



**Target Company Statement  
in Response to the Takeover Offer by Spark  
dated 23 March 2017**

**YOUR DIRECTORS RECOMMEND THAT YOU  
REJECT THE SPARK  
OFFER**

**THIS IS AN IMPORTANT DOCUMENT AND REQUIRES YOUR IMMEDIATE ATTENTION**



**If you have any questions in respect of this document or the offer, you  
should seek advice from your independent financial or legal adviser**



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## CHAIRMAN'S LETTER

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Dear Shareholder,

You recently received a conditional Takeover Offer from Spark New Zealand Trading Limited (Spark), attempting to acquire your shares in TeamTalk Limited (TeamTalk) for 80c per share, dated 9 March 2017 ("the Spark Offer" or "the Offer").

The Directors of TeamTalk unanimously recommend that you **REJECT** the Spark Offer. **TO REJECT THE OFFER, SIMPLY IGNORE IT AND DO NOTHING.**

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**Spark's Offer of 80c for each of your TeamTalk shares is significantly below the Independent Adviser's valuation range of \$1.52 to \$2.11 per share.**

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The Grant Samuel independent adviser's report states that **"as the Spark Offer of \$0.80 per share is below Grant Samuel's assessed value range for TeamTalk shares there is no compelling reason to accept the offer"**.

The Directors see the Spark Offer as opportunistic and an attempt to exploit a low point in TeamTalk's share price trading. Further, we are firmly of the view the Spark Offer of 80c per share does not reflect the fair value of TeamTalk's shares. The reasons why the Directors believe you should REJECT the Offer are set out below and in this Target Company Statement ("the Statement"):

1. The 80c offer price is significantly below the independent adviser's valuation range of \$1.52 to \$2.11 per share.
2. The timing of the Offer is opportunistic and conditional, made at the low point in TeamTalk's recent financial history and before TeamTalk benefits from its implemented strategic plan.
3. The Offer fails to reflect the standalone value of TeamTalk's new strategy, strong leadership and forecast growth.
4. The Offer price of 80c per TeamTalk share fails to value TeamTalk's three businesses appropriately as separate components.
5. Spark's Offer does not value the significant synergies and strategic benefits that would be captured by Spark.

Spark's Offer represents a low, one-time cash pay-out to you. TeamTalk will consider a resumption of dividends in the calendar year 2018.

The Spark Offer contains a Commerce Commission approval condition and such a process could take several months to reach a conclusion. This means that TeamTalk shareholders may not know for some time whether or not the Offer will be successful and whether they will receive their pay-outs from Spark.

TeamTalk has more than 1,500 shareholders and Spark confirmed on 9 March 2017 that not a single one of them had agreed to sell any of their shares to Spark.

**TO REJECT THE OFFER, SIMPLY IGNORE THE DOCUMENTS FROM SPARK AND DO NOTHING.**

I encourage you to read this document carefully. If you are in any doubt about how to respond to Spark's Offer, seek financial advice from an independent, qualified financial and/or legal adviser. We will keep you updated on any significant developments so long as the Offer remains open.

If you have any questions, please call or email Andrew Miller, TeamTalk's CEO: Email: [amiller@teamtalk.co.nz](mailto:amiller@teamtalk.co.nz)  
Mobile: +64 27 458 4525

On behalf of the Directors of TeamTalk Limited, I thank you for your continued support and look forward to delivering the full value of TeamTalk to our shareholders.

Yours faithfully



Roger Sowry  
Chairman, TeamTalk Limited  
Mobile: +64 27 445 5753



# Section 1

Directors'

Recommendation

## DIRECTORS' RECOMMENDATION

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The Directors of TeamTalk unanimously recommend that you **REJECT** Spark's Offer in respect of all of your TeamTalk shares.

The Directors did not encourage or solicit Spark's Offer.

### WHY YOU SHOULD REJECT SPARK'S OFFER

1. The Offer price of 80c is significantly below the Independent Adviser's valuation range of **\$1.52 to \$2.11** per TeamTalk share.
2. The timing of the Offer is opportunistic. It is attempting to exploit a low point in TeamTalk's recent trading history and comes at a time when TeamTalk's new management team is implementing the turnaround plan to deliver significant value for TeamTalk shareholders.
3. The Directors firmly believe that Spark's Offer fails to reflect the value of TeamTalk shares accurately under either of the following bases:
  - a. Under TeamTalk's current business plan, which is being implemented by the new management and is well on track to achieve strong profitable growth; or
  - b. The sum of the parts value of TeamTalk's businesses.
4. Furthermore, there are synergies and strategic benefits over and above the fair value of TeamTalk that an acquirer such as Spark would capture through integrating CityLink, TeamTalk Mobile Radio and Farmside. Given the strategic nature of these businesses, TeamTalk shareholders should be compensated for a significant proportion of these benefits.

Further details are set out on the following pages.

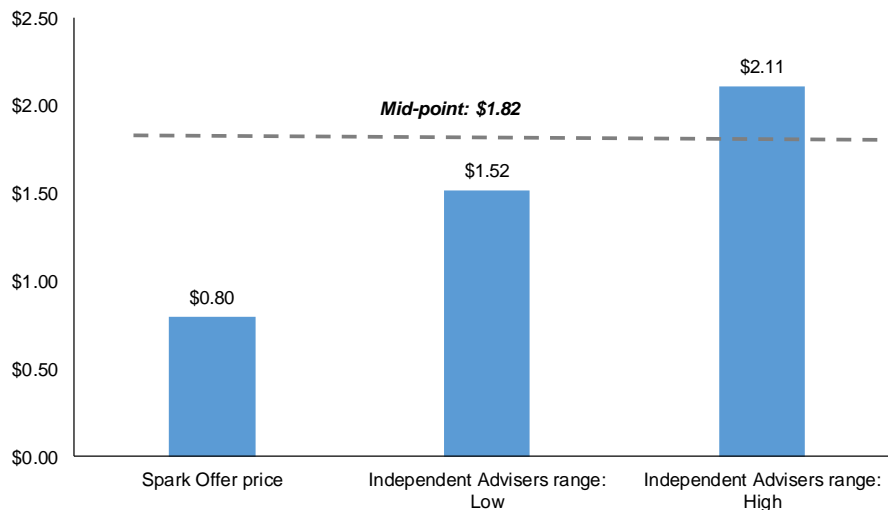
The Directors strongly encourage you to take these factors into account, together with the assessment of the Independent Adviser as to the merits of the Offer when considering your options in response to Spark's Offer. The Independent Adviser's Report is set out in Appendix 1 of this Statement.

## 1. THE 80c OFFER PRICE IS SIGNIFICANTLY BELOW THE INDEPENDENT ADVISER'S VALUATION RANGE OF \$1.52 TO \$2.11 PER SHARE

**Spark's Offer of 80c per TeamTalk share is below the Independent Adviser's assessed value range of \$1.52 to \$2.11 per TeamTalk share.**

As required by the Takeovers Code, TeamTalk appointed Grant Samuel as Independent Adviser to assess the merits of Spark's Offer. As part of this analysis, they have provided a value range for TeamTalk shares. Their full report is set out in Appendix 1 of this Statement.

The Offer price is \$1.31 below the high end of Grant Samuel's valuation range of \$2.11, \$1.02 below the mid-point of Grant Samuel's valuation range of \$1.82, and \$0.72 below the low end of Grant Samuel's valuation range of \$1.52, as shown in the chart below.



Spark makes much of comparing its Offer price of 80c to the historic low share price levels prior to the Offer and stating that the takeover premium is substantial. However, this is only when compared to an aberration in TeamTalk's trading performance, which related to a difficult financial period in 2016 under previous management. Comparing Spark's Offer price of 80c to the historic share price of TeamTalk is not an appropriate method to assess the value of TeamTalk.

A company and its share price are typically valued with respect to its expected future earnings and cash flows. TeamTalk shareholders should consider the expected future profits and cash flows of TeamTalk, when considering value:

- TeamTalk has provided profit after tax guidance to 30 June 2018 of \$4.1 million to \$5.6 million<sup>1</sup>. The Spark Offer of 80c implies a market capitalisation of \$22.7 million. Based on these projections, Spark's Offer is at a price-earnings ratio (PE ratio) of between 4.1 and 5.5 times. This is very low when compared to Spark's

<sup>1</sup> Key assumptions for the prospective financial information and the assumptions that underpin them are set out in the Independent Adviser's Report, found in Appendix 1 of this document



own PE multiple of around 16 times to 30 June 2018<sup>2</sup>. Spark has strategic challenges and its earnings are forecast to be flat between 2017 and 2018<sup>3</sup>. Spark is attempting to capture the benefit of TeamTalk's strong forecast growth (to the detriment of TeamTalk's shareholders) by buying TeamTalk at a low price, capturing TeamTalk's earnings, extracting revenue and synergy cost benefits, and then have those earnings rated on Spark's much higher valuation multiple.

- TeamTalk will also consider a resumption of dividends in the calendar year 2018 to provide TeamTalk shareholders with a return on their investment in addition to any future gain in the share price. The Spark Offer represents a low, one-time cash pay-out to TeamTalk shareholders.

The Independent Adviser has concluded that "as the Spark Offer of \$0.80 per share is below Grant Samuel's assessed range for TeamTalk shares there is no compelling reason to accept the offer"

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<sup>2</sup> Source: *Craigs Investment Partners brokers note, dated 16 February 2017*

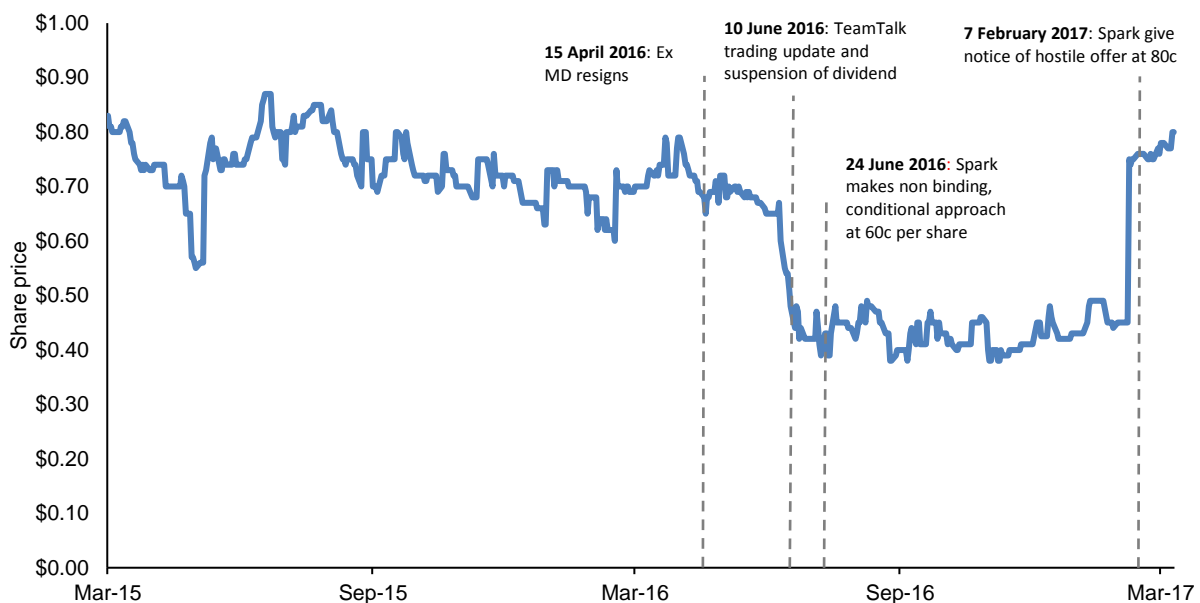
<sup>3</sup> *Ibid*

## 2. The timing of the Offer is opportunistic and conditional, made at the low point in TeamTalk’s recent financial history and before TeamTalk benefits from its implemented strategic plan

**The Spark Offer has tactically been made at a time before TeamTalk benefits from its recently implemented strategic plan and before this is reflected in TeamTalk’s share price.**

The Offer is attempting to exploit the challenges that TeamTalk faced during 2016, including TeamTalk’s previous Managing Director departing on 16 April 2016 and a trading downgrade for 2016, including a dividend suspension, as announced on 10 June 2016. Spark made its first indicative and highly conditional approach to TeamTalk on 24 June 2016 at 60c per share, which was rejected outright by the TeamTalk Board.

TeamTalk’s shares were trading above 80c at times during the 2015 calendar year. TeamTalk shares closed at 69c on the day immediately before the Managing Director’s resignation on 15 April 2016 and then fell further during 2016, post the trading update on 10 June 2016.



The issues TeamTalk faced during 2016 have largely been addressed. TeamTalk has a new management team and is now profitable again, as the half-yearly results to 31 December 2016 have highlighted. TeamTalk will consider the resumption of a dividend in the calendar year 2018.

If the Offer succeeds, TeamTalk’s shareholders will not capture the long-term benefits from the investment that has already been made in the new strategy.

TeamTalk’s Directors are strongly of the view that TeamTalk is better placed to optimise the value of these businesses in a more appropriate timeframe than can be realised by selling to Spark at 80c per TeamTalk share.

### **3. THE OFFER FAILS TO REFLECT THE STANDALONE VALUE OF TEAMTALK'S NEW STRATEGY, STRONG LEADERSHIP AND STRONG FORECAST GROWTH**

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**The Spark Offer fails to reflect the strength of TeamTalk's underlying businesses and growth opportunities.**

During the financial year to 30 June 2016 (FY2016), TeamTalk completed a strategic review of its operations and structures, which resulted in a new group strategy and business plan. As part of this process, TeamTalk also identified a number of organic growth opportunities and operational performance initiatives. The Board of TeamTalk supports these initiatives and is firmly of the view that they will result in significant improvements in shareholder value. These value gains have not yet been reflected in TeamTalk's share price and are not valued appropriately under the Spark Offer.

The new TeamTalk strategy and operating model was signalled to TeamTalk shareholders at last year's AGM and then discussed further in the half-yearly results to 31 December 2016, released on 1 March 2017. These results are contained in Appendix 2 of this document.

