Independent Adviser's Report

Lyttelton Port Company Limited

Prepared Pursuant to Rule 21 of the New Zealand Takeovers Code in Relation to a Full Takeover Offer from Christchurch City Holdings Limited

September 2014

Statement of Independence

Northington Partners Limited confirms that it:

- Has no conflict of interest that could affect its ability to provide an unbiased report; and
- Has no direct or indirect pecuniary or other interest in the proposed transaction considered in this report, including any success or contingency fee or remuneration, other than to receive the cash fee for providing this report.

Northington Partners Limited has satisfied the Takeovers Panel, on the basis of the material provided to the Panel, that it is independent under the Takeovers Code for the purposes of preparing this report.

northington PARTNERS
investment banking • corporate finance

Table of Contents

Abbreviations and Definitions

CAGR	Compound average growth rate
CCHL	Christchurch City Holdings Limited, the wholly-owned investment arm of Christchurch City Council
Code	The Takeovers Code
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
FY	Financial Year
GFC	Global financial crisis
Kotahi Agreement	An agreement announced in June 2014 between freight and logistics company Kotahi (jointly owned by Fonterra and Silver Fern Farms), POT and PrimePort Timaru
Lock-up Agreement	The agreement between CCHL and Port Otago pursuant to which CCHL has agreed to purchase from Port Otago (subject to the provisions of the Code) 15,825,477 shares in the Company
LPC or Company	Lyttelton Port Company Limited
Northington Partners	Northington Partners Limited
NPAT	Net Profit After Tax
NTA	Net Tangible Assets
NZ$	New Zealand dollars
NZX	NZX Limited
Offer	The offer from CCHL on 25 August 2014 to purchase all of the shares in LPC that it does not already own
Offer Price	NZ$3.95 for each LPC ordinary share
Port Otago	Port Otago Limited
POT	Port of Tauranga Limited
Special Dividend	A dividend of 20 cents per share (with full imputation credits attached to the extent available) to be declared and paid by LPC before the closing date of the Offer, which CCHL has stipulated as a condition of the Offer
Takeover Notice	The notice from CCHL received by LPC on 6 August 2014 setting out CCHL's intention to make the Offer
TEU	Twenty foot equivalent unit
Total Offer Consideration	$4.15 per share, being the aggregate of the Offer Price and the Special Dividend
VWAP	Volume weighted average price
WACC	Weighted average cost of capital

1.0 Assessment of the Merits of the Offer

1.1 Introduction

Lyttelton Port Company Limited ("**LPC**" or "**Company**") is a public company listed on the NZSX, the main board equity securities market operated by NZX Limited ("**NZX**"). LPC operates the Port of Lyttelton, New Zealand's third largest port and the biggest port in the South Island. Further details on LPC are set out in Section 2.0.

LPC is majority owned by Christchurch City Holdings Limited ("**CCHL**"), the wholly-owned investment arm of Christchurch City Council. CCHL currently owns or controls 81,499,857 shares in LPC, being 79.70% of the total shares on issue. A brief profile of CCHL is set out in Appendix 1.

On 6 August 2014, CCHL sent LPC a notice ("**Takeover Notice**") setting out its intention to make a takeover offer for all the shares in LPC it does not already own ("**Offer**"). As part of the Offer process, CCHL also entered into a lock-up agreement ("**Lock-up Agreement**") with Port Otago Limited ("**Port Otago**") to acquire Port Otago's 15,825,477 shares in LPC, representing 15.48% of the total shares on issue. Assuming a limited number of conditions are met, the Lock-up Agreement requires Port Otago to accept the Offer.

The Offer is at a cash price of $3.95 ("**Offer Price**"), and is subject to the condition that LPC declares and pays a dividend of 20 cents per share (with full imputation credits attached to the extent available) prior to the closing date of the Offer ("**Special Dividend**"). If the Offer is declared unconditional and proceeds, LPC shareholders who accept the Offer will receive both the Offer Price and the Special Dividend, providing an effective total consideration (for shareholders who can fully utilise the imputation credits) of $4.15 per share ("**Total Offer Consideration**").

CCHL's Offer was sent to LPC shareholders on 25 August 2014, and will remain open for acceptance until 23 September 2014.

1.2 Offer Conditions

The Offer is subject to a number of conditions, the full details of which are set out in the Offer document already sent to LPC shareholders. Key conditions are also summarised in Appendix 2 of this report. Each condition may be waived by CCHL, other than the conditions relating to:

- CCHL achieving acceptances that, when taken together with its current shareholding, will allow CCHL to hold or control 90.00% or more of the total voting rights in LPC. However, as described further in Section 1.4.2 below, we note that the satisfaction of this condition is effectively assured by the existence of the Lock-up Agreement with Port Otago.
- LPC declaring and paying the Special Dividend. We note that LPC's Board of Directors resolved on 1 September 2014 to declare payment of the Special Dividend, so this condition is highly likely to be satisfied.

The other Offer conditions (which are standard in a takeover offer of this type) are solely for the benefit of CCHL and are designed to protect CCHL from substantial changes to LPC or the markets within which LPC operates while the Offer is open for acceptance.

1.3 Requirements of the Takeovers Code

LPC is a "Code Company" for the purposes of the Takeovers Code ("**Code**"). CCHL's Offer and the Company's response to the Offer must therefore comply with the provisions set out in the Code.

Rule 21 of the Code requires the directors of LPC to obtain a report from an independent adviser on the merits of the Offer. The Company's directors requested Northington Partners Limited ("**Northington Partners**") to prepare the Rule 21 report, and our appointment was subsequently approved by the Takeovers Panel. Further details on the regulatory requirements and scope of this report are set out in Appendix 3.

This report will accompany the Target Company Statement to be sent to all LPC shareholders and sets out our opinion on the merits of CCHL's Offer. This report should not be used for any other purpose and should be read in conjunction with the declarations, qualifications and consents set out in Appendix 8.

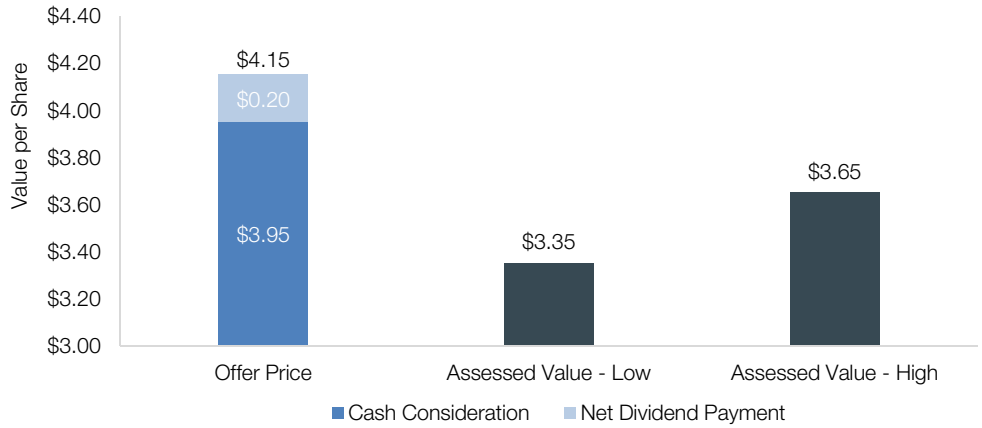
1.4 Summary of Our Assessment

1.4.1 Value of the Offer

In our opinion, the full underlying value of LPC's shares is in a range between $3.35 and $3.65 per share, with a mid-point value of $3.50 per share. This value range represents the value of acquiring 100% of the equity in LPC and therefore includes a premium for control. Our valuation range is determined primarily on the basis of a discounted cash flows ("**DCF**") approach, considering LPC's current financial position, future capital expenditure plans, earnings outlook and risk profile. Full details of our valuation approach and conclusions are set out in Section 4.0.

Figure 1 below compares the Total Offer Consideration with our assessment of the full underlying value of LPC's shares. The Total Offer Consideration of $4.15 per share is approximately 14% higher than the top end of our value range ($3.65 per share) and we therefore conclude that the Offer is fully priced.

Figure 1: Comparison of Total Offer Consideration to our Assessed Valuation Range



We suggest that the significant premium contained in the Total Offer Consideration could potentially be attributed to the additional value that CCHL needed to offer Port Otago in order to secure agreement to acquire its shares. As discussed in the following section, CCHL cannot move to a 100% ownership position without buying the Port Otago shares and CCHL may have determined that paying the premium for the shares it doesn't already own is more than compensated for by the strategic value gained by moving to 100% ownership.

1.4.2 90% Compulsory Acquisition Threshold

If all the conditions of the Offer are satisfied or waived by CCHL and the Offer is declared unconditional, the existence of the Lock-up Agreement with Port Otago means CCHL's control position in the Company will increase to at least 95.18%, exceeding the compulsory acquisition threshold of 90.00%. The extent to which CCHL's control position will exceed 95.18% will depend on the level of other LPC shareholders who accept the Offer.

If the Offer is declared unconditional, CCHL will be entitled to effect the compulsory acquisition provisions of the Code to acquire the remaining shares it was not able to acquire under the Offer. CCHL indicated in its Offer document that it intends to exercise this right, meaning that all LPC shareholders who do not sell their shares into the Offer will eventually be compelled to sell. As discussed further in the following section, the price paid to shareholders under the compulsory acquisition framework will be partly dependent on the level of acceptances under the Offer.

After the compulsory acquisition procedure is completed, LPC will be delisted from the NZX Main Board and be wholly-owned by CCHL.

1.4.3 Price Paid Under Compulsory Acquisition Procedure

LPC shareholders initially have the option to either accept or reject the Offer. Shareholders that accept the Offer will receive the Offer Price and will have no involvement in the compulsory acquisition process.

Shareholders can reject the Offer by doing nothing and waiting for the compulsory acquisition process to take its course. The timeframes for the process and the rights and obligations of all relevant parties are tightly prescribed. In this particular case, CCHL will be compelled to send an acquisition notice to the outstanding shareholders (who do not accept the Offer) no later than 30 days after the Offer period ends. Among other things, the acquisition notice will state that the price offered for the outstanding shares under the compulsory acquisition process will be the same as the Offer Price.

The final consideration paid for the shares and the alternatives available to outstanding shareholders at this point are however dependent on whether CCHL receives acceptances for more than 50% of the shares that are subject to the Offer. The possible outcomes are as follows:

- Acceptances Exceed 50%: In this case, LPC shareholders who do not accept the Offer must sell their shares to CCHL at the Offer Price. Under the Code, there is no right to object to the price that will be paid.
- Acceptances for 50% or Less: LPC shareholders have 14 days after the dispatch of the acquisition notice to send written objections to CCHL. If objections are received by shareholders that own the lesser of:
  - 2% or more of all LPC shares; or
  - 10% or more of the shares outstanding at the conclusion of the Offer period,

  then the Takeovers Panel will appoint an independent expert to determine the "fair and reasonable" value of the shares ("Expert Value Determination"). This value will be the total consideration that is paid for all LPC shares that are acquired under the compulsory acquisition process.

If the price determined by the independent expert is more than the Offer Price per share, then the additional amount will be immediately payable by CCHL to all LPC shareholders who did not accept the

Offer. Conversely, if the price determined by the independent expert is less than the Offer Price per share, then CCHL may recover the difference from all outstanding LPC shareholders (i.e. outstanding LPC shareholders would be paid less than the Offer Price).

Importantly in this case, the calculations used to determine whether acceptances received under the Offer have exceeded the 50% threshold exclude the shareholding in LPC owned by Port Otago (given Port Otago is regarded as an "associate" of CCHL for the purposes of the Code). The combined shareholding of CCHL (79.70%) and Port Otago (15.48%) amounts to 95.18% of the total shares on issue, and acceptances will therefore exceed the 50% threshold if LPC shareholders holding more than 2.41% of the total shares on issue accept the Offer (i.e. being more than 50% of the 4.82% of shares not currently owned or controlled by CCHL and Port Otago).

If acceptances under the Offer are lower than 50% of the shares subject to the Offer (excluding the Port Otago shares), then it will only take objections from a relatively small number of objecting shareholders to require the Expert Value Determination. For example, assuming that acceptances are received for 40% of the 4,935,945 shares outstanding, then objections from shareholders with more than 296,157 shares will be sufficient to trigger the process (based on 10% of the 2,961,567 (60%) shares that did not accept the Offer). We note that one individual shareholder holds 555,000 of the shares subject to the Offer, and would therefore be in a position to unilaterally exceed the 10% objection threshold and require an Expert Value Determination under this scenario[1].

1.4.4 Likelihood of Alternative Offers

In our view, the likelihood of an alternative offer emerging for LPC is virtually nil. If CCHL declares the Offer unconditional, CCHL will hold or control at least 95.18% of the shares in the Company and any alternative takeover offer would therefore require the support of CCHL. For CCHL to sell into such an alternative offer would constitute a significant about-turn; it has clearly signalled through the Offer that it intends to invoke the compulsory acquisition procedures of the Code to ensure that LPC will become a wholly-owned subsidiary.

1.4.5 Summary of our Assessment

Given the circumstances of the Offer, the potential outcomes are very limited. If the Offer is declared unconditional, CCHL will exercise its right to compulsorily acquire any shares that remain outstanding when the Offer closes. Shareholders who do not accept the Offer will therefore ultimately be compelled to sell their shares to CCHL. The only uncertainty relates to:

- Whether shareholders will be paid the Offer Price of $3.95 per share or an alternative price set pursuant to an Expert Value Determination; and
- The timing of the payment for the shares.

When determining whether or not to accept the Offer, shareholders need to form a view as to the likelihood that a sufficient number of shareholders will both reject the Offer, object to the Offer Price of $3.95 per share, and that the subsequent Expert Value Determination will exceed the Offer Price. Our mid-point valuation assessment (summarised above in Section 1.4.1) of $3.50 per share is significantly lower than the Total Offer Consideration of $4.15 per share[2]. While other independent experts may have

[1] In fact, this individual shareholding will exceed the 10% threshold at any level of acceptances lower than 50%.
[2] If the Offer is declared unconditional, all shareholders will receive the fully imputed dividend of $0.20 per share, irrespective of whether they accept or reject the Offer. As our valuation is assessed prior to the payment of the Special Dividend, our mid-point valuation of $3.50 per share would reduce to $3.30 per share after the Special Dividend is paid. At that point in time, it is appropriate to compare our adjusted value of $3.30 per share to the Offer Price of $3.95 per share.

different views to ours, we suggest that there is a material risk that the Expert Value Determination will be lower than the Offer Price.

