cutting through complexity

FX Networks

Independent Report on the Merits of the proposed acquisition by Vocus (New Zealand) Holdings Limited

August 2014

Statement of independence

KPMG confirms that it:

a) Has no conflict of interest that could affect its ability to provide an unbiased report; and

b) 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.

KPMG 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 purpose of preparing this report.

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The Directors
FX Networks Limited
Level 3, 138 The Terrace
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New Zealand

15 August 2014

Dear Directors

Independent Report on the Merits of the proposed acquisition of FX Networks by Vocus (New Zealand) Holdings Limited

FX Networks Limited has received a takeover offer from Vocus (New Zealand) Holdings Limited, a wholly-owned subsidiary of Vocus Communications Limited, for 100% of the Company's shares. FX Networks is widely held and, as a result, the Proposed Transaction is subject to the requirements of the New Zealand Takeovers Code.

The Directors of FX Networks Limited have requested that KPMG prepare an Independent Adviser's Report on the Merits of the Proposed Transaction to assist FX Networks shareholders in assessing the offer.

We have prepared the following Independent Report for this purpose in accordance with our engagement letter dated 11 September 2013 and subsequent engagement addendum letter dated 14 April 2014.

Yours sincerely

Justin Ensor
Partner

Troy Newton
Partner

Contents

Glossary

Board	The Board of Directors of FX Networks Limited
CAGR	Compound Annual Growth Rate
Cash Amount	NZ$79.30 for each FX Networks Share
Cash Cap	NZ$20.3m
Code	New Zealand Takeovers Code
Company	FX Networks Limited
Discounted Issue Price	AU$4.40 per Vocus share issued as consideration
DSL	Digital Subscriber Line
Equity Consideration	16.76 ordinary shares in Vocus for each FX Networks Share
EV	Enterprise Value
FX Networks	FX Networks Limited
FX Networks Shareholders	Refers to an Ordinary Shareholder in FX Networks Limited
Gb	Gigabit
Gbps	Gigabits per second
IRU	Indefeasible Right of Use
KPMG	KPMG Corporate Finance
LFC	Local Fibre Company
Offer Consideration	The sum of the aggregate Cash Amounts (up to the Cash Cap) and the aggregate Equity Consideration in such proportions as elected by the respective shareholders of FX Networks
Proposed Transaction	The proposed acquisition of all of the shares in FX Networks by Vocus NZ
RBI	Rural Broadband Initiative
Report	This Independent Adviser's Report prepared by KPMG in relation to the Proposed Transaction
Shares	Refers to Ordinary Shares in FX Networks Limited
Tb	Terabit (equal to 1,000 Gb)
Tbps	Terabits per second
UBA	Unbundled Bitstream Access
UCLL	Unbundled Copper Local Loop
UFB	Ultra-Fast Broadband
Vocus	Vocus Communications Limited
Vocus NZ	Vocus (New Zealand) Holdings Limited
Vocus Offer	Offer document in respect of the Proposed Transaction appended to Pre-Bid Agreement dated 1 July 2014

1. Introduction

1.1 Background of the Proposed Transaction

FX Networks Limited ("FX Networks" or "the Company") has received a takeover offer from Vocus (New Zealand) Holdings Limited ("Vocus NZ") to acquire 100% of the Company's ordinary shares ("the Proposed Transaction"). Vocus NZ is a wholly owned subsidiary of ASX listed Vocus Communications Limited ("Vocus").

The Offer Consideration for the Proposed Transaction is comprised of a combination of Vocus shares (at a fixed issue price) ("Equity Consideration") and cash ("Cash Amount") up to a maximum aggregate cash amount of NZ$20.3m ("Cash Cap").

FX Networks is widely held and, as such, the Proposed Transaction is subject to the requirements of the Takeovers Code ("Code"). Rule 21 of the Code requires that the Directors of FX Networks obtain an Independent Adviser's Report ("IAR") on the merits of the Proposed Transaction

The Directors of FX Networks have engaged KPMG Corporate Finance ("KPMG", "us" or "we") to prepare an IAR on the merits of the Proposed Transaction.

1.2 Purpose and scope of the Independent Adviser's Report

1.2.1 Purpose and scope

The Directors of FX Networks have requested that KPMG prepare an Independent Adviser's Report (the "Report") to examine the Merits of the Proposed Transaction for FX Networks shareholders.

Our scope has been to assess the Merits of the Proposed Transaction. "Merits" is a term used within the New Zealand Takeovers code, which provides the rules and framework for conducting takeovers and mergers in New Zealand.

1.2.2 Definition of Merits

Rule 21 of the New Zealand Takeovers Code requires an Independent Adviser to report on the Merits of an offer. The term "merits" is not explicitly defined either in the Takeovers Code itself or in any other statute pertaining to securities law or commercial law in New Zealand. Whilst the Takeovers Code does not prescribe a meaning of the term "merits", it suggests that it includes both positive and negative aspects in respect of a transaction.

Accordingly, the term "Merits" encompasses a wide range of issues associated with the Proposed Transaction. Specifically, assessing the Merits of the Proposed Transaction requires consideration of the following factors:

- the rationale for the Proposed Transaction;
- the terms and conditions of the Proposed Transaction;
- the estimated value range of FX Networks relative to the proposed consideration in the Vocus Offer;
- the advantages and disadvantages for FX Networks shareholders of the Proposed Transaction proceeding; and
- the implications for shareholders if the Proposed Transaction does not proceed.

1.3 Offer Consideration

The Offer Consideration assumes an Initial Equity Value of NZ$61.5m. In addition, Vocus NZ will assume, refinance or repay certain existing debt obligations of the Company including:

- existing finance leases;
- existing bank debt;
- convertible notes held by certain shareholders; and
- shareholder loans.

These items have a combined value of NZ$53.7m, implying a total enterprise value ("EV") for FX Networks of NZ$115.2m and a transaction EV / EBITDA multiple of 8.6 times FY14 earnings (7.4 times forecast FY15 earnings).

Individual FX Networks shareholders have the option to receive the Offer Consideration either:

- entirely in Vocus shares, at a ratio of 16.76 Vocus shares for one FX Networks share ("Equity Consideration");
- entirely in cash ("Cash Amount"); or
- a combination of Equity Consideration and Cash Amount.

The Cash Amount is calculated on the basis of the Initial Equity Value of $61.5m. FX Networks shareholders can elect to receive the Cash Amount only to the extent that the aggregate of the Cash Amounts paid to FX Networks Shareholders does not exceed the Cash Cap of NZ$20.3m. If the aggregate of the Cash Amounts that FX Networks shareholders elect to receive exceeds the Cash Cap then Cash Amounts will be allocated to FX Networks Shareholders on a pro-rata basis with any outstanding consideration then paid in Vocus shares.

Vocus shares are currently trading above the discounted issue price of AU$4.40 per share. As a result the effective value of the Offer Consideration is greater than the Initial Equity Value.

1.4 Evaluation of the Merits of the Proposed Transaction

In our opinion, after having regard to all relevant factors, the Offer Consideration and the terms and conditions of the Proposed Transaction, we are of the view that:

- The Equity Consideration is above KPMG's assessment of the underlying value of the Company (this is partly due to the significant increase in the price of Vocus shares following the announcement of the Proposed Transaction);
- The Cash Amount is within KPMG's assessment of the underlying value of the Company;
- The Proposed Transaction provides FX Networks Shareholders an opportunity to realise the value of their existing investment.
- The Offer Consideration provides a greater degree of liquidity to FX Networks Shareholders than their current holdings (albeit not to the same extent for those shareholders that will be subject to escrow provisions restricting the sale of Vocus shares in the 12 months following the Transaction);
- Vocus' share price may increase or decrease in the future. Shareholders need to consider their exposure to future price volatility (particularly those shareholders whose shares are subject to escrow);

- The Proposed Transaction provides Shareholders the ability to retain some interest in the future of the Company via holding Vocus shares, however FX Networks Shareholders would be diluted as a consequence of the Proposed Transaction (that is: they would hold a smaller proportion of the outstanding Vocus shares than they currently hold of FX Networks Shares);
- The Proposed Transaction enables Shareholders to receive a proportional share of any synergistic benefits that may arise from the Transaction via their retained Vocus shares;
- As Vocus is an Australian domiciled company, shareholders resident in New Zealand will not be able to utilise franking credits issued by Vocus (due to the lack of mutual recognition of Australian franking credits and New Zealand imputation credits). This could result in the double taxation of dividends for New Zealand shareholders. There may potentially be further adverse tax impacts for specific shareholders depending on their particular circumstances. We recommend that Shareholders obtain independent tax advice in respect of the tax implications of the Offer Consideration having regard to their specific personal circumstances and tax status;
- The Proposed Transaction provides the benefits of an IPO (liquidity, governance, access to capital) without having to incur the time, cost or management distraction of undertaking the listing process directly;
- In the event that FX Networks Shareholders elect not to accept the Offer and the Proposed Transaction does not proceed, the Company will be required to refinance its overdraft facilities in the short term (current overdraft limit expires on 30 September 2014).

When considered relative to the potential alternatives we conclude that the Proposed Transaction confers all of the benefits of the alternatives while limiting the negative impacts.

1.5 Information relied upon

Appendix 1 details the information we have received and relied upon in completing this report.

1.6 Report restrictions

The report is based upon financial and other information provided by FX Networks. KPMG has considered and relied upon this information. KPMG believes that the information provided was reliable, complete and not misleading and has no reason to believe that any material facts have been withheld.

The information provided has been evaluated through analysis, enquiry and review for the purposes of forming an opinion as to the merits of the Proposed Transaction to its shareholders. However, KPMG does not warrant that these enquiries have identified or verified all of the matters which an audit, extensive examination or due diligence investigation might disclose.

KPMG has not undertaken a due diligence investigation and has not audited or verified in any way any financial information provided. It is understood that the financial information provided to KPMG was prepared in accordance with generally accepted accounting principles in New Zealand.

It is assumed that the information provided to KPMG does not reflect any material bias, either positive or negative. KPMG has no reason to believe otherwise. The major assumptions inherent in this information were reviewed by KPMG and are believed to be reasonable in the context of current economic, financial or other conditions.

However, KPMG in no way guarantees or otherwise warrants the achievability of future profits, cashflows or dividends. Forecasts are inherently uncertain. They are predictions by management of future events which cannot be assured and are necessarily based on assumptions, many of which are beyond the control of management. The actual future results can be significantly more or less favourable.

The statements and opinions expressed in this Report have been made in good faith and on the basis that all relevant information for the purposes of preparing this Report has been provided by FX Networks' management and that all such information is true and accurate in all material aspects and not misleading by reason of omission or otherwise. Accordingly, neither KPMG nor its partners, 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.

KPMG provided a draft of this Report to the Directors of FX Networks solely for the purpose of confirming the factual accuracy of the Report. There was no alteration to the conclusion as a result of issuing the draft Report.

Our report was prepared on 6 August 2014 based on the information available at the time. KPMG has no obligation to update our report or revise the information contained therein due to events and transactions occurring subsequent to the date of our report.

1.7 Qualifications, declarations and independence

Detailed in Appendix 2 are our statements regarding qualifications, independence and declarations.

2. Details of the Proposed Transaction

2.1 Overview

Vocus NZ is offering to acquire all of the ordinary shares ("Shares") in FX Networks. Vocus NZ is a wholly owned subsidiary of ASX listed Vocus (ticker code VOC.AU).

2.2 Consideration offered

2.2.1 Offer Consideration

The Offer Consideration assumes an Initial Equity Value of NZ$61.5m. In addition, Vocus NZ will assume, refinance or repay certain existing debt obligations of the Company including:

- existing finance leases;
- existing bank debt;
- convertible notes held by certain shareholders; and
- shareholder loans.

These items have a combined value of NZ$53.7m, implying a total enterprise value for FX Networks of NZ$115.2m and a transaction EV / EBITDA multiple of 8.6 times FY14 earnings (7.4 times forecast FY15 earnings).

Individual FX Networks shareholders have the option to receive the Offer Consideration either:

- entirely in Vocus shares, issued at a discounted price of AU$4.40 ("Equity Consideration");
- entirely in cash ("Cash Amount"); or
- a combination of Equity Consideration and Cash Amount.

The Cash Amount is calculated on the basis of the Initial Equity Value of $61.5m. FX Networks shareholders can elect to receive the Cash Amount only to the extent that the aggregate of the Cash Amounts paid to FX Networks Shareholders does not exceed the Cash Cap of NZ$20.3m.

Vocus shares are currently trading above the discounted issue price of AU$4.40 per share. As a result the effective value of the Offer Consideration is greater than the Initial Equity Value.

2.2.2 Offer Consideration – discounted Vocus shares

The Equity Consideration offered for each outstanding FX Networks Share is 16.76 Ordinary Shares in Vocus. The Vocus Shares to be issued as consideration will rank equally with the existing shares issued by Vocus.

The Offer Consideration has been calculated on the basis that Vocus shares issued as Equity Consideration will be issued at a discount to their current market price ("Discounted Issue Price"). The Offer document proposes a Discounted Issue Price of AU$4.40 per Vocus share.

Vocus shares were placed in a trading halt on 30 June 2014 pending an announcement to the market regarding the Proposed Transaction. On the last trading day prior to the Offer (27 June 2014), Vocus shares closed at AU$4.76 per share (implying a premium of approximately 8% over the Discounted Issue Price).

Vocus shares resumed trading on 2 July 2014 and closed at AU$5.15. Since then Vocus shares have traded in a range between AU$4.86 and AU$5.80, implying a premium of between 10% and 32% over the Discounted Issue Price.

On 31 July 2014 Vocus shares closed at AU$5.10 and the NZD/AUD cross rate was 0.913, implying an effective value for the Equity Consideration of NZ$93.63 per FX Networks share.

Offer Consideration (Equity Consideration)					
Price per FX share implied by the Equity Consideration					
FX Networks shares outstanding	#				776,124
Initial Equity Value	$NZD			$	61,548,139
Assumed exchange rate	NZD/AUD				0.9299
Discounted Issue Price (per Offer)	$AUD			$	4.40
Discounted Issue Price (per Offer)	$NZD			$	4.73
Max number of Vocus shares to be issued					13,007,640
Ratio: Vocus shares per FX share					16.76
Market price of Vocus shares			**Low**		**High**
Trading range July 2014	$AUD	$	4.86	$	5.80
Premium over Discounted Issue Price			10%		32%
Current market price of Vocus shares (31/7)	$AUD			$	5.10
Current NZD/AUD exchange rate (31/7)	NZD/AUD				0.9129
Market value of Equity Consideration	$AUD			$	66,338,962
Effective value of Equity Consideration	$NZD			$	72,668,378
Effective value of Equity Consideration	**$NZD per FX share**			**$**	**93.63**

2.2.3 Offer Consideration – cash

FX Networks shareholders may elect to receive a portion of their total consideration in cash ("Cash Amount") rather than Vocus shares. The Cash Amount offered is NZ$79.30 per FX Networks share.