#### **New management team**

In the last four months of the 2016 calendar year, TeamTalk appointed new management, including: CEO, Andrew Miller, CFO, Jason Bull, and Transformation Officer, John Fischer. They have made significant progress in re-setting strategy and have developed a new business plan for TeamTalk. Their initiatives are starting to deliver positive results, as outlined in the half-yearly results to 31 December 2016, which are summarised below and included in Appendix 2.

#### **Summary of strategic plan**

At the 2016 AGM, TeamTalk outlined its strategic priorities:

1. Return to profit, following a loss after tax for the full year to 30 June 2016;
2. Reduce debt whilst meeting its capital requirements; and
3. Reconsider a resumption of dividends as soon as those objectives have been achieved.

TeamTalk is focusing on, and delivering to, these strategic priorities, as discussed below.

#### **1. Profitability**

On 1 March 2017, TeamTalk announced its first half result for the six months ended 31 December 2016, showing a return to profitability:

- Net cash flow from the group's operations increased 27.7% to \$5.36m from \$4.20m;
- Net debt for the group was down from \$35.47m to \$33.89m;
- Inventory was down 49% to \$1.39m from \$2.70m;
- CityLink broadband revenue increased 7% to \$7.38m, up from \$6.89m, with EBIT up 14.5% at \$2.87m, up from \$2.50m;
- TeamTalk Mobile Radio revenue increased by 4% to \$10.6m from \$10.2m, and EBIT was up by 13.4% to \$0.93m from \$0.82m; and

- As announced on 28 February 2017, TeamTalk has agreed the essential terms of a new 3-year banking facility to March 2020 with Westpac New Zealand Limited (“Westpac”).

The radio and broadband divisions are performing well and in the six months to December 2016 increased revenue and earnings before interest and taxation. While Farmside again detracted from the result for the period, TeamTalk is addressing this head-on. Work began to restructure Farmside late last year. Farmside’s costs are forecast to be 22% lower in the second half to 30 June 2017 and we are anticipating that the division’s operational costs to be significantly lower in the financial year to 30 June 2018 compared with the current year’s budget.

These savings together with the enhanced performance of our CityLink and TeamTalk Mobile Radio businesses, as well as an expected reduction and deferral of major capital expenditure for the CityLink network in Wellington, mean the company is well-positioned to deliver significantly stronger cash flows for shareholders in 2017 and beyond.

The return to profitability is a direct result of the focus and determination of the Board and senior management to turn the company and its financial performance around. These results demonstrate that TeamTalk’s executive team is successfully delivering on our new strategic business plan to increase revenue, reduce costs and capital expenditure, refocus the company and realise TeamTalk’s inherent potential.

There are several material initiatives underway including an enhanced focus on margins and costs, improvements in our ‘Go to Market’ model, and greater engagement with partners, that the Board believes will continue to deliver sustainable growth and increase profitability. These initiatives are expected to yield even better results over the next 6-18 months.

## **2. Debt**

Net debt for the group has reduced from \$35.47 million to \$33.89 million as at 31 December 2016. We plan to further reduce debt to around \$31 million by 30 June 2017 and then it is expected to be materially lower by 30 June 2018. This is a targeted reduction in debt from 30 June 2016 to 30 June 2018 of around 33%.

We have the full support of our banking partners, Westpac, who have agreed on the essential terms of a new three-year banking facility for the company through to 31 March 2020 to replace the existing facility which expires at the end of August 2017.

As at 28 February 2017, TeamTalk’s net debt was \$33.2 million.

## **3. Dividends**

The Board looks forward to considering a resumption of a dividend in the calendar year 2018.

## **Capital Expenditure**

During 2016, TeamTalk reported it needed to undertake substantial capital expenditure. TeamTalk is forecasting capital expenditure until FY2020 to be in the range of 12-14% of revenue per annum as the company upgrades its nationwide mobile radio network to digital and invests in its Wellington fibre network. This is in line with industry benchmarks. From 2021 onwards, capital expenditure is expected to reduce significantly to within a range of around 6-8% of revenue.

**Profit guidance provided to the market**

The turnaround to date, together with the improved performance of CityLink and TeamTalk Mobile Radio and the reduction in debt and capex requirements, mean that the company is well-positioned to deliver significantly stronger cash flows for shareholders in 2017 and beyond.

TeamTalk provided market guidance for the full year to 30 June 2017 in the range of EBIT of \$4.7 million to \$5.2 million, and profit after tax of \$2.0 million to \$2.4 million.

TeamTalk provided further market guidance for the 12 months to 30 June 2018 of EBIT to be in the region of \$8.0 million to \$9.5 million and profit after tax in the region of \$4.1 million to \$5.6 million. Cost reduction will be a key part of this significant earnings growth, with \$2.1 million of cost savings anticipated at Farmside alone.

*The key assumptions which underpin these forecasts are set out in the Independent Adviser's Report, in Appendix 1 of this document.*

**Price-earnings multiple implied by Spark's offer**

An Offer price of 80c per share implies a market capitalisation for TeamTalk of \$22.7 million. Compared to TeamTalk's profit after tax guidance for 30 June 2018, the Spark Offer is at a low price-earnings ratio (PE ratio) of between 4.1 and 5.5 times, compared to Spark's own PE multiple of around 16 times to 30 June 2018<sup>4</sup>.

Spark is therefore offering to TeamTalk shareholders a very large discount to Spark's own valuation rating.

**Spark's Offer of 80c per share fails to reflect the strength of TeamTalk's underlying businesses and growth opportunities. This is confirmed by the Independent Adviser's valuation range for TeamTalk shares of \$1.52 to \$2.11.**

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<sup>4</sup> Source: Craigs Investment Partners brokers note, dated 16 February 2017

#### **4. THE OFFER PRICE OF 80c PER TEAMTALK SHARE FAILS TO APPROPRIATELY VALUE TEAMTALK'S THREE BUSINESSES AS SEPARATE COMPONENTS**

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**The Offer price of 80c per TeamTalk share implies a value of \$55.9 million for the CityLink, TeamTalk Mobile Radio and Farmside businesses. TeamTalk's Directors are firmly of view that there is a significant value gap between this and the underlying value of these businesses (excluding any value for the synergies and strategic benefits that would accrue to Spark).**

TeamTalk's Directors believe that:

- TeamTalk's key assets are of strategic value, as confirmed by recent approaches and indications of interest from a range of parties, in addition to Spark. A sale of some of TeamTalk's assets and a corresponding reduction in debt levels, if realised, could prove to be the best option for maximising value for TeamTalk's shareholders.
- CityLink's assets would be difficult to replicate in the short to medium term:
  - CityLink owns around 270 kilometres of fibre in streets and around 70 kilometres of fibre in buildings across Wellington and Auckland.
  - There is value in having a network which is already built. It is unlikely that a replacement or competing fibre network could be built quickly, given the civil works required to dig up streets and undertake other earthworks, particularly in the CBD areas.
  - The Independent Adviser's value range for CityLink is \$44.6 million - \$52.7 million.
  - The Directors are of the view that the costs to replicate the CityLink network could be higher than the Independent Adviser's assessed range above.
- TeamTalk Mobile Radio's networks would also be challenging to reproduce in the short term:
  - It provides access to 450 high sites and spectrum across New Zealand and has over 90% of the trunked radio market.
  - The typography of New Zealand requires niche skill sets to establish and maintain a nationwide radio network.
  - The Independent Adviser's value range for TeamTalk Mobile Radio is \$30.8 million - \$38.5 million.
  - The Directors are of the view that the costs to replicate TeamTalk's mobile radio network are likely to be within the assessed value range above.
- The Independent Adviser assesses a value range for Farmside of \$9.6 million to \$12.0 million. TeamTalk has been approached by a number of parties interested in Farmside. They want to explore a range of strategic initiatives, which if implemented, could realise cash proceeds to TeamTalk. Our analysis and feedback from these approaches indicates that there are significant revenue and cost synergy benefits to third party acquirers. TeamTalk is focused on returning Farmside to profitability and generating cash flow. A significant portion of the cost reduction initiatives have already been implemented, with around \$2.1 million of annualised cost savings to be achieved within the Farmside business alone in the year to 30 June 2017. These savings should be fully reflected in the FY2018 results.

The Independent Adviser's value range for TeamTalk's three businesses is \$85.0 million - \$103.2 million. Deducting a value for corporate costs (of \$6.3 million - \$7.7 million) implies a combined enterprise value of \$78.7 million - \$95.5 million. The Spark Offer implies an enterprise value of \$55.9 million.

Therefore, the Spark Offer is \$22.8 million to \$39.6 million lower than the Independent Adviser's assessment of the enterprise value of TeamTalk.

In addition, there would potentially be additional synergies and strategic benefits that Spark would capture if they were to acquire TeamTalk (including reduced corporate costs from integrating the three business units within their operations). See the next section for a discussion of these benefits.

The Independent Adviser's analysis demonstrates the very large gap between the value of TeamTalk and Spark's Offer price of 80c per share.

**The Independent Adviser notes in its report:**

**"CityLink is an attractive business with established fibre networks in Wellington and Auckland that would be costly to replicate. CityLink has strong and predictable cash flows"**

**"TeamTalk's mobile radio business has a nationwide network infrastructure that represents a competitive advantage for providing mobile radio solutions to customers that require nationwide communications"**

**TeamTalk believes that Spark's threat to build its own fibre network in Wellington and Auckland is not credible in the near term.**

As noted above, building fibre broadband networks in the CBD areas of large cities is highly challenging, costly and comes with significant risk. Further, civil works in these areas would require Council consents, which may only be provided with conditions attached such as the requirement to work outside of business hours or put in place traffic management plans. Indeed, Spark itself has spoken to the significant challenge when its representatives recently stated that: "The TeamTalk acquisition is preferable to alternative strategies to build new networks in Auckland and Wellington".

## 5. SPARK'S OFFER DOES NOT VALUE THE SIGNIFICANT SYNERGIES AND STRATEGIC BENEFITS THAT WOULD BE CAPTURED BY SPARK

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**The Offer does not provide value to TeamTalk shareholders for the "substantial synergy prize" available to Spark.**

TeamTalk's Directors believe that the merger of TeamTalk's businesses into Spark would generate a substantial level of synergies for Spark, as a result of:

- The CityLink fibre network position, particularly in Wellington. Spark has outlined the ownership of fibre networks as a key strategic priority;
- The operations and product offering that TeamTalk Mobile Radio would provide Spark;
- Farmside's strong footprint in the rural customer market, which Spark has publicly stated it is actively targeting; and
- Reduced corporate costs from integrating the business units within Spark's operations.

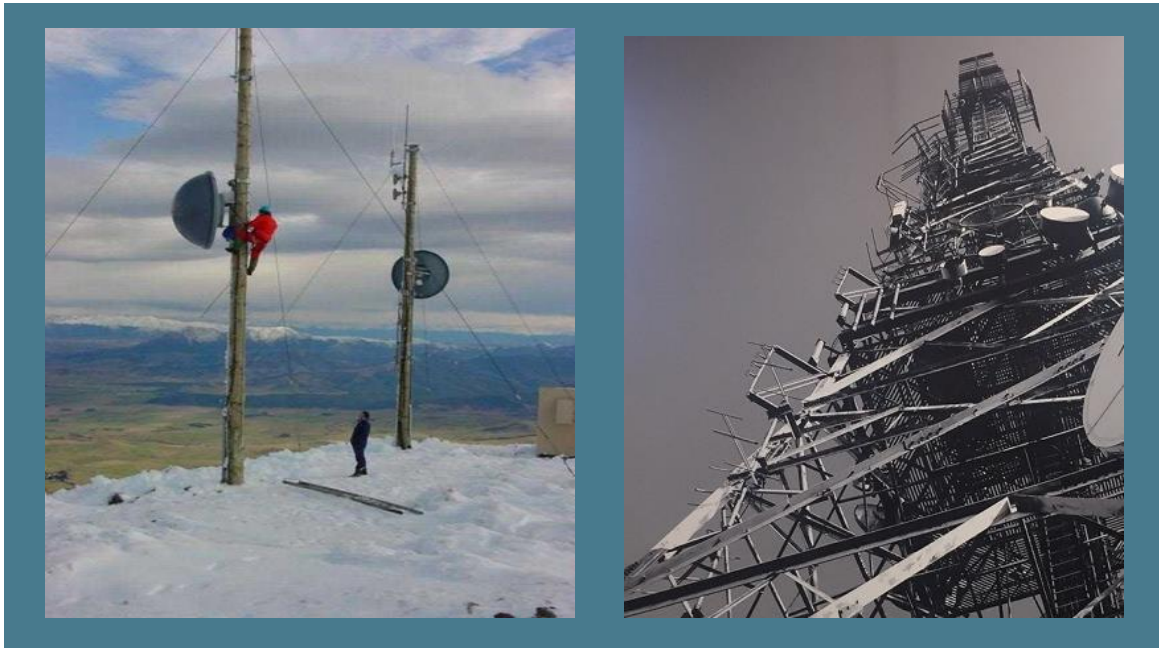
The Independent Adviser has not separately valued the likely synergy benefits.

Spark has stated it will conduct a strategic integration review and assessment of TeamTalk with the likely intention of implementing synergy and cost out initiatives, and focusing on growing TeamTalk's business through leveraging Spark's capabilities and sector expertise.

If the full Offer is successful, all of these strategic benefits and synergies will be captured by Spark and its shareholders with no value benefit for TeamTalk shareholders.

Given the significant strategic value and potential interest in TeamTalk's assets, we would expect TeamTalk shareholders to gain a significant proportion of these synergies as part of any sale transaction.





# Section 2

## Details of the Offer

## DETAILS OF THE OFFER

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Spark, a wholly owned subsidiary of listed company, Spark Limited, has made a conditional takeover offer to buy all the ordinary shares in TeamTalk Limited.

TeamTalk did not encourage or solicit Spark's Offer.