We therefore suggest that shareholders who are comfortable that the Offer Price of $3.95 per share exceeds the underlying fair value of the shares should accept the Offer. This will ensure that payment is received in the shortest possible timeframe and eliminates the risk that the eventual payment received for the shares is lower than the Offer Price (as could be the case under the compulsory acquisition process outlined above in Section 1.4.3).

1.4.6 Acceptance or Rejection of the Offer

This report represents one source of information that LPC shareholders may wish to consider when forming their own view on whether to accept or reject the Offer. It is not possible to contemplate all shareholders' personal circumstances or investment objectives and our assessment is therefore general in nature. The appropriate course of action for each shareholder is dependent on their own unique situation. If appropriate, shareholders should consult their own professional adviser(s).

2.0 Industry Background

2.1 Global Seaborne Trade

More than 80 per cent of global merchandise trade by volume is carried by sea and handled by ports worldwide. The trade competitiveness of most countries depends heavily on effective access to international shipping services and port networks.

The annual volume of global seaborne cargo is estimated to have reached over 9 billion tonnes for the first time in 2012, having expanded on average by 3.1 per cent every year since 1970[3]. At this pace, and assuming no major upheaval in the world economy, global seaborne trade is expected to increase by 36 per cent by 2020 and to double by 2033. While bulk trade accounts for the largest share of global seaborne trade by volume, the containerized cargo contribution grew more than threefold between 1985 and 2010[4].

Developing countries are driving growth in global merchandise trade, with intra-Asian and South-South links emerging strongly. Africa and Latin America are increasingly becoming suppliers of China's primary commodity needs and, in return, China's consumer goods are being exported more and more to these regions. These developments are shaping the configuration of maritime transportation and placing unprecedented pressure on ports worldwide, with congestion and delays now common occurrences. Although significant infrastructure investment is required to alleviate these problems, it is expected that congestion and schedule pressure will remain an issue for some time because of the high capital costs and long lead time required for port development.

Despite the growth in trade, seaborne trade nevertheless remains subject to some persistent downside risks affecting the world economy and trade. Freight rates have remained low and volatile in the various market segments (container, liquid and dry bulk).

2.2 Trends in Global Shipping

Despite the very small size of its market, New Zealand is serviced by a significant number of international shipping companies and is therefore heavily affected by trends in global shipping. Some of the major trends being observed in the global shipping industry at present are as follows:

- Overcapacity: Following the global financial crisis ("GFC"), there has been significant overcapacity in shipping. Collectively, shipping lines incurred losses of US$10 billion in 2009 and, with difficulty implementing rate rises, have struggled to remain profitable since[5]. Shipping lines have laid up ships, formed alliances, implemented slow-steaming to reduce fuel costs and deployed larger ships to improve profitability.
- Larger Vessels and Deeper Draught Requirements: Shipping companies are moving to larger vessels to increase capacity and profitability. This will likely result in fewer shipping line operators visiting fewer New Zealand ports because not all ports are capable of handling larger vessels without significant additional capital expenditure.
- Cargo Consolidation: Cargo consolidation over a smaller number of ports lowers the operating and administration costs for shipping companies. This has led the shipping companies to

[3] UNCTAD, Review of Maritime Transport 2013
[4] Ibid
[5] Source: Rockpoint Corporate Finance Limited

develop regional hubs which serve as the single port for each region, with cargo transported within the regions using rail, road, or coastal shipping alternatives.

- **Consolidation of Ownership:** Consolidation in the container shipping industry, such as Maersk Sealand's acquisition of P&O Nedlloyd and TUI's (parent of Hapag-Lloyd) acquisition of CP Ships, has resulted in major changes to existing shipping links over recent years. These changes affect port calls, ship frequency, and cooperation arrangements.
- **Increased Specialisation:** Increased specialisation is occurring in the areas of ownership, equipment and cargo.

2.3 Shipping in New Zealand

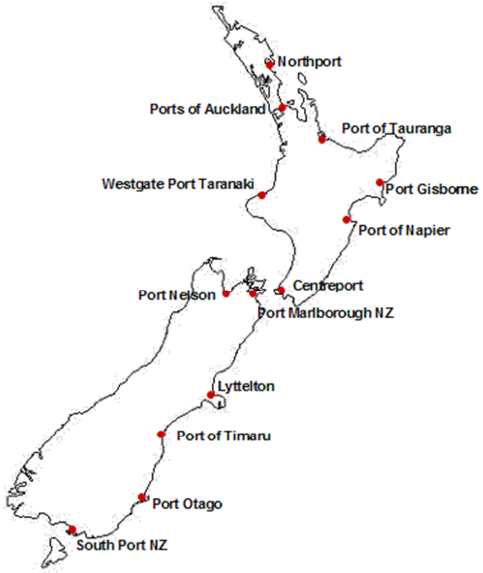
Close to 99% of New Zealand's imports and exports by volume are transported to market by sea. In 2012/13, 850 foreign cargo vessels made 4,978 visits to New Zealand ports[6]. The top 10 shipping lines account for the vast majority of port calls and ship capacity for container cargo (excluding specialised bulk ships for forest products, mineral fuels, and vehicles).

Foreign shipping lines handle virtually all of New Zealand's international seaborne cargo, which totalled approximately 59 million tonnes for the year ended 30 June 2014. Around 74% of the domestic coastal traffic is carried by international shipping lines transiting the New Zealand coast, with the remaining 26% being carried by domestic shipping lines[7].

2.4 Current Competitive Environment for New Zealand Ports

Figure 2 shows the locations of the major commercial ports currently operating in New Zealand. While all ports have some form of Local Authority ownership, four ports are partially privatised and are publicly traded. These are Northport, Port of Tauranga ("**POT**"), LPC, and South Port.

Figure 2: New Zealand Major Commercial Ports



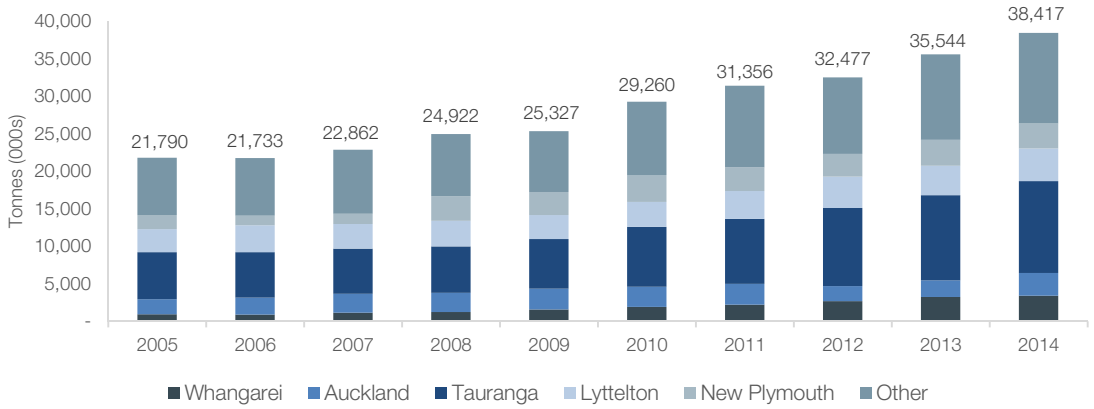
Over the last 10 years, New Zealand's growth in international trade has been driven primarily by exports. Total export volumes grew at a compound average growth rate ("**CAGR**") of 6.5%, growing from around

[6] Source: Maritime New Zealand
[7] Ministry of Transport

21.8 million tonnes in 2005 to 38.4 million tonnes in 2014. By contrast, imports grew from around 19.1 million tonnes in 2005 to 20.8 million tonnes in 2014, a far more modest CAGR of 1% over the 10 year period.

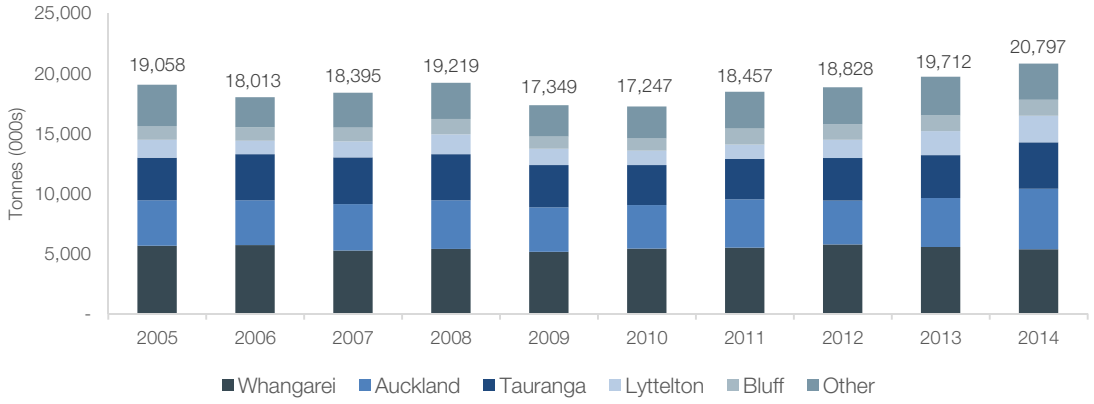
Figure 3 and Figure 4 below summarise the growth in international trade, split between the largest of New Zealand's commercial ports. A particularly notable feature is the near doubling of export volumes through POT.

Figure 3: Port Exports by Port (2005-2014)



Source: Statistics New Zealand

Figure 4: Port Imports by Port (2005-2014)



Source: Statistics New Zealand

Table 1 below provides an indication of the relative market share of the international trade (by volume) for each of New Zealand's major commercial ports for the year to June 2014. We note that these statistics do not include domestic trade volumes and should therefore only be used to provide a guide to the relative size of each port.

Table 1: Port Share of International Trade by Volume (Year to June 2014)

	Trade Volume (000 tonnes)			Relative Market Share (%)		
Region	Import	Export	Total	Import	Export	Total
Northport	5,358	3,407	8,765	26%	9%	15%
Auckland	5,029	3,020	8,049	24%	8%	14%
Tauranga	3,853	12,232	16,086	19%	32%	27%
New Plymouth	657	3,356	4,014	3%	9%	7%
Gisborne	-	2,312	2,312	0%	6%	4%
Napier	475	3,100	3,575	2%	8%	6%
Wellington	939	1,153	2,093	5%	3%	4%
Nelson	143	1,076	1,218	1%	3%	2%
Picton	-	655	655	0%	2%	1%
Lyttelton	2,222	4,342	6,564	11%	11%	11%
Timaru	548	603	1,151	3%	2%	2%
Otago	235	1,721	1,956	1%	4%	3%
South Port	1,338	985	2,323	6%	3%	4%
Other	-	455	455	0%	1%	1%
Total	**20,797**	**38,417**	**59,215**	**100%**	**100%**	**100%**

Source: Statistics New Zealand

Although there is limited competition between ports for bulk trades (with the exception being major capital projects such as Holcim (New Zealand) Limited choosing Timaru and Auckland as the location for its two bulk imported cement terminals), competition is strong for container trade. The high level of competition is largely due to the following factors:

- Inter-port Substitution: New Zealand has a relatively high geographic density of ports, reflecting a lack of industry rationalisation following the establishment of efficient domestic road and rail links. This high density provides customers with the opportunity to switch between ports.
- Powerful Customers: Major importers and exporters, together with large international shipping lines, act as an effective constraint on the pricing and service levels of ports. Recent consolidation in the international shipping arena has served to increase the bargaining power of some shipping lines.
- Surplus Port Capacity: Many ports have relatively low average levels of utilisation and could accommodate higher volumes of cargo and vessels without the need for significant additional capital expenditure.

Being first port of call is becoming increasingly important with the trend to greater "hubbing" by shipping lines. Competition is most fierce between "port pairs". Port pairs are competing ports which are often played off against each other by shipping lines due to their regional proximity to each other. In New Zealand, the most intense competition exists between Auckland and Tauranga, Napier and Wellington, and Lyttelton and Otago.

2.5 Future Competitive Environment for New Zealand Ports

Some of the key issues that will affect the future competitive environment for New Zealand ports are set out below.

2.5.1 Containerisation of Cargos

New Zealand container volumes have grown by 2-3 times GDP growth over the last 10 years and this trend is expected to persist in the short to medium term. Increased containerisation of cargos requires ports to adapt to container-driven business and also affects the types of vessels using port facilities.

2.5.2 Hub Ports

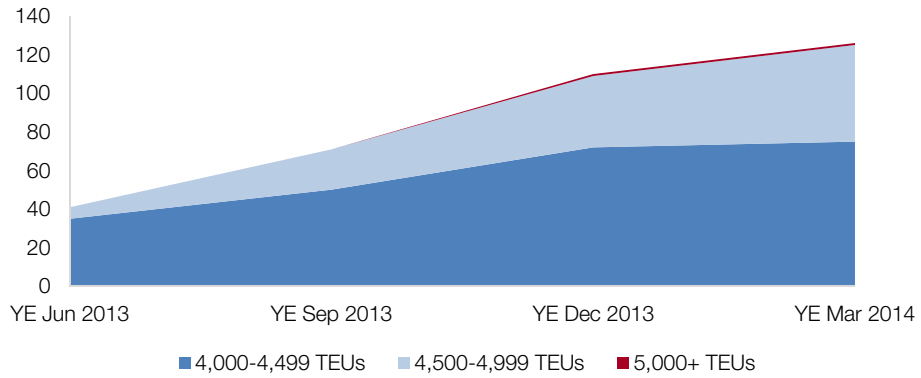
The current trend of hub ports is likely to continue to have material implications. Hub ports will be required to invest in additional capacity, while other ports will compete with road and rail to reposition to/from hub ports[8]. Following its recently approved $4.6 billion 10-year strategic investment plan[9], Kiwirail is likely to present a significant threat to many regional ports by offering high capacity rail connections for cargo consolidation onto larger ports. Investment is also likely to be required in coastal shipping.

2.5.3 Vessel Sizes

As noted earlier, in order to maximise efficiencies and economies of scale, international shipping lines are increasing the size of their vessels. Since 2004, the average container-carrying capacity of the largest ship in the 159 countries covered by UNCTAD's database has almost doubled (from 2,812 twenty foot equivalent units ("**TEUs**") 10 years ago to 5,540 TEUs in 2013), and the size of the largest existing ships has also almost doubled (from 8,238 TEUs to 16,020 TEUs)[10].

As demonstrated in Figure 5 below, the proportion of larger capacity ships visiting New Zealand ports has increased significantly over the last year, and included the first visit by a 5,000+ TEU vessel.