Offer Consideration (Cash Amount)			
Cash consideration per FX share			
Initial Equity Value	$NZD	$	61,548,139
FX Networks shares outstanding	#		776,124
Cash Amount per FX share	**$NZD per FX share**	**$**	**79.30**

Vocus will make up to 33% (NZ$20.3m) of the Initial Equity Value available in cash ("Cash Cap"). If the aggregate of the Cash Amounts that FX Networks shareholders elect to receive exceeds the Cash Cap then Cash Amounts will be allocated to FX Networks Shareholders on a pro-rata basis with any outstanding consideration then paid in Vocus shares.

Any Cash Amount received will not be subject to Escrow requirements (refer: section 2.3.2).

2.2.4 Offer Consideration (33% Cash Amount, 67% Equity Consideration)

If all FX Networks shareholders elected to receive 33% of the total consideration in cash, and the balance in Vocus shares, then the combined effective net proceeds would be NZ$(88.90) per FX Networks share. This reflects the fact that the Cash Amount component does not include the benefit from the discount at which Vocus shares are to be issued.

Offer Consideration (33% cash, 67% Vocus shares)			
Effective price per FX share if the maximum cash amount is accepted			
Total FX Networks shares outstanding	#		776,124
FX shares settled in Vocus shares	#		520,003
FX shares settled in cash	#		256,121
Effective value of Equity Consideration	$NZD per FX share	$	93.63
FX shares settled in Vocus shares	#		520,003
Total value of Equity Consideration received	$NZD	$	48,687,813
Cash Amount per FX share	$NZD per FX share	$	79.30
FX shares settled in cash	#		256,121
Total value of Cash Amount received	$NZD	$	20,310,886
Total value of Offer Consideration	$NZD	$	68,998,699
Total value of Offer Consideration	**$NZD per FX share**	**$**	**88.90**

2.3 Key conditions of the Vocus Offer

The Vocus Offer is subject to the following key conditions:

2.3.1 Consents

The Vocus Offer is conditional upon FX Networks securing consent from the following parties in respect of any change of control clause in the commercial contracts between the relevant party and FX Networks:

- Unison (Fibre & Networks);
- Electricity Ashburton;
- Alpine Energy;
- Network Waitaki;
- Kordia;
- Vodafone;
- REANNZ;
- Chorus;
- Telecom;
- Network Tasman;
- Aurora Energy;
- Citylink
- Innovation Waikato; and
- The landlords of eight buildings currently rented and occupied by FX Networks.

2.3.2 Escrow Shares

The Offer is conditional upon a minimum of 50% of the Vocus shares that are issued as Consideration pursuant to the Offer being subject to escrow arrangements. These arrangements require that 100% of the escrowed Vocus Shares are to be retained for six months after issue and 50% are to be retained for 12 months. This arrangement excludes the first 40,000 Vocus Shares received by each escrowed Shareholder. Escrowed shares may be charged as security against borrowings from a tier one bank and, in the event that the bank seeks to enforce its security, Vocus will release those shares from escrow.

Each FX Networks shareholder has the option to decide whether or not to commit their Vocus shares to escrow. FX Networks shareholders must reach agreement amongst themselves which shares/shareholders are to be escrowed such that the minimum 50% escrow condition is satisfied.

FX Networks management has advised that several of the Company's larger shareholders have already provided verbal indications as to whether they intend to receive cash or shares and whether they would be willing to commit those shares to escrow. While no specific arrangement has been formalized at the date of this report, on the basis of the preliminary indications represented by management there would already be a sufficient number of escrowed shares to satisfy this condition of the Offer.

3. Overview of FX Networks

3.1 Business overview

3.1.1 Company history

FX Networks is a privately held company incorporated in 2003, with its registered offices in Wellington, New Zealand.

FX Networks owns and operates one of the three inter-city fibre optic networks in New Zealand. FX Networks offers products and services to enterprise and ISP customers, focused on high-performance Internet, Ethernet, fibre, voice and storage.

Key milestones

- May 2003 - Company Established
- June 2003 - Contracted use of Railways Fibre and Railways Route
- October 2004 - Acquired an ISP (COMNET -120 Enterprise Customers)
- September 2006 - FX Auckland Wellington Backbone completed
- December 2006 - Government Shared Network (now One.Govt) live
- Dec 2006 to Dec 2008 - Police, TVNZ, Kordia and others signed to One.Govt
- December 2008 – East-West North Island fibre build rings completed
- June 2010 – REANNZ network contract secured
- June 2013 – completion of East Cape construction project for Chorus
- July 2013 – REANNZ joint network project announced

3.1.2 Shareholders

As at 31 July 2014, FX Networks had 776,124 shares on issue held by approximately 105 shareholders. The Company's top 20 shareholders are shown in the table below.

FX Networks - Top 20 shareholders as at 31 July 2014		
Shareholder	**Shares**	**%**
Peregrine	259,976	33.50%
Penrith Holdings	145,110	18.70%
Stuart Lobley	92,286	11.89%
Putake Networks	37,309	4.81%
Anne Fane De Salis FT	32,372	4.17%
Vincent Titchmarsh	24,103	3.11%
Jurgeleit	18,641	2.40%
CSL Pension Scheme	12,581	1.62%
Henrietta Tayler	12,311	1.59%
Pauline Hill	10,325	1.33%
Locke FT	9,340	1.20%
Baobab Holdings	9,000	1.16%
Alan Hulme	8,914	1.15%
David Craine	7,500	0.97%
Susan Taylor	6,984	0.90%
Thompson & Bransgrove	5,167	0.67%
Gavin De Salis	4,488	0.58%
Charlotte Bray	4,389	0.57%
Brownsover	3,065	0.39%
Arthur Milnes	2,681	0.35%
Top 20 shareholders	**706,542**	**91.03%**
Other shareholders	**69,582**	**8.97%**
Total	**776,124**	**100.00%**

Source: FX Networks share register (Companies Office records)

3.1.3 Products & services offered

FX Networks operates two businesses – telecommunications and civil construction services. Telecommunication services include backhaul services, private networking services and Internet Service Provider ("ISP"), while the construction division, "FX Works", undertakes internal and external cable laying projects. These services are categorized into annuity and project operations respectively.

Annuity services

- Managed network services: Managed network services include backhaul for Telco's and ISPs with high speed, high capacity, point-to-point services on the FX network. FX Networks' backhaul network provides an intermediate connection between local area networks and other wholesale networks, such as those operated by Chorus and Vodafone.

- Internet service provider (ISP): the provision of high speed internet service to medium and large organizations.

- Other non-core services: Other non-core services include IP Telephony, Cloud Storage and Voice services. FX Networks also offers On-Net Storage Services which provides archiving for high volumes of data such as corporate emails, system backups and graphical imagery data.

Project services (one-off revenues)

- Dark fibre: The demand for dark fibre has increased with the introduction of Ultra-Fast Broadband ("UFB") and the Rural Broadband Initiative (RBI). Historically, the revenue model for the sale of dark fibre was an initial upfront payment for a 21-year

Indefeasible Right of Use ("IRU"). Over time, FX Networks has also sold dark fibre for shorter periods resulting in annuity revenue with monthly or annual rental payments.

- Civil construction: The FX construction business, "FX Works", installs fibre optic cables in the ground. This service was established to provide internal construction capability in building the FX fibre asset. FX Works also generates external revenues through construction contracts with other service providers.

3.1.4 Fibre network

Geography

FX Networks owns and operates 3,600 kilometres of fibre optic network connecting many of the major cities and towns in NZ. FX has 35 'Meet Us' Points-Of-Presence and operates from 58 locations throughout the North and South Island. Partnerships with other service providers enable FX to access Points-Of-Presence throughout the country. The Company's partner companies include Enable Networks, Chorus, Telecom, Vodafone and Vector.

Capacity

FX Networks provides high capacity, high-speed bandwidth capable of transferring data and voice at speeds up to 100Gbps.

FX Networks has the newest national backhaul infrastructure in New Zealand. The Company is currently in discussions with Vodafone and Telecom to upgrade their capacity on selected routes using the FX Network.

Price and margin protection are significant factors influencing the telecommunications market. As a consequence large capital investments are subject to increasing scrutiny by larger operators. Management advise that FX Works is often able to provide additional capacity to carriers at a materially lower cost relative to the costs that those carriers would incur if they were to construct additional capacity themselves.

3.1.5 Customers

FX Networks has over 200 active customers including; the One.Govt contract, NZ Police, Vodafone, Telecom, Kordia, Transpower and REANNZ. Annuity services account for the majority of the businesses revenue and growth.

- Direct customers: Currently made up of 200+ customers supported by a local sales team which drive revenue streams from upgrades and / or cross selling of products to existing customers and by securing new customers.
- Wholesale customers, resellers and channels: Resellers (Channels Partners) have the right to on sell all FX Private Networks and Internet Service Products and are responsible for fulfilling the sales and providing first line customer support functions. There are currently 20 Channel Partners which account for over 40% of the annuity revenue each year. Wholesale partners include Orcon, Gen-i and IBM.

- Carrier services: The separation of Chorus and Telecom has enabled FX Networks to compete within this market offering a nationwide fibre network, pipeline services and construction contracts for UFB and RBI. For example, the contract with Chorus to build a 200km cable on the East Cape of NZ.

3.2 Financial performance and position

3.2.1 Historical financial performance

A summary of FX Networks' recent financial performance is set out in the table below.

Historical financial performance					
$'000 (NZD)					3m YTD
Year ending 31 March	2011	2012	2013	2014	2015
	Actual	Actual	Actual	Actual	Actual
Revenue					
Annuity Network Services	19,429	28,199	33,632	36,907	10,193
Other Telco Services	97	1,871	2,173	80	216
Dark Fibre	859	1,830	3,668	8,523	2,500
Construction	16,950	7,987	10,968	13,224	1,083
	37,336	**39,887**	**50,442**	**58,735**	**13,991**
COGS					
Annuity Network Services	(13,734)	(16,041)	(18,709)	(21,380)	(5,825)
Miscellaneous	(71)	(851)	(885)	(56)	(0)
Dark Fibre	(122)	(381)	(1,587)	(2,390)	(1,302)
Construction	(10,247)	(6,261)	(7,295)	(9,407)	(910)
	(24,175)	**(23,533)**	**(28,476)**	**(33,233)**	**(8,037)**
Payroll	(5,465)	(7,220)	(8,254)	(8,532)	(2,534)
Other Operating Expenses	(2,799)	(2,814)	(2,922)	(3,613)	(1,443)
EBITDA	**4,897**	**6,318**	**10,789**	**13,356**	**1,977**
Other income & expense	(207)	(124)	179	(81)	(2,009)
Depreciation	(6,009)	(7,611)	(8,221)	(8,708)	(2,529)
EBIT	**(1,319)**	**(1,417)**	**2,747**	**4,568**	**(2,561)**
Interest expense	(4,830)	(5,559)	(5,791)	(5,405)	(1,370)
EBT	**(6,148)**	**(6,976)**	**(3,044)**	**(837)**	**(3,932)**
Tax expense	1,763	1,896	819	(399)	-
NPAT	**(4,385)**	**(5,080)**	**(2,225)**	**(1,236)**	**(3,932)**
KPIs					
Annuity gross margin %	*29.3%*	*43.1%*	*44.4%*	*42.1%*	*42.9%*
Dark fibre gross margin %	*85.8%*	*79.2%*	*56.7%*	*72.0%*	*47.9%*
Construction gross margin %	*39.5%*	*21.6%*	*33.5%*	*28.9%*	*15.9%*
EBITDA %	*13.1%*	*15.8%*	*21.4%*	*22.7%*	*14.1%*
Interest cover (EBIT times)	(0.3)	(0.3)	0.5	0.8	(1.9)

Source: FX Networks management (Project Harrison Data Room)

Key observations on recent financial performance:

- The majority of FX Networks' total revenue is derived from annuity network services (primarily backhaul and ISP). Gross margin on annuity network services revenue has been maintained at between 42- 44% over the past three years.
- Dark fibre sales represent the proceeds from the sale of rights to use fibre assets owned by FX Networks. Dark fibre revenues approximately doubled in each year between FY12 and FY14 as the NZ Government released announcements regarding the UFB and RBI initiatives.
- Construction revenue has remained relatively steady over FY13 and FY14. The year-to-date performance of FY15 is in line with expectations.
- The increase in FX Networks EBITDA from FY11-14 has been driven largely by the revenue growth in annuity network services and dark fibre sales.

- In the first quarter of FY15, FX Networks settled a dispute with a significant customer. This resulted in a $2.5m sale of dark fibre and a cash payment of $2.0m (included in "Other expenses") to the customer by way of settlement.

3.2.2 Normalisation of historical financial performance

FX Networks' management has identified adjustments to the historical financial performance presented above which they consider necessary to reflect a normalised view of the financial performance of the business over the historical period.

We set out these adjustments to operating profit (EBITDA) below.

Normalisation of EBITDA

Normalisation of earnings (EBITDA)					
$'000 (NZD)					
Year ending 31 March		2011 Actual	2012 Actual	2013 Actual	2014 Actual
EBITDA		**4,897**	**6,318**	**10,789**	**13,356**
Normalisation adjustments	**Ref**				
Restructuring costs	a		50	211	137
Wireless project set up costs	b		59	55	
Revenue/billing adjustment	c	(200)	200		
Timing adjustments	d		(205)	205	
Normalisation adjustments		**(200)**	**104**	**470**	**137**
Normalised EBITDA		**4,487**	**6,291**	**11,760**	**13,493**

Source: FX Networks management (Project Harrison Data Room)

A brief description of each of the normalisation adjustments is provided below.

a) Restructuring costs: relate to one-off costs incurred in staff redundancies and restructuring activities undertaken during FY12 and FY13. These costs have been reversed as they do not represent recurring costs to the business.

b) Wireless project set up costs: are expenses incurred in relation to a contractor hired to establish a wireless capability in FY12 and FY13. This project was discontinued in late 2012.

c) Revenue/billing adjustment: relates a customer invoice that was erroneously raised at the end of FY11 and subsequently reversed and credited back to the customer in FY12.

d) Timing adjustments: relate to cut off adjustments to construction revenues to recognise the stage of completion at the FY12 and FY13 year ends which were previously calculated incorrectly.

3.2.3 Forecast financial performance

A summary of FX Networks' forecast financial performance is set out in the table below.

The earnings growth experienced in FY14 is projected to continue over the coming years with management forecasting EBITDA to increase to $21.9m by FY18. However, for the three months to 30 June 2014, the Company is currently running approximately 8.0% behind forecast revenue.

