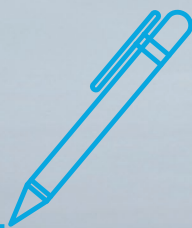


Co-Sec

CONFIDENTIAL



Exploration of key trends across the resource sector



THE IMPACT OF COVID-19 ON THE WORK OF INDEPENDENT EXPERTS

The significant volatility in local and global equity markets over the last few months clearly demonstrates the impact that COVID-19 is having on Australian companies.

Uncertainties regarding the economic outlook, consumer and business confidence, customer demand and supply chain management have all resulted in lower and more volatile asset valuations which has impacted on an independent expert's work.

Independent Expert's Reports (IERs) are generally prepared for the following reasons:

- Takeover bids
- Schemes of arrangement
- Compulsory acquisitions
- Acquisitions approved under section 611(7) of the Corporations Act
- Selective capital reductions
- Related party transactions
- Buy backs

Regulatory Guide 111 (RG 111) gives ASIC's views on how an expert can help security holders make informed decisions about transactions and broadly sets out, inter alia:

- how experts should analyse a proposed transaction
- the different valuation methodologies used by experts and the treatment of assumptions
- general requirements for all expert reports

In light of COVID-19, there are a number of factors set out in RG 111 that independent experts will need to ensure are rigorously considered as part of their reporting process

Listed company multiples

Earning guidance and analysts' forecasts may not yet have been updated to reflect the impact of COVID-19. It is important that when undertaking analysis of listed

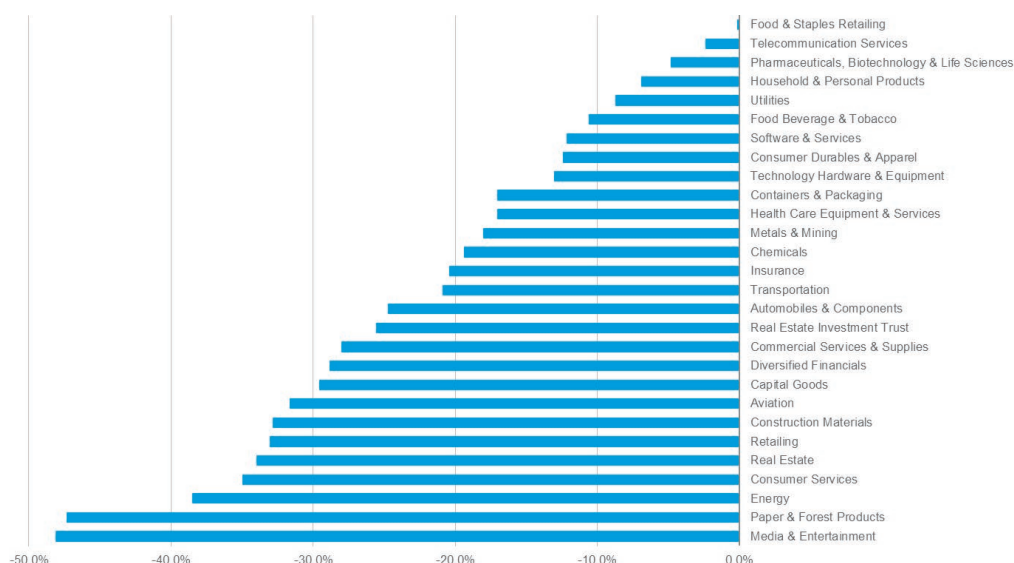
company forecast earnings and related multiples, we are comparing apples with apples. The forecast earnings of the commissioning party should reflect the impact of COVID-19 on earnings. It is critical, therefore, to ensure that the earnings and earnings multiples of the comparable listed companies used to assess an appropriate earnings multiple to be applied to the commissioning party's earnings have also been prepared on the same basis. If this is not the case, appropriate adjustments will need to be made to ensure the comparability of listed company multiples.

Comparable transactions

Whilst comparable transactions (transaction involving similar entities to the target company) may provide an indication of market based multiples, transactions undertaken prior to COVID-19 may not reflect current market conditions and volatility. An expert will, therefore, need to closely consider the relevance of pre COVID-19 transactions and/or consider the impact of current economic conditions when reviewing comparable transactions as a basis for assessing the multiple to be applied to the target company's earnings.

To demonstrate the impact of COVID-19 on earnings multiples and company valuations across a range of industries, the chart below sets out the average movement in share price by industry classification between 1 January 2020 and 30 April 2020. Those industries hardest hit include media and entertainment, energy, real estate and retailing whilst, not surprisingly, less impacted industries include food and staples retailing, telecommunication services, pharmaceuticals and household and personal products.