Figure 5: Port Calls (Unique Ship Visits) in New Zealand by Ship Capacity



Source: Ministry of Transport

Larger container vessels work to increasingly tight timetables, requiring very high levels of efficiency in the New Zealand ports that service them. A trend towards larger vessels creates issues for those ports that cannot currently accommodate them (either through lack of available wharves or channel depth).

[8] Rockpoint Corporate Finance Limited
[9] In 2010, the Government approved a $4.6 billion 10-year strategic plan for KiwiRail, with the principal objective of creating a sustainable rail freight business within a decade.
[10] UNCTAD, Review of Maritime Transport 2013

2.5.4 Forestry Industry Activity

Ports that rely heavily on the forestry trade face considerable difficulties in determining the investment required to meet the predicted "wall of wood". This uncertainty has not been assisted by the volatility of commodity prices and the current high New Zealand dollar.

2.5.5 Constraints on Port Expansion

New Zealand ports are typically located in central urban waterfront locations. They are therefore restricted in their ability to expand through either having no spare land or restrictions placed on their ability to reclaim land. Even where it is not urban pressures that place limits on the potential for expansion, simple geography may be a limiting factor. Restricted land transport links (both road and rail) are also viewed as a key current or potential constraint on increased activity.

2.5.6 Supply Chain Reconfiguration

Shippers have recently been more active in defining supply chains, a role traditionally provided by the shipping lines. An example is the agreement announced in June 2014 between freight and logistics company Kotahi (jointly owned by Fonterra and Silver Fern Farms), POT and PrimePort Timaru ("**Kotahi Agreement**").

Key aspects of the Kotahi Agreement, together with a separate long-term agreement between Kotahi and Maersk Line (the world's largest container shipping company), are as follows:

- Kotahi has committed to provide up to 1.8 million TEU export cargo containers to the Port of Tauranga over the next 10 years, commencing 1 August 2014;
- Kotahi has committed significant export cargo to Timaru Container Terminal Limited ("**TCTL**")[11], for the next 10 years commencing 1 August 2014;
- The Port of Tauranga has committed to investment in infrastructure to enable visits from the larger 6,500 TEU container ships within the next few years;
- Port of Tauranga will, subject to certain conditions, issue shares to Kotahi and Kotahi will take a stake in TCTL; and
- Kotahi has committed to provide up to 2.5 million TEU export cargo containers to Maersk Line for the next 10 years, commencing 1 August 2014.

[11] In August 2013, POT entered into a strategic alliance with PrimePort Timaru that resulted in POT acquiring container terminal operating assets of PrimePort. POT set up a new wholly-owned subsidiary, TCTL, to operate the terminal effective from 28 November 2013.

3.0 Profile of Lyttelton Port Company

3.1 Corporate History of LPC

The management of the harbour and port facilities in Lyttelton was originally the responsibility of the Lyttelton Harbour Board. The Harbour Board was established in 1877 and was responsible for the management of both the commercial and recreational facilities of the harbour. The Harbour Board consisted of 13 members elected at the Local Body Elections every three years.

Following the introduction of the Port Companies Act 1988, the commercial and non-trading (recreational and safety) roles of the Harbour Board were separated by forming LPC. The commercial assets, land and other facilities required to operate a commercial port were transferred from the Harbour Board to the Company. The Harbour Board was abolished in 1989 and the Company was charged to manage the port in the same manner as any other commercial business.

Upon its formation, the shares in LPC were allocated to regional and territorial authorities – the Ashburton, Banks Peninsula, Hurunui, Selwyn and Waimakariri District Councils and the Christchurch City Council. In 1996, the first moves were made to offer individual members of the public a shareholding in LPC with the decision by the Hurunui and Selwyn District Councils to sell their entire shareholdings in the Company and the decision by the Waimakariri District Council to sell part of its shareholding. To enable this to occur, LPC listed on the New Zealand Stock Exchange in July 1996 with a public float of 19% of the Company.

In April 1997, the Waimakariri District Council decided to sell the remainder of its shares and the Banks Peninsula District Council decided to sell all but a small number as well. As a result, the level of public shareholding rose to 25%. This was further increased to about 30% with the decision by the Ashburton District Council to sell half of its shares shortly thereafter.

Up until October 2005, the Christchurch City Council (via CCHL) had maintained a shareholding in LPC of 65%. In October 2005, CCHL entered into an arrangement with the Ashburton District Council to purchase its remaining 4% shareholding, thereby taking CCHL's shareholding in LPC to 69%.

In February 2006, CCHL made its first full takeover offer for all of the shares in LPC. The takeover was made in conjunction with Hong Kong-based Hutchison Port Holdings, a subsidiary of Hutchison Whampoa. Port Otago acquired a blocking stake in LPC during the offer period, and thereby effectively prevented the full takeover from proceeding.

Since the failed 2006 takeover attempt, CCHL used the Code's "creep" provisions[12] to acquire more shares in the Company, eventually allowing it to reach the 79.70% level it currently owns or controls.

3.2 Current Operations of LPC

As the major deep-water port in the South Island, Lyttelton plays a key role in the global transport network, offering a full range of worldwide shipping services. The operations of LPC comprise three distinct activities: container services, port services, and marine services. A summary of each activity is set out below.

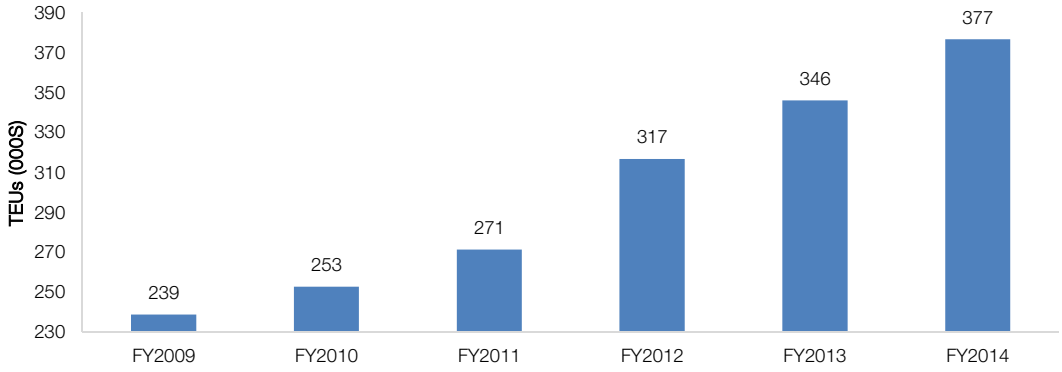
[12] The Code's creep provisions essentially allow a majority shareholder (holding more than 50% but less than 90% of a company's shares) to acquire in any one year up to an additional 5% shareholding without the requirement to make a takeover offer.

3.2.1 Container Services

The principal operations of the Container Services division centre around LPC's container terminal, which offers specialised cargo handling and stevedoring services for containers and bulk cargoes. The division also encompasses CityDepot, an inland port located at Woolston where services are provided for washing, repairing and storing containers as well as warehousing.

The container trade has grown significantly in recent years and has necessitated LPC making a greater investment in container facilities. As set out in Figure 6 below, during the period FY2009 to FY2014, LPC's container terminal throughput grew from 239,000 TEUs to 377,000 TEUs, a volume increase over the 5 year period of around 58%. This increase has arisen both from new business and generic growth based on a solid economic performance within the Canterbury region. Growth in the container terminal has been driven by a mixture of import and export volumes, with export growth coming from the immediate catchment area and also through Lyttelton being used as a point to consolidate cargo prior to shipping to hub ports in Asia.

Figure 6: LPC Container Terminal Throughput (FY2009 to FY2014)



Source: LPC

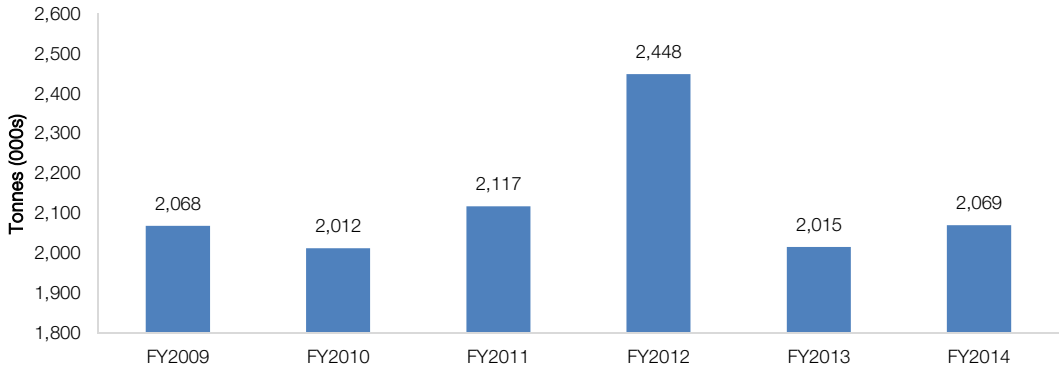
Although the Kotahi Agreement (see Section 2.5.6 above) is expected to negatively impact volumes by around 50,000 TEUs in FY2015, LPC expects that volumes will recover in the short-medium term on the back of on-going growth in global container trade. Strategies designed to support future growth are further discussed in Section 3.3 below, while the major risk factors that could limit increased volumes through the container terminal and the port generally are set out in Section 3.7.

3.2.2 Port Services

The Port Services division offers wharves, secure storage sheds, bulk discharge and other facilities for a wide range of conventionally stevedored cargoes.

Lyttelton is the biggest coal export port in New Zealand, moving around 2.07 million tonnes of coal in the year to 30 June 2014. The vast majority of LPC's coal volumes are based on a fixed term supply agreement with Solid Energy which commenced in 2003. As set out in Figure 7 below, although volumes generally trended up during the period FY2009 to FY2012, a significant decrease was experienced in FY2013. The reduction in FY2013 volumes was directly attributable to the financial difficulties experienced by Solid Energy on the back of a sharp decline in international coking coal prices.

Figure 7: LPC Coal Volumes (FY2009 to FY2014)

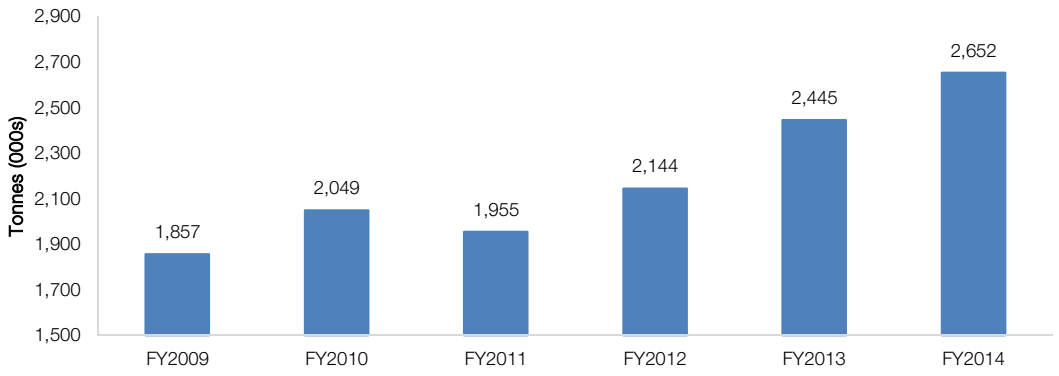


Source: LPC

Although coal volumes recovered slightly in FY2014, it is unlikely that volumes will increase materially in the short term without a recovery in coal prices.

Other trades within the Port Services division relate predominantly to bulk fuel, dry bulk cargo (fertiliser, cement, and grains), cars, logs, and fishing. As set out in Figure 8 below, bulk goods volumes increased from 1.86 million tonnes in FY2009 to 2.65 million tonnes in FY2014. The major contributors to the increased volumes during this period included a significant uplift in export log volumes (which more than doubled on the back of strong international demand, and more recently as the result of harvesting wind-blown timber) and strong volumes of dry bulk cargo, particularly cement and fertiliser.

Figure 8: LPC Bulk Goods Volumes (FY2009 to FY2014)



Source: LPC

3.2.3 Marine Services

The Marine Services division provides water-based services to LPC customers, such as berthage, piloting, towage and navigation services within the harbour. Dredging, dry dock bookings and marine safety are also part of the Marine Services operations.

3.3 Rebuilding the Port

3.3.1 The Impact of the Canterbury Earthquakes

The Canterbury earthquakes of 2010 and 2011 significantly damaged LPC's physical infrastructure and reduced its ability to operate efficiently. Damage to key infrastructure included:

- Wharves moved seawards, seawalls and landward ends slumped, piles, beams and tiebacks fractured and paved container-handling areas suffered extensive damage.
- At Cashin Quay (container terminal), the container cranes jolted off their rails, berth pockets were in-filled, and the breakwater at the seaward end slumped.
- Z Berth was severely impacted, and the foundations of the Independent Fisheries cool store were destroyed.
- At CityDepot, paving cracked and buildings were structurally damaged.

Although emergency repairs to critical infrastructure were completed in order to maintain port operations, many of the remediation measures have been temporary in nature. As previously discussed, container volumes have increased considerably since the earthquakes to the point where there is currently significant pressure on the port's now fragile infrastructure. With further growth in freight volumes predicted in the medium term, it is critical that the recovery of the port is advanced quickly and effectively so that LPC can continue to support Canterbury's economy.

3.3.2 Lyttelton Port Recovery Plan

In June 2014, Earthquake Recovery Minister Gerry Brownlee announced he would use powers conferred under the Canterbury Earthquake Recovery Act 2011 to fast-track the redevelopment of the port. A direction was issued to Environment Canterbury ("**ECan**") and LPC to develop a recovery plan ("**Recovery Plan**"), which would side-track the standard processes required under the Resource Management Act 1991.

The Recovery Plan will be developed in three phases, as set out in Table 2 below.

Table 2: Lyttelton Port Recovery Plan Process

Phase 1 (June –October 2014)	Phase 2 (October 2014 – July 2015)	Phase 3 (July 2015 onwards)
LPC lead: ▪ Development of a long term vision for the repair, rebuild, restoration and enhancement of the port ▪ Consultation with stakeholders and the community ▪ Presentation of a proposal to ECan (with accompanying data, technical reports, impact assessments, consultation reports, and suggested staging and funding of the proposal)	ECan lead: ▪ Development of a preliminary draft Recovery Plan ▪ Consultation with stakeholders and the community ▪ Hearing process on the preliminary draft Recovery Plan ▪ Finalisation of a draft Recovery Plan ▪ Submission of the draft Recovery Plan to the Earthquake Recovery Minister	Earthquake Recovery Minister lead: ▪ Public notification of the draft Recovery Plan ▪ Written comments invited from the public ▪ Finalisation of the Recovery Plan ▪ Public notification of the final Recovery Plan ▪ Implementation of the final Recovery Plan

Source: ECan

The first phase of the Recovery Plan process is well underway, with the release in late June 2014 of LPC's long-term vision for the port ("**Port Lyttelton Plan**"). Currently open for public submissions, key aspects of the Port Lyttelton Plan include:

- A $1 billion development plan;
- Reclamation of land to the east of the port (into Te Awaparahi Bay) for a new container terminal (which could take up to 15 years to complete); and
- Better public access to the western side of the port where a new marina and commercial development complex is proposed.