KPMG

Forecast financial performance					
$'000 (NZD)					
Year ending 31 March	**2014 Actual**	**2015 Fcast**	**2016 Fcast**	**2017 Fcast**	**2018 Fcast**
Revenue					
Annuity Network Services	36,907	44,711	56,503	63,764	70,818
Other Telco Services	80	2,025	2,052	2,052	2,052
Dark Fibre	8,523	7,077	3,717	3,717	3,717
Construction	13,224	11,510	12,106	12,041	12,000
	58,735	**65,323**	**74,378**	**81,574**	**88,587**
COGS					
Annuity Network Services	(21,380)	(23,951)	(30,280)	(34,378)	(38,119)
Miscellaneous	(56)	(1,087)	(1,094)	(1,094)	(1,094)
Dark Fibre	(2,390)	(2,728)	(1,125)	(1,125)	(1,125)
Construction	(9,407)	(8,367)	(10,320)	(10,320)	(10,320)
	(33,233)	**(36,133)**	**(42,819)**	**(46,917)**	**(50,658)**
Payroll	(8,532)	(9,058)	(9,524)	(10,061)	(11,404)
Other Operating Expenses	(3,613)	(3,331)	(3,621)	(3,933)	(4,640)
EBITDA	**13,356**	**16,801**	**18,414**	**20,663**	**21,885**
Other income & expense	(81)	(2,057)	(48)	(48)	(48)
Depreciation	(8,708)	(9,064)	(8,000)	(8,361)	(9,265)
EBIT	**4,568**	**5,680**	**10,366**	**12,254**	**12,572**
Interest expense	(5,405)	(5,061)	(4,249)	(3,384)	(2,245)
EBT	**(837)**	**619**	**6,117**	**8,870**	**10,327**
Tax expense	(399)	(401)	(1,713)	(2,484)	(2,892)
NPAT	**(1,236)**	**218**	**4,404**	**6,386**	**7,435**
KPIs					
Annuity gross margin %	*42.1%*	*46.4%*	*46.4%*	*46.1%*	*46.2%*
Dark fibre gross margin %	*72.0%*	*61.5%*	*69.7%*	*69.7%*	*69.7%*
Construction gross margin %	*28.9%*	*27.3%*	*14.8%*	*14.3%*	*14.0%*
EBITDA %	*22.7%*	*25.7%*	*24.8%*	*25.3%*	*24.7%*
Revenue growth	*16.4%*	*11.2%*	*13.9%*	*9.7%*	*8.6%*
EBITDA growth	*23.8%*	*25.8%*	*9.6%*	*12.2%*	*5.9%*
Interest cover (EBIT times)	0.8	1.1	2.4	3.6	5.6

Source: FX Networks management (Project Harrison Data Room)
Note: FX Networks has provided KPMG with prospective financial information for the purpose of our analysis. A summary of the underlying assumptions, provided by FX Networks, is detailed in Appendix 7 to this Report.

Key observations regarding the forecast are as follows:

- Annuity network services revenue is expected to grow at a CAGR of 17.7% over the next five years (reflecting increased data usage). The gross margins generated by annuity services are forecast to remain relatively flat over the forecast period at a level broadly consistent with historical experience;
- Construction revenues are forecast to remain relatively flat over the forecast period. Construction gross margin is forecast to decline in FY16 due to an increasingly competitive market and the completion of several large projects that have been, and are expected to continue, generating high gross margin. From 2016 onwards more conservative margins are forecast;
- Dark fibre sales of $8.5m in FY14 largely relate to a one-off sale of $7.1m to REANNZ in June 2013 at a gross margin of 72%. Dark fibre revenues are forecast at $3.7m to $7.1m per annum throughout FY15 to FY18. The forecast assumes gross margin consistent with historical experience;

- Operating expenses are forecast to increase at a slower rate than revenue as the Company benefits from increasing scale and operating efficiency.
- The 2015 forecast has been amended to reflect the settlement with a key customer (referred to in the preceding section).
- FX Networks' management believes that the full year forecast remains a fair and accurate reflection of expected performance despite the Company being 8% behind budget for the three months year-to-date.

3.2.4 Financial position

A summary of FX Networks' financial position is set out in the table below.

Financial position	
$'000 (NZD)	
As at 31 March (except as noted)	**30-Jun-14 Actual**
Current assets	
Trade & other receivables	3,976
Total current assets	**3,976**
Current liabilities	
Trade & other payables	9,020
Other current liabilities	1,637
Total current liabilities	**10,657**
Operating working capital	**(6,680)**
Non-current assets	
Fixed assets	85,612
Work-In-Progress	425
Tax payable	7,652
Other assets	2,797
Total non-current assets	**96,486**
Non-current liabilities	
Income-In-Advance account	5,420
Deferred tax liability	4,712
Total non-current liabilities	**10,132**
Net operating assets	**79,674**
Debt	
Bank loans	26,770
Finance leases	16,158
External debt	**42,928**
Shareholder loans	6,490
Total term debt	**49,418**
Cash at bank	-
Overdraft	3,894
Net debt (term debt + O/D - cash)	**53,312**
Total assets	100,462
Total liabilities	74,100
Net assets	**26,362**
Equity	
Share Capital	39,895
Retained Earnings	(9,601)
Net Income (YTD)	(3,932)
Total Equity	**26,362**
Gearing	70%

Source: FX Networks management (Project Harrison Data Room)

As of 30 June 2014, FX Networks owned approximately 3,600 kilometers of fibre optic backbone network throughout New Zealand, with a depreciated book value of fixed assets amounting to $86.0m at balance date.

Network assets have been funded by a combination of debt and equity. In recent periods, shareholder loans have been contributed in order to sustain business activities and capital expenditure.

At 30 June 2014, FX Networks' gearing ratio (calculated as net debt as a proportion of total enterprise value) was 70%. That is: approximately two-thirds of the Company's funding is debt (including shareholder loans), and one-third is equity capital. This is a high level of gearing relative to our comparable company dataset.

In the event that FX Networks Shareholders elect not to accept the Offer and the Proposed Transaction does not proceed, the Company will be required to refinance its overdraft facilities in the short term (current overdraft limit expires on 30 September 2014).

Working capital requirements

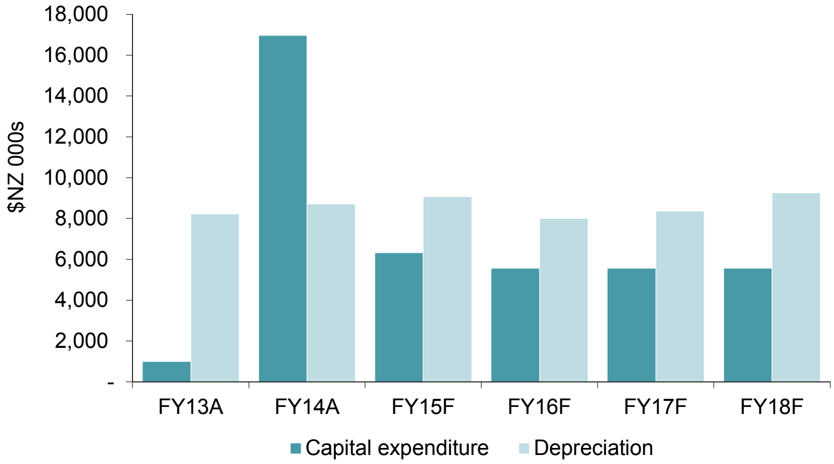
Working capital of FX Networks largely comprises accounts receivable, accounts payable and income in advance. Historically, FX Networks has generally operated with a negative operating working capital balance (which reflects its terms of trade). This is forecast to continue in the future.

Capital expenditure & depreciation

FX Networks' forecast capital expenditure and depreciation charges are summarised in the graph below. From FY15 onward capital expenditure is materially less than depreciation as much of the capital investment required to achieve the forecast growth has already been made over the last decade. FX Networks is currently depreciating its duct and fibre on the basis of a 21 year useful life. We understand that Vocus assumes a 30 year economic life for depreciating its fibre assets. The FX Networks depreciation charge is therefore higher than that which would be derived if applying Vocus' accounting policies.

Capex was particularly high in FY14 due to the installation of new Infinera Intelligent Transport Network equipment and East Cape fibre acquisition.

Capital expenditure vs. Depreciation



Source: FX Networks management (Project Harrison Data Room), KPMG analysis

4. Profile of Vocus

4.1 Business overview

4.1.1 Company history

Vocus owns and operates a telecommunications network connecting Australia and New Zealand to the global Internet backbone in the USA. Vocus utilises its domestic network to provide telecommunications services to ISP and telecommunications markets.

Vocus' additional telecommunications services also include data centre storage and dark fibre solutions. Vocus was founded by James Spenceley in March 2008 and has made a number of acquisitions since then.

Key highlights:

- March 2008 – Vocus is founded by James Spenceley
- June 2010 – Vocus is acquired by First Opportunity Fund Limited and listed on the ASX
- November 2010 – Vocus acquires the data centre business of E3 Networks for $A5.9m
- May 2011 – Vocus acquires the Perth IX data centre business for $A6.3m
- May 2011 – Vocus acquires dark fibre network (Digital River Networks) in May 2011 for $A4.0m
- November 2011 – Establishes first Points-Of-Presence in Singapore
- May 2012 – Vocus acquires the NZ data centre business Maxnet for $NZ9.5m
- July 2012 – Vocus raises an additional $A14.7m of capital in a private placement
- December 2012 – Vocus acquires fibre and data centre operator Ipera Communications Pty Ltd for $A9.8m
- February 2013 – Vocus declares its first dividend
- March 2014 - Vocus announces completion of institutional equity placement raising approx. $48.7 million of additional equity capital
- June 2014 - Vocus acquires 10% equity interest in Sea-Me-We 3 cable between Perth and Singapore
- July 2014 - Vocus announces proposal to acquire 100% of FX Networks

4.1.2 Company structure

Vocus is a publicly held company listed on the ASX. Vocus was acquired by the First Opportunity Fund ("FOF") in a reverse merger on 30 June 2010 which included a public offer of FOF shares.

Significant shareholders in Vocus as at 30 June 2014 include:

- Investec Wentworth Private Equity (10.76%);
- Perpetual Investments (9.34%);
- Commonwealth Bank of Australia (6.41%);
- Tameion (5.53%);

- Renaissance Smaller Coys (5.10%);
- James Spenceley (4.52%);
- Paul McConnell (3.93%).

As at 17 July 2014 there were 92.9m Vocus ordinary shares quoted on the ASX. Depending on the relative proportions of stock and Cash Amount that FX Networks shareholders elect to receive, Vocus will issue between 8.8m and 13.1m new Vocus shares as Equity Consideration for the Proposed Transaction. On that basis, the current shareholders of FX Networks would hold between approximately 9% and 12% of the diluted equity in Vocus upon completion of the Proposed Transaction.

4.1.3 Products & services offered

Vocus provides four essential core services: internet transit, voice services, data centres and fibre cables on core routes in capital cities. These core services can be broken down into the following seven key products and services.

Internet transit

- Vocus IP Transit: Vocus IP Transit solutions provide dedicated, carrier grade access to the Vocus network. Vocus' main network route is carried via the Southern Cross (AUS/NZ/USA) undersea cable. In addition, Vocus has a separate low latency connection to Singapore and onwards to Asia and Europe via Sea-Me-We-3.
- Vocus Wholesale DSL: Vocus offers wholesale layer 2 and 3 Digital Subscriber Line ("DSL") services. Vocus layer 2 DSL services provide access to both iiNet's and Telstra's DSL Access Multiplier coverage. Vocus layer 3 DSL services provide a DSL services bundled with IP transit. This service is designed to be competitive against the aggressive pricing seen from the larger Access Multiplier owners.
- Pacific IX: Pacific IX is an internet exchange which allows participants to connect and exchange traffic between Sydney & Auckland.

Voice services

- Vocus Wholesale Voice: Vocus offers wholesale voice services including: CTS (Call Termination Service), Number Allocation, Number Portability, E1 and IP Access and Carrier Interconnect, Vocus Wholesale Voice Coverage & Availability.

Data centres

- Vocus Colocation: Vocus Colocation has Data Centres in Melbourne, Sydney, Newcastle, Perth, Auckland and Christchurch.

Fibre cables

- Vocus Dark Fibre: Vocus Dark Fibre provides point-to-point connectivity to deliver multi-gigabit speed services. Vocus Dark Fibre is available in Adelaide, Brisbane, Melbourne, Perth and Sydney.
- Vocus Ethernet: Vocus offers Metro, National and International Carrier Grade Ethernet services. Vocus Ethernet provides services are designed to support real time applications such as Video and Voice.

4.1.4 Fibre network – Geography, Capacity

Vocus has an international network which connects Australia and New Zealand to the rest of the world, and a national network (including metro connectivity in major cities) primarily in Australia and New Zealand. Vocus has the following Points of Presence by country:

- Australia (28);
- New Zealand (13);
- USA (4);
- Singapore (1); and
- Hong Kong (1).

Figure X: The Vocus Global Network

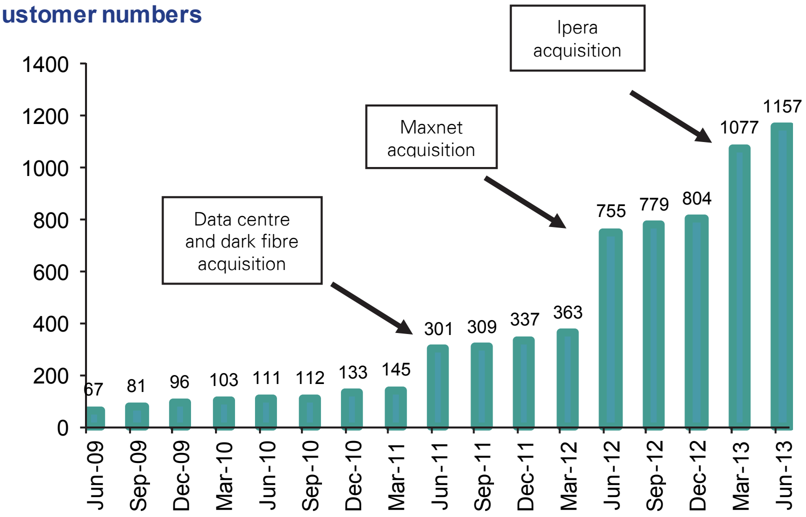
Source: Vocus Communications Limited

4.1.5 Customers

Vocus had a customer base of approximately 1,130 at the end of 2013. Vocus' FY13 full year results presentation reported that the company had exhibited customer growth of 58% in FY13.

A significant proportion of Vocus' customers have been generated via acquisition, the most recent being the acquisition of the fibre and data centre business, Ipera Communications Pty Ltd ("Ipera"), which added a further 195 customers in the third quarter of FY13.