### Key features of the Offer

The terms of Spark's Offer are set out in the Offer Document you will have already received. The main features of the Offer are:

1. The Offer Price is 80c per TeamTalk share. The Independent Adviser's assessed value range is \$1.52 to \$2.11 per TeamTalk share.
2. The Offer must remain open until 11.59 pm on 22 April 2017, unless it is extended or withdrawn.
3. The Offer may only be withdrawn with the approval of the Takeovers Panel. If the Offer conditions are not satisfied or waived the Offer will lapse. If the Offer is withdrawn or the conditions are not satisfied no shares will be taken up by Spark under the Offer.
4. The Offer is conditional on (among other things) Spark receiving acceptances for 90% or more of TeamTalk's shares. Spark can waive this condition. If it does, then its Offer will instead be conditional on acceptances for more than 50% of the shares in TeamTalk.
5. The Offer is also conditional on:
  - Clearance being given, or authorisation being granted, under the Commerce Act 1986 for Spark to complete the acquisition of all of the TeamTalk shares in accordance with the Offer;
  - Over 20 other conditions. While these conditions are not unusual in offers of this nature, they have the effect of making the outcome uncertain.
6. If Spark does acquire 90% or more of the TeamTalk shares, it will be entitled to, and has said it would, exercise its rights to buy all the remaining shares in TeamTalk compulsorily, from the holders who did not accept the Offer.

### Options available to TeamTalk shareholders

You have three options in response to Spark's Offer. You can:

- Accept the Offer for all of your TeamTalk shares.
- Accept the Offer for some, but not all, of your TeamTalk shares.
- Choose to not accept the Offer. If you choose this option, you do not need to take any action.

### Acceptance of the Offer

If you do not want to accept Spark's Offer and want to keep your TeamTalk shares, you do not need to take any action.

If you wish to accept the Offer, use the Acceptance and Transfer Form that accompanied Spark's Offer Document (and carefully follow the instructions on that form). Acceptances, once given, cannot be withdrawn.

## Timing

The Offer will close at 11.59 pm on 22 April 2017 unless extended by Spark (the "Offer Period"). You have until the end of the Offer Period to decide whether to accept the Offer, but should you choose to accept the Offer your acceptance should be delivered such that it is post-marked or received by Spark before the end of the Offer Period.

Spark is not required to pay you until seven days after the later of:

- the date on which your acceptance is received; or
- the date on which the Offer becomes unconditional; or
- 22 April 2017.

This means that Spark is not required to pay you for your TeamTalk shares until 1 May 2017 at the earliest. However, the Offer Period may be extended by Spark for a further 60 days in which case the date for payment could be as far away as the end of June 2017.

If you do intend to accept, there is no benefit to you in accepting the Offer until near the closing date and, in any event, before 22 April 2017.

## Post the Offer closing

If Spark receives acceptances to the Offer which will result in it holding or controlling 90% or more of the TeamTalk shares, Spark will become entitled to, and intends to, compulsorily acquire the remaining shares in TeamTalk in accordance with the Takeovers Code. If this occurs, TeamTalk will be de-listed by NZX and its shares will cease to be quoted on the NZX Main Board.

If Spark does not receive acceptances to the Offer that will result in it holding or controlling 90% or more of the TeamTalk shares, the Offer will either lapse or Spark may waive this condition and the offer will instead be conditional on Spark receiving acceptances in respect of more than 50% of the TeamTalk shares. If this occurs:

- TeamTalk will remain listed by NZX and its shares will continue to be quoted on, and traded through, the NZX Main Board. TeamTalk will continue to be entitled to ask NZX to cancel its listing or quotation of its shares on the NZX Main Board, subject to any prior approval of shareholders required by NZX.
- TeamTalk shareholders can expect to see substantial changes in how TeamTalk operates. Spark will be in a position to control the composition of the TeamTalk Board. Spark has stated in its Offer Document that it will "seek appropriate representation on the TeamTalk Board and will participate in decisions relating to TeamTalk, and its future, through the TeamTalk Board". It will be restricted by NZX Listing Rules in its ability to undertake related party dealings above certain value thresholds (this means transactions of substance between TeamTalk and Spark will be subject to independent scrutiny and review). Spark may decide to sell TeamTalk Mobile Radio, CityLink and / or Farmside. It has stated that "the capital structure of TeamTalk will be reviewed (including TeamTalk's dividend policy, raising capital and taking on debt)". The view of the Directors is that this will not present an ideal or long-term sustainable position for either Spark or TeamTalk shareholders, and that this outcome will change the risk profile of TeamTalk.
- Support for a share price at the Offer level of 80c per TeamTalk share, or higher, may be achieved as a result of a stronger outlook for the financial performance of the business or if there is a belief that a further offer for 100% of the shares may be made or an alternative transaction for the sale of a major business group. However, there is a risk that the share price may retreat below 80c.

**The foregoing is a summary of the terms of the Offer. The full terms of the Offer are contained in Spark's Offer Document dated 9 March 2017 which has been sent to TeamTalk's shareholders.**



# Section 3

## Takeovers Code Information

## TAKEOVERS CODE INFORMATION

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This Target Company Statement (“the Statement”) has been prepared by TeamTalk Limited (“TeamTalk”) pursuant to Rule 46 of the Takeovers Code in relation to a full takeover offer made by Spark New Zealand Trading Limited (“Spark”).

### **1. Date**

1.1. This Target Company Statement is dated 23 March 2017.

### **2. Offer**

2.1. This Statement relates to a full takeover offer by Spark to acquire all of the ordinary shares in the capital of TeamTalk for a cash purchase price of 80c per share (“the Offer”).

2.2. The full terms of the Offer are set out in Spark’s Offer Document dated 9 March 2017.

### **3. Target Company**

The name of the target company is TeamTalk Limited (NZX:TTK)

### **4. Directors of TeamTalk**

4.1. The Directors of TeamTalk are:

- (a) Roger Sowry (Chairman)
- (b) George Paterson
- (c) Tone Borren
- (d) Reg Barrett
- (e) Geoff Davis
- (f) Nathan York

### **5. Ownership of Shares of TeamTalk**

5.1. All of the equity securities issued by TeamTalk are designated as ordinary shares and are referred to in this Statement as “the TeamTalk Shares” or “the Shares.” There is no other class of shares or other equity securities issued by TeamTalk.

5.2. The number and percentage of TeamTalk Shares which are held or controlled by the Directors and Senior Officers of TeamTalk and their associates is set out in the Schedule to this Statement.

5.3. The Senior Officers of TeamTalk are:

- (a) Andrew Miller (Chief Executive Officer)
- (b) Jason Bull (Chief Financial Officer)
- (c) John Fischer (Chief Transformation Officer).
- (d) Kevin Brown (General Manager, Commercial)
- (e) David Struthers (Head of Sales)
- (f) Mark Finnigan (Head of HR and Health & Safety)

- 5.4. Except as set out in the Schedule of this Statement, no Director or Senior Officer of TeamTalk or their associates holds or controls any TeamTalk Shares.
- 5.5. TeamTalk does not know of any person who holds or controls 5% or more of any TeamTalk Shares,
- 5.6. During the two year period ending on the date of this Statement:
- (a) No TeamTalk Shares have been issued to any Director or Senior Officer of TeamTalk or their associates; or
  - (b) No Director or Senior Officer of TeamTalk or their associates has obtained a beneficial interest in any TeamTalk Shares under any employee share scheme or other remuneration arrangement.

## **6. Trading in TeamTalk Shares**

- 6.1. During the six month period before the latest practicable date before the date of this Statement (being 20 March 2017):
- (a) No Director or a Senior Officer of TeamTalk or their associates has acquired or disposed of any TeamTalk Shares; and
  - (b) To the knowledge of TeamTalk there is not, nor was there during that period, any person who holds or held or controls or controlled 5% or more of any class of TeamTalk Shares and accordingly no such person has acquired or disposed of any TeamTalk Shares.

## **7. Acceptance of Offer**

- 7.1. No Director or Senior Officer of TeamTalk or any of their associates, has accepted or intends to accept the Offer.

## **8. Ownership of Equity Securities of Spark**

- 8.1. Except as set out in the Schedule, neither TeamTalk, nor any Director or Senior Officer of TeamTalk nor any of their associates, hold or control any equity securities of Spark or of Spark's listed parent company, Spark New Zealand Limited.

## **9. Trading in Equity Securities of Spark**

- 9.1. Neither TeamTalk, nor any Director or Senior Officer of TeamTalk nor any of their associates, has acquired or disposed of any equity securities of Spark or Spark's listed parent company, Spark New Zealand Limited during the six month period before the latest practicable date before the date of this Statement, being 20 March 2017.

## **10. Arrangements between Spark and TeamTalk**

- 10.1. As at the date of this Target Company Statement, no agreement or arrangement (whether legally enforceable or not) has been made, or is proposed to be made, between Spark or any of its associates and TeamTalk or any related company of TeamTalk, in connection with, in anticipation of, or in response to, the Offer.

## **11. Relationship between Spark, and Directors and Senior Officers of TeamTalk**

- 11.1. No agreement or arrangement (whether legally enforceable or not) has been made, or is proposed to be made, between Spark or any associates of Spark, and any of the Directors or Senior Officers of TeamTalk or any related company of TeamTalk (including particulars of any payment or other benefit

proposed to be made or given by way of compensation for loss of office, or as to their remaining in or retiring from office), in connection with, in anticipation of, or in response to, the Offer.

- 11.2. None of the Directors or Senior Officers of TeamTalk are also Directors or Senior Officers of Spark, or any related company of Spark.

**12. Agreement between TeamTalk and Directors and Officers of TeamTalk**

- 12.1. TeamTalk's CEO, Andrew Miller, participates in a Long-Term Incentive Scheme. The Scheme entitles the CEO to receive a cash bonus if TeamTalk's total shareholder return, measured by reference to dividends paid and share price appreciation over a three year period from each entitlement grant under the Scheme, exceeds a prescribed target. The effective date of the last entitlement grant was 1 September 2016, and has a measurement period to 31 August 2019. If a takeover offer for TeamTalk becomes unconditional, resulting in an effective change in control of a majority of TeamTalk's Shares, either TeamTalk or the participant may terminate the Scheme. In that case, the measurement period and vesting calculation is brought forward to the date that the takeover offer becomes unconditional. Total shareholder return is then measured up to the unconditional date of the takeover offer. While these arrangements were not entered into in connection with, in anticipation of, or in response to Spark's Offer, this early termination provision will be exercisable if the Offer becomes unconditional.

**13. Interests of Directors and Officers of TeamTalk in Contracts of Spark (or a related Company of Spark)**

- 13.1. No Director or Senior Officer of TeamTalk or their associates has an interest in any contract to which Spark, or any related company of Spark, is a party.

**13A Interests of TeamTalk's substantial Security Holders in Material Contracts of Spark (or a Related Company of Spark)**

- 13A.1 To the knowledge of the Directors and Senior Officers of TeamTalk, there is no person who holds or controls 5% or more of the TeamTalk Shares and accordingly there is no such person who has an interest in any material contract to which Spark or any related company of Spark is a party.

**14. Additional Information**

- 14.1. In the opinion of the Directors, there is no additional information that is not set out in, or accompanying, this Statement that is, within the knowledge of TeamTalk, required to make the information in the Offer Document is correct or not misleading.

**15. Recommendation**

- 15.1. The Directors of TeamTalk recommend that shareholders **reject the Offer**.
- 15.2. The reasons for that recommendation are set out in Section 1 of this Statement.

**16. Actions by TeamTalk**

- 16.1. There are no material agreements or arrangements (whether legally enforceable or not) entered into by TeamTalk or its related companies as a consequence of, in response to, or in connection with, the Offer.
- 16.2. There are negotiations underway for the sale of equity securities of a related company of TeamTalk. In accordance with Rules 38 and 39 of the Code the parties are aware that any transaction which is entered into while the Offer is outstanding would be subject to the approval by ordinary resolution of TeamTalk's shareholders.

## **17. Equity Securities**

- 17.1. There are currently 28,368,994 TeamTalk Shares on issue. These are fully paid. TeamTalk shareholders have, in respect of each TeamTalk Share, subject to the NZX Main Board Listing Rules and TeamTalk's constitution:
- (a) the right to an equal share in dividends authorised by the TeamTalk Board;
  - (b) the right to an equal share in distribution of surplus assets of TeamTalk;
  - (c) the right to participate in any further issues of TeamTalk Shares by TeamTalk; and
  - (d) the right to cast one vote on a show of hands or the right to cast one vote on a poll (for each TeamTalk Share held) on any resolution, including a resolution to:
    - (i) appoint or remove a Director or the auditor;
    - (ii) alter TeamTalk's constitution;
    - (iii) approve a major transaction by TeamTalk;
    - (iv) approve an amalgamation involving TeamTalk (other than an amalgamation of a wholly owned subsidiary); and
    - (v) put TeamTalk into liquidation.

## **18. Financial Information**

- 18.1. Every person to whom the Offer is made is entitled to obtain from TeamTalk a copy of our most recent annual report (being the report for the financial year ended 30 June 2016) from [www.TeamTalk.co.nz](http://www.TeamTalk.co.nz), or by making a written request to:  
Jo Thornton – Executive Assistant to Chief Executive  
[JThornton@teamtalk.co.nz](mailto:JThornton@teamtalk.co.nz)  
20 Kent Terrace  
Wellington 6011
- 18.2. A copy of TeamTalk's half-yearly report (being the report for the period ended 31 December 2016) is set out in Appendix 2 to this Statement.
- 18.3. There have been no further interim reports of TeamTalk since the half-yearly report.
- 18.4. On 1 March 2017, along with the half-yearly report TeamTalk released guidance for the 12 months to 30 June 2017 in the range of:
  - (a) EBIT of \$4.7 million to \$5.2 million;
  - (b) Profit after tax of \$2.0 million to \$2.4 million.A copy of that statement is also included in Appendix 2.
- 18.5. **Material changes in the financial position, trading position and prospects of TeamTalk since the annual report for the year ended 30 June 2016 were included in and along with TeamTalk's half-yearly report.**
- 18.6. There is no other information about the assets, liabilities, profitability and financial affairs of TeamTalk that could reasonably be expected to be material to the making of a decision by Shareholders to accept or reject the Offer.



