of the COVID-19 outbreak on consumer sentiment, unemployment and retail activity. Nonetheless, reduced industry growth rates are also the product of increased competition and reduced consumer spending.

Australian apparel retailing is characterised by low market share concentration, with most participants being small, independent operators. However, the number of businesses operating in the sector has reduced from 12,406 in 2010 to 10,713 in 2020 due to an increased presence of large international players and heightened merger and acquisition activity. Nonetheless, the four largest players in the industry are expected to account for less than 40% of industry revenue, driven by fluctuating consumer preferences and low barriers-to-entry, especially for online-only stores.

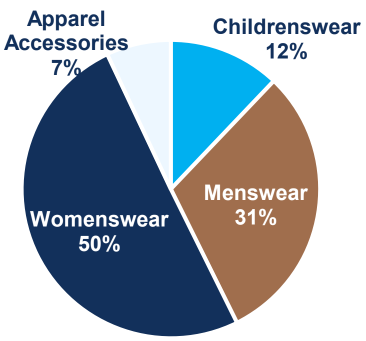
There has been a growing demand for online channels, particularly within the context of the coronavirus pandemic. According to IBISWorld, online apparel sales now generate a revenue of over $2.5 billion, accounting for approximately 10% of total online shopping. This growth has also been driven by free delivery and return policies, increasing the convenience and affordability of online shopping. In contrast to the growing online presence, traditional bricks-and-mortar retailers have seen a reduced share of the overall retail clothing industry. Similar trends have been occurring globally, as highlighted by the retail sales data for the United States shown below.

3.2 Customers and services

All demographics are consumers in the clothing retailing industry, with women's clothing being the industry's largest segment. Clothing products can be broadly categorised into:

- **Women's clothing:** Women tend to spend a higher proportion of their disposable income on clothing than men do, partially due to the increased seasonality of women's clothing.
- **Men's clothing:** Demand for menswear has risen over the past five years as men's attitudes towards fashion have shifted. Particularly amongst younger generations, the frequency of replacing clothing has increased. This has encouraged several retailers to cater specifically to the menswear market.
- **Accessories:** Comprises items such as hosiery, scarves, gloves, ties, and headwear. Due to the essential nature of some accessories, and their use by all demographics, this segment has consistently accounted for a substantial share of industry revenue.
- **Children's and infants' clothing:** Due to the increased age of first-time parents (with higher disposable incomes), this segment has attracted larger revenues in recent years. Nonetheless, there is fierce competition from discount department stores, which offer lower prices for parents' conscious of their children quickly out-growing their current wardrobe.

Figure 2: Major market segmentation



Source: Passport 2019

3.3 Profitability

The clothing retailing industry has seen declining profit margins over the past five years, with larger firms generally relying on high turnover to compensate for the lower profit margins. These trends have been caused by weakened consumer spending, growing competition (particularly online stores) and higher rental costs. Furthermore, drastic discounting strategies have diminished profit margins as retailers try to clear inventory, generate demand, and remain competitive.

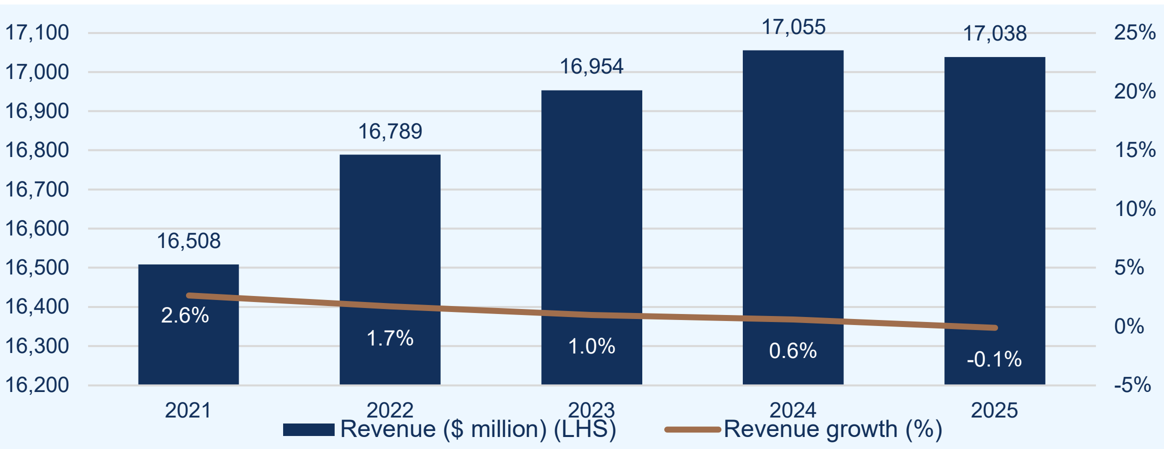
The key drivers of profitability for the clothing retailing industry include:

- **Real household disposable income:** An increase in disposable income enables consumers to increase discretionary spending on clothing, providing an opportunity for the industry to expand. Within the context of the COVID-19 pandemic, real household disposable income is expected to decrease in 2020.
- **Consumer sentiment:** When consumers feel more certain about their financial situation, they are likely to spend more on consumer goods, including clothing. Consumer sentiment is expected to decline and become negative in 2020.
- **Demand from online shopping:** Alongside rapid advancements in technology, there has been an increased presence of online clothing stores. Particularly within the current COVID-19 environment, demand for online shopping has risen, increasing industry competition from online-only stores. Whilst online-only stores threaten traditional bricks-and-mortar retailers, a significant proportion of traditional retailers have developed multichannel strategies to benefit from the growth in online shopping.
- **Demand from department stores:** Due to economies of scale, department stores such as Myer or David Jones can offer various clothing options at reduced prices, thereby competing with clothing retailers. Many department stores buy in bulk and often source goods directly from manufacturers, enabling lower prices compared to the industry average. Demand from department stores is forecast to increase in 2020 despite the COVID-19 outbreak.
- **Exchange rates:** The cost of imported clothing declines when the Australian dollar appreciates, which boosts demand for overseas goods. The Australian clothing industry imports most of its products, thus changes in the value of the Australian dollar can have a significant impact on industry costs. Over the next year, the Australian dollar is expected to depreciate relative to its major trading partners, making consumers more likely to purchase clothing from domestic retailers rather than overseas stores. However, this trend is also likely to increase purchase costs for industry players.

3.4 Outlook

Despite the significant fall in revenue in the year ended 30 June 2020, the clothing retailing industry is expected to recover over the next few years. Industry revenue is forecast to grow at an annualised 1.2% over the next five years to reach $17.0 billion by 2025. This includes strong growth in 2021 as the industry is projected to recover from the negative effects of the COVID-19 outbreak.

Figure 3: Forecast industry revenue growth in Australia



Source: IBISWorld

4 PROFILE OF THE PAS GROUP

4.1 Background

PAS was established in 2004 and listed on the ASX in 2014, is headquartered in Melbourne and had approximately 1,200 employees across Australia prior to entering administration earlier this year.

PAS carried on a business as wholesalers and retailers of apparel and accessories. PAS' retail operations focussed on a multiple sales channel strategy across 218 retail stores, outlets and concessions with a diversified product range across 19 owned, licenced and private brands and 20-character, music and film licences. It targeted a broad range of customer demographics by age, gender, location and price point. PAS also had 1.4 million Loyalty Members with a highly engaged repeat customer base which generated in excess of 70% of the retail revenue.

PAS operated in predominantly two segments, being Retail and Wholesale.

- **Retail:** The Retail segment includes revenues and profits generated by a retail and online footprint associated with women's, men's and children's apparel and related products. This included 225 retail sites and a number of online sites.
- **Wholesale:** The wholesale segment includes revenues and profits associated with the wholesaling of women's, men's and children's apparel, sporting equipment and related products.

As discussed in Section 1, the PAS Group Companies were placed into voluntary administration on 29 May 2020. Since then the JETS Swimwear business has been sold and the Deed Administrators have entered into the Asset Sale Agreements in relation to the Designworks and Yarra Trail businesses and the Implementation Deed to give effect to the proposed transfer of PAS shares to the PAS Purchaser.

4.2 Overview of the Remaining Operations

Following entry into the Asset Sale Agreements, the Remaining Operations of PAS, proposed to be acquired by the PAS Purchaser under the Implementation Deed, consist of the retail operations of Review, and Black Pepper, the Fiorelli brand as well as the Corporate support division.

The retail operations can be summarised as follows:

Table 2: PAS' Remaining Operations

	REVIEW	BLACK PEPPER
Gender	Female	Both
Target age range	24 - 40	60 +
Products	Dresses, tops, skirts, knitware, pants, jackets, coats, assessories	Shirts, tees, polos, pants, shorts, tops, skirts, jeans, jackets, knnitware, dresses
# of Stores	26 Stores and 57 Myer Concessions	86 Stores
Brands	Review	Black Pepper and Breakaway
Revenue FY20	$66.1 million (approx 53% of PAS Group retail revenue)	$58.7 million (approx 47% of PAS Group retail revenue)
Headcount	485	458

Review Retail Operations

The Review business was established in 1985 and the brand has been built on a unique position offering feminine products inspired by vintage with a modern twist. The brand focuses on fashion for women aged between 24 and 40 and the key attributes of the brand are:

- Timeless Classics – celebrating vintage design in a modern way
- Sophisticated Playfulness – beautiful elegance with a playful character.