Customer numbers



Source: Vocus Communications Limited 2013 Full Year Results Presentation (29 August 2013)

Vocus' customers are concentrated in its internet access and IP transit business which derived 40.7% of total revenues in FY13.

Management note that sourcing additional customers in Fibre and Ethernet is a key growth area for Vocus with network utilisation during FY13 at only 8.7%.

Vocus revenue by product set

AU$'000s	FY12		FY13	
	$	%	$	%
Internet	20,489	45%	27,075	41%
Data centre	9,356	21%	15,602	23%
Fibre and ethernet	5,392	12%	15,089	23%
Voice	9,842	22%	8,734	13%
	45,078	**100%**	**66,500**	**100%**

Source: Vocus Communications Limited FY13 annual report

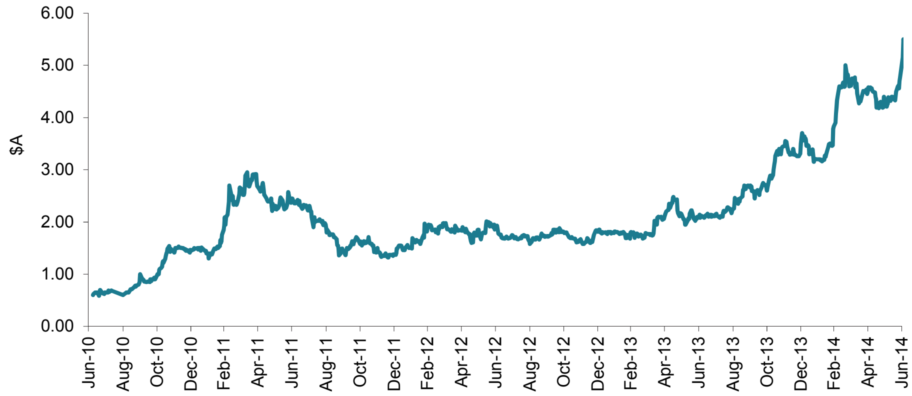
4.2 Share price and historical performance

The Equity Consideration in the Proposed Transaction is comprised of ordinary shares in Vocus. Vocus is currently listed on the Australian Stock Exchange ("ASX").

4.2.1 Historical stock performance

The share price of Vocus over the period from June 2010 to June 2014 is shown in the chart below.

Vocus share price history since inception (closing price)



Source: CapitalIQ

Key observations regarding the historical share price of Vocus are as follows:

- Vocus shares traded at $A0.60 on listing (8 July 2010). Since that time Vocus' share price has increased by approximately 643% (70% CAGR) excluding dividends. Much of this increase is on the back of the full year FY13 earnings announcement (released 29 August 2013), which highlighted revenue and EBITDA growth of 47.8% and 35.7% respectively.
- Prior to official announcement of the transaction, Vocus trading was halted on the Australian Stock Exchange (ASX) on 27 June 2014 at AU$4.76. On 31 July 2014 Vocus stock closed at AU$5.10.
- Vocus did not pay a dividend between FY10 and FY12. In FY13 Vocus paid an interim dividend of 0.4cps, followed by a final dividend of 0.6cps, taking the full year FY13 dividend to 1.0cps. In February 2014, the Directors declared an interim dividend of 0.8cps, twice the amount paid out 12 months prior. All dividends were fully franked.

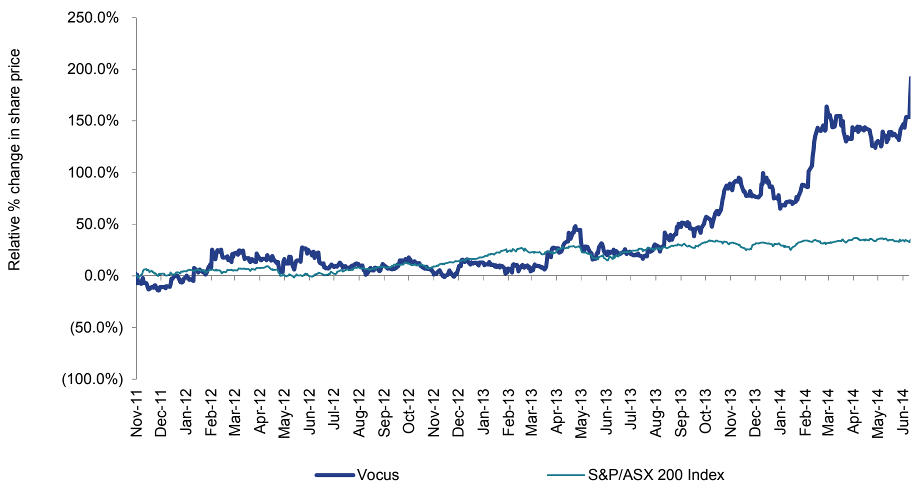
4.2.2 Benchmark analysis

To assess the performance of an investment in Vocus shares over the historical period (July 2010 – April 2014) we have benchmarked Vocus against the S&P ASX200 Index ("ASX200")[1].

Relative historical share price performance of Vocus and the ASX200 is shown in the chart below. Since November 2011 Vocus has outperformed relative to the ASX200.

[1] The ASX 200 Index consists of 200 companies listed on the ASX. The index covers approximately 78% of the Australian equity market and includes constituents from sectors such as information technology, financials, energy, materials, consumer discretionary, consumer staples, health care, telecommunication services, and utilities. The ASX 200 is composed of the ASX's top 200 companies by market capitalisation that have high liquidity and a minimum free float threshold of 30%.

Share price performance - benchmark analysis



Source: CapitalIQ

4.3 Index transition

In order to be eligible for inclusion in any of the Standard & Poors (S&P) ASX indices, a stock must meet certain criteria in respect of its listing, size and liquidity.

In March 2013, Vocus was admitted to the S&P ASX All Ordinaries index (which represents the top 500 listed Australian companies, weighted by market capitalisation). In March 2014, Vocus was admitted to the S&P ASX 300 index (which represents the top 300 listed Australian companies).

The acquisition of FX Networks may result in Vocus being added to the ASX200 Index. The ASX200 is recognised as the institutional investment benchmark in Australia and inclusion in the index is likely to result in Vocus' shares gaining a higher profile with investors and equity analysts. This may in turn lead to greater liquidity in the stock and a potential re-pricing upwards. This may partly account for the significant increase in Vocus' share price following the announcement of the Proposed Transaction.

5. Economic and industry overview

5.1 Economic overview

The New Zealand Institute of Economic Research (NZIER) predicts that New Zealand's economic growth will pick up over the next two years. Key observations in the latest NZIER Consensus Forecasts (NZIER, Consensus Forecasts, 2014) include:

- The economic recovery is further strengthening, with the Canterbury rebuild being a key driver. There is also a broadening recovery across other investment, exports and household spending;
- The NZD is expected to gradually ease from current levels, but will remain high relative to historical averages;
- Interest rates have begun to increase. NZIER expects the 90 day bank bill rate, which mirrors floating mortgage rates, to rise by 1.7 percentage points by early 2016. The floating mortgage rate is currently around 6% and could rise to 7.6% by early 2016; and
- Consumer price inflation will gradually lift from an annual average rate of 1.5% in December 2013, to 2.4% by 2016. The acceleration is gradual but will be approaching the top half of the RBNZ's 1% to 3% target.

These factors suggest a positive economic environment for FX Networks, however increasing interest rates will impact the Company's earnings given its high level of gearing.

5.2 Industry overview

The telecommunications industry can be defined broadly as fixed & mobile calling, messaging and managed & unmanaged data services. These products are delivered across a variety of platforms, including mobile, wireless and fixed line (copper, fibre and hybrid fibre-coaxial) connections. Owing to the changing nature of the underlying technologies involved, the telecommunications industry is developing significant overlaps with other industries such as IT services, entertainment, and information services.

In New Zealand and internationally there is an ongoing migration from copper networks to fibre networks to support the growth in high volume, data-intensive communications services. The Government's UFB initiative, which aims to increase the availability of fibre connectivity throughout New Zealand, is consistent with this trend. While the New Zealand fibre uptake rate cannot be predicted with certainty, it is expected that over time consumer demand will shift from copper-based services toward fibre-based services in order to benefit from their higher data speeds. This trend benefits FX Networks which provides backhaul services to other carriers and ISPs.

The telecommunications industry in New Zealand is heavily regulated, with price and non-price terms for many services set by the Commerce Commission in accordance with the Telecommunications Act 2001. The key regulated copper services are Unbundled Copper Local Loop ("UCLL"), Unbundled Bitstream Access ("UBA") and Unbundled Copper Low Frequency Service. Only fibre services provided as part of the UFB initiative are regulated. FX Networks is therefore not directly affected by Commerce Commission price controls; however regulated pricing and standards of service have an important impact on the competitive environment in which the Company operates as copper services are a substitute for fibre (albeit the services and performance levels may differ).

5.3 UFB initiative

The Ultra-Fast Broadband ("UFB") initiative was a key National party policy introduced during the 2008 general election. Following National's election, Crown Fibre Holdings was formed in October 2009 to manage the Government's $1.5bn investment in this scheme. The Government's objective is to accelerate the roll-out of UFB to 75 percent of New Zealanders by 2020. The focus in the first six years is on priority broadband users such as businesses, schools and health services, plus green field developments and certain parts of residential areas. A complimentary scheme, the Rural Broadband Initiative ("RBI") aims to bring high speed internet to the 25% of the country not covered by the UFB scheme.

A key part of the UFB initiative is Government co-investment with Local Fibre Companies ("LFCs") through Crown Fibre Holdings.

LFCs are required to allow non-discriminatory access to their infrastructure, to aid competition. Further, LFCs are not permitted to also be Retail Service Providers ("RSPs"). This required separation between network operators and retail providers and ultimately lead to the structural separation of Telecom Corporation of New Zealand Ltd and the demerger of its network arm into the separate legal entity Chorus Ltd. Telecom's structural separation has been widely recognized as having a major impact on the New Zealand telecommunications landscape.

Until structural separation, the Telecom Retail business unit bought almost all its fibre and backhaul requirements from Telecom Wholesale and Chorus (which owns the fibre and copper network assets) business units. Once Chorus was established as a separate company, Telecom has been free to purchase network capacity from a number of industry players, spending hundreds of millions of dollars each year on such services. This has created a much larger market for FX Networks and its competitors.

Another impact of the UFB initiative is the prospect of UFB "overbuild", whereby infrastructure built as part of the UFB initiative overlaps with existing fibre networks, built by companies such as Citylink, Vector, Unison and others. Overbuild increases the competitive pressures in areas where it may be occurring. Whilst overbuild is a possibility, there are also incentives for the LFCs to partner with other network companies in meeting their obligations under the UFB initiative. This is especially the case where LFCs may face capital budgeting constraints, or where other network companies may have cost advantages. An example is the recent signing of a contract between Chorus and FX Networks to build a 200km cable from Gisborne to Hicks Bay on the East Cape.

FX Networks management has stated that the UFB initiative has sparked interest in their construction and network services. Examples of this include UFB supply agreements entered into with infrastructure builders which complement their own service offering. Currently, the FX Network reaches over 90% of the interconnect points for the UFB initiative.

5.4 Demand drivers

Demand can be considered across the telecommunications industry as a whole, and also across individual segments within the industry. The migration from copper to fibre, and fibre uptake in general, is a key talking point within the industry, with intense commercial, regulatory, political and public interest into how this is managed. Chorus has stated that it is focused on leading the transition from copper to fibre-based services.

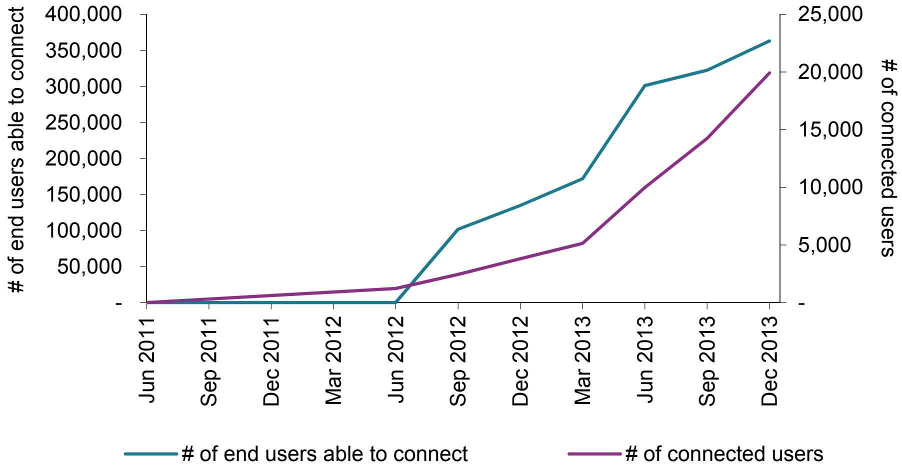
For retail users, demand for internet and networking services is driven by the quality and availability of communication and entertainment technologies. Fibre uptake is encouraged by the emergence of technologies such as Internet TV, which have large bandwidth needs and require a stable data feed.

The growth for fibre broadband will come at the expense of copper broadband as the two technologies are substitute products. Fibre is recognized as having the capability to handle the rapid growth in data usage ahead. However the copper price is expected to have an impact on fibre uptake in the near-term, as consumers show reluctance to pay more unless they require the advanced application and services that can only be used on fibre.

Whilst the quality of the product is greater than the previous copper offering, it is recognized that the UFB initiative has resulted in infrastructure being built ahead of demand. When this demand arrives is as yet uncertain, and is driven by the rate of uptake by new business, communication and entertainment technologies.

Despite uncertainty over the copper price and the precise timing for uptake of fibre, overall fibre uptake is expected to grow as the UFB initiative makes connection available to more users. Recent experience has shown that the rate of connection relative to premises passed has increased in recent months, as larger RSPs such as Telecom have offered UFB plans. This trend is illustrated in the graph below.

Ultra-Fast Broadband Connections and Uptake



Source: MBIE Broadband Deployment Update (December 2013)
Note that data on the 'number of end users able to connect' only became available in September 2012.

5.5 Competitors

5.5.1 Backhaul network

The other companies in New Zealand that own national backhaul networks are Telecom Wholesale, Vodafone (through the acquisition of TelstraClear), and Kordia. These companies therefore represent FX Network's key competitors in the provision of wholesale services. Telecom Wholesale and Vodafone dominate this market, whilst Kordia claims to have the third largest network in New Zealand. The lack of published statistics makes this difficult to verify.

5.5.2 ISP

FX Networks acts as a wholesale ISP, selling to retailer ISPs who then sell to end consumers. As such they do not compete directly with other ISPs, but rather compete with other network providers to provide the wholesale ISP service.