With container volumes through Lyttelton expected to double within a decade, and then double again by 2041, the proposed new container terminal underpins all aspects of the Port Lyttelton Plan and is central to the aim of alleviating capacity constraints that would otherwise exist. The new terminal would be designed to handle greater freight volumes and the possible growth in container-ship size, and would also allow some of the port's general cargo operations to move from the inner harbour onto the current container terminal at Cashin Quay.

The initial land reclamation work to enable the new terminal has covered over 6.0 hectares, with on-going work expected to expand the total area to 10 hectares. However, the long term plan is much bigger and over time LPC hopes the port will expand by 35 hectares.

In addition to the plans for the waterfront facilities set out in the Port Lyttelton Plan, LPC is also improving the capacity of its inland port, CityDepot in Woolston. Planning is also underway for another inland port at Rolleston. Both inland ports are part of LPC's long-term planning to meet future freight demands, and it is envisaged they will offer improved levels of freight efficiency through the use of rail infrastructure to transfer cargo from truck to train for the final leg into Lyttelton.

3.4 Capital Structure and Ownership

As at 7 August 2014, LPC had 102,261,279 ordinary shares on issue held by approximately 775 shareholders. The Company's top 10 shareholders are set out in Table 3 below. LPC is obviously very closely held, with the top two shareholders owning more than 95% of the Company's shares.

Table 3: Top 10 Shareholders

	Shareholder	Number of Shares Held	Shareholding Percentage
1	Christchurch City Holdings Limited	81,499,857	79.70%
2	Port Otago Limited	15,825,477	15.48%
3	Michael Walter Daniel, Nigel Geoffrey Burton & Michael Murray Benjamin	555,000	0.54%
4	Custodial Services Limited	140,597	0.14%
5	Gordon Mervyn Kelly	127,000	0.12%
6	Louise Isabel Gobby & William Alexander Gillespie	92,000	0.09%
7	New Zealand Central Securities Depository Limited	91,208	0.09%

Table 3: Top 10 Shareholders (Continued)

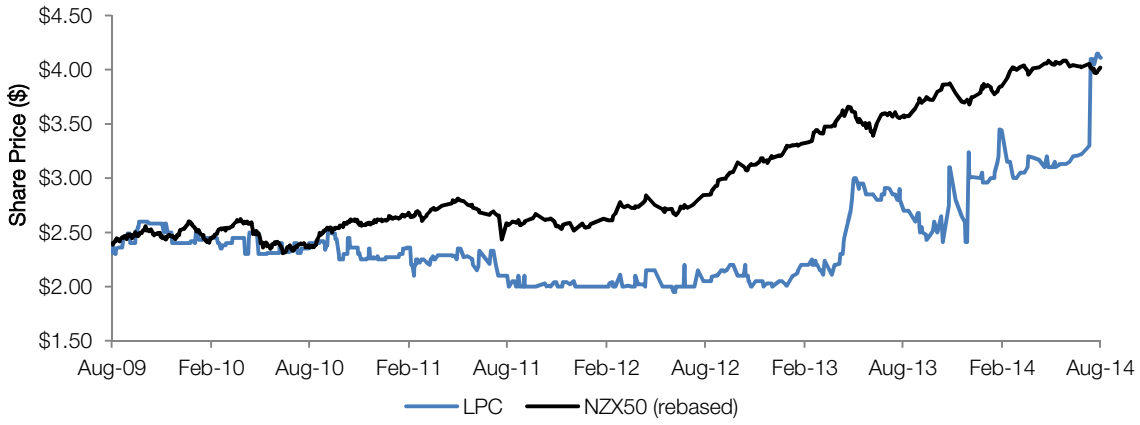
	Shareholder	Number of Shares Held	Shareholding Percentage
8	FNZ Custodians Limited	80,400	0.08%
9	UBS New Zealand Limited	76,892	0.08%
10	Frank Stewart & Carol Blake Stewart	70,000	0.07%
	Top 10 Shareholders	**98,558,431**	**96.38%**
	Remaining Shareholders	3,702,848	3.62%
	Total Shares on Issue	**102,261,279**	**100.00%**

Source: LPC

3.5 Share Price Performance and Liquidity

The performance of LPC's shares since August 2009 relative to the NZX50 Index is shown below in Figure 9. LPC's share price generally underperformed the index over this five year period, as the market reacted to the Company's significant challenges following the Canterbury earthquakes. As repair work began, LPC's insurance position has been worked through, and the longer term plans and outlook for the port became better understood, the gap in share price performance relative to the index narrowed slightly. That gap has subsequently closed on the back of the spike in the share price following the release of CCHL's Takeover Notice.

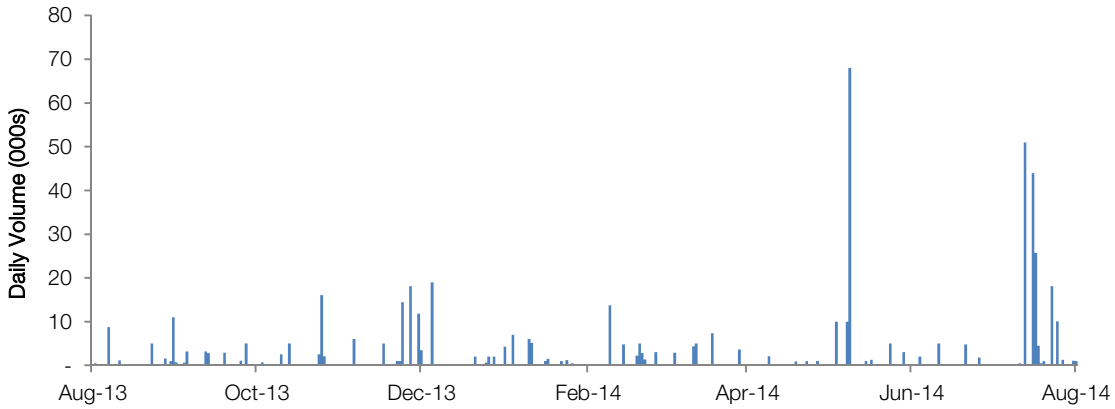
Figure 9: LPC Share Price Performance Relative to NZX50 Index



Source: Capital IQ / Northington Partners' analysis

Given the significant shareholding in LPC held by each of CCHL and Port Otago, the Company's shares have historically suffered from low liquidity. Figure 10 below sets out the daily trading volumes in LPC's shares during the 12 month period to August 2014, showing many days without any trades and typically low volumes on the days when trading did take place.

Figure 10: LPC Share Liquidity



Source: Capital IQ / Northington Partners' analysis

Further details on the liquidity of LPC's shares during the last 12 months are set out in Table 4 below.

Table 4: LPC Share Liquidity Last 12 Months

	12 Months to 20 August 2014
Average Daily Share Trading Volume	2,080
Total Shares Traded	524,240
Shares on Issue	102,261,279
Total Volume / Shares on Issue	0.51%

Source: Capital IQ / Northington Partners' analysis

Share price performance over the last six months is shown in Figure 11, while the Volume Weighted Average Price ("VWAP") for a number of observation periods prior to the announcement of the Offer is summarised in Table 5. LPC shares have generally traded in a range between $3.10 and $3.20 per share over the period.

Figure 11: LPC Share Price Performance – Last Six Months

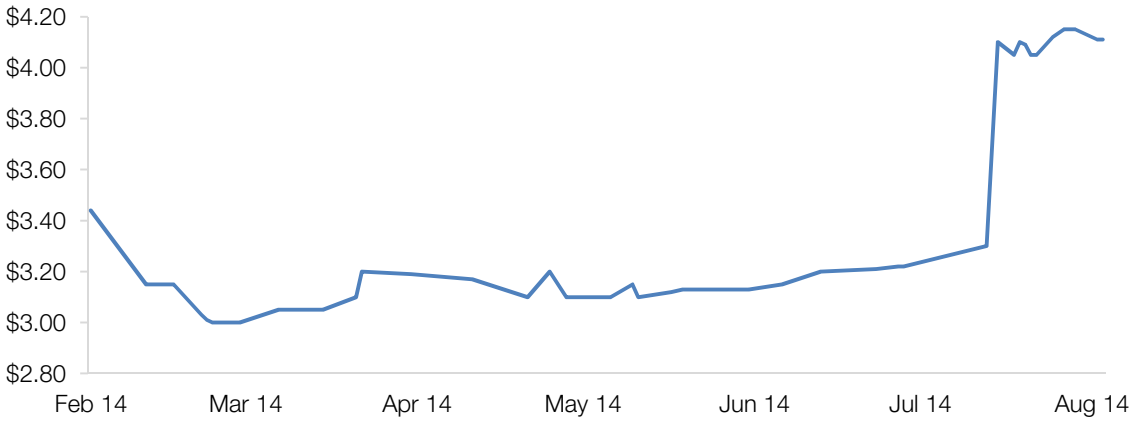


Table 5: LPC Volume Weighted Average Price (to 1 August 2014)

	Last 6 Months	Last 3 Months	Last Month
Volume Weighted Average Price	$3.11	$3.12	$3.22

Source: Capital IQ as at 20 August 2014

3.6 Financial Information

3.6.1 Financial Performance

A summary of the financial performance of LPC for the five year period between FY2010 and FY2014 is set out in Table 6 below.

Table 6: LPC Historical Financial Performance

	12 months 30 June 2010 ($000)	12 months 30 June 2011 ($000)	12 months 30 June 2012 ($000)	12 months 30 June 2013 ($000)	12 months 30 June 2014 ($000)
Revenue	**87,327**	**91,625**	**104,546**	**110,657**	**115,823**
Employee expenses	(34,289)	(36,507)	(40,488)	(42,357)	(47,267)
Materials and consumables	(19,216)	(17,165)	(22,646)	(25,668)	(28,761)
Administrative and other expenses	(4,581)	(5,724)	(6,688)	(6,925)	(6,825)
EBITDA	**29,241**	**32,229**	**34,724**	**35,707**	**32,970**
Depreciation and amortisation	(11,945)	(11,564)	(10,928)	(10,911)	(11,042)
EBIT	**17,296**	**20,665**	**23,796**	**24,796**	**21,928**
Effect of Canterbury earthquakes					
Additional costs	-	(12,375)	(15,222)	(8,002)	(15,054)
Insurance proceeds received	-	46,288	18,379	16,103	357,612
Depreciation on Earthquake Assets	-	-	-	(4,664)	(4,664)
Assets written off / derecognised	-	(28,988)	-	-	(1,109)
EBIT (Reported)[1]	**17,296**	**25,590**	**26,953**	**28,233**	**358,713**
Net financing expenses	(3,866)	(4,551)	(3,567)	(3,578)	3,241
Changes in fair value of cash flow hedges	(72)	204	(415)	1,176	684
Profit Before Tax	**13,358**	**21,243**	**22,971**	**25,831**	**362,638**
Income tax credit / (expense)	(4,422)	3,072	(6,183)	(7,742)	(18,728)
Profit After Tax	**8,936**	**24,315**	**16,788**	**18,089**	**343,910**

Source: LPC Audited Financial Statements (FY2010-FY2014).

1. EBIT post effect of Canterbury earthquakes

The main features of LPC's historical financial performance can be summarised as follows:

- In recent years LPC has demonstrated steady revenue growth (FY2010 - FY2014 CAGR of 7.3%) as a result of increased container and bulk goods volumes (including fuel, logs, dry goods and vehicles).
- Notwithstanding materially lower coal volumes, LPC achieved annual revenue growth of around 5% in FY2014, driven primarily by solid container and bulk volumes. FY2014 EBITDA (excluding the impact of insurance settlements) is marginally lower than FY2013 due to increased expenditure on several initiatives in areas including health and safety, capacity and productivity.
- A significant feature of LPC's accounts in the last four years has been the various adjustments made to reflect the effect of the Canterbury earthquakes. LPC received an insurance settlement

payment of $357m (of a total settlement of $438m) in FY2014, significantly distorting LPC's reported net profit in that year.

3.6.2 Financial Position

Table 7 summarises LPC's financial position for the last five years.

Table 7: LPC Statement of Historical Financial Position

	30 June 2010 ($000)	30 June 2011 ($000)	30 June 2012 ($000)	30 June 2013 ($000)	30 June 2014 ($000)
Assets					
Cash	168	692	1,153	969	322,174
Insurance Receivable	-	-	28,971	27,684	-
Trade and other receivables	12,752	22,958	14,321	14,988	16,340
Property, Plant & Equipment	210,220	201,361	216,901	215,164	248,914
Other Assets	9,367	11,901	12,190	11,872	10,038
Total Assets	**232,507**	**236,912**	**273,536**	**270,677**	**597,466**
Liabilities					
Trade and other payables	8,151	12,058	10,304	10,887	13,932
Employee entitlements	5,697	7,363	8,206	7,745	8,302
Loans and borrowings	57,912	40,752	55,925	30,570	-
Deferred tax liabilities	14,986	12,116	18,139	24,977	34,456
Other liabilities	11,908	9,420	8,971	6,419	7,655
Total Liabilities	**98,654**	**81,709**	**101,545**	**80,598**	**64,345**
Equity					
Share Capital	21,457	21,457	21,457	21,457	21,457
Hedging reserve	(2,967)	(2,763)	(3,178)	(2,003)	(141)
Retained earnings	115,363	136,509	153,712	170,625	511,805
Total Equity	**133,853**	**155,203**	**171,991**	**190,079**	**533,121**

Source: LPC Audited Financial Statements (FY2010-FY2014).

The main features of LPC's financial position are summarised as follows:

- The significant current cash balance as at 30 June 2014. This represents the remaining cash from the insurance settlement received in February 2014, and will be used to fund the significant capital expenditure requirements over the next 10 years.
- LPC was carrying approximately $36.5m of bank debt when the cash settlement was received. Part of the proceeds was used to pay down the debt and the Company is now debt free.

3.6.3 Cash Flows

Table 8 below summarises LPC's historical cash flows for the period FY2010 to FY2014.