## **19. Independent Advice on Merits of the Offer**

- 19.1. Grant Samuel, is the independent adviser and has prepared a report on the merits of Spark's Offer under Rule 21 of the Takeovers Code ("**Independent Adviser's Report**"). A full copy of the Independent Adviser's Report is set out in Appendix 1 to this Statement.

## **20. Prospective Financial Information**

- 20.1. The Independent Adviser's Report and this Statement contain prospective financial information in relation to TeamTalk and its operating divisions in respect of the financial years ending 30 June 2017 and 30 June 2018. The principal assumptions on which the prospective financial information is based are set out in sections 3.3 (at p. 11-12), 3.4 (at p. 13-14), 4.3 (at p. 20), 5.3 (at p. 23) and 6.3 (at p. 26) and are referred to and expanded upon elsewhere in the Report.

- 20.2. The prospective financial information is based upon current expectations and involve risks and uncertainties. Although TeamTalk believes the assumptions underlying the forward looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward looking statements will be realised.

## **21. Market Prices of Quoted Equity Securities Under Offer**

- 21.1. The closing price on the NZX Main Board operated by NZX Limited of TeamTalk Shares on:
- (a) 17 March 2017, being the latest practicable working day before the date on which this Target Company Statement is sent to Shareholders, was \$0.78; and
  - (b) 4 February 2017, being the last day on which the NZX Main Board was open for business before the date on which TeamTalk received Spark's Takeover Notice in respect of the Offer, was \$0.45.
- 21.2. The highest and lowest closing market price of TeamTalk Shares on the NZX Main Board and the relevant dates during the six months before the date on which TeamTalk received Spark's Takeover Notice (7 February 2017) were as follows:
- (a) the highest closing market price was \$0.49 on 21 January 2017; and
  - (b) the lowest closing market price was \$0.38 on 11 November 2016.

## **22. Other Information**

### **Rounding**

- 22.1. Unless otherwise indicated, all shareholding percentages in this Statement are rounded to two decimal places.

### **Reliance on information**

- 22.2. In preparing this Statement, TeamTalk has relied on the completeness and accuracy of information provided by or on behalf of various persons, including Spark and Link Market Services.

## **23. Approval of TeamTalk Statement**

- 23.1. The contents of this Statement have been approved by the TeamTalk Board.

## **24. Certificate**

To the best of our knowledge and belief, after making proper enquiry, the information contained in or accompanying this Statement is, in all material respects, true and correct and not misleading, whether by omission of any information or otherwise, and includes all the information required to be disclosed by TeamTalk under the Takeovers Code.

**SIGNED BY:**



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Roger Sowry, Chairman



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Tone Borren, Director



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Andrew Miller, CEO



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Jason Bull, CFO

## SCHEDULE

### TEAMTALK SHARES OWNED OR CONTROLLED BY DIRECTORS, SENIOR OFFICERS AND THEIR ASSOCIATES

Name	Description	Number of TeamTalk Shares held or controlled	Designation of TeamTalk Shares	Percentage of total number of TeamTalk Shares
Roger Sowry & SA Sowry (jointly)	Chairman of Directors & associate	10,000	Ordinary shares	0.035%
Tuaropaki Communications Limited ("TCL")	TCL is an associate of Nathan York, a Director of TeamTalk	1,137,249	Ordinary shares	4.01%
Custodial Services Limited as nominee for Tone Borren	Director	47,394	Ordinary shares	0.167%
Kevin Brown & Karen Anne Brown	General Manager Commercial & Associate	264,426	Ordinary shares	0.932%

### SHARES IN SPARK OR ITS LISTED PARENT SPARK NEW ZEALAND LIMITED OWNED OR CONTROLLED BY TEAMTALK, DIRECTORS, SENIOR OFFICERS AND THEIR ASSOCIATES

Name	Position	Number of Shares held or controlled	Designation	Percentage of total number of Spark New Zealand Limited Ordinary Shares
Custodial Services Limited as nominee for Tone Borren	Director	3,000	Ordinary shares in Spark New Zealand Limited	0.00016%
Kevin Brown & Karen Anne Brown	General Manager Commercial & Associate	4,800	Ordinary shares in Spark New Zealand Limited	0.00026%
David Struthers	Head of Sales	5,374	Ordinary shares in Spark New Zealand Limited	0.00029%

## APPENDIX 1 – Independent Adviser’s Report

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# TeamTalk Limited

## Independent Adviser's Report

On the Full Takeover by Spark New Zealand Trading Limited

March 2017

Grant Samuel confirms that it:

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

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

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## Glossary

<b>Term</b>	<b>Definition</b>
<b>BCP</b>	Business Continuity Plan
<b>DMR</b>	Digital Mobile Radio
<b>DR</b>	Disaster Recovery
<b>EBIT</b>	Earnings before interest and tax
<b>EBITDA</b>	Earnings before interest, tax, depreciation and amortisation
<b>FTTP</b>	Fibre-To-The-Premise
<b>FY16</b>	The financial year ended 30 June 2016
<b>FY17</b>	The financial year ending 30 June 2017
<b>NZX</b>	New Zealand Stock Exchange
<b>Offer</b>	The full takeover offer for TeamTalk Limited from Spark New Zealand Trading Limited
<b>RBI</b>	Rural Broadband Initiative
<b>Spark</b>	Spark New Zealand Trading Limited, a subsidiary of Spark New Zealand Limited
<b>TeamTalk</b>	TeamTalk Limited
<b>UFB</b>	Ultra-Fast Broadband
<b>VWAP</b>	Volume weighted average share price



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# 1. Terms of the Full Takeover Offer by Spark

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## 1.1 Background

TeamTalk Limited (**TeamTalk**) provides telecommunications services in New Zealand and is listed on the New Zealand Stock Exchange (**NZX**). The group has three companies:

- **TeamTalk Mobile Radio** – which operates mobile radio and wireless networks;
- **CityLink** – which operates fibre optic networks primarily in the Wellington and Auckland central business districts; and
- **Farmside** – which is a rural telecommunications provider.

On 7 February 2017 Spark New Zealand Trading Limited (**Spark**) gave notice of its intention to make a full takeover offer under the Takeovers' Code to acquire 100% of the ordinary shares on issue in TeamTalk for consideration of \$0.80 per share (the **Spark Offer** or the **Offer**). The Offer was sent to TeamTalk shareholders on 9 March 2017 and remains open for acceptance until 22 April 2017, unless extended.

## 1.2 Details of the Full Takeover Offer from Spark

The Offer is for all of the ordinary shares in TeamTalk. The material conditions of the Offer are:

- acceptances are received from TeamTalk shareholders which will result in Spark becoming the holder or controller of 90% or more of the voting rights in TeamTalk. Spark will be entitled to waive this condition at any time and if it becomes the holder or controller of more than 50% of the TeamTalk shares on issue it can declare the offer unconditional and can acquire all the accepting shares;
- a clearance being given, or authorisation being granted by the Commerce Commission for Spark to complete the proposed acquisition of TeamTalk shares in accordance with the offer;
- no dividends, bonus issues or other payments or distributions are declared, paid or made by TeamTalk including by way of a share buy back, redemption or cancellation or any other form of capital reduction;
- the business of each member of the TeamTalk Group is carried on in the normal and ordinary course, consistent with past practices; and
- TeamTalk not making any announcement or issuing any profit earnings guidance or warning to the effect that EBITDA or net profit after tax for either the 12 month period ending 30 June 2017 or the six month period ending 31 December 2017 will or may reasonably be less, by 10% or more, than EBITDA or net profit after tax for the corresponding 12 month period ended 30 June 2016 or the six month period ended 31 December 2016.

A range of other conditions included are designed to protect Spark against any substantial change in the form and operations of TeamTalk or the markets in which it operates. While the Offer is open for acceptance any conditions of the Spark offer may be waived by Spark. The full list of conditions is set out in the Offer document sent to TeamTalk shareholders.

## 1.3 Requirements of the Takeovers Code

The Takeovers Code came into effect on 1 July 2001, replacing the NZX Listing Rules and the Companies Amendment Act 1963 requirements governing the conduct of company takeover activity in New Zealand. The Takeovers Code seeks to ensure that all shareholders are treated equally and on the basis of proper disclosure are able to make informed decisions on shareholding transactions that may impact on their own holdings.

TeamTalk is a Code Company for the purposes of the Takeovers Code. Rule 6 of the Takeovers Code, the fundamental rule, states that a person (along with its associates) who holds or controls:

- (a) no voting rights, or less than 20% of the voting rights, in a code company may not become the holder or controller of an increased percentage of the voting rights in the code company unless, after that event, that person and that person's associates hold or control in total not more than 20% of the voting rights in the code company;

- (b) 20% or more of the voting rights in a code company may not become the holder or controller of an increased percentage of the voting rights in the code company.

Rule 7 of the Takeovers Code sets out the exceptions to the fundamental rule. Rule 7 states that a person may become the holder or controller of an increased percentage of the voting rights in a code company under the following circumstances:

- (a) **by an acquisition under a full offer;**
- (b) by an acquisition under a partial offer;
- (c) by an acquisition by the person of voting securities in the code company or in any other body corporate from one or more other persons if the acquisition has been approved by an ordinary resolution of the code company in accordance with the code;
- (d) by an allotment to the person of voting securities in the code company or in any other body corporate if the allotment has been approved by an ordinary resolution of the code company in accordance with the code;
- (e) if: (i) the person holds or controls more than 50%, but less than 90%, of the voting rights in the code company; and
  - (ii) the resulting percentage held by the person does not exceed by more than 5 the lowest percentage of the total voting rights in the code company held or controlled by the person in the 12-month period ending on, and inclusive of, the date of the increase;
- (f) if the person already holds or controls 90% or more of the voting rights in the code company.

The Takeovers Code specifies the responsibilities and obligations for both Spark and TeamTalk as bidder and target respectively. TeamTalk's response to the Spark Offer, known as a Target Company Statement, must contain the information prescribed in the Second Schedule of the Takeovers Code, and is to include or be accompanied by an Independent Adviser's Report (or summary thereof).

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## 2. Scope of the Report

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### 2.1 Purpose of the Report

The Independent Directors of TeamTalk have engaged Grant Samuel & Associates Limited (**Grant Samuel**) to prepare an Independent Adviser's Report to comply with the Takeovers Code in respect of the Spark Offer. Grant Samuel is independent of TeamTalk and Spark and has no involvement with, or interest in, the outcome of the Spark Offer.

Rule 21 of the Takeovers Code requires the Independent Adviser to report on the merits of an offer. The term "merits" has no definition either in the Takeovers Code itself or in any statute dealing with securities or commercial law in New Zealand. While the Takeovers Code does not prescribe a meaning of the term "merit", it suggests that "merits" include both positives and negatives in respect of a transaction.

A copy of this report will accompany the Target Company Statement to be sent to all TeamTalk shareholders. This report is for the benefit of the shareholders of TeamTalk. The report should not be used for any purpose other than as an expression of Grant Samuel's opinion as to the merits of the Spark Offer. This report should be read in conjunction with the Qualifications, Declarations and Consents outlined at Appendix F.

### 2.2 Basis of Evaluation

Grant Samuel has evaluated the Spark Offer by reviewing the following factors:

- the timing and circumstances surrounding the Spark Offer;
- the estimated value range of TeamTalk and the price of the Spark Offer when compared to that estimated value range;
- the current trading conditions for TeamTalk;
- the attractions of TeamTalk's business (including to Spark);
- the risks of TeamTalk's business;
- the likelihood of alternative offers or alternative transactions that could realise fair value;
- the likely market price and liquidity of TeamTalk shares in the absence of the Spark Offer; and
- any advantages or disadvantages for TeamTalk shareholders of accepting or rejecting the Spark Offer.

### 2.3 Approach to Valuation

Grant Samuel has estimated the value range of TeamTalk with reference to its full underlying value. In Grant Samuel's opinion the price to be paid under a full takeover should reflect the full underlying value of the company. The support for this opinion is two fold:

- the Takeovers Code's compulsory acquisition provisions apply when the threshold of 90% of voting rights has been reached. In this instance, the Takeovers Code seeks to avoid issues of premiums or discounts for minority holdings by providing that a class of shares is to be valued as a whole with each share then being valued on a pro rata basis. In other words, a minority shareholder is to receive its share of the full underlying value. Grant Samuel believes that the appropriate test for fairness under a full or partial takeover offer where the offeror will gain control is the full underlying value, prorated across all shares. The rationale for this opinion is that it would be inconsistent for one group of minority shareholders, those selling under compulsory acquisition, to receive a different price under the same offer from those who accepted the offer earlier; and
- under the Takeovers Code the acquisition of more than 20% of voting rights in a "code" company can only be made under an offer to all shareholders unless the shareholders otherwise give approval. As a result, a controlling shareholding (generally accepted to be no less than 40% of the voting rights) cannot be transferred without the acquirer making an offer on the same terms and conditions to all shareholders (unless shareholders approve). Prior to the introduction of the Takeovers Code some market commentators held the view that where a major shareholder had a controlling shareholding, any control premium attached only to that shareholding. One of the core foundations of the Takeovers Code is that all shareholders be treated equally. In this context,

any control premium is now available to all shareholders under a takeover offer (in a scenario where an offeror will gain control), regardless of the size of their shareholding or the size of the offeror's shareholding at the time the offer is made.

Accordingly, Grant Samuel is of the opinion that not only because shares acquired under a compulsory acquisition scenario will receive a price equivalent to full underlying value, but because the control premium is now available to all shareholders, the share price under either a full or partial takeover offer where the offeror will gain control should be within or exceed the prorated full underlying valuation range of the company.

TeamTalk has been valued at fair market value, which is defined as the estimated price that could be realised in an open market over a reasonable period of time assuming that potential buyers have full information.

Grant Samuel's opinion is to be considered as a whole. Selecting portions of the analyses or factors considered by it, without considering all the factors and analyses together, could create a misleading view of the process underlying the opinion. The preparation of an opinion is a complex process and is not necessarily susceptible to partial analysis or summary. For the avoidance of doubt, appendices A to F form part of this report.