Pricing and quality of connection are the critical success factors that FX Networks relies on to challenge their competition. FX networks rely on a lower operating cost structure and small organization size to provide low cost and responsive services, whilst striving to offer high standards of customer service.

A table summarising FX Network's key competitors and the extent of their operations is summarized below.

Competitors		
Name	**Products that compete with FX Networks**	**Extent of operations**
Chorus	Network provider (LFC), construction	National
Vodafone	Network provider, construction, ISP	National
Northpower Limited	Network provider (LFC)	Northland
Waikato Networks Limited	Network provider (LFC)	Waikato and Lower North Island
Enable Services Ltd	Network provider (LFC)	Canterbury
Telecom Wholesale	Network provider	National
Vector	Network provider	Auckland, Wellington
Unison Networks	Network provider	Hawkes Bay, Rotorua and Taupo
Kordia	Network provider	National
Gen-I	Dark fibre; WAN and business networking services	National
Woosh	Wholesale ISP; Network provider	National
Telecom Retail	Wholesale ISP	
Now	ISP	National
CallPlus (Slingshot)	ISP	National
MaxNet	ISP	National
Orcon (now owned by Call Plus)	ISP	National
Revera	Cloud storage	National
Datacom	Cloud storage	National

5.6 Barriers to entry

To establish a national backhaul fibre network, a new entrant would need to develop or acquire an asset base and labour force capable of replicating such a network, either in whole or in part. Further, the existence of other backhaul networks owned by Telecom Wholesale and Vodafone mean that building further infrastructure would result in duplication of networks, which is highly unlikely to provide an economic return on the investment made.

6. Valuation of FX Networks

6.1 Summary of valuation conclusions

KPMG has assessed the fair market value of the equity in FX Networks in the range of $55.0m to $66.0m with a point estimate of $60.5m ($78.00 per share). The value range is based on an assessed enterprise value range of $108.7m to $119.7m less net debt and debt equivalents totaling $53.7m at the valuation date.

6.2 Methodology

KPMG has utilised two valuation methodologies in assessing the value of FX Networks:

- Discounted cash flows ("DCF"); and
- Capitalisation of earnings.

6.2.1 Discounted cash flows (DCF)

The DCF method is the theoretically preferred approach to valuation and involves discounting expected future cash flows at a discount rate reflecting the time value of money and the risks associated with the expected future cash flows to derive a net present value for the cash flow stream of the business. A terminal value at the end of the explicit forecast period is then determined and that value is also discounted back to the valuation date to provide an overall value for the business.

FX Networks management provided KPMG with financial forecasts which we have had regard to in formulating our DCF analysis.

6.2.2 Capitalisation of earnings

The capitalisation of earnings approach involves estimating a sustainable level of future earnings for a business and applying an appropriate multiple to those earnings, capitalising them into a value for the business.

The multiples applied in an earnings based valuation are based on data from listed companies and recent transactions in a comparable sector, but with appropriate adjustment after consideration has been given to the specific characteristics of the business being valued (including such factors as control and liquidity).

We adopt EBITDA as the earnings measure for the purposes of our capitalisation of earnings valuation analysis. We consider this to be the most appropriate measure of earnings due to the variation in depreciation accounting policies between companies.

6.3 Valuation date

We have assessed the value of FX Networks as at 30 June 2014, being the latest date at which balance sheet information is available (from management accounts). Subject to there having been no material changes to the Company operations or financial position since that date, our valuation assessment would also apply at the date of this report.

6.4 Standard of value

KPMG's valuation of FX Networks has been prepared on the basis of fair market value as a going concern.

Fair market value has been determined on a stand-alone basis, and is defined as what a hypothetical prudent purchaser, who is a willing but not anxious buyer, would be prepared to pay to a seller, who is willing but not anxious to sell, in circumstances where both the buyer and seller are fully informed of all operational and financial arrangements in relation to the business, and they are negotiating in an open and unrestricted market.

Fair market value assumes the existence of a notional market based on the economic conditions prevailing at the valuation date. It also assumes the asset would be exposed for sale on the market for a reasonable period.

Further, our valuation does not necessarily reflect the value to a ‘special purchaser’ who has particular connections or relationships with the company and may be able to obtain buyer specific synergies with the company being valued. A ‘special purchaser’ may pay more than a fair market valuation in recognition of the perceived extra benefits which may be available to such a purchaser.

6.5 Discounted cash flows (DCF)

We have considered the value of FX Networks using a DCF methodology using financial forecasts for the Company for the five financial years to FY18 provided by management.

Using a DCF valuation methodology (and a WACC discount rate in the range of 9.5% to 10.6%) we estimate the fair market value of the equity in FX Networks to be in the range of $50.6m to $62.8m with a point estimate of $56.7m ($73.05 per share).

6.6 Capitalisation of earnings

We have also considered the value of FX Networks business on a capitalisation of earnings basis. In deriving an appropriate multiple for the purposes of valuation we have had regard to:

- The observed earnings multiples for listed comparable companies; and
- Transaction multiples implied by recent comparable transactions within the telecommunications sector.

6.6.1 Comparable company trading multiples

The valuation of FX Networks has been considered in the context of market observed multiples of comparable companies operating within the telecommunications sector. The table below provides a summary of comparable listed companies and their observed trading multiples.

Comparable trading telecommunication companies (NZ/Australia)				
Company Name	Market capitalisation (NZ$m)	EBITDA multiple (x) Historic	Forecast	Implied growth
Australia				
Amcom Telecommunications Ltd.	564.8	13.0x	11.0x	18%
BigAir Group Limited	169.4	11.3x	8.8x	29%
iiNet Ltd.	1,269.6	8.8x	7.5x	18%
Inabox Group Limited	19.5	8.2x	n/a	n/a
M2 Group Ltd	1,123.7	9.5x	8.0x	20%
Macquarie Telecom Group Limited	131.0	5.7x	5.2x	8%
My Net Fone Limited	162.8	18.8x	14.8x	27%
Telstra Corporation Limited	69,678.9	7.8x	7.4x	5%
TPG Telecom Limited	4,711.2	14.0x	10.8x	30%
Vocus Communications Limited	476.5	18.9x	13.4x	40%
Median		**10.4x**	**8.8x**	**20%**
Average		**11.6x**	**9.7x**	**22%**
New Zealand				
Chorus Limited	687.7	3.7x	3.8x	-3%
Telecom Corporation	4,900.5	6.4x	6.4x	1%
Median		**5.1x**	**5.1x**	**-1%**
Average		**5.1x**	**5.1x**	**-1%**
Overall median		**9.2x**	**8.0x**	**18%**
Overall average		**10.5x**	**8.8x**	**18%**

Source: Capital IQ (30 June 2014), KPMG analysis
NM = not meaningful
n/a = not available
Note: The comparable companies selected have varying financial year ends. The data presented above is the based on trading results for the last twelve months and the forecast next twelve months' results;

A description of each of the companies above is set out in Appendix 3. When observing the table above the following points should be noted:

- The multiples are based on closing share prices as at 30 June 2014. Multiples that are extracted from listed company share prices invariably represent transaction multiples for a small or minority parcel of shares and are therefore normally traded at a discount to the underlying value of the company as a whole. The multiple for a 100% control of a company may be at a premium to listed comparable company multiples;
- Companies with higher earnings growth tend to trade at higher multiples;
- There are considerable differences between the operations and scale of the comparable companies when compared with FX Networks. Care needs to be exercised when comparing multiples of New Zealand companies with internationally listed companies. Differences in regulatory environments, share markets and broader economic conditions, taxation systems and accounting standards hinder comparisons; and
- Given the potential differences in the depreciation policies between companies we have focused on EBITDA multiples in our analysis.

6.6.2 Comparable transactions

The valuation of FX Networks has been considered having regard to the earnings multiples implied by the price at which broadly comparable businesses have transacted. A selection of relevant comparable transactions is set out below:

Comparable telecommunication transactions (NZ/Australia)				
Announced Date	Target	Investor	Implied enterprise value (NZ$m)	Implied EV / EBITDA (Historical)
9-Dec-13	Telecom New Zealand Australia Pty Limited	TPG Telecom Limited	479.3	8.2x
6-Aug-13	Intelligent IP Communications Pty Ltd	BigAir Group Limited	24.3	15.3x
18-Mar-13	EFTEL Limited	M2 Telecommunications[1]	59.5	16.9x
17-Mar-13	Dodo Australia Holdings Pty Ltd	M2 Telecommunications[1]	259.5	10.2x
7-Dec-12	Ipera Communications Pty	Vocus Communications Ltd	12.5	4.1x
2-Nov-12	BayCity Communications Limited	TeamTalk Ltd.	43.8	7.5x
24-Sep-12	Engin Ltd.	EFTEL Limited	11.5	3.5x
12-Jul-12	TelstraClear Limited (nka:Vodafone Fixed Limi	Vodafone New Zealand Ltd.	840.0	5.6x
16-Apr-12	Primus Telecom Holdings Pty Ltd	M2 Telecommunications[1]	247.3	4.8x
Median			**59.5**	**7.5x**
Average			**219.7**	**8.5x**

Source: Capital IQ (31 July 2014), Mergermarket, KPMG analysis

Note: (1) M2 Telecommunications Group Limited is now known as M2 Group Limited

(2) We are aware of the transaction between CallPlus Services Limited and Orcon Limited in June 2014 however there is no publically available information relating to the transaction price.

In Appendix 4 we provide brief descriptions of the comparable transactions included above.

6.6.3 Capitalisation of earnings valuation

Having regard to the comparable listed company multiples and recent industry transaction multiples detailed above, we consider an appropriate EV/EBITDA multiple for FX Networks' business to be in the range of 8.5 to 9.5 times FY14 EBITDA, or 7.0 to 8.0 times forecast FY15 EBITDA.

We assess an enterprise value for FX Networks, on a capitalisation of earnings basis, in the range of approximately $109.2m to $126.9m.

Capitalisation of earnings valuation summary		
NZ$'000s		
Multiple of historical EBITDA	**Low**	**High**
EBITDA (FY14)	13,356	13,356
EBITDA multiple (historical)	8.50x	9.50x
Enterprise value	**113,530**	**126,886**
Multiple of forecast EBITDA	**Low**	**High**
EBITDA (FY15)	15,603	15,603
EBITDA multiple (forward)	7.00x	8.00x
Enterprise value	**109,221**	**124,824**

After deducting net debt at the valuation date ($53.7m) we estimate the equity value for FX Networks (using a capitalisation of earnings valuation methodology) to be in the range of $55.5m to $73.2m with a point estimate of $64.4m ($82.93 per share).

Capitalisation of earnings - equity value		
NZ$'000s		
	Low	**High**
Enterprise value range	109,221	126,886
Net debt at valuation date	(53,691)	(53,691)
Equity value range	**55,530**	**73,195**
Midpoint equity value		**64,363**
Shares outstanding		776,124
Midpoint equity value ($/share)		**$ 82.93**

6.7 Valuation conclusion

KPMG has considered the value of FX Networks using DCF and capitalisation of earning methodologies. Having regard to this analysis we consider that the fair market value for 100% of the equity in FX Networks (on a per share basis) is in the range of approximately $70.90 to $85.10m with a midpoint estimate of $78.00 per share).

The Cash Amount offered is NZ$79.30 per FX Networks share. This is within our assessed value range.

The Equity Consideration offered for each outstanding FX Networks Share is 16.76 ordinary shares in Vocus. At 31 July 2014 the closing price for Vocus shares was AU$5.10. The NZD/AUD cross rate on that date was 0.9129. On that basis, the effective net proceeds to FX Networks shareholders from the Equity Consideration would be NZ$93.63 per FX Networks share. This exceeds our assessed value range.

Comparison of Vocus Offer to KPMG valuation ranges

6.8 Transaction synergies

FX Networks' management have identified the following potential synergies of combining the operations of Vocus and FX Networks:

- Purchase of international capacity and improved return on Vocus' IRU for Southern Cross capacity;
- Leverage of trans-Tasman services for FX Networks' New Zealand based customers requiring Australian data centre services;
- Domestic transit for Vocus' business;
- Cross sell of Vocus services and products to FX Networks' customer base;
- Enhanced voice platform for FX Networks' customers;
- Enhanced data centre services;
- Integration of FX Networks' storage offering;
- Effective route to market, unique relationships with common customers;
- Competitive advantage/scale to compete against larger incumbents; and
- Diversification and vertical integration.

Management have not quantified the potential value of these synergies. We note that any attempt to quantify deal synergies should also take into account the estimated cost to achieve any synergy benefits and the time value of money. All of the items identified above are expected to be value accretive to some extent.

We note that, for the most part, Vocus and FX Networks operate similar businesses in different locations which improve the likelihood of realising cost synergies (reduced cash outflows) through scale, in particular through rationalisation of back office functions.

6.8.1 Sharing of synergies

Given that the consideration for the offer is comprised of shares in Vocus, any synergistic benefits that accrue to Vocus post-Transaction will be effectively shared on a pro-rata basis between existing Vocus shareholders and FX Networks shareholders. Upon completion, FX Networks shareholders will hold 9-12%of the diluted equity in Vocus and will therefore accrue 9-12% of the synergies to the extent they are reflected in the market price of Vocus shares and that those shares continue to be held by FX Networks' shareholders.

7. Merits of the Proposed Transaction

7.1 Definition of Merits

Our scope is to report on the Merits of the Proposed Transaction. The term "Merits" encompasses a wide range of issues associated with the Proposed Transaction. Specifically, assessing the Merits of the Proposed Transaction requires consideration of the following factors:

- the rationale for the Proposed Transaction;
- the terms and conditions of the Proposed Transaction;
- the estimated value range of FX Networks relative to the Offer Consideration;
- the advantages and disadvantages for FX Networks shareholders of the Proposed Transaction proceeding; and
- the implications for shareholders if the Proposed Transaction does not proceed.

7.2 Value of the Vocus Offer

7.2.1 Equity Consideration

The Equity Consideration offered for each outstanding FX Networks Share is 16.76 ordinary shares in Vocus. On 31 July 2014the latest closing price for Vocus shares was AU$5.13 and the NZD/AUD cross rate was 0.9129.

On that basis, the effective net proceeds to FX Networks shareholders from the Equity Consideration would be NZ$93.63 per FX Networks share. This exceeds our assessed value range.

Potential for future price volatility

Vocus is listed and, in the absence of compelling evidence to the contrary, its traded price provides the most reliable indication of the company's underlying fair market value. However, Vocus' share price has increased significantly and exhibited considerable volatility post-announcement (Vocus' share price has traded in a range between AU$4.86 and AU$5.80, a movement of almost 20% over a period of less than five weeks and an increase of between 2% and 22% over the most recent pre-announcement close price.