Table 8: LPC Statement of Historical Cash Flows

	12 months 30 June 2010 ($000)	12 months 30 June 2011 ($000)	12 months 30 June 2012 ($000)	12 months 30 June 2013 ($000)	12 months 30 June 2014 ($000)
Cash receipts from customers	84,829	91,086	101,728	109,072	115,672
Cash paid to suppliers and employees	(56,828)	(56,988)	(71,261)	(77,265)	(86,965)
Net proceeds as a result of Canterbury earthquakes	-	23,321	(15,222)	9,392	370,242
Net Interest	(3,866)	(4,595)	(3,561)	(3,754)	1,173
Income tax paid	(4,333)	(4,382)	(274)	28	(3,269)
Net Cash from Operating Activities	**19,802**	**48,442**	**11,410**	**37,473**	**396,853**
Proceeds from sale of PP&E	3	135	59	46	65
Acquisition of property, plant and equipment	(15,147)	(27,826)	(25,911)	(11,486)	(42,435)
Acquisition of intangible assets	(258)	(102)	(270)	(863)	(762)
Other	-	-	-	-	-
Net Cash from Investing Activities	**(15,402)**	**(27,793)**	**(26,122)**	**(12,303)**	**(43,132)**
(Repayments) / proceeds of borrowings	776	(17,160)	15,173	(25,355)	(30,470)
Dividends paid	(5,011)	(2,965)	-	-	(2,046)
Net cash from Financing Activities	**(4,235)**	**(20,125)**	**15,173**	**(25,355)**	**(32,516)**
Net Cash Flow	**165**	**524**	**461**	**(185)**	**321,205**

Source: LPC Audited Financial Statements (FY2010-FY2014).

The impact of the earthquakes has had a material impact on operating cash flows since FY2011, with net proceeds of about $17.5m in the three years prior to the large settlement in FY2014. Because capital expenditure increased markedly above "standard" levels in both FY2011 and FY2012, LPC has not paid a dividend since FY2011.

3.7 Key Issues and Outlook

3.7.1 Capacity Constraints and the Recovery Plan

Following the Canterbury earthquakes, increased container volumes have placed significant pressure on the port's fragile infrastructure. Significant capacity constraints are expected to materialise unless the recovery of the port is advanced quickly and effectively. The Port Lyttelton Plan (the first phase of the Recovery Plan process) contemplates a step-change in the ability of the port to cater for increased growth through the development of a new, modern container terminal.

However, with a total capital expenditure budget potentially exceeding $1.0 billion over a 10-15 year period, the redevelopment plan is subject to a wide range of implementation risks. Additionally, if the new initiatives cannot be implemented in a timely fashion, short-term capacity constraints could become more pronounced and increase the risk that customers will seek alternative solutions.

3.7.2 Labour Relations / Health and Safety

Given the sheer size and diverse nature of port operations, there are a number of industry bodies that represent various sectors of the port workforce. While relations between ports and the unions have improved significantly over recent years, ports are still exposed to the significant financial impact of industrial disputes. That risk is clearly heightened for LPC as it introduces measures to improve efficiency in the container terminal, and continues to work hard to improve its health and safety record.

3.7.3 Port Access

Following earthquake damage to the Sumner road, LPC remains exposed to its reliance on the Lyttelton tunnel as the main access route to the port. The potential cost and timeframe for reopening the Sumner road remain uncertain, and there would be no practical alternative access to the port if the tunnel is closed for any reason. While the probability of a long-term tunnel closure is arguably low, the impact of such an event on LPC's operations and profitability would be severe.

3.7.4 Port Consolidation

Given global industry trends, many commentators still believe that port consolidation in New Zealand is inevitable in order to sustain long-term profitability. Despite the call for such reform from port customers, management and industry bodies, the attitudes of parochial shareholders could limit the prospects for rationalisation in the short term. Those ports that remain of the view that local ownership outweighs the market advantages of port consolidation run the risk of being excluded from the mix when the changes do occur. Some ports may be significantly affected by competitors that can utilise economies of scale to provide better prices and more extensive services to their customers.

The 2013 transaction between POT and PrimePort Timaru is one example where a smaller regional port has looked to strengthen its strategic position by developing a relationship with one of the larger operators. The recently announced alliance between Ports of Auckland and Napier Port has similar objectives. While LPC is not formally engaged in discussions with other port companies, it is definitely aware of the potential strategic benefits that may accrue from consolidation and believes it is well placed to feature in any significant initiatives that require a South Island partner.

4.0 Valuation of LPC

4.1 Valuation Summary

Our valuation assessment of LPC's business is primarily based on a DCF approach. The valuation model has an explicit forecast period of 10 years and is used to construct a projection for annual free cash flows for the LPC business. The value of all future cash flows after the 10-year projection period is incorporated via a terminal value calculation.

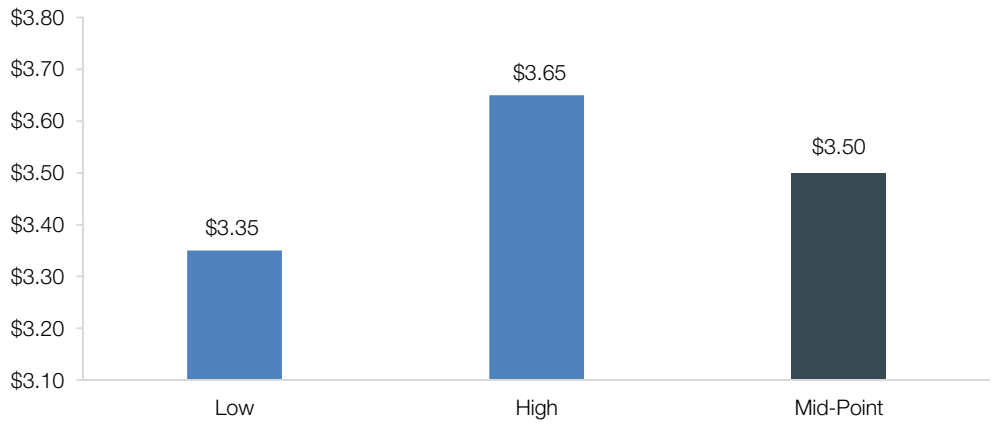
We have estimated a fair value range for LPC between $3.35 and $3.65 per share, assessed prior to allowance for the payment of the Special Dividend. A summary of the full acquisition value range is set out in Table 9 and Figure 12.

Table 9: Summary of Assessed LPC Value

Component	Low Value	High Value	Mid-Point Value
Total Enterprise / Equity Value	$342.6m	$373.3m	$358.3m
Number of Shares on Issue	102,261,279	102,261,279	102,261,279
Value per Share	**$3.35**	**$3.65**	**$3.50**

Source: Northington Partners analysis

Figure 12: Summary of Assessed LPC Value per Share



Source: Northington Partners analysis

We have also estimated some standard valuation multiples as the basis for a cross-check of the primary valuation range derived from the DCF model. Results from this analysis indicate that our assessed valuation range is appropriate when compared to the observed trading and transaction multiples for other port companies in New Zealand and overseas.

Details of our adopted valuation approach and assumptions are provided in the remainder of this section.

4.2 Valuation Methodology

In general terms, the value of equity in any company can be determined using a deductive approach that starts with an estimate of the underlying enterprise value. Enterprise value represents the aggregate value of the company's on-going operations assuming that the assets are entirely equity funded. In order to estimate the aggregate value of equity, the enterprise value is adjusted to account for the level of debt carried by the company and the values of any other assets and liabilities of the company that are not needed to maintain the core operations of the business.

A summary of the steps needed to estimate the aggregate equity value of LPC is set out in Table 10 below.

Table 10: General Framework for Assessing Equity Value

	Step	Comment
	Value of Operating Assets	Represents the aggregate value of the operating assets of the business. Can be estimated using a variety of methods (see discussion in Section 4.2.1 below).
Plus	Surplus Assets (if any)	The value of assets that are not required to support the on-going operation of the business and which can therefore be sold.
Less	Net Debt	Defined as interest-bearing debt less cash reserves.
Less	Other Liabilities (if any)	Accounts for other liabilities that would be borne by the new owner of the company, such as the net present cost of derivative exposures.
equals	Equity Value	Directly comparable to Market Capitalisation

In almost all cases, estimating enterprise value is the most difficult part of the process.

4.2.1 Alternative Methodologies

For a company viewed on a going-concern basis, enterprise value should be determined as a function of the estimated level of cash returns that the operating assets are expected to generate in the future. The specific approach that is used to estimate this value is dependent on the nature of the company and the expectations regarding future performance. The two main approaches usually adopted in the valuation of publicly listed companies are summarised as follows:

- Earnings Multiple: This method determines enterprise value by applying a valuation multiple to the assessed level of maintainable annual earnings (or cash flows), where the multiple is chosen to reflect the risk associated with the future performance of the business. Depending on the nature of the business, earnings can be appropriately measured at the EBITDA, EBITA, EBIT, or NPAT levels.
- Discounted Cash flows: A DCF approach is based on an explicit forecast of the annual cash flows that will be generated over a specified forecast period (typically between 5 and 10 years). The value of cash flows that may occur after the end of the explicit forecast period are incorporated into the valuation process by capitalising an estimate of maintainable cash flows for the terminal period. A DCF model is therefore usually made up of two components:
  - (i) The present value of the projected cash flows during the forecast period; and
  - (ii) The present value of all other cash flows projected to occur after the explicit forecast period. This component is commonly referred to as the terminal value.

Each approach has some advantages and disadvantages, and the most appropriate choice is dependent on the characteristics of the business under consideration and the quality of the market data that is available. The key advantage of the earnings multiple approach is its simplicity. Total enterprise value can be determined on the basis of the actual earnings results for the most recent financial reporting period or the

equivalent projection for next year. Companies with well-established operations should be in a position to supply reasonably reliable earnings projections for the next one or two years, and the valuation model is therefore only reliant on an independent assessment of the appropriate earnings multiple. Estimates of an appropriate multiple are typically based on data derived from other companies that are considered to be comparable to the target company in relation to growth prospects, capital expenditure requirements, and risk profiles.

Unfortunately, it is extremely rare that the target company will have any close comparables with respect to all of these important characteristics. In many cases, earnings multiples extracted from a set of businesses within exactly the same industry will have a wide range of values that reflect company specific factors rather than the underlying risk level of the industry itself. It then becomes a matter of judgement to make a series of adjustments to the implied multiples to properly account for the differences between the companies. These adjustments are often arbitrary and very difficult to benchmark.

In the majority of cases, the earnings multiple approach is therefore most suited to businesses with a relatively stable earnings outlook, low capital expenditure requirements, and limited growth opportunities. For companies with these characteristics, the multiples derived from market data are more likely to accurately reflect the market's perception of the underlying quality of the projected earnings stream.

The DCF approach can provide a better valuation treatment for companies with future growth prospects and high capital expenditure requirements. Because each of these factors can be explicitly incorporated into the valuation process, the DCF model directly accounts for many important value drivers of the business under consideration. Accessing the necessary data for a DCF model can however be problematic, especially when there is no credible process by which to construct the future forecasts of free cash flows. The discounting process is also reliant on an estimate for the required rate of return. Because this estimate is not directly observable and must be derived from data collected from other comparable companies, the DCF value is also reliant on the existence of other companies that have the same risk profile.

4.2.2 Preferred Valuation Approach

Given the significant level of capital expenditure projected over the next 10 years, we believe that a DCF approach is most appropriate for the LPC business. It is very difficult to accurately reflect the impact of these capital cash flows in a multiple-based approach.

A DCF approach allows direct consideration of the LPC cash flows and the changes that will occur with any significant changes to the operating environment. The main weakness of this approach is that it is quite sensitive to the assumed value for the required rate of return. Because this rate cannot be directly observed from either traded security prices or transactions, it must be estimated using a model or other assumptions that cannot be directly validated and which can easily produce a wide range of reasonable values.

4.3 Valuation of LPC Shares

4.3.1 Assessed Enterprise Value Range

We have determined the underlying enterprise value of LPC using a post-tax DCF model, based on an explicit forecast period of 10 years. The value of all future cash flows after the forecast period is incorporated via a terminal value calculation. Our assessment considers the going-concern value of LPC under its existing management and ownership structure, and reflects the value of a 100% control position.

Forecast Cash Flows

In simple terms, total standalone value is determined as the present value of all future cash flows that are expected to accrue to LPC, assuming that the company has no gearing. The impact of the target debt level

is incorporated into the valuation model via the required rate of return, which is based on the weighted average cost of debt and equity.

The construction of free cash flow estimates for valuation purposes uses the following steps.

Table 11: Free Cash Flow Framework

	Cash Flow Item	Comment
	Revenue	Derived separately for each key business unit, with allowance for volume-driven increases and.
less	Operating Expenditure	Based on historical cost benchmarks, budgeted costs for FY2015 and allowances for future cost inflation.
equals	EBITDA	
less	Cash Tax Payments	Tax liability based on above EBITDA figure less an allowance for tax depreciation. There is no adjustment for any interest costs.
less	Capital Expenditure	Predominantly based on the CAPEX schedule prepared by LPC, reflecting the current remediation program.
equals	Free Cash flow	Cash flow available to service both debt and equity providers.

Inputs for the forecast cash flow model have been largely drawn from the existing LPC budget models and long-term planning documents. All key assumptions have been discussed with LPC management, tested and benchmarked against actual results, and adjusted (where necessary) to reflect our views of appropriate inputs for the current valuation exercise.

A summary of the key variables and assumptions is set out in Table 12. The relative importance of each assumption can be deduced from the sensitivity analysis set out later in this section.

Table 12: DCF Model Key Assumption

Model Input	Assumed Value
Model Structure	Covers an explicit projection period of 10 years, with allowance for a terminal value to account for projected cash flows beyond year 10. Our assumed valuation date is 30 June 2014.
Port Prices	▪ Prices have been forecast separately for each of the main port services: Coal Terminal, Stevedoring, Wharfage, Birth Hire, Navigation, Towage and "Other". ▪ Price changes are generally in line with LPC budget for FY2015 and LPC projection for FY2016, after which we assume modest annual growth of 1.5%. This assumption reflects our expectation of continued competitive positioning by other New Zealand ports and on-going price pressure from LPC's customers. ▪ Pricing for the Coal Terminal is in line with the provisions of the Solid Energy contract, which expires in 2026. Under the contract, LPC receives an annual fixed payment as well as a volume-based payment (based on tonnage charges which will increase annually at prescribed rates).