Review has previously captured a large share of the value chain through operating a vertical retail model, selling into 26 owned retail stores and outlets and 57 Myer store concessions.

Review has recently negotiated an exclusive three-year agreement with Myer that covers all 57 concessions. The agreement has resulted in Myer committing to increased store space, as well as improved locations within the stores. Review experienced significant growth in concession sales prior to the COVID-19 pandemic and is regularly in the top four performing concessions within Myer.

In the year ended June 2019 the Review business reported net sales of $66.1 million. However, after allocation of an appropriate proportion of shared services costs (included below in PAS Corporate) the business has operated at an EBITDA loss since FY19 and is expected to do so in at least the near-term.

This division has been part of management restructuring activities with 10 stores closed in financial year ("**FY**") ending 30 June 2019 ("**FY19**"), 18 stores closing in FY ending 30 June 2020 ("**FY20**") and 9 stores closed in the three months ended 30 September 2020 ("**YTD FY21**"). The remaining 26 stores and outlets (excluding the 57 Myer concessions) are located in NSW 7, Qld 5, Vic 7, WA 2, SA 2, ACT 2 and NZ 1.

Review's 485 employees primarily include store managers and personnel across the retail portfolio, with 42 employees operating as a support function to the brand and footprint. The support office operates from PAS' Mount Waverley head office.

Black Pepper Retail Operations

Established in 1976, Black Pepper makes quality lifestyle leisurewear for both men (Breakaway) and women (Black Pepper).

Black Pepper is considered the leading leisurewear brand for the older female consumers in Australia and has enjoyed a strong following for a sustained period. Black Pepper is renowned for innovative design, quality fabrications sourced from around the world to create a unique quality garment.

Breakaway offers casual style for the Australian man. The brand positions itself as practical, quality, smart, comfortable and timeless that is suited to an active and outdoor lifestyle. Fabrics are specifically designed for durability, easy care and easy wear.

The Black Pepper and Breakaway brands are sold through the 86 store retail portfolio across Australia and New Zealand, with a growing online presence. Breakaway wholesale is sold via independents and Myer.

In the year ended June 2019 the Black Pepper business reported net sales of $58.7 million. However, after allocation of an appropriate proportion of shared services costs (included below in PAS Corporate) the business operated at EBITDA loss since FY19 and is expected to do so in at least the near-term.

This division has been part of management restructuring activities with 14 stores closed in FY19, 6 stores closed in FY20 and 35 stores closing in YTD FY21 . The remaining 86 stores and factory outlets are located in NSW 26, Vic 22, NZ 11, Qld 8, SA 9, WA 4, TAS 4 and ACT 2.

The Black Pepper division's 458 employees primarily includes store managers and personnel across the retail portfolio, with 39 employees operating as a support function from PAS' Mount Waverley head office.

Fiorelli Operations

Fiorelli is a company within the PAS Group which owns the Fiorelli licence. It was established in 1986 and acquired by the PAS Group in 2006. The Fiorelli brand is currently only operating in sunglasses, however it has historically operated in handbags, accessories and watches. The PAS Group receives a small amount of royalty revenue from the Fiorelli license, with it generating less than $50,000 in profit (prior to the allocation of shared service costs) in the last two years, and hence has not been analysed in detail in this report.

PAS Corporate

The PAS corporate divisions provided support predominantly to the Review and Black Pepper divisions in the following areas:

- Digital advertising, marketing and public relations
- Human resources
- Property negotiation
- IT and e-commerce development.

In the year ended June 2019 the PAS Corporate division reported a normalised divisional EBITDA loss of $10.42 million. The vast majority of these costs are required to operate the retail networks of the Review and Black Pepper divisions, with approximately $1.0 million estimated to relate to operating the ASX corporate operations (e.g. share registry, ASX fees and audit fees).

4.3 Financial Performance

PAS' management has prepared the following summary of the historical financial performance of the Remaining Operations, which has been extracted from the audited consolidated statements of financial performance for the FY ending 30 June 2018 ("**FY18**"), FY19, FY20 and for the YTD FY21.