## 2.4 Profile of Spark

Spark (previously known as Telecom NZ) was formed in 1987 as the telecommunications division of the New Zealand Post Office, a Government department. In 1990, Telecom NZ was privatised and shortly thereafter was listed on the NZX. In 2011, Spark demerged into two separate publicly listed companies: a retail services provider – Telecom NZ (now Spark) and a network and services operator – Chorus Limited (**Chorus**). The structural separation of Telecom NZ's retail business from the network business was a pre-requisite for Chorus's participation in the government's Ultra-Fast Broadband (**UFB**) scheme. In 2014, Telecom NZ changed its name to Spark.

Today Spark comprises the following business divisions:

- **Spark Home, Mobile & Business**, which provides products, services and support to consumer and small business customers. It provides a full range of content, data and voice services across fibre and copper broadband, 3G and 4G mobile and nationwide Wi-Fi zones. The key priorities for Spark Home, Mobile and Business are to drive growth in the mobile and small business markets whilst holding market share in the broadband market. This division generated EBITDA of \$778 million in the financial year ended 30 June 2016;
- **Spark Digital**, which provides solutions for business, enterprise and Government customers. Spark Digital's services comprise integrated telecommunications services including data centre services. This division generated EBITDA of \$410 million in the financial year ended 30 June 2016; and
- **Spark Connect**, which is responsible for all the Group's network and IT operations and servicing of wholesale and international customers. Spark Connect also provides critical support services to Spark such as billing, credit collections, provisioning, procurement and property management. This division generated an EBITDA loss of \$(182) million in the financial year ended 30 June 2016

As at 30 June 2016 Spark had approximately 2.29 million mobile connections and 675,000 broadband connections. Spark employs approximately 5,600 people.

A summary of Spark's financial performance, position and cash flows for the financial years ended 30 June 2014, 2015 and 2016 is provided below:

**Spark Summary Financial Information (NZ\$ millions)**

<b>Year end 30 June</b>	<b>2014A</b>	<b>2015A</b>	<b>2016A</b>
<b>Financial Performance</b>			
Revenue	3,638	3,531	3,497
EBITDA	936	962	986
EBIT	485	509	540
NPAT	323	375	370
<b>Cash Flows</b>			
Operating cash flow	614	630	716
Investing cash flow	10	(456)	(488)
Financing cash flow	(530)	(304)	(256)
<b>Net cash flow</b>	<b>94</b>	<b>(130)</b>	<b>(28)</b>
<b>Financial Position</b>			
Total Assets	3,243	3,206	3,237
Total Liabilities	(1,535)	(1,428)	(1,553)
<b>Net Assets</b>	<b>1,708</b>	<b>1,778</b>	<b>1,684</b>

Source: Spark Annual Reports FY14 to FY16

As at 17 March 2017, Spark had a market capitalisation of approximately \$6.45 billion. The company is listed on the NZX and Australian Stock Exchange and has approximately 27,500 shareholders. It is the third largest company measured by market capitalisation on the NZX.

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## 3. Profile of TeamTalk

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### 3.1 Company History

TeamTalk was formed by former Post Office technician David Ware in 1992 with finance from a US venture capital company. The company launched a mobile radio service in August 1994 from sites in Auckland and Wellington. When TeamTalk's US parent suffered financial difficulties, the company was purchased by management and in 1998 New Zealand investment company Active Equities acquired a 50% shareholding and recapitalised the company. In 2001 TeamTalk purchased Telecom NZ's mobile radio business and as part of this transaction Telecom NZ acquired a 19.9% stake in the company. TeamTalk repurchased the Telecom NZ shares in June 2003. TeamTalk was listed on the NZX in 2004 issuing 4.6 million shares at \$1.75 per share. Since listing on the NZX TeamTalk has made the following acquisitions:

- in October 2005, TeamTalk acquired the assets of MCS Network Ltd (**MCS**), a company with mobile radio networks covering Auckland and the upper North Island for \$1.9 million. MCS was integrated into TeamTalk Mobile Radio;
- in July 2006 TeamTalk acquired a 35% stake in Araneo, a last-mile telecommunications infrastructure company. In October 2007, TeamTalk increased its stake in the company to 55.9%. TeamTalk subsequently acquired 100% ownership and Araneo was amalgamated with TeamTalk Mobile Radio;
- in December 2006, TeamTalk acquired a 67% shareholding in Wellington based fibre network company CityLink for \$12.7 million. TeamTalk now has full ownership of CityLink; and
- in November 2012 TeamTalk acquired BayCity Communication Limited, trading as the Farmside Group, for an upfront purchase price of \$31.0 million. Farmside is New Zealand's largest satellite broadband provider focused on the rural sector.

TeamTalk appointed a new CEO, Andrew Miller, in September 2016 following the resignation of TeamTalk's founder and Managing Director, David Ware, in April 2016. On 10 August 2016 TeamTalk announced that it had commissioned a review of TeamTalk's strategy and the subsequent evaluation of strategic options.

### 3.2 Profile of TeamTalk's Business Divisions

Today, TeamTalk has three companies:

- **Mobile Radio (TeamTalk)**, comprising the traditional mobile radio business of TeamTalk along with associated finance leasing, data and GPS tracking products and the wireless broadband business of TeamTalk. During FY16, this division generated EBITDA of approximately \$4.0 million, representing 32% of group EBITDA;
- **Wired Networks (CityLink)**, which provides broadband connectivity and ancillary related services to a range of wholesale customer and end users in the Wellington and Auckland CBD's. During FY16 this division generated EBITDA of \$7.2 million, representing approximately 57% of group EBITDA; and
- **Internet Service Provider (Farmside)**, which provides internet and telecommunications services primarily to rural residential customers. During FY16, Farmside generated EBITDA of \$1.4 million, representing approximately 11% of group EBITDA.

### 3.3 Financial Performance

The financial performance of TeamTalk for the years ended 30 June 2014 to 2016 (**FY14** to **FY16**), together with the forecasts for the year ending 30 June 2017 and 2018 (**FY17** and **FY18**), are shown below. The forecasts for FY18 are from the five year forecast through to the financial year ended 30 June 2022.

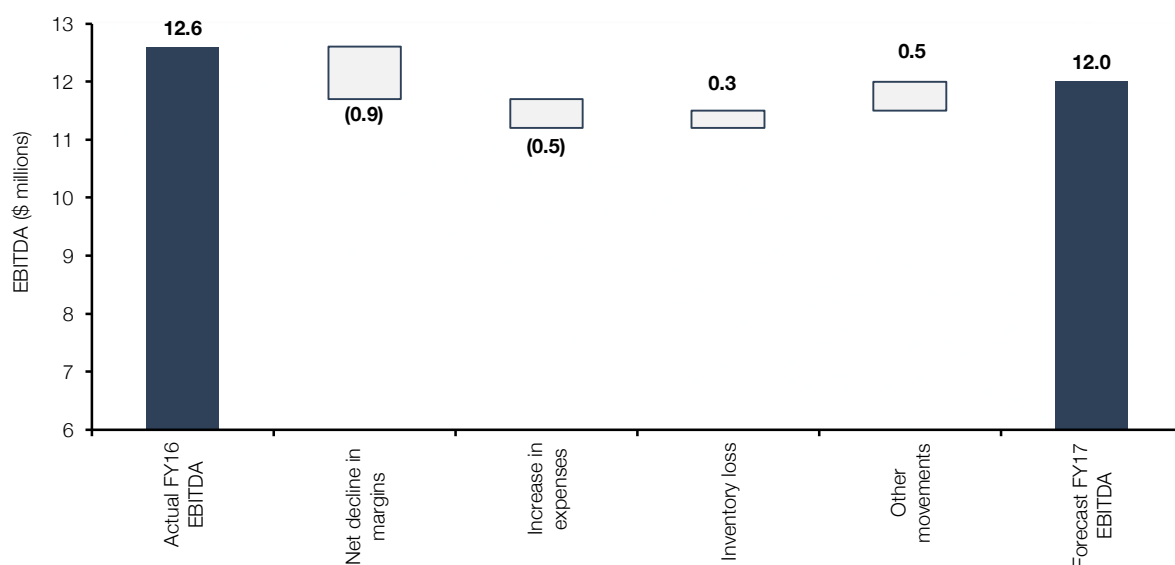
#### TeamTalk Financial Performance (NZ\$ millions)

Year end 30 June	2014A	2015A	2016A	2017F	2018F
Sales	60.3	57.8	57.3	56.1	56.4
Networking operating costs	(14.1)	(14.8)	(15.4)	(13.4)	(12.6)
Other operating costs	(13.7)	(12.4)	(12.9)	(13.2)	(12.8)
<b>Gross margin</b>	<b>32.6</b>	<b>30.5</b>	<b>28.9</b>	<b>29.5</b>	<b>31.0</b>
Gross margin %	54.0%	52.8%	50.5%	52.6%	55.0%
Other income	0.7	0.6	0.8	0.6	0.6
Employee related expenses	(12.6)	(12.6)	(11.8)	(12.8)	(10.5)
Other administrative expenses	(5.0)	(5.4)	(5.2)	(5.3)	(4.8)
<b>EBITDA</b>	<b>15.7</b>	<b>13.2</b>	<b>12.6</b>	<b>12.0</b>	<b>16.3</b>
EBITDA margin %	26.0%	22.8%	22.1%	21.4%	28.9%
Depreciation & amortisation	(7.4)	(7.1)	(9.1)	(6.8)	(6.8)
<b>EBIT before impairments</b>	<b>8.3</b>	<b>6.1</b>	<b>3.6</b>	<b>5.2</b>	<b>9.5</b>
Net interest	(2.1)	(2.7)	(2.2)	(1.5)	(2.6)
Asset impairments	(2.4)	(1.7)	(1.8)	-	-
Goodwill impairments	(11.4)	-	(1.0)	-	-
Tax income/ (expenses)	(0.8)	(0.4)	0.1	(1.3)	(1.9)
<b>Profit after tax</b>	<b>(8.3)</b>	<b>1.3</b>	<b>(1.3)</b>	<b>2.4</b>	<b>5.0</b>

The following points should be taken into consideration when reviewing the table above:

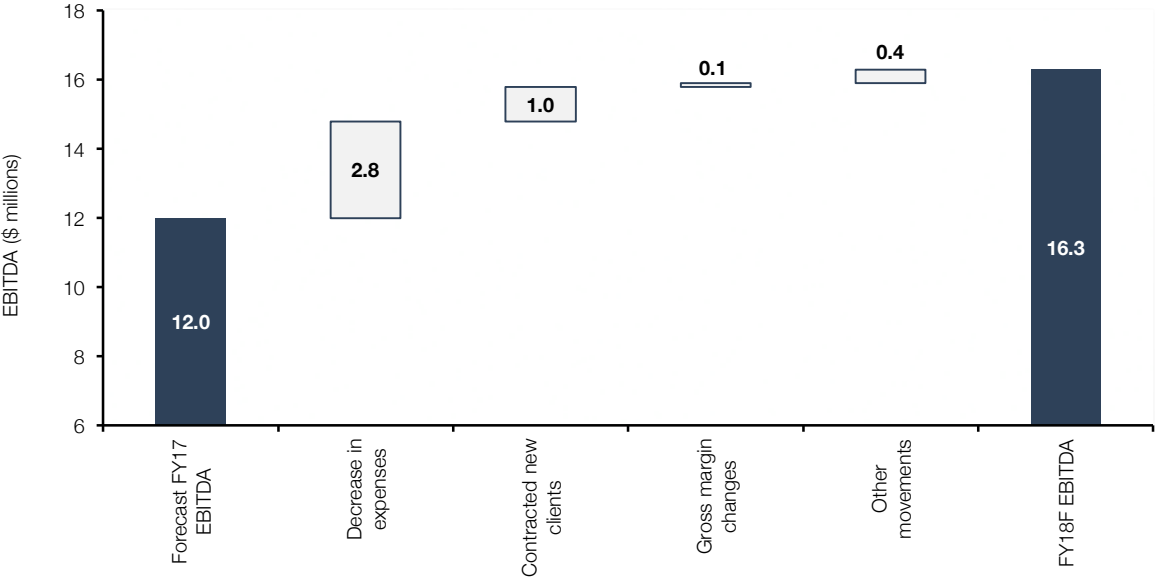
- TeamTalk's FY17 forecast incorporates actual results for 8 months to 28 February 2017;
- TeamTalk's EBITDA is forecast to decline from \$12.6m in FY16 to \$12.0m in FY17 primarily due to a decline in gross margin from satellite services offset by increased margin from the Government subsidised Rural Broadband Initiative (**RBI**) (-\$0.9 million), an increase in sales, general and administration costs (-\$0.5 million), a reduction in inventory losses (+0.3 million) and other movements (+\$0.5 million).

#### EBITDA Bridge Diagram – FY16A to FY17F



- TeamTalk is forecasting EBITDA to increase to \$16.4 million in FY18 driven by \$2.8 million in expense reductions, \$1.0 million in gross margin from new client wins, and \$0.5m of other changes. The FY18 forecast reflects TeamTalk’s new strategic plan.

**EBITDA Bridge Diagram – FY17F to FY18F**



- the majority of the difference between FY17 and FY18 EBITDA comprises identified overhead cost reductions that are currently being implemented and the margin from new contracted business which is projected to be revenue generating by the commencement of FY18;
- as Farmside’s customers have migrated from satellite to RBI solutions, TeamTalk has had to impair, or write off, investments in satellite equipment; and
- during FY14 TeamTalk impaired \$11.4 million of goodwill that was recorded upon the acquisition of Farmside. During FY16 TeamTalk impaired a further \$1.0 million of goodwill relating to the Farmside acquisition.