Port Volumes	▪ Future volume growth for most LPC trades is ultimately linked to real GDP growth in the region, reflecting the long term trend that international port volumes have increased at the same rate as GDP.
	▪ Assumed volumes for FY2015 largely reflect LPC budgets. Key features include:
	  ▪ Container volumes reflect the anticipated impact of the Kotahi Agreement, assuming that the Fonterra volumes from its Clandeboye plant will be shipped through Timaru from 1 August 2014.
	  ▪ Coal volumes are based on Solid Energy projections and reflect a significant decrease from the FY2014 volume (by approximately 20%).
	  ▪ Fuel volumes for FY2015 are expected to be about 8% lower than FY2014 due to the temporary unavailability of part of the tank farm after land slip damage in March 2014.
	▪ Medium term coal volumes are highly uncertain, and will be dependent on both the future market price for coal and the strength of Solid Energy's recovery. We assume limited annual growth (2.0% per annum) from FY2016 onwards, and note that assumed volumes by the end of the projection period (1.9m tonnes) still remain below the volumes achieved over the previous 5 years (circa 2.1m tonnes).
	▪ Notwithstanding the impact of the Kotahi Agreement in FY2015, LPC expects container volumes to continue to grow strongly over the balance of the projection period (at an average annual growth rate of 4.5%). Our base case growth assumption is more conservative, with an average growth rate of 4.0%.
	▪ Bulk Fuel and Other Trade volumes are assumed to increase at 2.0% per year from FY2016 onwards.

Operating Costs	▪ Projected expenses are separated into Labour and Other Costs for each of the following categories: Container Terminal, Coal Facility, Facilities, Marine, Maintenance, Corporate & IT. Fixed and variable components are identified and the variable portion is driven by an appropriate volume driver (e.g. container volume for the container terminal). ▪ Resulting operating costs and EBITDA margins are then benchmarked against both historical results and LPC projections. LPC is currently focused on a major initiative to improve productivity (particularly in the container terminal) and is targeting an improvement in EBITDA margin. ▪ Our modelling assumes some improvement is achieved, but caps the maximum EBITDA margin at a level well below LPC's target.

Table 12: DCF Model Key Assumption (Continued)

Model Input	Assumed Value
Capital Expenditure	LPC has carried out extensive pre-feasibility work on the port remediation and development plan, and continues to refine its cost estimates for the capital program. Based on discussions with LPC, the overall capex plan has been split into two components: i. Replacement Capital: Relates to the replacement or repair of existing port infrastructure which has suffered earthquake damage, and which is needed to support on-going core operations over the projection period. Total projected cost is approximately $550m (including an allowance for contingencies and cost escalation), of which about $480m was still to be spent as at our valuation date. ii. Expansion Capital: Relates to a range of development projects which are designed to expand the port facilities and position LPC for longer-term volume growth. The expenditure is not needed to support the scale of business operations projected over the next 10 years. Total projected cost is approximately $650m (including an allowance for contingencies and cost escalation). Our valuation assessment incorporates the Replacement Capital only. While LPC is currently interested in pursuing the expansion projects, we believe that the eventual scope, timing and revenue implications of the developments are too uncertain to reliably incorporate into our valuation framework. Commitment to the Expansion Capital will remain conditional on LPC gaining sufficient comfort that future volume will eventually exceed the capacity that will be in place after the Replacement Capital program has been completed. In addition to the Replacement Capital, we also assume business-as-usual capex of $12.0m per annum.
Terminal Value Assessment	Terminal value is estimated as a multiple of maintainable operating cash flows, less an allowance for stay-in-business capital expenditure. Based on current evidence, we conservatively assume a multiple of 15x net cash flow (implied EBITDA multiple of close to 10x).
Treatment of Insurance Proceeds	As at 30 June 2014, LPC had a cash balance of approximately $322m, largely attributable to the net insurance settlement proceeds of $385.2m received in February 2014. From a valuation perspective, we have treated the cash as pre-funding for the earthquake remediation program and have included the forecast interest income on the cash balance as a revenue source. The interest income is very material at the start of the projection period (budget of around $9m in FY2015) and then declines through time as the cash is used to fund the capital expenditure program. This level of cash is obviously unusual and, if interpreted as a financing item, would be excluded from the valuation. However, because the insurance proceeds directly relate to the replacement of core operating assets, we believe that the benefit of the timing mismatch between the receipt of the insurance proceeds and the payment for the capital expenditure should be included in the valuation.
Other Issues	▪ LPC has a number of contingent cash flows relating to its final insurance arrangements, including some outstanding tax liabilities (in FY2015 and FY2019) associated with the cash settlement in FY2014. LPC has also previously publicly announced that there is one outstanding matter with a third party that may result in the Company making an additional recovery. Our projected cash flows are based on relatively conservative assumptions that have been determined in conjunction with LPC management. ▪ While LPC continues to evaluate the redevelopment of facilities to support cruise ship visits, we have not included any allowance for this potential investment. Plans remain highly uncertain and even if they are pursued, are unlikely to have a material impact on value.
Required Rate of Return	We have estimated the required rate of return for LPC using the standard Weighted Average Cost of Capital ("**WACC**") model. As discussed further below, we conclude that an appropriate post-tax cost of capital for LPC is 8.50%.

Required Rate of Return

Reliable transactional evidence relating to the market's required rate of return on businesses similar to LPC cannot be directly observed. It is also not possible to derive an estimate of the required return from the limited number of transactions that have occurred because the level of detailed information that is needed to support the calculation is not publicly available.

An estimate of the appropriate required rate of return for the LPC business has therefore been largely drawn from the WACC model. This value represents the average required rate of return for the debt and equity components that are used to finance the LPC business, and is expressed on a post-tax basis.

While estimating the cost of debt for LPC is relatively straightforward, determining an appropriate cost of equity is more problematic and controversial because the expected return on equity cannot be directly observed. This issue is exacerbated by the fact that although most investors will accept that the required return on equity should be a positive function of the underlying risk of the investment, there is no unanimity of views regarding the appropriate method for measuring the appropriate risk level.

A significant level of judgement must be applied in the implementation of the WACC model and the resulting estimates should be applied with caution. Appendix 4 sets out a brief description of the model that we have used, the adopted input values, and the resulting estimates from the model. Based on this analysis and a consideration of all other relevant factors, we believe that an appropriate WACC range for the LPC business is between 8.20% and 8.90%, with a mid-point value of 8.50%.

Mid-Point Value Assessment

Our mid-point estimate for the LPC standalone value is presented in Table 13, based on a valuation of operating assets derived from our DCF model. Note that the starting cash balance ($322m as at 30 June 2014) is included as part of the aggregate value of the projected cash flows for the 10-year projection period, reflecting our treatment of the cash as pre-funding for the planned earthquake remediation program. Based on this approach, net debt on the valuation date is zero and the assessed equity value of the business is the same as the enterprise value.

Table 13: Mid-Point Value for LPC

Component	Mid-Point Value ($m)
Value Years 1 – 10 (Including Cash)	$131.4m
Terminal Value (PV)	$226.9m
Aggregate Enterprise / Equity Value	$358.3m
Number of Shares on Issue	102,261,279
Value per Share	**$3.50**

Source: Northington Partners analysis

Sensitivity Analysis

We have performed a standard sensitivity analysis to determine the relative importance of the assumptions on which the DCF model is based. This analysis examines the impact of changes to each of the key assumptions listed in Table 14 on the assessed value of the LPC business. For each assumption, we have established what we believe to be a reasonable range of potential outcomes and then re-estimated the DCF model value at each of the extreme values of this range while holding all other assumptions constant.

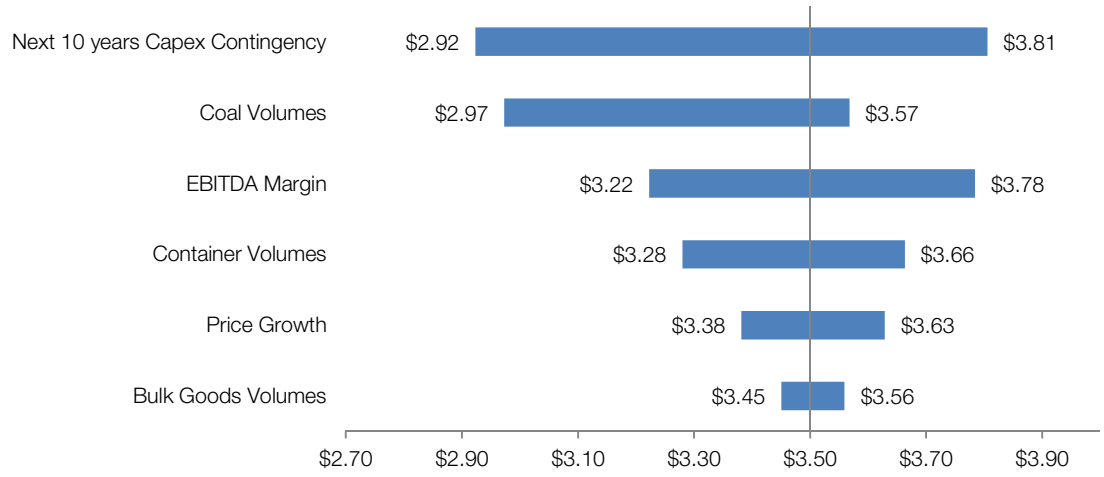
Table 14 describes the ranges used for each assumption.

Table 14: Selected Value Ranges for Sensitivity Analysis

Assumption	Mid-Point Assumption	Sensitivity Range
Capex Contingency	Project Specific	Cost increase of 10% on downside and cost saving of 5% on upside
Coal Volumes	1.6m tonnes in FY2015	Volumes either reduce to zero on the downside or bounce back to 2.0m tonnes in FY2017 and grow at 2.0% thereafter
EBITDA Margin	Steady State level starting in FY2017	Steady state level +/- 2.0%
Container Volume Growth	4.0% per annum from FY2017	Steady state of 2.5% or 5.0% (+1.0%/- 1.5%)
Price Growth	1.5% per annum from FY2017	Steady state of 1.0% or 2.0% (+/- 0.5%)
Bulk Goods Volume	2.0% per annum from FY2017	Steady state of 1.0% or 3.0% (+/- 1.0%)

Figure 13 shows the range of estimated values (expressed on a per share basis) for our assumed changes in each of the key assumptions.

Figure 13: Sensitivity of Fair Value (per share) to Changes in Key Assumptions



LPC value is most sensitive to three key drivers:

- The eventual cost of the remediation / redevelopment plan. Assuming no change to the program timing, a 1% increase or decrease in the total capital costs moves the current value by about 1.77%. Given the nature of these capital projects, we have allowed for greater downside in the sensitivity analysis but note that LPC is by necessity working towards a cost cap – the scope and timing of the program will need to be managed to remain within the total cost envelope.
- Our sensitivity for coal volumes reflects some extreme outcomes. These range between a downside scenario which reflects a cessation of export volume (15% decrease in value) to an upside which anticipates a return to historical levels.
- Value is relatively sensitive to changes to the steady state EBITDA margin, which we suggest will ultimately be dependent on the outcome from the initiatives currently being pursued to improve efficiencies in the container terminal. We have allowed for a 2.0% change from the base case assumption, resulting in a 8% change in the assessed share value.

Future trade volumes in the container terminal are also an important value driver. While the base case assumption of 4.0% growth is considerably lower than the increase recently achieved (CAGR of approximately 7.0% from FY2009 to FY2015B), we have incorporated more risk to the downside to reflect the on-going competitive environment and the potential for operational disruptions during the redevelopment process.

Summary of Standalone LPC Value

We have used the results from the sensitivity modelling to form a view on the appropriate value range for LPC. Our analysis has considered the value impact of reasonable changes in each key parameter and the valuation results for various scenarios regarding the future performance of the LPC business. Our conclusions regarding a reasonable range of values are set out in Table 15.

Table 15: Assessed Value Range for LPC

Component	Low Value	High Value	Mid-Point Value
Total Enterprise / Equity Value	$342.6m	$373.3m	$358.3m
Number of Shares on Issue	102,261,279	102,261,279	102,261,279
Value per Share	**$3.35**	**$3.65**	**$3.50**

Source: Northington Partners analysis

We conclude that the fair value for LPC's shares on a standalone basis lies between $3.35 and $3.65. These values provide a range of plus or minus $0.15 around the mid-point value of $3.50 per share, and the total range of $0.30 represents approximately 8.6% of the mid-point value.

4.3.2 Implied Valuation Multiples for LPC

Some implied valuation multiples for LPC are presented in Table 16 based on actual financial results for FY2014 and projected results for FY2015. We believe that this data provides a useful valuation benchmark for our assessment of the fair value range for LPC when compared to the trading and transaction multiples for a range of comparable companies.

Table 16: Implied Valuation Benchmarks for LPC

Valuation Benchmark	Low Value	High Value	Mid-Point Value
Enterprise Value	$342.6m	$373.3m	$358.3m
EBITDA Multiple – FY2014 (Actual)	10.4x	11.3x	10.9x
EBITDA Multiple – FY2015 (Budget)	12.4x	13.5x	12.9x

Source: Northington Partners analysis

Observed trading multiples for port companies both here and overseas are presented in Table 17, while market evidence from recent transactions is presented in Table 18. Some background information for each transaction or comparable company is presented in Appendix 5 and Appendix 6 respectively.

Table 17: Comparable Company Analysis

Company	Country	EV ($m)	EV/EBITDA	EV/EBIT
New Zealand & Australia Port Companies				
Asciano	Australia	10,199	9.3x	13.8x
The Port of Tauranga	New Zealand	2,337	16.5x	19.6x
Marsden Maritime (Northland Port)	New Zealand	118	14.7x	14.8x
South Port New Zealand	New Zealand	96	7.7x	9.7x
Average			**12.0x**	**14.5x**
New Zealand & Australia Infrastructure Companies				
Sydney Airport	Australia	17,764	16.9x	24.8x
Auckland International Airport	New Zealand	5,629	16.1x	19.5x
Infratil	New Zealand	4,745	8.9x	12.4x
Ariadne Australia	Australia	77	10.7x	13.2x
Average			**13.2x**	**17.5x**
International Port Companies				
DP World	United Arab Emirates	23,324	14.3x	20.1x
China Merchants Holdings (International)	Hong Kong	14,958	13.4x	15.6x
Hutchison Port Holdings Trust	Singapore	14,344	17.1x	23.9x
Cosco Pacific	Hong Kong	6,925	9.8x	14.4x
Westshore Terminals Investment Corporation	Canada	2,834	15.6x	16.7x
Transmontaigne Partners	United States	1,183	14.2x	24.4x
Logistec	Canada	534	9.4x	11.6x
Average			**13.4x**	**18.1x**
Overall Average			**13.0x**	**17.0x**

Source: Capital IQ and other Public Reports as at 20 August 2014

Evidence from the selected set of listed comparables is relatively consistent, with average EBITDA multiples in a range between 12.0x – 13.4x. In relation to New Zealand port companies, we note that POT is currently trading at a multiple of 16.5x EBITDA, reflecting the business' continued sound performance in FY2014 and a number of growth initiatives announced over the last year. Ports of Auckland has also recently announced a strong result for FY2014 on the back of large increases in trade volumes (both containerised and bulk freight), and is pursuing a number of supply chain partnerships to support future growth.