Table 3: PAS' financial performance

$'000	FY18	FY19	FY20	YTD 21
Revenue	**139,874**	**124,813**	**99,445**	**20,984**
Total Direct Costs	(48,742)	(44,456)	(36,722)	(9,633)
Contribution Margin	**91,132**	**80,357**	**62,723**	**11,352**
Advertising, Marketing & PR	(3,888)	(4,421)	(4,108)	(497)
Employment Costs	(50,142)	(47,993)	(43,431)	(11,335)
Property & Occupancy Costs	(28,091)	(25,580)	(19,495)	(3,916)
General Expenses	(6,883)	(6,298)	(6,429)	(3,012)
Other (Expenses) / Income	2,125	1,443	8,270	8,895
EBITDA	**4,252**	**(2,492)**	**(2,470)**	**1,486**
Depreciation and amortisation expense	(6,497)	(6,164)	(5,412)	(1,465)
Impairment loss	(4,213)	-	(14,253)	-
EBIT	**(6,458)**	**(8,657)**	**(22,135)**	**21**
Interest expenses	(604)	(943)	(1,297)	(133)
Profit before tax	**(7,062)**	**(9,600)**	**(23,432)**	**(112)**
Income tax benefit/(expense)	(498)	1,233	3,879	(64)
Profit after tax	**(7,560)**	**(8,367)**	**(19,553)**	**(176)**
Other information				
Sales growth		-11%	-20%	n/m
Contrib. margin %	65%	64%	63%	54%
EBITDA margin %	3%	-2%	-2%	7%

Source: PAS

Notes:

1. *EBITDA for YTD21 includes increased sales at lower margins to maximise cashflow, significantly reduced advertising expenditure, government JobKeeper subsidies of approximately $9.3 million, reduced rentals and other short-term saving expenditure reductions. On a normalised basis the business would have reported an EBITDA loss.*
2. *Impact of AASB16 – Lease accounting has been excluded from all years to aid comparability.*

In relation to the historical financial performance of the Remaining Operations of PAS, we note the following:

- Revenue declined between FY18 and FY19 as a result of store closures and difficult trading conditions caused in part by a highly promotional environment. Revenue further declined in FY20 as a result of the economic impact of COVID19 and suspension of retail trading in many states and particularly Victoria.
- Contribution margin declined due to difficult trading conditions, with the significant fall in the current financial year due to heavy discounting to clear slow-moving stock.
- Advertising, marketing & PR has remained relatively stable between FY18 and FY20, with the significant fall in the current period a result of significantly reduced advertising spending during COVID19.
- Employment costs have reduced over the last three financial years as a result of reduced store numbers and more recently due to reduction of staff hours during COVID19 restrictions.
- Property & occupancy costs have reduced over the last three financial years as a result of reduced store numbers and more recently due to rental reductions as a result of COVID19 restrictions.
- Other expenses / income were immaterial until FY20. The high level of income in FY20 and YTD21 reflects the wage subsidies received as a result of COVID19, with approximately $9.3 million received in YTD21.

Based on the FY19 results, on the existing cost base revenue would need to increase by more than 10%, with no increase in operating costs before the business would break even. Accordingly, without the government subsidies received in YTD21, the Remaining Operations of PAS have operated at a loss for at least the last three financial years and have little prospect of becoming profitable in the short term.

4.4 Financial Position

Management has prepared the following summary of the historical financial position of the Remaining Operations which have been extracted from the audited consolidated statements as at 30 June 2018, 30 June 2019, 30 June 2020 and 30 September 2020.

In relation to the historical financial position of PAS set out below, we note the following:

- Inventories relate primarily to stock in stores and in transit for the Review and Black Pepper retail operations.
- Property, plant and equipment relates primarily to shop fitouts and IT systems.
- Right of use assets are the right to use the leased stores and were recognised for the first time in June 2020 in accordance with AASB 16 – Lease Accounting. This asset is fully offset by the current and non-current lease liability.
- Intangibles includes goodwill of $18 million, brand names of $15 million and capitalised software and web development costs of $3 million.
- Other non-current financial assets relate to intercompany loans and is largely offset by borrowings.
- Provisions relate predominantly to employee leave liabilities with other amounts relating to provisions for make good and outstanding gift vouchers.

Table 4: PAS' financial position

$'000	30-Jun-18	30-Jun-19	30-Jun-20	30-Sep-20
Current assets				
Cash and cash equivalents	(4,569)	307	6,707	8,560
Trade and other receivables	2,912	2,772	5,438	5,965
Inventories	20,751	20,864	15,538	12,381
Other current assets	2,242	3,013	1,705	613
Total current assets	**22,609**	**27,477**	**29,388**	**27,518**
Non-current assets				
Trade and other receivables	32	46	17	17
Property, plant and equipment	10,213	7,720	5,335	4,233
Right of use asset		-	13,394	9,073
Deferred tax assets	6,587	8,339	15,913	15,983
Intangible assets	48,097	49,069	47,328	47,252
Total non-current assets	**64,929**	**65,174**	**81,988**	**76,559**
Total assets	**87,538**	**92,650**	**111,376**	**104,077**
Current liabilities				
Trade and other payables	(10,491)	(10,762)	(12,498)	(11,599)
Borrowings	-	-	(3,868)	(3,410)
Provisions	(4,062)	(4,286)	(5,147)	(5,596)
Financial liabilities	-	-	-	(254)
Lease liabilities	-	(1,103)	(9,317)	(5,874)
Tax liabilities	(5)	(3)	(50)	(21)
Other liabilities	(2,375)	(3,371)	(868)	(856)
Total current liabilities	**(16,934)**	**(19,526)**	**(31,747)**	**(27,610)**
Non-current liabilities				
Provisions	(659)	(717)	(755)	(741)
Other non-current liabilities	(2,571)	(1,621)	-	-
Lease liability	(600)	-	(7,061)	(5,358)
Deferred tax liability	(5,091)	(5,227)	(10,659)	(10,362)
Total non-current liabilities	**(8,922)**	**(7,564)**	**(18,474)**	**(16,461)**
Total liabilities	**(25,856)**	**(27,090)**	**(50,222)**	**(44,071)**
Net assets	**61,682**	**65,560**	**61,154**	**60,006**