### 3.4 Financial Position

The financial position of TeamTalk as at 30 June 2015 and as 2016, and as at 31 December 2016 is outlined below:

<b>TeamTalk – Financial Position (NZ\$ millions)</b>			
<b>As at</b>	<b>Jun 15</b>	<b>Jun 16</b>	<b>Dec 16</b>
Trade & other receivables	6.9	7.2	6.0
Inventory	2.3	1.8	1.4
Trade & other payables	(8.9)	(8.9)	(10.2)
Deferred income	(7.0)	(6.5)	(5.7)
Other working capital assets & liabilities	1.6	0.7	0.6
<b>Net working capital</b>	<b>(5.1)</b>	<b>(5.7)</b>	<b>(7.9)</b>
Property, plant & equipment	40.7	37.0	39.2
Intangible assets	23.7	21.3	21.2
Deferred tax	(0.4)	1.2	1.4
<b>Net operating assets</b>	<b>58.9</b>	<b>53.8</b>	<b>53.9</b>
Loans & borrowings	(35.5)	(33.7)	(33.9)
Derivatives	(0.2)	(0.8)	(0.2)
Cash & finance lease receivables	0.7	0.9	1.8
<b>Net assets/ Equity</b>	<b>23.8</b>	<b>20.2</b>	<b>21.6</b>

The following points are relevant when reviewing the table above:

- TeamTalk's property, plant and equipment assets primarily consist of transmission equipment and hardware. A breakdown of TeamTalk's property, plant and equipment balance as at 30 June 2016 is provided below:

#### **Breakdown of Property, Plant and Equipment as at 30 June 2016 (\$ millions)**

<b>Category</b>	<b>Cost</b>	<b>Accumulated Depreciation</b>	<b>Book Value</b>
Transmission equipment and network	120.3	(87.2)	33.0
Assets under construction	2.4	-	2.4
Other assets	7.3	(5.7)	1.6
<b>Total</b>	<b>129.9</b>	<b>(93.0)</b>	<b>37.0</b>

- as at 30 June 2016 intangible assets comprised \$19.8 million in goodwill arising from the acquisition of CityLink, TeamTalk Mobile Radio and Farmside and \$1.5 million in value assigned to customer contracts and other intangibles;
- as of 28 February debt was \$33.2 million. Debt is relatively high due to the purchase of Farmside in 2012 which resulted in debt increasing by \$20 million. In addition, despite relatively poor cash flow generation, TeamTalk continued to pay dividends of 20 cents per share and only stopped paying dividends in June 2016; and
- TeamTalk recently announced that it has agreed the essential terms of a new three year bank facility through to March 2020. TeamTalk has a plan in place to reduce its debt balance by approximately 33% by 30 June 2018.

### 3.5 Cash Flows

The cash flows for TeamTalk for FY15 and FY16, together with the forecast FY17 are shown below:

<b>TeamTalk – Cash Flows (NZ\$ millions)</b>			
<b>Financial year end 30 June</b>	<b>2015A</b>	<b>2016A</b>	<b>2017F</b>
Customer receipts	59.8	57.3	58.2
Payments to supplier & employees	(47.8)	(45.0)	(44.7)
Income tax paid	(1.4)	(0.6)	(1.1)
Net interest paid	(2.1)	(1.8)	(1.4)
<b>Net cash flow from operations</b>	<b>8.5</b>	<b>9.9</b>	<b>11.0</b>
Net purchase of property, plant & equipment	(6.2)	(5.7)	(7.9)
Other investing cash flows	0.2	-	-
<b>Net cash flow from investing</b>	<b>(6.0)</b>	<b>(5.7)</b>	<b>(7.9)</b>
Net drawdown/(repayment) of borrowings	0.9	(1.8)	(3.1)
Dividends paid	(3.3)	(2.3)	-
<b>Net cash flow from financing</b>	<b>(2.4)</b>	<b>(4.1)</b>	<b>(3.1)</b>
<b>Net cash flow</b>	<b>-</b>	<b>0.1</b>	<b>-</b>
Opening cash	0.4	0.4	0.5
<b>Closing cash</b>	<b>0.4</b>	<b>0.5</b>	<b>0.5</b>

In reviewing the above table the following should be noted:

- TeamTalk's dividends reduced in FY16 due to the lower profitability levels. The company will not be paying a dividend in FY17; and
- TeamTalk is forecasting capital expenditure until FY20 to be in the range of 12-14% of revenue p.a. as the company invests in a nationwide DMR network and its Wellington fibre network. From FY21 onwards capital expenditure is expected to reduce significantly to within a range of approximately 6-8% of revenue.

### 3.6 Capital Structure and Ownership

As of 10 March 2017 TeamTalk had 28,368,994 shares on issue held by approximately 1,510 shareholders. The Company's top 10 shareholders are shown below:

#### TeamTalk – Top 10 Shareholders as 10 March 2017

Shareholder	Shares (000s)	%
Barry Payne, Brett Gould & Sandra Payne	1,223	4.3
Tuaropaki Communications Limited	1,137	4.0
National Nominees Limited	805	2.8
Forsyth Barr Custodians Limited	755	2.6
Jarden Custodians Limited	690	2.4
Sydney Crowther & Faith and Stephen Palairet	529	1.9
Accident Compensation Corporation	510	1.8
Roy Wilson	400	1.4
FNZ Custodians Limited	400	1.4
Deborah & Mark Thomson	399	1.4
<b>Top 10 Shareholders</b>	<b>6,848</b>	<b>24.1</b>
Other Shareholders	21,521	75.9
<b>Total</b>	<b>28,369</b>	<b>100.0</b>

TeamTalk's shares are widely held with the top 10 shareholders controlling 24.1% of the shares on issue and the largest shareholder controlling 4.3% of the shares on issue.

### 3.7 Share Price Performance

The share price and trading volume history of TeamTalk shares since the beginning of January 2015 is depicted below:

#### TeamTalk Share Price Performance Since the Beginning of 2015



The following comments are relevant when reviewing the graph above:

- on 23 January 2015 TeamTalk revised its first half profit expectations downwards for the first half of its 2015 financial year on the back of lower growth and unexpected one-off items. TeamTalk's share price subsequently declined from \$1.70 per share to \$1.15 per share; and
- on 10 June 2016 TeamTalk announced that its second half results had not met expectations with EBITDA lower than previously advised to the market in February 2016. TeamTalk's share price declined from a closing price of \$0.67 per share on 9 June 2016 to \$0.42 per share on 23 June 2016. From 24 June 2016 to just prior the Spark Offer, TeamTalk's shares have traded within a range of \$0.38 to \$0.49 per share.

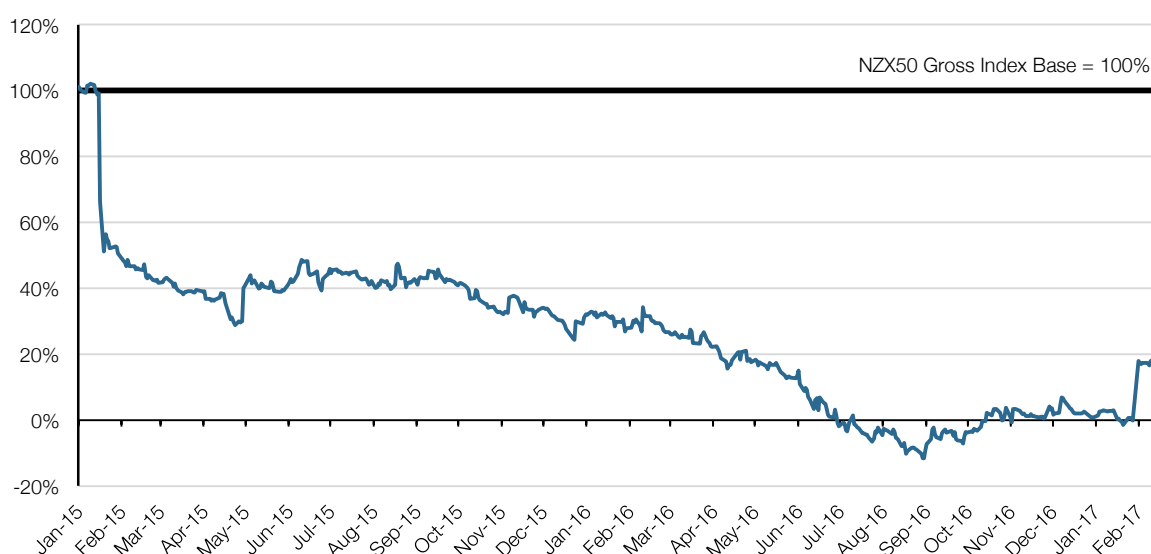
The following table shows the price and volume of TeamTalk shares traded over the past 12 months:

**TeamTalk – Share Trading Summary (\$NZ)**

Time period	Low	High	VWAP	Volume (millions)
Post Offer announcement	\$0.71	\$0.80	\$0.76	1,989
<b>Pre-Offer announcement</b>				
1 months	\$0.44	\$0.50	\$0.47	149
3 months	\$0.38	\$0.50	\$0.44	437
6 months	\$0.38	\$0.50	\$0.43	1,801
12 months	\$0.38	\$0.79	\$0.55	5,643

TeamTalk’s share price against the NZX 50 Gross Index is shown below:

**TeamTalk Share Price Performance Versus the NZX50 Gross Index since the beginning of 2015**



TeamTalk has significantly underperformed the NZX50 Gross Index since the beginning of 2015. During this period the NZX50 Gross Index has increased by approximately 26% while TeamTalk’s share price decreased by 74% immediately prior to the Spark Offer being announced.

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## 4. Profile of TeamTalk Mobile Radio

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TeamTalk's Mobile Radio division primarily operates in the mobile radio market in New Zealand. Mobile radio are wireless communications systems and devices based on radio frequencies (as opposed to cellular networks). An overview of the market is provided below:

### 4.1 Market Profile

The mobile radio market in New Zealand is estimated to generate annual revenue of approximately \$65 million per annum (excluding hardware sales).<sup>4</sup> There are two distinct segments in the mobile radio market – conventional radio and trunked radio. In a conventional radio system, the user manually selects the channels to communicate on and in a trunked system the channels are assigned to the user automatically. Trunked systems take advantage of the dynamic that not everyone will require a channel at the same time so the number of users that can be supported grows exponentially with the number of channels. For this reason, trunked systems are considered more suitable for larger groups of users and conventional systems are typically more suited for smaller groups of users.

#### *Conventional Mobile Radio Market*

The conventional mobile radio market segment is significantly larger than the trunked radio segment, representing approximately 84% of the total market by estimated annual revenue. TeamTalk is estimated to have a circa 9% share of the conventional radio market.<sup>5</sup> There are a range of participants in the conventional radio segment, largely operating geographically concentrated or regional networks. Customers are typically first responder organisations such as Ambulance and Police, and medium-to-large companies operating in sectors where secure communication between employees is required.

#### *Trunked Mobile Radio Market*

The trunked radio segment represents approximately 16% of the total mobile radio market in New Zealand by estimated annual revenue. TeamTalk Mobile Radio is the dominant player with an estimated market share of greater than 90%. Customers are typically large corporates, transport and construction companies and government departments. TeamTalk Mobile Radio is the only company that offers a nationwide network and accordingly its customers are primarily organisations that require nationwide mobile radio solutions. For customers where a regional solution is required TeamTalk Mobile Radio faces competition from other network providers such as Push Wireless and Orion Networks. An overview of the primary participants in the New Zealand trunked mobile radio market is provided below:

#### **Overview of the Primary Participants in the New Zealand Trunked Mobile Radio Market**

<b>Company</b>	<b>Description</b>
<b>TeamTalk Mobile Radio</b>	<ul style="list-style-type: none"><li>TeamTalk Mobile Radio is the primary provider of trunked radio services and large conventional networks in New Zealand, primarily to emergency services and large organisations that require nationwide solutions. The company also provides conventional and digital radio services to smaller organisations.</li></ul>
<b>Tait Communications</b>	<ul style="list-style-type: none"><li>Tait Communications (<b>Tait</b>) is a Christchurch based manufacturing company specialising in providing mobile radio solutions worldwide. Tait has a Digital Mobile Radio (<b>DMR</b>) Tier III solution. It supports a consortium of Tait dealers comprising Push Wireless, Skycom and Mt Campbell Communications, who deploy regional networks using Tait products.</li></ul>
<b>Motorola Solutions</b>	<ul style="list-style-type: none"><li>Motorola Solutions is a global supplier of mission-critical communications products services and solutions. In New Zealand Motorola Solutions offers Tier II solutions. The company supports a consortium of Motorola dealers in the form of Orion Networks using Motorola network products.</li></ul>

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<sup>4</sup> TeamTalk estimate.

<sup>5</sup> Market share information has been calculated by TeamTalk using radio license data as at June 2016.

<b>Push Wireless</b>	<ul style="list-style-type: none"> <li>▪ The Push Wireless consortium holds radio licenses for digital networks in the Waikato, Bay of Plenty and Wellington regions along with Mt Campbell Communications in Nelson. These groups are all using Tait DMR Tier III networks and are supported by Tait in Christchurch.</li> </ul>
<b>Netcomm</b>	<ul style="list-style-type: none"> <li>▪ Netcomm offers access to a Motorbo<sup>6</sup> DMR Tier II trunked network in the central North Island.</li> </ul>
<b>Orion Networks</b>	<ul style="list-style-type: none"> <li>▪ The Orion Network solution is based on Motorola's DMR Tier II Connect Plus product. The Orion networks are operated by Genesis in Auckland, TL Parker in Christchurch, Richardson's Communication in Hamilton and MC Communications in Taranaki.</li> </ul>

## Key Industry Trends

Key trends that are expected to impact the mobile radio market in New Zealand include:

- **Increased awareness of requirement for mobile radio in future telecommunications mix**

A consequence of the Christchurch and Kaikoura earthquakes is that Government departments and large companies have become more aware that mobile radio should form part of their future telecommunications mix for Disaster Recovery and Business Continuity Planning (**DR/BCP**) purposes as cellular networks do not provide the same level of resilience as mobile radio networks in the event of natural disaster.