The market value of Vocus' shares may increase or decrease in the future. Escrowed shareholders in particular are exposed to both upside and downside risk in the event that the share price either increases or decreases in the future.

We note that the five brokers that cover the stock have target prices in the range of AU$5.20 to AU$6.40 with an average of AU$5.60 and a median of $5.40 (source: Bloomberg 17 July 2014).

7.2.2 Option to receive portion of Consideration in cash

Under the terms of the Offer FX Networks shareholders have an option to receive a portion of their consideration in cash (up to a maximum of $20.3m in aggregate). This provides an opportunity to achieve immediate liquidity.

The Cash Amount offered is NZ$79.30 per FX Networks share. This is within our assessed value range.

7.2.3 Other considerations - positive

If the Proposed Transaction proceeds, positive impacts to FX Networks current shareholders would include:

- The Equity Consideration is comprised of Vocus shares, which are listed on the ASX. FX Networks Shareholders will benefit from the price discovery/transparency, liquidity, financial reporting disclosure and increased governance associated with a listed investment;
- Shareholders will have the ability to indirectly receive a proportional share of any post-Transaction synergies via their retained Vocus shares;
- Exchanging FX Networks Shares for Vocus shares will provide Shareholders with a more diversified investment (both in terms of geographical spread and across business/service types).

7.2.4 Other considerations - negative

If the Proposed Transaction proceeds, negative impacts to FX Networks current shareholders would include:

- FX Networks Shareholders would be diluted (that is: they would hold a smaller proportion of the outstanding Vocus shares than they currently hold of FX Networks Shares);
- FX Networks largest Shareholder (Peregrine Company Managers Ltd) currently holds a 33.5% stake which, while not providing control, is sufficient for blocking purposes. Under the terms of the Equity Consideration Peregrin would hold approximately 4% of Vocus post-Transaction which is too small a stake to confer any meaningful influence. This may be a consideration for Peregrin;
- Escrow requirements: the Offer is conditional upon 50% of the Vocus Shares received pursuant to the Offer being subject to escrow arrangements. These escrow arrangements require all of the escrowed shares to be retained for six months after issue and 50% to be retained for 12 months. This arrangement excludes the first 40,000 Vocus Shares received by each Shareholder;
- As Vocus is an Australian domiciled company, shareholders resident in New Zealand will not be able to utilise franking credits issued by Vocus (due to the lack of mutual recognition of Australian franking credits and New Zealand imputation credits). This could result in the double taxation of dividends for New Zealand shareholders. There may potentially be further adverse tax impacts for specific shareholders depending on their particular circumstances. We recommend that Shareholders obtain independent tax advice in respect of the tax implications of the Offer Consideration having regard to their specific personal circumstances and tax status.

7.2.5 Possible outcomes under the Vocus Offer

The Vocus Offer is for 100% of the fully diluted share capital in FX Networks. The Pre-Bid document includes a requirement for Target Shareholders that have entered into the Lock-Up Agreement to exercise their Drag-Along Rights in respect of minority shareholders to ensure that Vocus acquires 100%.

The Vocus Offer is conditional upon achieving 90% acceptance (which would trigger the compulsory acquisition provisions of the Code).

As a consequence of the Drag-Along Rights, we consider that there is only a remote technical risk that Vocus will not satisfy its condition of achieving 90% acceptance.

7.3 Implications of rejecting the Vocus Offer

If the Vocus Offer is rejected FX Networks Shareholders will be left holding an illiquid investment with no clear path to achieve an exit in the near term.

At 30 June 2014 FX Networks had total debt outstanding of $53.7m. The Company's gearing ratio was 70%. In each of the last three financial years, the Company's earnings before interest and tax (EBIT) has been insufficient to cover its interest expense.

The forecasts provided by FX Networks indicate that the Company will become cashflow positive during FY15.

However, the Company may face cashflow constraints in the short term. In the event that the Vocus Offer is rejected by FX Networks Shareholders, the Company will need to immediately refinance its bank debt as the current facility is due to expire in September 2014. The terms of any future refinancing are uncertain and there is a potential risk that the Company secures funding on less favourable terms than are currently in place.

7.4 Alternative options for achieving liquidity and/or exit

In the event that the Proposed Transaction does not proceed, and the directors remain committed to achieving an exit event, FX Networks will need to consider alternative options for exit. These may include:

- Initial Public Offering ("IPO");
- Competing offer (Trade buyer) ; or
- Competing offer (Financial investor).

We summarise below the positive and negative implications of these alternatives.

7.4.1 IPO

Positive implications for FX Networks Shareholders

- Provides liquidity & price discovery;
- Provides a mechanism to facilitate subsequent future capital raisings.

Negative implications for FX Networks Shareholders

- A listing process would incur significant costs (these include preparing an Investment Statement and/or Prospectus, preparing prospective financial information, completing financial & legal due diligence, Share Registrar fee, underwriting fees, marketing & printing expenses, listing fees). Guidance provided by NZX estimates these costs at approximately 5-10% of funds raised;
- The process of undertaking an IPO would be expected to take around four to six months to complete and would require significant input from management and the board (distracting them from the day-to-day running of the business);
- An IPO may not provide any potential value uplift to FX Networks Shareholders other than liquidity (i.e. no potential for synergistic benefits);
- There is significant uncertainty as to whether an IPO could be successfully executed and at what price.

7.4.2 Competing offer (Trade sale)

Positive implications for FX Networks Shareholders

- A trade sale may provide FX Networks the opportunity (albeit highly uncertain) to secure some portion of the synergistic benefits through the sale negotiation process.

Negative implications for FX Networks Shareholders

- The prospect of a competing bid from another trade buyer is speculative at this point – we are not aware of any other offers or expression of interest;
- The Vocus Offer implies a value that exceeds KPMG's assessed value range for the Company (on a scrip basis). We consider it unlikely that an alternative trade buyer would be willing to pay a materially higher price.

7.4.3 Competing bid (financial investor)

Positive implications for FX Networks Shareholders

- A financial investor would provide capital to strengthen the Company's balance sheet and fund capex;
- A financial investor would provide additional governance and strategic advice in order to maximise the value of their investment;
- A capital injection by a financial investor would allow FX Networks Shareholder to retain their interest (albeit diluted) in the Company and enable them to participate in potential future upside.

Negative implications for FX Networks Shareholders

- A financial investor is likely to be conservative in their bid price, in order to maximise their returns from the investment. We are aware of previous indicative approaches to provide capital, which were at a significantly lower price per Share;
- Dilution of existing Shareholders;
- No synergistic benefits;
- A purely financial buyer (such as a private equity buyer) would most likely only seek to acquire a partial stake. Shareholders would not necessarily achieve liquidity as a result of this transaction;
- The prospect of a capital injection from a financial investor is speculative at this point – we are not aware of any current offers other than one private equity offer, received in April 2014, which is discussed in more detail in the following section.

Private Equity offer

In April 2014 FX Networks received a competing offer ("PE Offer") from an Australia-based private equity firm ("the PE Bidder"). FX Networks directors elected not to pursue the PE Offer at that time as it was considered inferior to the Vocus Offer. We have reviewed the terms of the PE Offer and make the following high level observations

Summary of the terms of the PE Offer

The key terms of the PE Offer were as follows:

- The PE Bidder valued the Company at an enterprise value of NZ$124.0m, and an equity value of $71.3m ($90.30 per share) subject to variation as described below;
- The PE Offer was for an unspecified shareholding amount (up to 100%);
- The PE Bidder offered to acquire shares from shareholders wishing to exit their investment in FX Networks. Exiting shareholders would have received consideration in cash;
- The PE Bidder would also repay outstanding shareholder loans and have new shares issued in consideration (effectively the PE Bidder would have purchased shareholder debt at face value and then swapped that debt for equity);
- The cash consideration to be paid to exiting shareholders may have varied from the headline $90.30 per share depending on:
    - how many shares FX Networks shareholders elected to sell into the PE Offer, relative to the number of shares that would be retained ("rolled"); and
    - the price at which remained FX Networks shareholders agreed to "roll" their shares (this is the price that would be used to determine how many new shares the PE Bidder would be issued with in exchange for repaying the shareholder loans).

  Under the terms of the PE Offer, exiting shareholders may have received as much as $98.70 per share if either:
    - a minimum of 50% of all FX Networks shares were "rolled" at $82.00; or
    - a minimum of 75% of all FX Networks shares were "rolled" at $87.50.

Positive implications for FX Networks Shareholders

- For those FX Networks Shareholders that wished to exit, the PE Offer provided an opportunity to do so immediately and in cash;
- The PE Bidder would have provided additional governance and strategic advice in order to maximise the value of their investment;
- FX Networks Shareholders would have had the ability to retain an interest (albeit diluted) in the Company, enabling them to participate in potential future upside;
- Dilution would have been minimal (only to the extent that "rolling" shareholders agreed to allow a lower per share price for the purposes of issuing new shares to the PE Bidder in consideration for repaying the shareholder loans).

Negative implications for FX Networks Shareholders

- Potential dilution of existing Shareholders;
- No synergistic benefits;
- We understand that the PE Bidder indicated a minimum holding period for the investment of at least three years. The "rolling" shareholders would not have achieved any near term liquidity benefits as a result of this transaction;
- The PE Bidder had not yet undertaken any commercial, financial or legal due diligence on the Company – the terms of the PE Offer were subject to substantial revision prior to finalisation and, as such, the indicative pricing of the Offer was highly uncertain;

- The PE Offer provided a benefit to exiting shareholders at the expense of "rolling" shareholders.

7.5 Merits of the Proposed Transaction

In our opinion, after having regard to all relevant factors, the Offer Consideration and the terms and conditions of the Proposed Transaction, we are of the view that:

- The Equity Consideration is above KPMG's assessment of the underlying value of the Company (this is partly due to the significant increase in the price of Vocus shares following the announcement of the Proposed Transaction);
- The Cash Amount is within KPMG's assessment of the underlying value of the Company;
- The Proposed Transaction provides FX Networks Shareholders an opportunity to realise the value of their existing investment.
- The Offer Consideration provides a greater degree of liquidity to FX Networks Shareholders than their current holdings (albeit not to the same extent for those shareholders that will be subject to escrow provisions restricting the sale of Vocus shares in the 12 months following the Transaction);
- Vocus' share price may increase or decrease in the future. Shareholders need to consider their exposure to future price volatility (particularly those shareholders whose shares are subject to escrow);
- The Proposed Transaction provides Shareholders the ability to retain some interest in the future of the Company via holding Vocus shares, however FX Networks Shareholders would be diluted as a consequence of the Proposed Transaction (that is: they would hold a smaller proportion of the outstanding Vocus shares than they currently hold of FX Networks Shares);
- The Proposed Transaction enables Shareholders to receive a proportional share of any synergistic benefits that may arise from the Transaction via their retained Vocus shares;
- As Vocus is an Australian domiciled company, shareholders resident in New Zealand will not be able to utilise franking credits issued by Vocus (due to the lack of mutual recognition of Australian franking credits and New Zealand imputation credits). This could result in the double taxation of dividends for New Zealand shareholders. There may potentially be further adverse tax impacts for specific shareholders depending on their particular circumstances. We recommend that Shareholders obtain independent tax advice in respect of the tax implications of the Offer Consideration having regard to their specific personal circumstances and tax status;
- The Proposed Transaction provides the benefits of an IPO (liquidity, governance, access to capital) without having to incur the time, cost or management distraction of undertaking the listing process directly;
- In the event that FX Networks Shareholders elect not to accept the Offer and the Proposed Transaction does not proceed, the Company will be required to refinance its overdraft facilities in the short term (current overdraft limit expires on 30 September 2014).

When considered relative to the potential alternatives we conclude that the Proposed Transaction confers all of the benefits of the alternatives while limiting the negative impacts.

Appendix 1 - Information relied upon

In completing the Report we have received and relied upon the following information.

Private information

- FX Network historical and forecast financial information
- FX Networks share register
- FX Networks capex schedule
- FX Networks monthly management accounts
- FX Networks normalisation adjustments
- Copy of the Takeover Notice and Offer Document dated 25 July 2014
- Discussions with FX Networks management

Public information

- Companies Office website
- Capital IQ
- Bloomberg
- NZIER forecasts
- Vocus Annual Reports and Presentations
- Statistics New Zealand
- Reserve Bank of New Zealand
- The Treasury
- ANZ Business Confidence Survey
- Thomson One
- Ministry of Business, Innovation & Employment (MBIE) Broadband Deployment Update (December 2013)

Appendix 2 – Qualifications & declarations

Qualifications

This Report has been prepared by KPMG Corporate Finance. KPMG Corporate Finance provides advisory services in relation to mergers and acquisitions, independent appraisal reports, valuations and other corporate advisory services.

The people responsible for preparing the Report were Justin Ensor, Partner, (CA, PGDip Applied Finance & Investment, Securities Institute of Australia, BCom University of Auckland) and Troy Newton, Partner, (CA, BCom). Justin and Troy each have significant experience in valuations, preparing independent appraisal reports and advising on mergers and acquisitions.

Declarations

KPMG Corporate Finance has prepared the Report at the request of the Independent Directors of FX Networks Limited.

It is not intended for the Report to be used for any other purpose.

The Report has been provided for the benefit of Shareholders of FX Networks Limited.

KPMG Corporate Finance consents to the issuing of this Report to the Shareholders of FX Networks Limited.

KPMG Corporate Finance provided a draft of this Report to the Independent Directors of FX Networks Limited to confirm the factual accuracy of the Report. There was no alteration to the conclusion as a result of issuing the draft Report.

KPMG Corporate Finance consider that they have had access to all relevant information.

The assumptions we have relied on to form our opinion are clearly indicated within the body of the Report.

KPMG will receive a fixed fee for the preparation of this report. The fee is not contingent on the outcome of the Proposed Transaction.

Independence

KPMG does not have at the date of this report, and has not had, any relationship with FX Networks or Vocus that could reasonably be regarded as capable of affecting our ability to provide an unbiased opinion in relation to this transaction.

KPMG Corporate Finance will receive a fee for the preparation of this report. This fee is not contingent on the conclusions of this report or the outcome of the voting in respect of the Proposed Transaction. We will receive no other benefit from the preparation of this report.

Consents

We consent to the issuing of this report in the form and content in which it is to be included in the notice of meeting to be sent to FX Networks shareholders. Neither the whole nor any part of this report, nor any reference thereto may be included in any other documentation without our prior written consent as to the form and context in which it appears.

Indemnity

FX Networks has agreed to indemnify KPMG to the maximum extent permitted by law, against any and all costs, expenses or liabilities we incur to any person:

- In relation to any claim against us by a third party arising from or connected with any breach of FX Networks' obligations to us;
- By relying on any information provided to KPMG by FX Networks or on FX Networks' behalf and which is false, misleading or incomplete.