Source: PAS

Notes: Impact of AASB16 – Lease accounting has been included in the 30 June 2020 and the 30 September 2020 results.

5 VALUATION METHODOLOGY

To estimate the fair market value of PAS, we have considered common market practice and the valuation methodologies recommended in RG 111. There are a number of methods that can be used to value a business including:

- The discounted cash flow method
- The capitalisation of future maintainable earnings 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. The choice of methods depends on several factors such as the nature of the business being valued, the return on the assets employed in the business, the valuation methodologies usually applied to value such businesses and availability of the required information. A detailed description of these methods and when they are appropriate is provided in Appendix 2.

In assessing the value of PAS shares we have taken account of the financial difficulties faced by the company.

RG111 requires experts to assess the value of a business that is subject to a DOCA based on the higher of the sum of the liquidation value of underlying assets or the value of the business as a whole. We consider this to be consistent with the definition of a liquidation basis of value, which is defined by the International Valuation Standard 104: Bases of Value as:

> *"The amount that would be realised when an asset or group of assets are sold on a piecemeal basis. Liquidation Value should take into account the costs of getting the assets into saleable condition as well as those of the disposal activity.*

The International Valuation Standard 104 notes that a liquidation can be either "orderly" or "forced" .

As the Remaining Operations of PAS:

- are operating at a loss (after normalising the impact of government COVID19 subsidies)
- have little prospect of becoming profitable in the short term (without a significant increase in revenue or decrease in costs)
- would need to incur significant costs to order stock for the winter 2021 season (and the existing summer 2020 stock will be obsolete by March 2021)
- have already been through an extensive sales campaign

our approach has been to value the shares on a liquidation (forced transaction) basis, as this is the most likely consequence of the transfer of shares not being approved. We have assumed the retail stores are closed in an orderly process while attempting to maximise the sale proceeds from the existing inventory.

6 VALUATION OF PAS

6.1 Approach

Leadenhall has determined the value of PAS' equity on a liquidation basis in accordance with RG 111. Our liquidation value takes into account PAS' current financial situation where it is currently loss-making on a normalised basis and that it does not have sufficient funding to pursue its operations for the foreseeable future. Furthermore, the sales process undertaken by the Deed Administrators indicates the value for the Remaining Operations would be maximised through a sale of its business assets.

Our liquidation valuation of PAS assumes the Remaining Operations of PAS aggregates the amount that could be realised if its assets were sold in a reasonably short time frame, which is the likely outcome if the Sale Transactions, including the transfer of PAS shares under the Implementation Deed do not complete.

6.2 Liquidation value

Our assessed value of the net assets of PAS Group on a forced liquidation basis is summarised below.

Table 5: Liquidation value of PAS shares

$'000	Consolidated Group	Liquidation Values Low	High
Current assets			
Cash and cash equivalents	21,743	21,743	21,743
Trade and other receivables	24,201	19,361	19,361
Inventories	12,381	2,476	6,191
Other current assets	613	-	-
Total current assets	**58,938**	**43,580**	**47,294**
Non-current assets			
Trade and other receivables	17	-	-
Property, plant and equipment	4,233	-	423
Right of use asset	9,073	-	-
Deferred tax assets	15,983	-	-
Intangible assets	47,306	-	473
Total non-current assets	**76,613**	**-**	**896**
Total assets	**135,551**	**43,580**	**48,191**
Current liabilities			
Trade and other payables	(28,724)	(28,724)	(28,724)
Borrowings	(5,309)	(5,309)	(5,309)
Provisions	(6,096)	(17,720)	(15,525)
Financial liabilities	(254)	(254)	(254)
Lease liabilities	(5,874)	(5,874)	(5,874)
Tax liabilities	(194)	(194)	(194)
Other liabilities	(856)	(856)	(856)
Total current liabilities	**(47,307)**	**(58,930)**	**(56,736)**
Non-current liabilities			
Provisions	(741)	(741)	(741)
Other non-current liabilities	0	0	0
Lease liability	(5,358)	(5,358)	(3,751)
Deferred tax liability	(10,362)	-	-
Total non-current liabilities	**(16,461)**	**(6,099)**	**(4,492)**
Total liabilities	**(63,768)**	**(65,030)**	**(61,227)**
Net assets	**71,784**	**(21,450)**	**(13,037)**