Average movement in share price by industry classification between 1 January 2020 and 30 April 2020



Value ranges

RG111.78 – 79 make reference to value ranges as follows:

“RG 111.78 An expert should usually give a range of values. The value of securities is typically subject to uncertainty and volatility. Placing a precise dollar value on them is likely to imply a misleading accuracy to a valuation.

RG 111.79 Nevertheless, the range of values should be as narrow as possible. If an expert cannot give a narrow range because of uncertainty (e.g. start-up companies), the expert should prominently explain in its report what factors create this uncertainty and how the expert is able to justify its findings despite the uncertainty. In our view, a broad range of values undermines the usefulness of the report.”

Given the uncertainty and volatility in the market, it will be more difficult for an expert to provide a narrow range of values. The expert will, therefore, need to ensure that sufficient focus is placed on the factors that create this uncertainty and how the expert is able to justify their findings despite the uncertainty

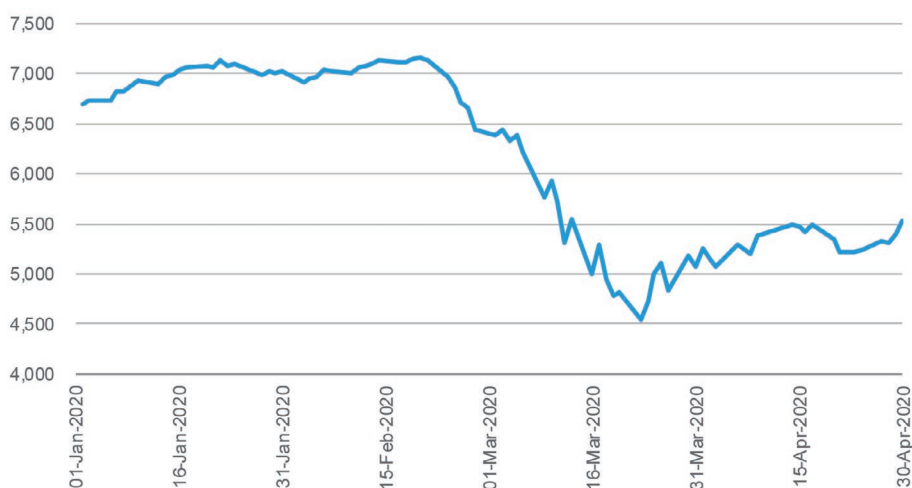
Changes in circumstances

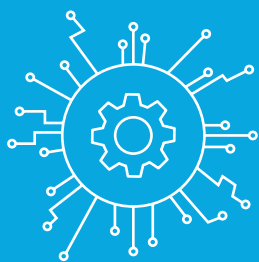
RG 111.102 states that “An expert who has delivered its report to the commissioning party should notify that party as soon as possible if the expert becomes aware of a significant change affecting the information in its report or if the expert believes that a material statement in the report is misleading or deceptive.”

RG 111.103 further states that “When a material change in circumstances has arisen since a report was prepared, a failure by the expert to provide a supplementary report to its client may constitute misleading or deceptive conduct. Security holders will rely on an expert report when making their decision, not when they first receive the report: ASIC v Solution 6 Holdings Ltd (1999) 30 ACSR 605 at 611. If an expert becomes aware of a material change in circumstances, then depending on the circumstances, it may be appropriate for a commissioning party to send a supplementary report, even if security holders would receive the report: (a) shortly before a meeting is held; or (b) towards the end of an offer period.”

The chart below sets out the movement in the ASX200 between 1 January and 30 April 2020.

S&P/ASX 200 Index





As a result of the significant market volatility, there is an increased risk of a material change in circumstances arising between the date of the report being prepared and the date that security holders make their decision. An expert should, therefore:

- closely monitor market announcements and share price movements up until the security holders make their decision
- ensure that the commissioning party notifies the expert if that party becomes aware of a significant change affecting the information in the expert report prior to a meeting being held or during the offer period
- immediately prior to the date that the security holders make their decision, obtain confirmation from the commissioning party that the information provided by the commissioning party is factually correct.

Final word

COVID-19 has thrown a curveball to independent experts who need to ensure that they understand and adequately consider the implications of the matters set out above. Assessing company valuations using listed company multiples and comparable transactions under an earnings based methodology both during and post COVID-19 will require more judgement and analysis to ensure valuations reflect the current economic environment.

For more information or enquiries please contact:



Glyn Yates
Director, National Head of
Corporate Finance
T 03 9286 8167
E glyn.yates@rsm.com.au



Andrew Clifford
Director, Corporate Finance
T 03 9286 8214
E andrew.clifford@rsm.com.au



Nadine Marke
Director, Corporate Finance
T 08 9261 9375
E nadine.marke@rsm.com.au