Appendix 3 - Comparable listed companies

A brief description of each of the comparable companies listed in Section 8 is outlined below:

Amcom Telecommunications Limited

Amcom Telecommunications Limited operates as an information technology (IT) and telecommunications company in Australia. The company offers data and network solutions, including Internet and Ethernet services, fibre-optic point-to-point connectivity solutions, managed router services, and VPN link services. In addition, the company offers IT services, such as systems; communications; information, communication, and technology consulting; and security, governance, risk, and compliance services. For the period ending 30 June 2013, Amcom reported revenue in excess of $180 million and $235 million of assets.

iiNet Limited

iiNet Limited provides Internet and telephony services to residential, regional government, and corporate customers in Australia. The company offers business solutions comprising Internet solutions, such as ADSL broadband; business bundles; virtual private network plans; bonded and naked DSL; mobile broadband solutions; SHDSL that offers high speed connectivity; and fibre connections. In addition, the company provides residential products comprising Internet services, such as ADSL broadband, naked DSL, mobile broadband, national broadband network, fibre plans, dialup Internet, and Wi-Fi hotspots services. It has approximately 650,000 ADSL subscribers, supporting 1.6 million broadband, telephony, Internet Protocol TV, and other services. For the period ending 30 June 2013, reported revenue was in excess of $1,072 million and $942 million of assets.

My Net Fone Limited

My Net Fone Limited provides voice communications, broadband Internet, and cloud based communications services to residential, business, government, and wholesale customers in Australia and internationally. The company offers home phone-VoIP, DSL Internet, national broadband network Internet, and mobile VoIP services. For the period ending 30 June 2013, reported revenue was $52.7 million.

Chorus Limited

Chorus Limited, a telecommunications utility company, provides fixed line communications infrastructure services in New Zealand. The company offers access to its network assets for phone and Internet providers to deliver their own voice, data, and Internet services to their customers. The company's infrastructure services also comprise direct fibre access service that offers a fibre optic connection between an end-user and their retail service provider's equipment in the local exchange. In addition, it offers access to its exchanges, poles, and other infrastructure to retail service providers and other network operators to place their equipment; and field services to end-customers on behalf of service providers. The company operates approximately 130,000 kilometres of copper cable, and approximately 32,000 kilometres of fibre cable connecting homes and businesses to local exchanges, and roadside cabinets. As of 30 June 2013, it had approximately 1,784,000 fixed line connections.

BigAir Group Limited

BigAir Group Limited, together with its subsidiaries, provides fixed wireless broadband solutions for businesses and campus environments in Australia. It operates in two segments, Fixed Wireless for Business and Community Broadband. The company owns and operates the fixed wireless Ethernet broadband network that covers Sydney, Melbourne, Brisbane, Perth, Adelaide, Newcastle, Gold Coast, Sunshine Coast, and Darwin cities. It also provides private data links for a wide area network to multi-site businesses, including retailers and national organizations; and high-speed Internet access services. In addition, the company offers outsourced managed Internet services in the tertiary student accommodation market. It provides broadband and data services primarily through its channel partners comprising ISPs, carriers, and other IT service companies.

Inabox Group Limited

Inabox Group Limited is a holding company and through its subsidiary buys capacity from telecom operators and sells it to direct resellers. The company's products include telecommunications products and services such as fixed wire services comprising traditional and digital phone lines; mobile voice and data services; Internet services; inbound telephone services; hosted voice services; hosting products, such as Web, domain name services, and Email; and mobile handsets and SIM cards, routers, and hosted voice hardware products.

Macquarie Telecom Group Limited

Macquarie Telecom Group Limited provides various telecommunication and hosting services to corporate and government customers in Australia. The company offers data network and Internet services, including Internet and broadband business services; wide-area-network optimization services; remote access services; IP VPN applications with MPLS and QoS, and IP migration services; IP network infrastructure; managed network and managed router solutions; and integrated data services. It also provides voice and mobile telecommunications services, such as business fixed line and VoIP solutions; SIP trunking; inbound call centre services; voice and Web conferencing services; and mobile broadband, network, voice, and data services.

M2 Group Limited

M2 Group Limited provides telecommunications services to residential and business customers in Australia and New Zealand. It operates in two operating segments, Retail and Wholesale. The Retail segment offers telecommunications services, including line rental services, mobile voice and data services, and terrestrial dial-up and high speed broadband Internet services. The Wholesale segment offers a suite of fixed line voice services, including line rental services, mobile voice and data services, terrestrial dial-up and high speed broadband Internet services, and mobile telephone hardware to the telecommunications reseller market. The company offers its products and services under the iPrimus, Dodo, Commander, and M2 Wholesale brand names.

Telstra Corporation Limited

Telstra Corporation Limited provides telecommunications and information services to individuals, businesses, governments, and enterprises in Australia and internationally. The company provides a range of telecommunication products, services, and solutions across mobiles, fixed and mobile broadband, telephony, and pay television to consumers; and communication based products and solutions to small-to-medium enterprises. In addition, the company provides wholesale telecommunication products and services to other carriers, carriage service providers, and Internet service providers, as well as invests in digital media content, services, and applications businesses. It serves approximately 15.1 million mobile customers in Australia; 7.8 million fixed voice customers; 3.9 million mobile customers in Hong Kong; 2.8 million fixed retail broadband customers; and 1.6 million customers on bundled plans.

TPG Telecom Limited

TPG Telecom Limited provides telecommunications services to residential users, small and medium enterprises, government, and large corporate enterprises primarily in Australia. The company offers ADSL2+, fibre optic and Ethernet broadband access, telephony services, internet protocol television, SIM only mobile plans, mobile broadband, and various business networking solutions. It also provides dialup, SHDSL, VoIP, phone card, domain name and Website hosting, post office protocol version 3 and Internet message access protocol email account, Internet protocol addressing, IPTV, and mail list server services.

Telecom Corporation of New Zealand Limited

Telecom Corporation of New Zealand Limited provides telecommunications and IT services primarily in New Zealand and Australia. IT operates in five segments: Retail, Wholesale & International, Gen-i, AAPT, and Technology & Shared Services.

1. Retail segment: provides fixed line, mobile, and Internet services to consumer, small and medium-sized enterprise (SME), corporate, enterprise, and wholesale customers;
2. Wholesale & International segment: offers voice, mobile, interconnects, managed data, and international products and services to telecommunications service providers;
3. Gen-i segment: integrates IT and telecommunications services to provide converged information and communication technologies solutions;
4. AAPT segment: offers telecommunications services to business and wholesale customers; and
5. Technology & Shared Services segment: maintains and develops Telecom’s New Zealand shared IT and network operations and other shared services.

The company also leases telecommunications equipment to third parties; procures and leases assets; and operates as an Internet service provider, as well as is involved in property investment activities. It has approximately 1 million fixed line residential and SME customers in New Zealand; 2 million mobile connections to consumer and business customers in New Zealand; 800,000 fixed and mobile Internet and broadband customers in New Zealand; 3,000 business clients across Australasia using Gen-i's ICT services; 6,000 business and 300 wholesale customers in Australia using AAPT's services; and 4,000 businesses customers connected with fibre.

Appendix 4 - Recent transaction evidence

A brief description of each of the transactions listed in Section 8 is outlined below:

Telecom New Zealand Australia Pty Limited / TPG Telecom Limited

TPG Telecom Limited entered into a binding agreement to acquire Telecom New Zealand Australia Pty Ltd from Telecom Corporation of New Zealand Limited for AUD 450 million on December 9, 2013.

Telecom New Zealand Australia Pty Limited provides managed telecommunication and related information technology management services to large enterprises.

Intelligent IP Communications / BigAir Group

BigAir Group acquired Intelligent IP Communications for AUD 20 million on August 6, 2013.

Intelligent IP Communications, a corporate unified communications carrier, provides IP telephony, video conferencing, private data networks, and secure high-speed Internet services to businesses worldwide.

EFTEL / M2 Group

On 6 May 2013, M2 Group acquired 100% shareholding of EFTEL for AU$49.4 million (including $5.6 million of assumed liabilities). EFTEL is a provider of broadband, wireless broadband, mobile, home phone services. M2 Group Limited is a company engaged in the supply of telecommunications services to residential and business customers. The transaction was expected to increase EFTEL's presence worldwide and enhance its product and service offering to its customers.

Dodo Australia / M2 Group

M2 Group acquired Dodo Australia Holdings from Larry Kestelman and Michael Slepoy for approximately AUD 200 million in cash and stock on March 17, 2013. In a related transaction, M2 Group Limited entered into a bid implementation agreement to acquire EFTEL Limited on March 18, 2013. The transaction was not conditional upon completion of EFTEL acquisition.

Dodo Australia provides telecommunication services to residential consumers and corporate markets in Australia.

Ipera Communications / Vocus Communications Ltd

Vocus acquired entered into a binding agreement to acquire Ipera Communications Pty. Ltd for AUD 9.7 million in cash and stock on December 7, 2012. The consideration was AUD 9.7 million with 50% of the purchase price subject to a 12 month earn out targets.

Ipera operates as a fibre and data centre operator in Australia. It offers services, such as ADSL1 and ADSL2, Ethernet over copper from 2Mbps up to 40Mbps, Ethernet over fibre from 2Mbps up to 10Gbps, dark fibre, wireless, and microwave wireless; and high speed Internet, private networks, virtual servers, virtual firewalls, dedicated servers, disaster recovery, cloud telephony, and colocation services.

BayCity Communications / TeamTalk

TeamTalk acquired BayCity Communications Limited for NZD 41.9 million on November 2, 2012.

BayCity Communications Limited provides IPSTAR satellite based communication services for business, government, and corporate customers in Australia and New Zealand.

Engin / EFTEL

EFTEL Limited acquired Engin Limited from Seven Group Holdings for AUD 9.1 million on September 24, 2012. The acquisition also includes acquisition of customer contracts and intellectual property of Engin.

Engin Limited provides broadband telephony services and sells related hardware products under the 'engine' name to residential and small business customers in Australia.

TelstraClear / Vodafone

Vodafone New Zealand acquired TelstraClear Limited from Telstra Corporation for NZD 840 million in cash on July 12, 2012.

TelstraClear Limited provides telecommunications and information services in New Zealand and internationally. The company's products and services for business customers comprise Internet services, which include broadband Internet, Dial Up Internet, domain name services, and email hosting services; mobile services, such as mobile voice, mobile data, and a range of mobile handsets; and voice services, such as local, national, and international call services, as well as IP, ISDN conference calling, managed voice, and toll-free services.

Primus / M2 Group

M2 Group entered into a binding equity Purchase Agreement to acquire Primus Telecom Holdings for approximately AU$190 million on April 16, 2012. Primus Telecom Holdings Pty Ltd is a telecommunications carrier providing internet, ecommerce, mobile and home phone telecommunications and Australian operations of Primus Telecommunications Group, Inc. The deal value was subject to adjustments. M2 also announced the launch of a fully underwritten one for four renounceable entitlement offers to all eligible shareholders to raise approximately AU$83.1 million to partially fund the acquisition. M2 Group funded the acquisition and refinance existing debt through proceeds received from the AU$83.1 million entitlement offer and a new 3 year, AUD 182.5 million senior bank facilities.

The acquisition is expected to add significant scale and will contribute to sales and support capability and also ensuring that M2 is well prepared for the National Broadband Network requirements.

TransACT Capital Communications / iiNet

iiNet Ltd acquired TransACT Capital Communications Pty from TVG Capital Partners Limited, ACTEW Corporation Ltd., Motor Trades Association of Australia Superannuation Fund, Jemena Asset Management Pty Ltd. and other shareholders for AUD 60.1 million on November 21, 2011.

TransACT Capital Communications provides subscription television, and phone and broadband services to residents and businesses in Canberra and Queanbeyan, Australia.

IntraPower / TPG Telecom

TPG Telecom Limited entered into a takeover bid implementation agreement to acquire remaining 80.1% stake in IntraPower Limited for AU$10.2 million on 14 July 2011.

IntraPower Limited provides on-demand information, communication, technology, and telecommunications services to small and medium sized businesses in Australia. It offers business on-demand, desktop on-demand, infrastructure on-demand, and data communication on demand solutions. The company's business on-demand solution delivers unified IT, voice, data communications, and infrastructure as a service using the next generation of cloud computing technology. It offers its products through a network of partners.

Pipe Networks / TPG Telecom

SP Telemedia Limited (ASX: SOT) (SPT) entered into a merger implementation agreement to acquire remaining 95.26% stake in PIPE Networks Limited (ASX: PWK) for approximately AUD 350 million on November 11, 2009.

PIPE Networks Limited provides telecommunications services to Internet service providers, telecommunications carriers, and the corporate marketplace in Australia. The company builds, owns, and maintains optical fibre network and delivers the Dark Fibre services.

People Telecommunications / M2 Group

M2 Group Ltd. (ASX: MTU) signed a scheme implementation agreement to acquire People Telecom Ltd. (ASX: PEO) for AUD 18.3 million on December 4, 2008.

People Telecommunications Pty Ltd., a telecommunications company, provides broadband hi-speed Internet access, fixed wire phone, and mobile phone services, as well as corporate data products for homes and businesses in Australia. In addition, it offers a suite of data solutions comprising Web hosting, domain registration, off-site storage, wide area network, and virtual private network services.

TPG Holdings / SP Telemedia Limited (now known as TPG Telecom Limited)

SP Telemedia acquired TPG Holdings Pty. Ltd. for AUD 244.5 million in cash and stock on February 7, 2008. Through the transaction SP Telemedia indirectly acquired a 70.25% stake in Chariot Limited through the acquisition of TPG. On 25 November 2009, following shareholder approval, SP Telemedia Ltd (trading as Soul) changed its name to TPG Telecom Ltd.

TPG Telecom Limited provides telecommunications services to residential users, small and medium enterprises, government, wholesale customers, and large corporate enterprises primarily in Australia. The company offers ADSL2+, fibre optic and Ethernet broadband access, telephony services, Internet protocol television, SIM only mobile plans, mobile broadband, and various business networking solutions.

PowerTel / Telecom

Telecom Corp. of New Zealand acquired PowerTel on April 23, 2007 for AUD 295.10 million in cash.

PowerTel Ltd. offers data, voice, and Internet solutions for small and medium businesses, large corporates, carriers, and other telecommunication service providers in Australia.

B Digital / SP Telemedia Limited (now known as TPG Telecom Limited)

SP Telecommunications (now known as TPG Telecom Limited) acquired the remaining 54.2% stake in B Digital for a reported value of approximately AUD 71.98 million in cash on November 1, 2006.

B Digital provides telecommunication services, including mobile post-paid and prepaid, Internet, voice over Internet protocol, and fixed wire services to consumers and businesses.