Source: Leadenhall analysis

Assessed Liquidation Value Analysis

The above statement of financial position differs from Table 4 in Section 4.4 as that analysis was prepared based on the Remaining Operations, whereas the above PAS Consolidated Group statement of financial position incorporates the residual impact of the businesses that have been sold (e.g. Designworks accounts receivable are to be collected by the Deed Administrators and the accounts payable are to be paid by them.) In determining the value of PAS' Consolidated Group net assets using a liquidation value analysis, we have made the following assumptions:

- **Cash:** PAS' bank accounts and term deposits are assumed to be fully realisable in a liquidation scenario. The balance includes the proceeds from the sale of JETS, Designworks and Yarra Trail. Although some of these amounts may be subject to potential setoffs where there are offsetting creditor positions, we have not included any potential reduction to the liabilities in this analysis and hence made no corresponding adjustment to the balance of realisable cash.
- **Trade and other receivables:** We have assumed 80% of the book value is recoverable in both the low and high cases to make allowance for the cost of recovery.
- **Inventories:** Inventory predominantly include finished goods and prepayments for stock in transit. In the low case we have assumed PAS will cease trading quickly and much of this stock will need to be sold via other channels. Accordingly, we have assumed a recovery of 20% of the book value in the low case. In the high case we have assumed the store network is progressively closed while attempting to maximise the sale proceeds from the summer stock currently in store. In this case we have assumed a recovery of 50% of the book value to allow for the cost of operating the stores and expected heavy discounting required to clear the stock.
- **Other current assets:** The balance of other current assets consist mainly of prepayments, including for insurance. We have assumed some of these prepayments will be difficult to obtain reimbursements for and / or it will not be cost effective to make a claim for the amount prepaid. As a result, we have assumed no value for these assets.
- **Property, plant and equipment:** The majority of this balance relates to furniture and fittings in the various stores, with a smaller amount relating to computer equipment. As the stores and computer equipment will be stripped out and disposed of, we have assumed a recovery of 0% of the book value in the low case and 20% in the high case. An additional amount has been included in provisions for the expected make good costs.
- **Right of use assets:** Right of use assets are incorporated on the statement of financial position as a result of AASB16 – Leases and recognise the future right to occupy the leased premises. As PAS' operations will be discontinued, the right to occupy the various premises has no value.
- **Deferred tax assets:** Deferred tax losses include a component of past tax losses. We have not ascribed any value to the deferred tax assets as they will provide no benefit.
- **Intangible Assets:** This balance consists of the capitalised value of goodwill, brand names and software. As a liquidation basis assumes PAS will cease trading, no value has been allocated to any of these assets. In support of this assumption, the Deed Administrators have undertaken a comprehensive process and did not receive offers of any significant amount for the brands.
- **Current Liabilities:** We have included all current liabilities as per the 30 September 2020 statement of position.
- **Provisions:** The book value of provisions predominantly relates to leave liabilities. Adjustments have been made for redundancy payments (including payments in lieu of notice) and also for make good costs on leased shop stores. As a result, we have increased the liability to $17.7 million in the low case and $15.5 million in the high case based on discussions with PAS management.
- **Lease Liabilities:** While PAS is liable for the rent for the remaining period of the lease term, we have assumed this liability could be minimised or reduced as many of the stores are in prime locations and incentives may make it attractive for new tenants to lease the premises. As a result, we have assumed a payment of 100% of the book value in the low case and 70% in the high case (i.e. a decreased liability in the high case, resulting in a higher total value).

- **Deferred tax liability:** We have not ascribed any value to the deferred tax liabilities.

In addition to the items recognised on the statement of financial position and by the Deed Administrators, the following items need to be considered when assessing the value of the equity.

- **Tax Losses:** As at 30 June 2019 PAS has carried forward revenue tax losses of $5.6 million recognised on its balance sheet. These are the balance as at 30 June 2019 (as the tax return has not been completed for 30 June 2020) but the revenue losses would be significantly higher as at the date of this report due to the substantial losses in FY20. We have not attributed any value to these tax losses as these would not be utilised in a liquidation of the business as no taxable income is likely to be generated to offset the losses.
- **Franking Credits:** The franking account balance as at 30 June 2019 was $40.1 million. This is also expected to approximate the balance as at 30 June 2020. On a liquidation basis, we have not attributed any value to PAS' franking credits as they will not be able to be distributed to Shareholders.
- **Listed Shell:** Whilst there arguably could be value to the listed company shell in a liquidation, it would likely be negligible in the context of PAS and would not change our conclusions on the liquidation value.