While LPC has benefited from the same sector-specific factors which have underpinned the performance of the other major New Zealand ports, we believe that LPC should be valued at a relative discount to POT. The POT business is approximately five times larger than LPC (based on FY2014 earnings) and expects to generate steady on-going growth from initiatives such as the Kotahi Agreement, the co-investment with Timaru and its strategy to become one of the first New Zealand ports capable of servicing larger ships. The LPC value should also reflect some level of discount to reflect:

- The timing, execution and cost risks in relation to the Recovery Plan;
- LPC's exposure to Solid Energy; and
- Expectations of a material reduction in operating earnings in FY2015 compared to FY2014. While LPC expects earnings to recover in the short-medium term, there is some uncertainty over the timing and extent of recovery.

Conversely, we would expect LPC to be valued at a premium to Southport because of LPC's larger size and far stronger growth potential.

Table 18: Recent Relevant Transactions

Target	Acquirer / Transaction	Country	Date	Implied EV ($m)	Implied EBITDA Multiple
Port of Newcastle	Hastings Funds Management & China Merchants Group	Australia	Apr-14	1,888	27.0x
Port of Brisbane	Caisse de dépôt et placement du Québec	Australia	Nov-13	5,870	27.0x
Port Kembla and Port Botany	NSW Ports Consortium	Australia	Apr-13	6,215	25.0x
Abbot Point Terminal 1	Mundra Port and Special Economic Zone	Australia	Jun-11	2,481	32.3x
Average					**27.8x**
PrimePort Timaru	Port of Tauranga	New Zealand	Aug-13	n/a	n/a
Asciano Services	Genesee & Wyoming Australia	Australia	Aug-12	12	n/a
Flinders Adelaide Container Terminal	Flinders Ports	Australia	Jul-12	285	12.3x
Port of Portland	Palisade Ports	Australia	May-12	173	6.1x
Port of Geelong	Asciano & RREEF Infrastructure	Australia	Feb-12	91	5.2x
Flinders Ports Group	Access Capital	Australia	Dec-11	1,123	11.2x
DP World Australia	Citi Infrastructure Investors	Australia	Dec-10	2,464	18.9x
Average					**10.7x**

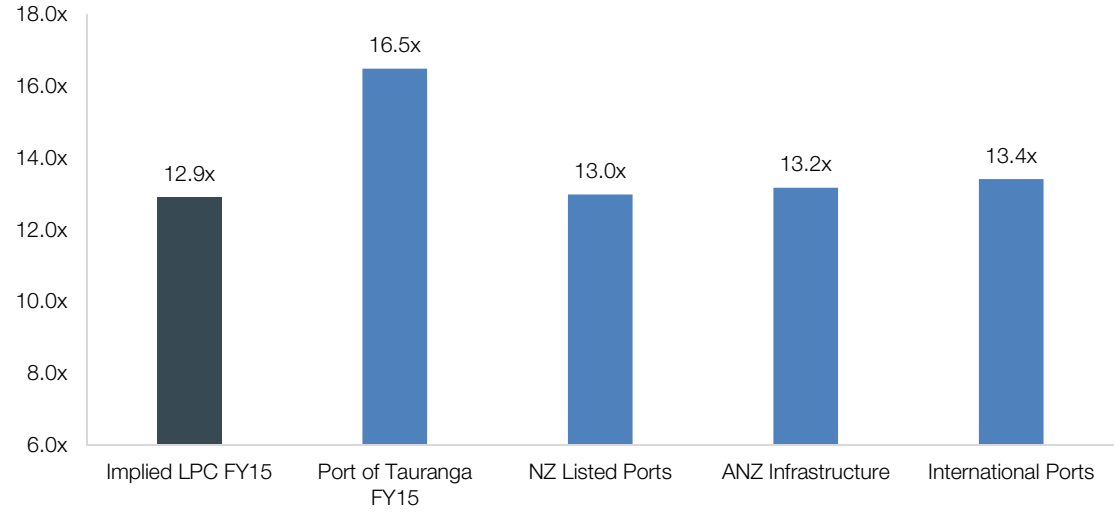
Source: Capital IQ and other Public Reports as at 20 August 2014

We believe that most of the available transactional evidence has only limited relevance to LPC:

- The recent transaction values achieved in the Australian market all represent extremely high EBITDA multiples (with an average of 27.8x). All of the transactions involve ports which are very large and which were sold through public sales processes that attracted considerable interest from a wide range of global infrastructure investors. The asset underlying each transaction is restricted to port infrastructure (including land) which is leased to a variety of port operators; the acquirers can therefore be characterised as long-term infrastructure asset owners who are targeting a low risk/return investment. In all cases, anticipated volume growth is strong and the businesses provide considerable scope for further growth through the future development of adjoining land. This level of embedded upside potential is materially higher than LPC's growth prospects and underpins the very high multiples implied by the observed transaction values.
- The only recent New Zealand transaction relates to POT's investment in PrimePort Timaru ("**PrimePort**"). The transaction involved POT taking a 50% interest in PrimePort (excluding investment properties) and simultaneously leasing the container terminal through a 100% subsidiary company for a concession period of 35 years. POT paid $21.6m for the investment, and we understand that most of the value was ascribed to the value of PrimePort's land and assets; relatively little value was attributed to the operations of the container terminal at the time of the transaction (circa 20,000 TEUs). Given the structure of the transaction and the state of the PrimePort business at the time, we suggest that it is not possible to derive any meaningful information as a benchmark for our LPC assessment.

A summary of the comparable company evidence is set out in Figure 14. Overall, we conclude that the valuation multiples for LPC that are implied from the fair value range are reasonable when compared to the available market evidence.

Figure 14: Summary of Comparable Company EV/EBITDA multiples



Source: Capital IQ and other Public Reports as at 20 August 2014

Note, NZ Listed Ports, ANZ Infrastructure & International Ports are historical average EV/EBITDA multiples.

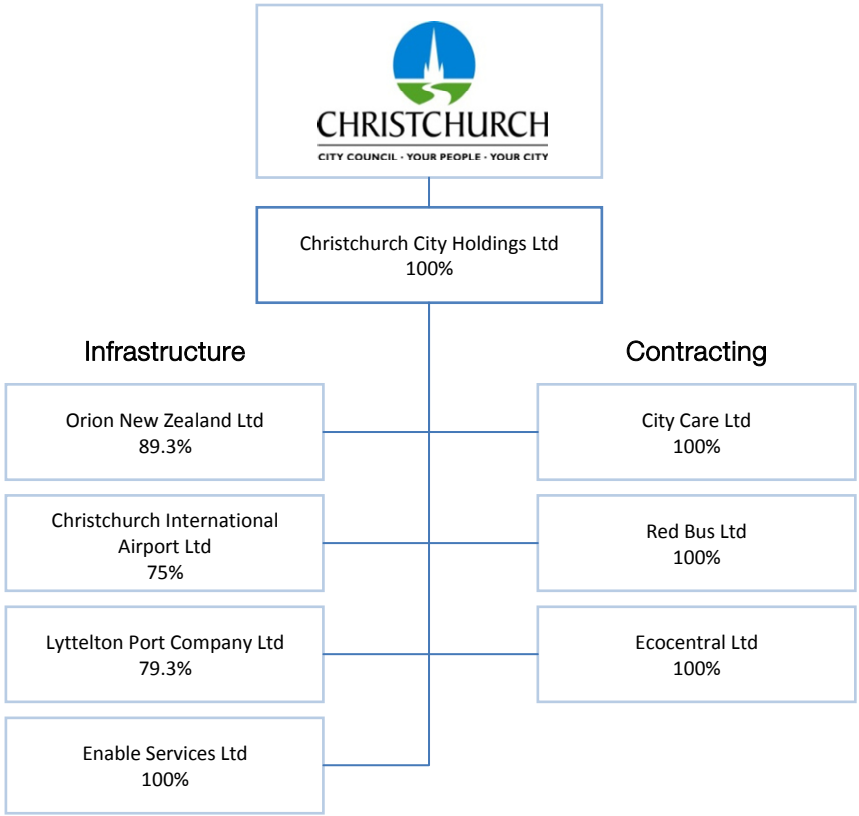
Appendix 1: Summary Profile of CCHL

CCHL is the wholly-owned commercial and investment arm of Christchurch City Council. The company was established in 1993 as a means of creating an independent and non-political buffer between the Council and its various Council-controlled trading organisations ("**CCTOs**").

Neither CCHL nor the Council plays any part in the management of the CCTOs - this is the responsibility of their respective boards and management who are charged with running their businesses in a commercial manner, and on an arm's length basis from CCHL and the Council.

As set out in Figure 15 below, CCHL manages the Council's investment in seven CCTOs.

Figure 15: CCHL Group Structure



Source: CCHL Website

The Council's investment in CCHL and its subsidiary companies was independently valued at just over $1.4 billion in June 2013. CCHL has a Standard and Poor's credit rating of A+ (negative outlook).

Further details on CCHL can be found on its website: www.cchl.co.nz

Appendix 2: Key Offer Conditions

A summary of the key conditions of CCHL's Offer are as follows (a more detailed list of the conditions are contained in the Offer):

- Acceptances being received by CCHL which will result in CCHL holding or controlling 90.00% or more of the total voting rights in LPC;
- LPC declaring and paying the Special Dividend prior to the closing date of the Offer; and
- Between 6 August 2014 and the date on which CCHL may declare the Offer unconditional:
  - No dividends, bonus issues or other distributions are declared or paid by LPC (other than the Special Dividend);
  - The business of LPC (including its subsidiaries) is carried on in the ordinary course;
  - No liquidator, receiver or similar official is appointed to any member of the LPC Group or any of its assets, and no action to appoint such a person is commenced; and
  - There not being any event that has or could be expected to have a material adverse effect on the financial position, trading operations or assets or liabilities of the LPC Group.

Appendix 3: Regulatory Requirements and Scope of this Report

Takeovers Code Requirements

The Code, which came into effect on 1 July 2001, sets out rules governing the conduct of company takeovers in New Zealand. The provisions of the Code apply to any company that is a "Code Company" (as defined in the Code). LPC is a "Code Company" because it is listed on the NZSX.

The fundamental rule of the Code is set out in Rule 6 and prevents any entity (together with its associates) from becoming the holder or controller of 20% or more of the voting rights in a "Code Company", or increasing its control position if it already owns 20% or more of the voting rights, other than via one of several courses of action prescribed in Rule 7 of the Code.

Pursuant to Rule 7 of the Code, a person may (among other exceptions) become the holder or controller of 20% or more of a Code Company "by an acquisition under a full offer". A "full offer" requires the offeror to make an offer for all the equity securities in the Code Company that it does not already own.

CCHL's Offer is a "full offer" for the purposes of the Code. CCHL's Offer and the response by LPC to the Offer must comply with the provisions set out in the Code. Rule 21 of the Takeovers Code requires the directors of LPC to obtain a report from an independent adviser on the merits of the Offer.

The exact meaning of the word "*merits*" is not prescribed in the Code and there is no well accepted, authoritative New Zealand reference that clearly establishes what should be considered when assessing the merits of a takeover offer. Although the Takeovers Panel has published a guidance note about the role of an Independent Adviser, it has been careful not to limit the scope of the assessment and states that the relevant factors that should be taken into consideration will depend on the features of the proposed transaction as well as the prevailing circumstances of the parties involved. However, the Takeovers Panel suggests that a merits assessment is broader than a valuation assessment and will include other positive and negative aspects of a transaction.

Basis of Assessment

Northington Partners has assessed the merits of CCHL's Offer by taking into account the following factors:

- Our estimate of the underlying value range of the ordinary shares in LPC (based on an assessment of the intrinsic value of the Company);
- A comparison of our estimated value range with CCHL's Total Offer Consideration (being the aggregate of the Offer Price and the Special Dividend);
- The prospects, attractiveness and risk profile of the Company; and
- The impact of the Offer and Lock-up Agreement with Port Otago on the control position of the Company.

Appendix 4: WACC Assessment

The post-tax weighted average cost of capital is calculated using the following formula:

$$k_a = \frac{D}{A} k_d (1 - t_c) + \frac{E}{A} k_e \qquad (1)$$

where, k_a = the weighted average cost of capital

k_e = the required return on equity capital

k_d = the required return on debt capital

$\frac{D}{A}$ = the ratio of debt to asset value (at market values)

$\frac{E}{A}$ = the ratio of equity to asset value (at market values)

t_c = the marginal corporate tax rate

Estimates of the WACC from equation (1) obviously require estimates of the required returns on each of the component sources of capital. Each component is discussed below.

Cost of Equity

Of the two components of the WACC, the expected return on equity is by far the more difficult to estimate. The most common estimation method used within the New Zealand market is based on some variant of the Capital Asset Pricing Model ("CAPM"), where changes are made to the standard model to account for the New Zealand dividend imputation scheme.

This model is reliant on the assumption that investors are only concerned with the impact of systematic risk factors on the required rate of return, as opposed to the total risk of the investment. Systematic risk relates to factors that affect all investments to some degree and which cannot be eliminated by holding a diversified portfolio of investments. While the theoretical foundation of this approach is well accepted, there is certainly no consensus as to whether New Zealand investors actually behave in accordance with the predictions of the model. Specific LPC risk factors such as trade volume uncertainty and operating cost control may well be incorporated into investors' determination of the appropriate return on investment from the LPC business.

The other main deficiency of the CAPM framework relates to the imprecision with which the model inputs are estimated. Key parameters such as the LPC asset beta and the post-tax market risk premium cannot be directly observed and are almost always estimated with considerable error. Because of this uncertainty surrounding the estimation process, there is scope for a wide divergence of possible input values that could be supported by the available evidence.

Despite these very important deficiencies, we believe that the CAPM model provides a useful starting point from which to derive a reasonable range of estimates for the required return on equity. While direct transactional evidence on the appropriate cost of equity is clearly preferable, it is very rarely available and must also be derived using some subjective assessments. The CAPM model has the advantages of being widely used, is mathematically precise, and is easy to implement. Results from the model must however be tempered by a pragmatic view of investor behaviour and acknowledge that a relatively wide range of values can be supported.