- **Shift to Digital Mobile Radio networks driven by user requirements**

Customer requirements are driving a shift from conventional analogue radio to digital radio networks. Digital radio can provide the features that are being demanded by customers including:

- enhanced worker safety (including emergency notifications, checking of lone workers, reporting on the location of workers and having a single button for communication);
- more efficient data transfer enabling improved worker productivity;
- improved audio quality. Digital radio filters out ambient noise for clearer voice communication than cell phones;
- customisable call types, which allow users to communicate more effectively. Calls can be public (one-to-many) or private (one-to-one);
- call priority levels provide increased levels of access to the radio network (normal calls, priority calls and emergency calls);

The lack of investment in New Zealand's existing mobile radio infrastructure, which is predominantly analogue, is also driving investment in DMR.

- **New Health & Safety legislation**

The more stringent requirements of the new Health & Safety legislation is resulting in companies having a greater interest in value-added mobile radio solutions such as lone worker, man down and location services. DMR is expected to provide opportunities to connect field workers directly to the customer's data and systems. Real-time applications for control room, safety, location/positioning services and infrastructure management will result in increased productivity.

- **Growth in the mobile radio market**

International market research is forecasting the mobile radio market to grow by more than 10% p.a. over the next five years. The move from analogue to digital technology, increased emphasis on health & safety and fit-for-purpose communications systems is driving demand for mobile radio systems worldwide.

## 4.2 Business Profile

TeamTalk's Mobile Radio business, trading as *TeamTalk*, was established in 1994 as a mobile radio service in Auckland and Wellington. In 2001 the business was expanded with the purchase of Telecom NZ's mobile radio business and in 2005 TeamTalk Mobile Radio acquired MCS's mobile radio services business which expanded the

<sup>6</sup> Motorbo is DMR Network offered by Motorola Solutions.

company's operations in the upper North Island. Today, TeamTalk Mobile Radio provides nationwide mobile radio and wireless broadband services. TeamTalk Mobile Radio also provides a range of GPS based dispatch and tracking services to organisations operating in the New Zealand transport sector.

TeamTalk's radio network features a number of unique aspects that would be difficult for a competitor to replicate:

- access to suitable elevated sites is difficult to gain. A new entrant would need to negotiate nationwide co-location agreements with multiple players to get access to sites. TeamTalk Mobile Radio currently has access to 450 high sites across New Zealand;
- it would be difficult to get sufficient workable spectrum, particularly in the more congested markets such as Auckland;
- to obtain backhaul links for the transmission sites to core switching nodes will require leasing capacity from network owners. The internet has not proved to be a reliable alternative for backhaul;
- New Zealand is a long skinny country making establishing and maintaining a radio network a challenge requiring different skills to a cellular network;
- TeamTalk has more than 90% of the trunked radio market. To get this business a competitor would likely have to cut prices; and
- TeamTalk Mobile Radio estimates the capital cost to replicate the existing radio network would be approximately \$35 million.

Mobile radio services represents approximately 80% of the revenues generated by TeamTalk Mobile Radio. The remaining 20% of revenues is generated by the wireless broadband business, which trades under the Araneo brand. Araneo has been delivering ethernet via wireless and microwave radio since 2004, specialising in remote connectivity.

TeamTalk's investment in its mobile radio network has not kept pace with cellular mobile networks that have evolved from 2G to 3G to 4G with 4.5G soon to be introduced. Following a long period of underinvestment, there is an opportunity for TeamTalk to invest in a nationwide Digital Mobile Radio (**DMR**) Network infrastructure to meet the DR/BCP needs of the market utilising the DMR and satellite. A DMR network is required to provide the additional features that government departments and enterprises are now requiring including messaging features, job dispatch, integration with back office systems, voice recording and gateways between mobile radio and smartphone applications.

A new DMR network will bring the following benefits to TeamTalk Mobile Radio:

- removes the need to spend business-as-usual capital expenditure on an ageing infrastructure;
- reduces on-site costs as these will be reduced as networks are consolidated;
- reduces maintenance costs;
- expands the capability and capacity of the network; and
- recaptures the lost market and brings increased EBIT through the provision of digital services.

The estimated cost of having a fully digital mobile radio network is approximately \$8 million to be spent over the next two financial years.

### 4.3 Financial Profile

The financial performance of TeamTalk's Mobile Radio division for FY15 to FY16, together with the forecast for FY17 and FY18 is outlined below:

#### Segment Performance – TeamTalk Mobile Radio (NZ\$ millions)

Year end 30 June	2015A	2016A	2017F	2018F
<b>Total revenue</b>	<b>20.8</b>	<b>20.3</b>	<b>20.6</b>	<b>21.2</b>
<i>Change in revenue %</i>	10.2%	(2.7%)	1.5%	2.9%
Total costs	(16.7)	(16.2)	(15.7)	(15.4)
<b>EBITDA</b>	<b>4.2</b>	<b>4.0</b>	<b>4.9</b>	<b>5.8</b>
<i>EBITDA margin %</i>	20.0%	19.9%	24.8%	27.3%
Depreciation	(2.4)	(2.6)	(2.3)	(2.4)
<b>EBIT</b>	<b>1.7</b>	<b>1.4</b>	<b>2.6</b>	<b>3.4</b>
Segment Assets	22.9	22.0	23.8	26.1
Segment Liabilities	(8.8)	(8.9)	(8.6)	(8.6)
<b>Segment Net Assets</b>	<b>14.1</b>	<b>13.1</b>	<b>15.2</b>	<b>17.5</b>
<i>EBIT / average net assets %</i>	13.1%	10.5%	19.8%	20.8%
Capital expenditure	2.1	2.0	2.2	4.8
<i>Capex as % of depreciation</i>	88%	77%	96%	200%

The following points are relevant when reviewing the table above:

- approximately 80% of the TeamTalk Mobile Radio division's revenue is recurring in nature;
- the forecasts for FY17 and FY18 are for modest growth pending the conversion to the DMR network;
- capital expenditure primarily on the DMR is planned to increase in FY18 and FY19 to \$4.8 million each year before reducing significantly to well below the level of depreciation; and
- TeamTalk Mobile Radio is forecasting increasing EBITDA margins through improved overhead expense controls. The majority of the overhead costs of running TeamTalk are borne by the TeamTalk Mobile Radio division. Cost savings in the Head Office are currently being implemented and are fully reflected in the FY18 forecasts.



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## 5. Overview of the Wired Networks Division (CityLink)

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### 5.1 Market Profile

#### Market Overview

TeamTalk's CityLink business primarily operates fibre network in the Auckland and Wellington CBD's. Fibre network owners provide access to two distinct customer types:

- **Wholesale customers**, which purchase fibre access on a wholesale basis:
  - **Telecommunications companies**, (including Spark, Vodafone and 2Degrees) which on-sell broadband services to their retail and commercial customers;
  - **ICT channel partners**, which combine fibre network access with other ICT products for their customers. Examples of ICT channel partners include Dimension Data and Datacom; and
  - **Retail services providers**, which provide fibre network access with other products to their customers. Examples include Trustpower, which bundles broadband and internet with electricity.Approximately two-thirds of CityLink's fibre revenue is generated from the wholesale market.
- **Direct**, which involves selling fibre network access directly to customers. Approximately one-third of CityLink's fibre revenue is from the direct channel.

CityLink's key competitors are Chorus, Vector and Vodafone New Zealand.

#### Key Industry Trends

Key trends that are impacting or expected to impact the fibre network market in New Zealand include:

- **Continued price pressure**

The UFB programme has set default price points for accessing the telecommunications access market which has resulted in a tightening of margins of infrastructure access providers such as CityLink. As a result, operators must innovate and provide superior services to ensure they maintain competitive in the market.
- **Increased speed of wireless services**

Continued development of wireless technology, including 4.5-5G broadband, is expected to continue to encourage new fixed and mobile applications. These technologies will ultimately substitute current wireless LTE service and potentially displace some terrestrial access services on these new market opportunities.
- **Internet of Things (IoT)**

The IoT is the internetworking of connected devices, buildings and other systems. Monitoring and controlling devices and systems is gaining momentum as smarter telemetry access technology is being deployed. The applications of this technology is far reaching including residential, urban and rural locations. The ability to cost effectively deploy IoT access is fundamental to the success of connecting these devices.
- **Business Continuity**

Following recent earthquakes, some businesses are seeking to improve resilience of their telecommunication networks. Options include diverse building access including fibre and wireless connectivity, intercity connectivity to re-establish a presence in different cities and options for remote working.
- **Increasing Momentum of Ultra-Fast Broadband (UFB)**

As at December 2016 there were 1.062 million users able to connect to fibre, representing 73% of the 1.459 million households and businesses targeted under part one of the UFB programme. Uptake to fibre reached 30.9% in December 2016 with 328,000 customers now accessing fibre. The historical trend in the number of users able to connect, the percentage completion of the programme, the number of connected users and the uptake percentage between December 2012 and 2016 are outlined below:

## UFB Statistics – December 2012 to 2016 (000s)

As at December	2012	2013	2014	2015	2016
Users able to connect	135	363	570	875	1,062
% complete	9%	25%	39%	60%	73%
Connected users	4	20	69	163	328
Uptake %	2.8%	5.5%	12.2%	18.6%	30.9%

### ■ **Increasing bandwidth demands**

Bandwidth demand is increasing rapidly driven by the growth in on-line entertainment, social media, cloud services and devices becoming more interconnected. This demand is expected to accelerate as fibre networks underpin the delivery of high speed 5G wireless networks, and bandwidth hungry video and entertainment applications. This increase in bandwidth demand is driving the growth in fibre networks.

## 5.2 Business Profile

TeamTalk's Wired Networks business, trading as *CityLink*, was established by the Wellington City Council in 1995 to provide fibre optic communications in the Wellington CBD. In 1999 the Wellington City Council sold its shareholding in CityLink. From 1995 until 2006 the business grew substantially and CityLink became recognised as a leader on how open access metropolitan fibre networks should be built, operated and marketed.

In 2006 TeamTalk invested in CityLink. The investment provided access to capital to enable CityLink to accelerate the network rollout in the Wellington CBD and to the outlying suburbs, and to develop a fibre network in the Auckland CBD. Today, CityLink owns and operates fibre optic telecommunications networks in the Auckland and Wellington CBD's. CityLink's networks provide a range of fibre and value added services including:

- **Broadband Services:** A fibre network that supports high speed broadband services including internet access and telecommunications access services;
- **Peering:** CityLink owns and operates New Zealand's Internet Exchanges. These exchanges provide a market place for Internet Service Providers, Corporates, and Content Providers (e.g. Microsoft) to cost effectively exchange terabytes of data each month;
- **Wi-Fi:** CityLink operates Wellington City's free Wi-Fi service throughout the CBD and the council wish this to be expanded. This service targets students and tourists requiring free, high speed Wi-Fi access. Since its inception in conjunction with the 2011 Rugby World Cup the service continues to expand its footprint and enhance services, supported by the Wellington City Council. CityLink also operates Wi-Fi for a range of other customers;
- **Data Centres:** CityLink operate three CBD datacentres, two in Wellington and one in Auckland. These centres provide hosting facilities for customer's equipment, cloud based service and an opportunity to sell further access services; and
- **Government Interconnect:** CityLink operates Telecommunications as a Service (**TaaS**) interconnection points in the Government's Infrastructure as a Services (**IaaS**) datacentres. This service interconnects the major TaaS providers to each other and content within the IaaS Datacentres. CityLink also manages the Interconnect Forum to set Interconnect standards on behalf of Government.

CityLink has 273 kilometres of fibre in streets (both underground and aerial) and 67 kilometres of fibre in buildings.

The UFB initiative is changing the dynamics of CityLink's traditional fibre markets. UFB creates an opportunity for CityLink to provide an expanded range of cheaper connectivity services with increased margins as experienced following the roll out of UFB in the Auckland CBD.

CityLink is a respected market player, recognised by its customers for its high-quality service. CityLink offers customised services that do not require third party suppliers (such as Chorus), therefore reducing service connection and restoration time. Many customers acknowledge this point of difference and have accredited CityLink as their provider of choice for access and network services.

CityLink will transfer part of its Wellington fibre network off the Trolley Bus infrastructure as Wellington City decommissions its Trolley Bus system. This will create an opportunity to re-architect the network to a multi-hub, star

configuration as deployed by traditional telecommunications companies. This will increase CityLink's ability to further enhance the speed of deployment and its range of services. The cost of undergrounding this portion of the network has been forecast by TeamTalk management at approximately \$6 million.

### 5.3 Financial Profile

The financial performance of CityLink for FY15 and FY16, together with the forecast for FY17 and FY18 is outlined below:

#### CityLink Summary Financial Performance (NZ\$ millions)

Year end 30 June	2015A	2016A	2017F	2018F
<b>Total revenue</b>	<b>13.5</b>	<b>13.9</b>	<b>14.5</b>	<b>15.2</b>
<i>Change in revenue %</i>	<i>(12.6%)</i>	<i>3.1%</i>	<i>4.3%</i>	<i>5.0%</i>
Total costs	(7.0)	(6.7)	(7.5)	(7.1)
<b>EBITDA</b>	<b>6.5</b>	<b>7.2</b>	<b>7.0</b>	<b>8.1</b>
<i>EBITDA margin %</i>	<i>48.4%</i>	<i>51.9%</i>	<i>48.3%</i>	<i>53.3%</i>
Depreciation	(1.8)	(1.9)	(1.9)	(1.9)
<b>EBIT</b>	<b>4.7</b>	<b>5.3</b>	<b>5.1</b>	<b>6.2</b>
Segment Assets	36.2	34.4	35.1	34.4
Segment Liabilities	(5.3)	(3.9)	(3.7)	(3.7)
<b>Segment Net Assets</b>	<b>30.9</b>	<b>30.5</b>	<b>31.4</b>	<b>30.7</b>
<i>EBIT / average net assets %</i>	<i>15.1%</i>	<i>17.4%</i>	<i>16.5%</i>	<i>20.0%</i>
Capital expenditure	2.0	1.7	1.2	1.2
<i>Capex as % of depreciation</i>	<i>113%</i>	<i>88%</i>	<i>63%</i>	<i>63%</i>

The following points are relevant when reviewing the table above:

- CityLink is forecasting a 5% growth in revenue in FY2018 driven by an increase in TaaS services and greater wifi penetration and BCP;
- CityLink enjoys strong margins as a consequence of ownership of its fibre networks in Auckland and Wellington;
- the replacement costs of the two networks has been estimated by TeamTalk management at approximately \$60 million; and
- TeamTalk reported an improved performance for CityLink in the first half of FY17 with EBIT up by 14.5% on the first half of FY16.