Liquidation Value Conclusion

As the calculated value of the net assets in both the high and low liquidation scenarios is less than zero, we have assessed the value of the equity as zero in all situations.

6.3 Cross Check to Estimated Outcome Statement

The Deed Administrators have provided us with the PAS Group estimated outcome statement ("**EOS**") as at 30 September 2020, which is an assessment of the residual value to creditors on the following basis:

- Voluntary Administration - which assumes the sale of retail operations facilitated by the Transaction Support and Distribution DOCA structure
- Liquidation – which assumed the sale of the Designworks and Yarra Trail businesses and a forced liquidation of the retail operations.

We have discussed this analysis with PwC but not conducted a detailed review. For the purposes of this cross check, we have adopted the Deed Administrators' assessment of realisable values and claims, as this represents their best estimate as to the expected surplus to or deficit to unsecured creditors as a consequence of the administration.

Table 6: Liquidation value of PAS after Sale of Designworks and Yarra Trail

PwC's Estimated Outcome Statement			
	Voluntary Administration	Liquidation High	Liquidation Low
Total circulating assets	47,624	55,328	53,342
Priority creditors	(25,440)	(42,725)	(53,317)
Surplus/(deficit) available to CBA	**22,184**	**12,603**	**25**
Non-circulating assets (net of costs)	-	-	-
Surplus/(deficit) available to creditors	**22,184**	**12,603**	**25**
Secured creditor - CBA	(4,026)	(4,026)	(4,026)
Surplus/(deficit) available to unsecured creditors	**18,158**	**8,577**	**(4,001)**
Adjustment for non-DOXG companies' returns	(1,798)	3,966	6,612
Surplus/(deficit) available to unsecured creditors	**16,360**	**12,543**	**2,611**
Unsecured creditors (excluding related entities)	(22,228)	(40,500)	(40,030)
Calculated value of 100% of Equity	**(5,868)**	**(27,957)**	**(37,419)**
Assessed value of 100% of Equity	**- Nil -**	**- Nil -**	**- Nil -**
Other information			
Cents in dollar return to unsecured creditors	73.6	31.0	6.5

Source: Summary of PwC analysis

In relation to the estimated outcome statement set out above, we note the following:

- The liquidation scenario assumes the sale of Designworks and Yarra Trail completes and the Remaining Operations (predominantly the retail operations) remain to be liquidated.
- The value of circulating assets is lower in the voluntary administration scenario as there will be no proceeds from the sale of inventory, which will be partially offset by the expected business sale proceeds. The impact of a business sale is addressed further below.
- The total of priority creditors is higher in the liquidation scenarios as additional rent will be payable while the stores are kept operating during the winding up process and additional professional fees will be payable. Also, an increased amount has been included for contingencies.
- As some of the PAS companies are not parties to the deed of cross guarantee ("**DOXG**"), an adjustment has been made for non-DOXG company returns as they are liquidated separately, and then any surplus returned to PAS.
- Unsecured creditors are higher in the liquidation scenario due primarily to additional contingent liability for make good and contracted rent upon exit. These contingent liabilities will be significantly reduced in the voluntary administration scenario as the acquirer of the business will take on the majority of these costs.

The above analysis supports our conclusions as the calculated value of the equity is less than zero.

6.4 Premium for control

A premium for control can be defined as an amount or a percentage by which the pro-rata value of a controlling interest exceeds the pro-rata value of a non-controlling interest in a business enterprise, to reflect the power of control. The requirement for an explicit valuation adjustment for a control premium depends on the valuation methodology and approach adopted. This valuation is based on a liquidation approach, which is premised on the ability to control the assets of an entity and therefore incorporates any relevant premium for control. Thus, no further adjustment is required.

6.5 Summary

Based on the analysis set out above we have assessed the value of a PAS share to be nil on a liquidation basis.