The version of the CAPM formula usually applied in the New Zealand market is often referred to as the Brennan-Lally model, which provides an estimate of the expected return on equity after corporate taxes, but before personal taxes. The model is written as[13]:

$$k_e = r_f(1-t_d) + \beta_E[PTMRP] \quad (2)$$

where, r_f = the risk-free rate of interest

$PTMRP$ = the Post-Tax Market Risk Premium

t_d = the weighted average over all investors of $(t_i - t_{gi})/(1-t_{gi})$

β_E = the equity beta of the investment.

t_i = investor i's tax rate on interest income

t_{gi} = investor i's tax rate on capital gains

If we further assume that the effective tax rate on capital gains is zero, then the estimate for t_d can be set equal to the value for t_i, the average marginal tax rate on interest income.

Implementation of the model described in equation (2) requires estimates for four input parameters: the riskless rate, the marginal tax rate on interest income, the PTMRP, and the asset beta of the target company. A summary of the CAPM model inputs for LPC is presented in Table 19 below.

Table 19 The Estimated Cost Of Equity (CAPM)

Parameter	Description	Low Estimate	High Estimate
r_f	Riskless Interest Rate	4.10%	4.10%
$PTMRP$	Post-Tax Market Risk Premium	7.00%	7.50%
β_A	Asset Beta	0.70	0.75
β_E	Equity Beta	1.00	1.07
t_d	Marginal Tax Rate on Interest Income	28.00%	28.00%
k_e	Post-Tax Nominal Cost of Equity	9.95%	11.00%

Our range of estimates for the cost of equity is primarily driven by the selected range of asset betas, which we believe is reasonably conservative given the data available.

Cost of Debt

Estimating the cost of debt is comparably straight forward. The standard approach simply adds a premium to the risk-free rate to reflect the default risk and illiquidity associated with any debt issued by the subject firm.

We estimate that an appropriate cost of debt for the LPC business is 5.60%, expressed on a pre-tax nominal basis. This estimate represents a margin of 150 basis points over the riskless rate, and includes an allowance for debt issuance costs.

[13] The model shown here reflects some simplifications that can be imposed as a result of some reasonable taxation assumptions.

Assumed Proportions of Debt and Equity

Following receipt of the insurance settlement in February 2014, LPC currently has no term debt and is unlikely to require debt funding in the short term at least. We have however assumed a long-term target gearing ratio of 30% in our WACC assessment.

WACC Summary and Conclusion

An estimate for the LPC required rate of return based on the build-up WACC model is summarised in Table 20. We conclude that an appropriate range for the post-tax nominal cost of capital for LPC is 8.20% to 8.90%, with a mid-point value of 8.50%.

Table 20 Summary of WACC Estimate

Component	WACC
Post-Tax Cost of Debt	4.00%
Post-Tax Cost of Equity	10.45%
Post-Tax WACC	8.50%

Appendix 5: Comparable Transaction Data

A description of the transactions listed in Section 4.3.2 is set out below.

Table 21: Details for Recent Relevant Transactions

Date	Target	Description	Acquirer / Transaction	Country	Implied EV (NZ$m)	Implied EBITDA Multiple
Apr-14	Port of Newcastle	Largest coal export port in the world, located in New South Wales, Australia.	Hastings Funds Management & China Merchants Group	Australia	1,888	27.0x
Nov-13	Port of Brisbane	Largest multi-cargo port in Queensland, Australia.	Caisse de dépôt et placement du Québec	Australia	5,870	27.0x
Apr-13	Port Kembla and Port Botany	Port Kembla represents the marine port of Port Kembla in Wollongong. Port Botany owns and operates a port in Sydney.	NSW Ports Consortium (IFM Investors, Cbus Industry Superannuation Fund, Health Employees Superannuation Trust Australia, Qsuper, AustralianSuper, Host-Plus & Abu Dhabi Investment Authority)	Australia	6,215	25.0x
Jun-11	Abbot Point Terminal 1	Comprises rail in-loading facilities, coal handling and stockpiling areas and a single trestle jetty and conveyor.	Mundra Port and Special Economic Zone	Australia	2,481	32.3x
Average						**27.8x**
Aug-13	PrimePort Timaru	Operates a multi-purpose port in South Canterbury, New Zealand.	Port of Tauranga	NZ	n/a	n/a
Aug-12	Asciano Services	Comprises an intermodal and freight terminal located in Alice Springs, Australia.	Genesee & Wyoming Australia	Australia	12	n/a
Jul-12	Flinders Adelaide Container Terminal	Owns and operates container terminal, based in Adelaide, Australia.	Flinders Ports	Australia	285	12.3x
May-12	Port of Portland	Owns and operates a deep-water bulk port located between ports of Melbourne and Adelaide in Australia.	Palisade Ports	Australia	173	6.1x
Feb-12	Port of Geelong	Operates as a bulk and break bulk seaport in Victoria, Australia.	Asciano & RREEF Infrastructure	Australia	91	5.2x
Dec-11	Flinders Ports Group	South Australia's port operator with 7 ports located at Port Adelaide, Port Lincoln, Port Pirie, Thevenard, Port Giles, Wallaroo and Klein Point.	Access Capital	Australia	1,123	11.2x
Dec-10	DP World Australia	A marine terminal operator and provides marine cargo handling services in Brisbane, Sydney, Melbourne, Adelaide and Fremantle.	Citi Infrastructure Investors	Australia	2,464	18.9x
Average						**10.7x**

Source: Capital IQ, Company Announcements and Financials, Northington Partners' Analysis

Appendix 6: Comparable Company Trading Data

Some further information and a summary description of the companies listed in Section 4.3.2 are set out below.

Table 22: Detailed Comparable Trading Multiples

Company Name	Country	EV (NZ$m)	Market Cap (NZ$m)	EV / LTM EBITDA	EV / NTM EBITDA	EV / LTM EBIT	EV / NTM EBIT	P /BV	EBITDA Margin	Net Income Margin
Asciano	Australia	10,199	6,501	9.3x	8.3x	13.8x	12.2x	1.6x	26%	9%
The Port of Tauranga	NZ	2,337	2,083	16.5x	16.5x	19.6x	19.8x	2.6x	53%	29%
Marsden Maritime Holdings (Northland Port)	NZ	118	118	15.5x	n/a	15.6x	n/a	0.9x	76%	68%
South Port New Zealand	NZ	96	91	7.7x	n/a	9.7x	n/a	3.1x	40%	21%
Sydney Airport	Australia	17,764	10,679	16.9x	16.9x	24.8x	24.3x	n/a	80%	11%
Auckland International Airport	NZ	5,629	4,524	16.1x	15.3x	19.5x	18.4x	1.8x	74%	41%
Infratil	NZ	4,745	1,365	8.9x	8.7x	12.4x	12.2x	1.2x	20%	8%
Ariadne Australia	Australia	77	79	10.7x	n/a	13.2x	n/a	0.9x	23%	11%
DP World	UAE	23,324	19,829	14.3x	13.2x	20.1x	18.5x	2.0x	42%	21%
China Merchants Holdings	HK	14,958	10,198	13.4x	23.1x	15.6x	32.4x	1.4x	84%	54%
Hutchison Port Holdings	Singapore	14,344	7,407	17.1x	13.1x	23.9x	22.1x	0.8x	43%	14%
Cosco Pacific	HK	6,925	5,185	9.8x	11.6x	14.4x	22.1x	0.9x	51%	38%
Westshore Terminals Investment Corporation	Canada	2,834	2,890	15.6x	13.6x	16.7x	14.9x	5.5x	54%	40%
Transmontaigne Partners	US	1,183	838	14.2x	12.6x	24.4x	20.5x	2.0x	44%	18%
Logistec Corp	Canada	534	525	9.4x	n/a	11.6x	n/a	3.1x	15%	10%
Average				**13.0x**	**13.9x**	**17.0x**	**19.8x**	**2.0x**	**48%**	**26%**
Median				**14.2x**	**13.2x**	**15.6x**	**19.8x**	**1.7x**	**44%**	**21%**

Source: Capital IQ

Table 23: Detailed Comparable Company Descriptions

Company Name	Description
Asciano	Asciano Limited engages in the ownership and management of ports and rail assets, and associated operations and services in Australia.
The Port of Tauranga	Port of Tauranga Limited operates and manages the Port of Tauranga in New Zealand.
Marsden Maritime Holdings (Northland Port)	Marsden Maritime Holdings Limited operates deep water port facilities primarily at Whangarei and Marsden Point, New Zealand.
South Port New Zealand	South Port New Zealand Limited provides and manages port and warehousing services in New Zealand.
Sydney Airport	Sydney Airport Limited owns and operates airport in Sydney, Australia.
Auckland International Airport	Auckland International Airport Limited provides airport facilities and supporting infrastructure in Auckland, New Zealand.
Infratil	Infratil Limited owns infrastructure businesses and investments in New Zealand and Australia.
Ariadne Australia	Ariadne Australia Limited is engaged in the car park infrastructure operation and management activities in Australia and New Zealand. The company is also involved in the ownership and operation of maritime infrastructure.
DP World	DP World Limited is engaged in the business of international marine terminal operations and development, logistics, and related services worldwide.

Table 21: Detailed Comparable Company Descriptions (Continued)

Company Name	Description
China Merchants Holdings	China Merchants Holdings (International) Company Limited, an investment holding company, operates as a port operator in Mainland China, Hong Kong, and internationally.
Hutchison Port Holdings Trust	Hutchison Port Holdings Trust, together with its subsidiaries, invests in, develops, operates, and manages deep-water container ports in Guangdong Province of China, Hong Kong, and Macau.
Cosco Pacific	COSCO Pacific Limited, an investment holding company, is engaged in managing and operating terminals; and container leasing, management and sale, and related businesses.
Westshore Terminals Investment Corporation	Westshore Terminals Investment Corporation, through its limited partner interests in Westshore Terminals Limited Partnership, operates a coal storage and loading terminal at Roberts Bank, British Columbia in Canada.
Transmontaigne Partners	TransMontaigne Partners L.P. operates as a terminaling and transportation company.
Logistec Corp	Logistec Corporation provides cargo handling and other services to marine, industrial, and municipal customers in Canada and the United States.

Source: Capital IQ

Appendix 7: Sources of Information Used in This Report

Other than the information sources referenced directly in the body of the report, this assessment is also reliant on the following sources of information:

- Annual reports for LPC from 2010 to 2013
- Audited financial statements for LPC for the period FY2010 to FY2014
- LPC's management budget for FY2015
- Discussions with senior management personnel of LPC
- The websites of LPC and CCHL
- CCHL's Takeover Notice dated 6 August 2014 and the Offer document distributed to LPC shareholders on 25 August 2014
- Various other documents that we considered necessary for the purposes of our analysis

Appendix 8: Declarations, Qualifications and Consents

Declarations

This report is dated 1 September 2014 and has been prepared by Northington Partners at the request of the directors of LPC to fulfil the reporting requirements pursuant to Rule 21 of the Code. This report, or any part of it, should not be reproduced or used for any other purpose. Northington Partners specifically disclaims any obligation or liability to any party whatsoever in the event that this report is supplied or applied for any purpose other than that for which it is intended.

Prior drafts of this report were provided to LPC for review and discussion. Although minor factual changes to the report were made after the release of the first draft, there were no changes to our methodology, analysis, or conclusions.

This report is provided for the benefit of all of the shareholders of LPC (other than CCHL, Port Otago or any entity associated with CCHL or Port Otago) that are subject to the Offer, and Northington Partners consents to the distribution of this report to those people. The engagement terms did not contain any term which materially restricted the scope of our work.

Qualifications

Northington Partners provides an independent corporate advisory service to companies operating throughout New Zealand. The company specialises in mergers and acquisitions, capital raising support, expert opinions, financial instrument valuations, and business and share valuations. Northington Partners is retained by a mix of publicly listed companies, substantial privately held companies, and state owned enterprises.

The individuals responsible for preparing this report are Greg Anderson B.Com, M.Com (Hons), Ph.D and Steven Grant B.Com, LLB (Hons). Each individual has a wealth of experience in providing independent advice to clients relating to the value of business assets and equity instruments, as well as the choice of appropriate financial structures and governance issues.

Northington Partners has been responsible for the preparation of numerous Independent Reports in relation to takeovers, mergers, and a range of other transactions subject to the Code and NZX Listing Rules.

Independence

In March 2006, Crighton Anderson (which has since merged with Northington Partners) prepared an Independent Adviser's Report required by Rule 21 of the Code in relation to the full takeover offer for LPC by CCHL. We were approved by the Takeovers Panel for the preparation of that report, and were in no way involved in the origination, structuring, funding, or execution of that proposed transaction.

Northington Partners has not been previously engaged on any other matter by LPC, Port Otago or CCHL or (to the best of our knowledge) by any other party to the proposed transaction. None of the Directors or employees of Northington Partners have any other relationship with any of the Directors or substantial security holders of the parties involved in the proposed Offer.

The preparation of this Rule 21 report will be Northington Partners' only involvement in relation to the Offer. Northington Partners will be paid a fixed fee for its services which is in no way contingent on the outcome of our analysis or the content of our report.

Northington Partners does not have any conflict of interest that could affect its ability to provide an unbiased report.

Disclaimer and Restrictions on the Scope of Our Work

In preparing this report, Northington Partners has relied on information provided by LPC. Northington Partners has not performed anything in the nature of an audit of that information, and does not express any opinion on the reliability, accuracy, or completeness of the information provided to us and upon which we have relied.

Northington Partners has used the provided information on the basis that it is true and accurate in material respects and not misleading by reason of omission or otherwise. Accordingly, neither Northington Partners nor its Directors, employees or agents, accept any responsibility or liability for any such information being inaccurate, incomplete, unreliable or not soundly based or for any errors in the analysis, statements and opinions provided in this report resulting directly or indirectly from any such circumstances or from any assumptions upon which this report is based proving unjustified.

We reserve the right, but will be under no obligation, to review or amend our report if any additional information which was in existence on the date of this report was not brought to our attention, or subsequently comes to light.

Indemnity

LPC has agreed to indemnify Northington Partners (to the maximum extent permitted by law) for all claims, proceedings, damages, losses (including consequential losses), fines, penalties, costs, charges and expenses (including legal fees and disbursements) suffered or incurred by Northington Partners in relation to the preparation of this report, except to the extent resulting from any act or omission of Northington Partners finally determined by a New Zealand Court of competent jurisdiction to constitute negligence or bad faith by Northington Partners.

LPC has also agreed to promptly fund Northington Partners for its reasonable costs and expenses (including legal fees and expenses) in dealing with such claims or proceedings upon presentation by Northington Partners of the relevant invoices.


northington PARTNERS
investment banking • corporate finance