Appendix 5 – Regulatory overview

Telecommunications Act 2001

The telecommunications sector in New Zealand is governed principally by the Telecommunications Act 2001 (the "Act"). The Act provides for certain telecommunications services to be regulated by the New Zealand Commerce Commission (the Commission). Most services can be regulated under the Act on price and non-price terms, while other services may only have non-price terms determined.

The price and non-price terms for the regulated services are determined by the Commerce Commission in Standard Terms Determinations ("STDs"). The Act specifies that the price determination must be made in accordance with any applicable pricing principles. Wholesale services are priced on a "cost-plus" basis (i.e. an initial pricing principle of benchmarking against prices for similar services in comparable countries that use forward looking cost-based pricing methods). However the UBA service is an exception, and is currently priced on a "retail-minus-a-discount" basis. Under an Amendment to the Act (Telecommunication Amendment Act 2011), UBA service pricing will also adopt the forward looking cost-based method set by the Commerce Commission, effective from 1 December 2014.

Given that Telecom is precluded from being an access seeker of the regulated UCLL service until 1 December 2014, it is potentially exposed to fluctuations in regulated input service costs in a different way from its competitors that can purchase all of those services. This creates an opportunity for FX Networks to supply Telecom at a lower price than Chorus.

Commerce Commission Pricing Review

On 3 December 2012, the Commerce Commission (the "Commission") released the final benchmarked UCLL decision which reduced the price by 3.8% to $23.52 per month. Chorus applied for a Final Pricing Principle ("FPP") review of the decision.

The Commission released the final benchmarked UBA decision on 5 November 2013, proposing a reduction in price of around 50% from $21.46 to $10.92 per month. Again industry participants were not satisfied with this decision and subsequently applied for an FPP review. Both UBA and UCLL pricing are to be determined by the Commission using FPPs, due to be completed by 1 December 2014.

The significant drop in proposed UBA price is because the Commission intends to move UBA to a cost-plus basis, as opposed to the current retail-minus pricing assessment. The price cut is significant and could have the impact that copper prices "undercut" fibre prices. Chorus has contended that this would have the impact of inhibiting fibre uptake, as it would become relatively more expensive. They further state that RSPs would remain focused on legacy services, as they can increase margins without a noticeable benefit to the consumer.[2] The Coalition for Fair Internet Pricing opposes Chorus' view, stating that increasing the price of copper will inhibit overall broadband uptake, counter to the Government's policy aims.

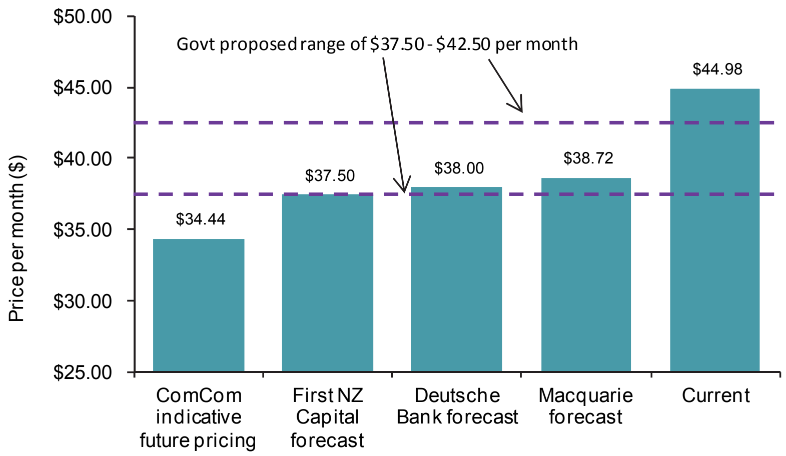
A complicating factor for the Commission's pricing review is that the Government has launched a review of the Telecommunications Act 2001. This review has the potential to

2 Chorus submission to the Commerce Commission, February 2013.

result in legislative override of the current policy framework and the Commerce Commission's pricing Review. The full review is not expected to be completed until March 2019 (www.beehive.govt.nz, 8 February 2013).

The copper price has a far-reaching impact on the telecommunications industry. A low price has been alleged to inhibit the uptake of UFB and fibre in general, and also to hold back Chorus' ability to invest. Given the uncertainty created by the differing policy and regulatory paths, the future outlook for copper pricing is uncertain. The graph below illustrates the price alternatives and broker estimates of likely outcomes.

Copper pricing



Source: Commerce Commission, Chorus broker research (ThomsonOne)

Review of the Telecommunications Act 2001

The Government's discussion paper proposes a phased approach to a review of the telecommunications regulatory framework, with an immediate focus on copper pricing. It proposes that Chorus' combined copper (UCLL and UBA) prices should be roughly equivalent with Chorus' contracted entry level fibre prices.

Telecommunications Development Levy ('TDL')

The Telecommunications (TSO, Broadband, and Other Matters) Amendment Act 2011 introduced the Telecommunications Development Levy (TDL), which is an industry levy of NZ$50 million per year between FY10 and FY16 and NZ$10 million each year thereafter (adjusted for CPI), to be paid by certain market participants (termed liable persons) annually in arrears. The levy can be used to pay for any TSO charges, non-urban telecommunications infrastructure, upgrades to emergency calling and other wider purposes, as long as a consultation process is followed.

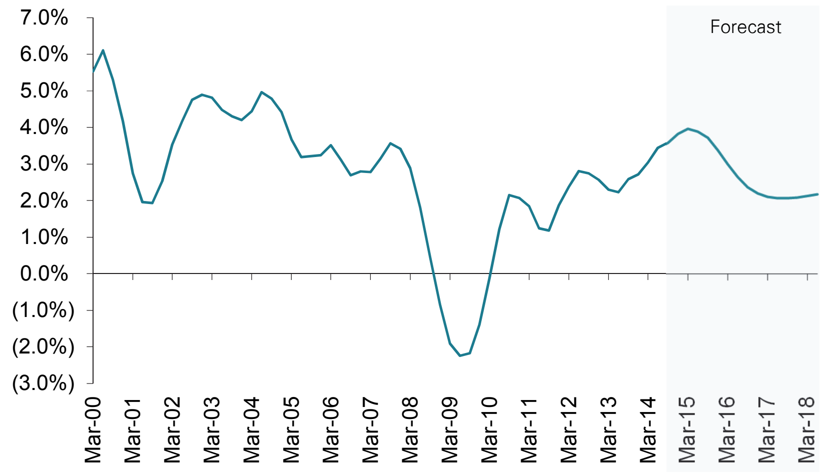
The amount payable by each liable person (including FX Networks) is determined annually by the Commission based on the proportion of revenue that each liable person receives from telecommunications services offered by means of a public telephone network. On 27 May 2014 the Commission determined the final allocations for the 2012/13 year. FX Network's allocation was $299,058, or 0.60% of the NZ$50 million levy.

Appendix 6 – Economic overview

GDP growth (historical and forecast)

After a slow recovery from recession, real GDP growth in the New Zealand economy reached 2.7% in 2013, the strongest annual average rate since March 2008.

Real GDP growth



Source: Statistics New Zealand, the Treasury

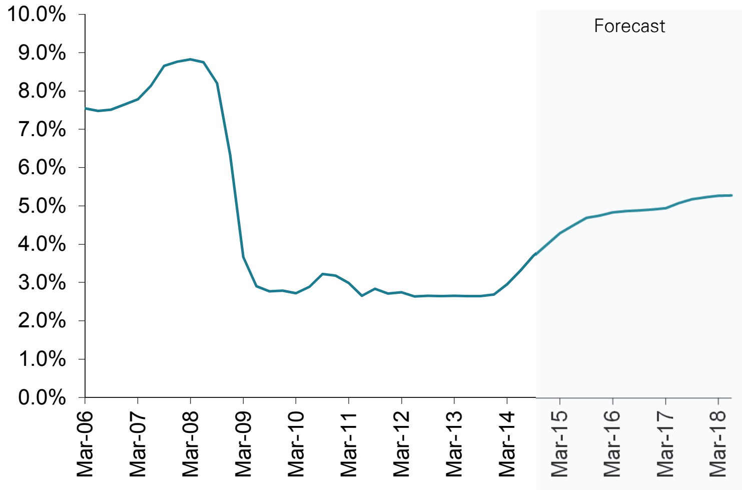
The economy is forecast to grow at an average pace of 2.5% per year over the five years to March 2018. (Treasury, 2014). Although the projection is for relatively stable GDP growth, the New Zealand economy is being influenced by several factors including:

- high house price inflation in Auckland and Christchurch;
- the $40 billion of post-earthquake rebuilding assumed to occur in Canterbury;
- sustained strength in the New Zealand dollar; and
- fiscal consolidation.

Wholesale interest rates

Interest rates are expected to remain supportive of economic growth over most of the forecast period. Ninety-day interest rates are expected to begin increasing from record low levels in mid-2014 as inflationary pressures rise in the economy. (Treasury, 2014)

90 day interest rates



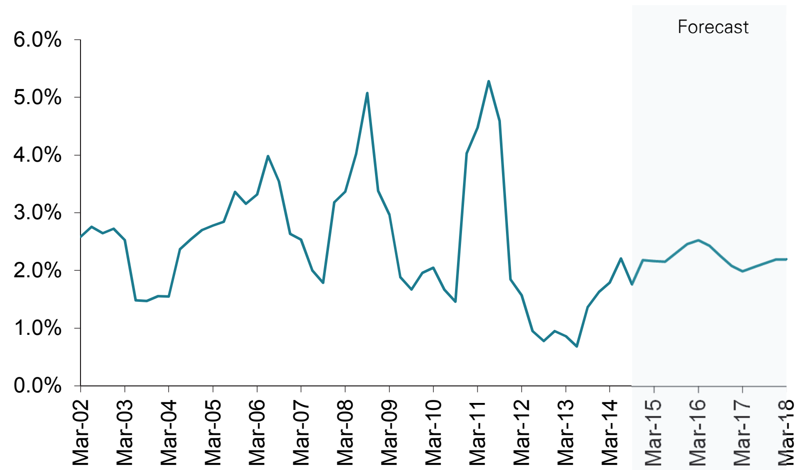
Source: RBNZ (2014), Statistics New Zealand, the Treasury

Ten-year government bond rates have been low over the second half of 2012 and early 2013 as New Zealand bonds have received additional demand from overseas investors looking to diversify portfolios. The New Zealand economy has also performed favourably on an international stage, attracting more funds. However, 10-year interest rates are expected to increase over the forecast horizon, primarily as global risk appetite increases as growth prospects improve. (Treasury, 2014)

Inflation

Consumers Price Index (CPI) inflation has recently reached the lowest levels seen in the past decade. The main drivers for the lower result are a higher exchange rate and ongoing heavy discounting by retailers as they try to maximise sales volumes.

CPI inflation



Source: NZIER, Statistics New Zealand, the Treasury

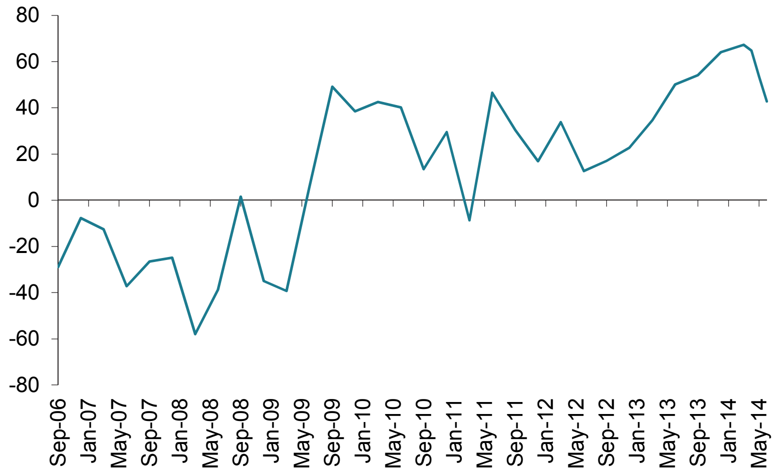
Overall, consumer price inflation is picking up and is expected to accelerate gradually to 2.4% by 2016, the upper part of the RBNZ's 1%-3% target range (NZIER, 2014).

Business confidence indicators

The latest ANZ business confidence survey shows elevated levels of confidence across the economy, with all sectors above historical averages.

Confidence indicators for profitability, employment and investment were all at elevated levels in March 2014, signaling a more broad based economic expansion (ANZ, 2014).

Business confidence index



Source: ANZ

Appendix 7 – Assumptions

Forecasts are inherently uncertain and are predictions by management of future events that cannot be assured and are necessarily based on assumptions, many of which are beyond the control of management.

General assumptions

There will be no material changes to the general economic, political, geographic, legislative or regulatory environments in which FX Networks operates. Further, there will be no change to the competitive dynamics of the markets in which FX Networks operates including any material change in competitor activity.

No new entrants will materially change the competitive environment.

There will be no material change in the general industry structure in which FX Networks operates, its relationships with third parties or conditions in respect of the markets for employees and staff in which it operates.

No Directors or key personnel will leave FX Networks and there will be no unanticipated loss of key customers or suppliers.

The historical financial information includes actual year-to-date transactions including costs incurred to date associated with the acquisition of FX Networks by Vocus. The forecasts do not include any future transaction costs associated with the acquisition.

Specific assumptions

Revenue

Annuity sales have been based on:

- Actual run rates at the date of producing the forecast;
- Known opportunities which FX Networks management has assessed as existing within the addressable market;
- Continued sales growth based on Management's expectations of FX Networks' addressable market; and
- A churn factor to reduce revenue based on historical annuity customer churn.

Dark fibre revenues are expected to grow based on managements' assessment of increased demand for fibre as data volumes continue to grow exponentially, resulting in a shortage of fibre for some of our key customers.

Construction revenues are based on contracted work and management's assessment of current pipeline opportunities. Longer term construction revenue is based on management's estimate of revenue based on the company's construction capacity and historical sales levels.

Cost of goods sold and gross margin

Annuity cost of goods sold includes an estimate of network productivity improvements, improved pricing and replacement of third party fibre with FX Networks fibre to improve annuity sales margins.

Gross margins on Dark Fibre are assumed to remain at historically observed levels.

2015 Construction gross margins remain high in FY15 based on the current pipeline of work. FX Networks has adopted a more conservative estimate of margins after FY15.

Operating costs

Operating costs are based on actual run-rates at the time of the forecast. Variable operating costs are forecast to increase in line with the growth in sales with an allowance for productivity improvements.

Interest and funding costs

Funding costs are based on actual funding cost rates at the date of the forecast adjusted for contractual obligations such as repayment of convertible notes.

Capital expenditure

Capital expenditure has been forecast based on management's estimate of capital expenditure requirements over the forecast term. Within forecast capital expenditure, are allowances for known fibre build requirements.

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