APPENDIX 1: GLOSSARY

Term	Meaning
Act	Corporations Act 2001(Cth)
AFCA	Australian Financial Complaints Authority
AIFRS	Australian equivalent to international financial reporting
ASIC	Australian Securities and Investments Commission
ASIC Relief	The PAS Purchaser applying for and obtaining from ASIC such exemptions or modifications from the takeover provisions in Chapter 6 of the Act as are necessary to enable the transfer of PAS shares to the PAS Purchaser in the Section 444GA Application
Asset Sale Agreements	The binding agreements entered into on 23 October 2020 by the Deed Administrators with entities associated with QLC for the sale of the assets and undertakings of the wholesale Designworks business and the predominantly wholesale Yarra Trail business
ASX	ASX Limited
AUD	Australian Dollar
Buyer	QLC
CAGR	Compound Annual Growth Rate
CAPM	Capital Asset Pricing Model
Chapter 6	Chapter 6 of the Act
Court	Federal Court of Australia
Deed Administrators	Martin Ford, Stephen Longley and David McEvoy of PwC
DOCA	Transaction Support and Distribution Deed of Company Arrangements
DOXG	Deed of cross guarantee between PAS Group Companies
EBIT	Earnings before interest and tax
EBITDA	Earnings before interest, tax, depreciation and amortisation
EOS	Estimated outcome statement prepared by the Deed Administrators
Explanatory Statement	Explanatory statement sent by the Deed Administrators to PAS shareholders prior to the hearing of the Section 444GA Application, containing information about the Sale Transactions, Section 444GA Application and the application for ASIC Relief.
Fair market value	The price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arms' length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts
FOS	Financial Ombudsman Service
FSG	Financial Services Guide
FY	Financial year
FY18	FY ending 30 June 2018
FY19	FY ending 30 June 2019
FY20	FY ending 30 June 2020
FY21	FY ending 30 June 2021
IER	Independent Expert's Report

Term	Meaning
Implementation Deed	Binding agreement signed by the Deed Administrators with entities and persons associated with QLC. It is intended the sale of PAS and its remaining businesses will complete pursuant to the Implementation Deed, involving a transfer of PAS shares under section 444G of the Act, with the option of those remaining businesses being acquired by the PAS Purchaser under an asset sale agreement if necessary approvals of the Section 444GA Application and ASIC Relief application are not obtained.
Item 7	Item 7 of Section 611 of the Corporations Act
Leadenhall	Leadenhall Corporate Advisory Pty Ltd
Liquidation value	The amount that would be realised when an asset or group of assets are sold on a piecemeal basis. Liquidation Value should take into account the costs of getting the assets into saleable condition as well as those of the disposal activity. Liquidation Value can be determined under two different premises of value: (a) an orderly transaction with a typical marketing period, or (b) a forced transaction with a shortened marketing period."
NPAT	Net profit after tax
P / E	Price to Earnings
PAS	The PAS Group Limited
PAS Group Companies	PAS and 18 of its Australian subsidiaries that went into voluntary administration on 29 May 2020
PAS Purchaser	PAS Group International Pty Ltd, the party that entered into the Implementation Deed
PBT	Profit before tax
Proposed Transaction	The acquisition of PAS' Remaining Operations by the PAS Purchaser under the Implementation Deed, including the transfer of PAS shares to the PAS Purchaser under section 444GA of the Act.
PwC	PricewaterhouseCoopers
QLC	Queens Lane Capital Pty Ltd
Remaining Operations	The retail operations of Review and Black Pepper as well as any other residual assets or liabilities in the corporate structure including the Fiorelli brand (excluding the JETS Swimwear business, which was sold prior to entry into the DOCAs, and the wholesale operations of Designworks and predominantly wholesale operations of Yarra Trail which are to be acquired under the Asset Sale Agreements).
RG111	Regulatory Guide 111: Content of Expert Reports
RG112	Regulatory Guide 112: Independence of experts
RG74	Regulatory Guide 74: Acquisitions Approved by Members
Sale Transactions	The Asset Sale Agreements and the Implementation Deed
Seafolly	Seafolly Holdings Pty Ltd
Section 444GA Application	Application intended to be issued to the Federal Court by the Deed Administrators under section 444GA of the Corporations Act 2001 (Cth)
Section 655(1)(a)	Section 655(1)(a) of the Corporations Act 2001
Section 606	Section 606 of the Corporations Act 2001
Shareholders	Shareholders in PAS
YTD FY21	The three months ended 30 September 2020

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: QUALIFICATIONS, DECLARATIONS AND CONSENTS

Responsibility and purpose

This report has been prepared for PAS for the purpose of assessing the fair market value of a PAS share on a liquidation basis. Leadenhall expressly disclaims any liability, 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 PAS and the Deed Administrators 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 PAS and the Deed Administrators for confirmation of factual accuracy.

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 the Deed Administrators and their colleagues, PAS, via the Deed Administrators (solely in their capacity as joint and several Deed Administrators of PAS and subject to the terms of the disclaimer agreed by the parties in Leadenhall's engagement letter), 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 PAS and the Deed Administrators and their colleagues or the failure by PAS and the Deed Administrators and their colleagues 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 Dave Pearson, BCom., CA, CFA, CBV, M.App.Fin; Simon Dalgarno, B.Ec, FCA, F.FINSIA; Richard Norris, BA (Hons), FCA, M.App.Fin, F.Fin; Bruce Li, BCom., CA, CA BV Specialist; and Vicky Lau, BCom., CA.

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.

Independence

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