## 6. Overview of the Rural Telecommunications Division (Farmside)

### 6.1 Market Profile

#### Market Overview

TeamTalk's Farmside business provides telecommunications services to the rural sector. Rural households have historically had limited or poor access to broadband internet, and this service has to date been provided wirelessly via satellite, wireless broadband and more recently mobile cellular networks. Access to broadband internet has improved significantly in recent years as the Government's Rural Broadband Initiative has been implemented. Today, Farmside delivers connectivity through satellite, DSL, homeline, digital voice and RBI services.

The RBI was launched in 2011 to improve broadband access for poorly connected premises in primarily rural areas not covered by the UFB and will provide DSL services to 57% of rural households and fixed wireless access to a further 30%. The RBI is mainly being delivered by Vodafone NZ and Chorus. Vodafone NZ is providing fixed wireless broadband to complement fixed line solutions and deliver peak downstream speeds of at least 5Mbps to circa 320,000 rural households.

As at December 2016 the RBI was 94% complete with approximately 301,000 rural households able to connect. Uptake was just under 40% with approximately 120,000 connected users. The historical trend in the number of users able to connect, the number of connected users, and the percentage completion of the programme and uptake percentage between December 2013 and 2016 is outlined below:

#### RBI Statistics – December 2013 to 2016 (000s)<sup>7</sup>

As at December	2013	2014	2015	2016
Users able to connect	179	231	280	301
% complete	56%	72%	87%	94%
Connected users	n.a.	n.a.	103	120
Uptake %	n.a.	n.a.	36.7%	39.7%

Source: Ministry of Business, Innovation of Employment Broadband Deployment Update

Farmside's primary competitors in the rural market are Vodafone, Spark, local wireless internet service providers and satellite provider Wireless Nation.

#### Key Industry Trends

##### ▪ Shift from satellite to rural broadband

As terrestrial communications networks have been expanded and improved there has been a shrinking market for satellite. RBI solutions offer faster speeds at a lower capital cost and as a result there has been a migration of customers from satellite to RBI solutions. This has been especially evident since TeamTalk's acquisition of Farmside. Satellite still has a role to play in DR and BCP planning for enterprise and corporate customers.

##### ▪ Increasing bandwidth demands

Growth in bandwidth demand is being driven by increasing network access and growing demand for content such as movies, games and sport. As volume content increases it is more expensive to deliver via satellite.

### 6.2 Business Profile

TeamTalk acquired Farmside in November 2012. Based in Timaru and Christchurch, Farmside is a niche telecommunications service provider to approximately 15,000 predominantly rural customers throughout New Zealand. Connectivity is primarily provided via RBI and satellite and associated VoIP and homeline voice packages. Farmside also provides ADSL.

Farmside customers are primarily retail although corporate sales contribute 5% of revenue. Just over 60% of Farmside's sales go through four billing partners – Farmlands, Farm Source, PGG Wrightson and Ruralco, which are

<sup>7</sup> Data on the number of connected users was not made available prior to June 2015.

the main rural product suppliers in New Zealand. Farmside is able to leverage the billing partner's relationships and marketing without taking on the credit risk.

Farmside is exposed to the evolution of new technologies and greater competition. Farmside experienced a progressive drop in satellite customers between FY12 and FY16 primarily due to the rollout of RBI by Vodafone but also as a consequence of quality and service issues experienced by customers. To mitigate these issues TeamTalk negotiated an alternative satellite provider, Optus. The change in provider is already resulting in an improved service for customers<sup>8</sup> and higher gross margins for Farmside.

There is demand for satellite services in the corporate market and possibly this should have been the priority sector to address when the decision to transfer the satellite service to Optus was commenced. There is a clear demand from companies and government for both DR/BCP services as well as supplying specialist services to remote luxury lodges, agricultural technology processes and for telemetry.

While Satellite has contracted as a market the last few years have seen strong double growth in Farmside's RBI product. The expansion of RBI and the impact of 4.5G has and will provide Farmside customers with a better choice of solutions. This has led to Farmside being the largest re-seller of Vodafone RBI solutions in New Zealand.

Farmside is being rightsized by the new management team of TeamTalk. By 30 June 2017 costs totalling almost \$2.1 million will be taken out of the business. These cost savings are expected to be fully reflected in the forecast FY18 year. While most of these cost savings will come from a reduction in staffing, other areas such as marketing, distribution and provisioning are also expected to contribute.

At the same time Farmside is embarking on programmes to simplify its billing plans, IT systems and longer customer contracts. Management is also considering which product lines are non-core and should be discontinued. The simplification of the marketing strategy along with cross selling other TeamTalk group products, such as mobile radio, are expected to contribute to further cost reductions and add to revenue.

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<sup>8</sup> As evidenced by Net Promoter Scores.

### 6.3 Financial Profile

The financial performance of Farmside for FY14 to FY16, together with the forecasts for FY17 and FY18 are outlined below:

#### Farmside Summary Financial Performance (NZ\$ millions)

Year end 30 June	2014A	2015A	2016A	2017F	2018F
<b>Total revenue</b>	<b>27.3</b>	<b>24.9</b>	<b>24.5</b>	<b>21.6</b>	<b>20.6</b>
<i>Change in revenue %</i>	<i>n.m.</i>	<i>(8.6%)</i>	<i>(1.7%)</i>	<i>(11.8%)</i>	<i>(4.7%)</i>
Total costs	(23.1)	(23.1)	(23.7)	(21.5)	(18.2)
<b>EBITDA</b>	<b>4.5</b>	<b>2.5</b>	<b>1.4</b>	<b>0.1</b>	<b>2.4</b>
<i>EBITDA margin %</i>	<i>16.3%</i>	<i>9.9%</i>	<i>5.6%</i>	<i>0.5%</i>	<i>11.7%</i>
Depreciation	(3.6)	(2.9)	(4.5)	(2.6)	(2.5)
<b>EBIT before impairments</b>	<b>0.8</b>	<b>(0.4)</b>	<b>(3.1)</b>	<b>(2.5)</b>	<b>(0.1)</b>
Asset impairments	(13.8)	(1.7)	(2.8)	-	-
<b>EBIT after impairments</b>	<b>(12.9)</b>	<b>(2.0)</b>	<b>(6.0)</b>	<b>(2.5)</b>	<b>(0.1)</b>
Segment Assets	19.0	17.0	14.2	14.5	12.9
Segment Liabilities	(3.2)	(2.7)	(4.1)	(4.6)	(4.6)
<b>Segment Net Assets</b>	<b>15.9</b>	<b>14.3</b>	<b>10.1</b>	<b>9.9</b>	<b>8.3</b>
<i>EBIT before impairments / average net assets %</i>	<i>3.8%</i>	<i>(2.6%)</i>	<i>(25.4%)</i>	<i>(25.0%)</i>	<i>(1.1%)</i>
Capital expenditure	2.2	2.0	2.1	4.5	0.9
<i>Capital expenditure as % of depreciation</i>	<i>62%</i>	<i>70%</i>	<i>45%</i>	<i>17.3</i>	<i>36</i>

The following points are relevant when reviewing the table above:

- customer numbers were flat in FY15 but grew by 3% in FY16. TeamTalk is forecasting a slight decrease in revenues for FY18 due to continued churn in the consumer market which is expected to be partially offset by growth in the corporate market;
- the biggest driver of Farmside's decrease in EBITDA over the past few years has been the greater than expected loss of satellite customers and the decline in profitability of the remaining users. The planned migration of satellite customers to the Optus satellite and RBI also resulted in a number of material non-cash charges and write-downs of satellite equipment and intangible assets;
- Farmside has not performed well since its acquisition in December 2012. With the benefit of hindsight the price paid was too high and the debt incurred has been a burden. In addition, the business may not have been managed as well as it could have with what is understood to be a narrow focus on customer numbers at the expense of profitability. The business did however attempt to grow customer numbers in RBI to back-fill the loss of satellite customers;
- the historical satellite services generated low margins. In comparison, the new Optus satellite arrangements provide a better quality service at significantly higher margins;
- over time Farmside expects residential customers to transition from satellite to broadband as it extends its rural coverage, but will focus on replacing these with business customers;
- the current focus is to reduce Farmside's overhead costs, with \$1 million of annual savings having already been achieved since the change in TeamTalk management, with a further \$1 million of annual savings planned to be implemented before the end of the current financial year; and
- the forecast increase in EBITDA in FY18 reflects, in part, the overhead cost reductions and the benefit of the new satellite service from Optus.

## 7. Valuation of TeamTalk

### 7.1 Summary

Grant Samuel's valuation of the equity in TeamTalk is \$43.0 - \$59.8 million, which equates to a share price of \$1.52 to \$2.11 per share. Grant Samuel's valuation is summarised below:

<b>TeamTalk – Valuation Summary</b>		
<b>\$ million except where otherwise stated</b>	<b>Low</b>	<b>High</b>
Enterprise value – TeamTalk Mobile Radio	30.8	38.5
Enterprise value – CityLink	44.6	52.7
Enterprise value – Farmside	9.6	12.0
Corporate costs	(6.3)	(7.7)
<b>Combined enterprise value</b>	<b>78.7</b>	<b>95.5</b>
Net debt for valuation purposes	(33.2)	(33.2)
Capital Expenditure Adjustment	(2.4)	(2.4)
<b>Equity value</b>	<b>43.0</b>	<b>59.8</b>
Fully diluted shares on issue (million)	28.4	28.4
<b>Value per share</b>	<b>\$1.52</b>	<b>\$2.11</b>

The valuation represents the estimated full underlying value of TeamTalk assuming 100% of the company was available to be acquired and includes a premium for control. The value exceeds the price at which, based on current market conditions, Grant Samuel would expect TeamTalk shares to trade on the NZX in the absence of a takeover offer or proposal similar in nature to the Spark Offer. The valuation reflects the strengths and weaknesses of TeamTalk and takes into account the following factors:

- CityLink is an attractive business with established fibre networks in Wellington and Auckland that would be costly to replicate. CityLink has strong and predictable cash flows;
- TeamTalk Mobile Radio has a nationwide network infrastructure that represents a competitive advantage for providing mobile radio solutions to customers that require nationwide communications. TeamTalk has the opportunity to invest in a nationwide DMR network to capitalise on its existing infrastructure, experience and customer relationships; and
- Farmside has performed poorly since its acquisition by TeamTalk driven by a customer shift from satellite to RBI solutions. TeamTalk is now focusing on right-sizing the business by reducing costs and transitioning residential customers from satellite to RBI solutions. Satellite is expected to remain economic for corporate customers and small business customers that cannot be easily reached by other communication methods.

A value range of \$78.7 to \$95.5 million has been attributed to TeamTalk's business operations. This valuation range is an overall judgement having regard to:

- the earnings multiples implied by transactions involving businesses of a comparable nature to each of TeamTalk's business and the multiples implied by the share prices of listed telecommunications businesses in Australasia;
- the attributes and earnings outlook of each of TeamTalk's business divisions; and
- the attractions and risks of each of TeamTalk's business divisions.

#### **Future capital expenditure**

The capital expenditure adjustment is the present value of the difference between depreciation and capital expenditure for the five financial years ending 30 June 2022.

### **Net debt for valuation purposes**

Grant Samuel has adopted net debt for valuation purposes of NZ\$33.2 million. This is TeamTalk's net debt at 28 February 2017.

### **Corporate costs**

For the purposes of valuation \$1.4 million of corporate costs have been capitalised. The costs of being a listed company of approximately \$0.5 million p.a. have been removed from the corporate costs for valuation.

## **7.2 Preferred Methodology**

### **Overview**

Grant Samuel's valuation of TeamTalk has been estimated on the basis of fair market value as a going concern, defined as the estimated price that could be realised in an open market over a reasonable period of time assuming that potential buyers have full information. The valuation of TeamTalk is appropriate for the acquisition of the company as a whole and accordingly incorporates a premium for control. The value is in excess of the level at which, under current market conditions, shares in TeamTalk could be expected to trade on the share market. Shares in a listed company normally trade at a discount of 15% - 25% to the underlying value of the company as a whole, but the extent of the discount (if any) depends on the specific circumstances of each company.

The most reliable evidence as to the value of a business is the price at which the business or a comparable business has been bought and sold in an arm's length transaction. In the absence of direct market evidence of value, estimates of value are made using methodologies that infer value from other available evidence. There are four primary valuation methodologies commonly used for valuing businesses:

- capitalisation of earnings or cash flows;
- discounting of projected cash flows;
- industry rules of thumb; and
- estimation of the aggregate proceeds from an orderly realisation of assets.

Each of these valuation methodologies has application in different circumstances. The primary criterion for determining which methodology is appropriate is the actual practice adopted by purchasers of the type of business involved. A detailed description of each of these methodologies is outlined at Appendix D.

### **Preferred Approach**

Grant Samuel has valued TeamTalk on a sum-of-the-parts basis using the capitalisation of earnings methodology as the primary valuation measure and a discounted cash flow (**DCF**) as a cross check. The DCF valuation used the five year forecast cash flows to 30 June 2022. A discount rate of 13.5% was applied. The resulting valuation was consistent with the valuation range shown in the Section 8.1.



### 7.3 Earnings Multiple Analysis

#### Implied Multiples

Grant Samuel estimates the value of TeamTalk on an un-gearred basis to be in the range of \$78.7 - \$95.5 million. This range implies the following multiples:

#### TeamTalk Group - Implied Multiples

	Amount \$m	Valuation Range	
		Low	High
<b>Enterprise value</b>		<b>78.7</b>	<b>95.5</b>
Multiple of EBITDA – FY16 actual	\$12.6m	6.2	7.6
Multiple of EBITDA – FY17 forecast	\$12.0m	6.6	8.0
Multiple of EBITDA – FY18 forecast	\$16.3m	4.8	5.9
Multiple of EBIT before impairments – FY16 actual	\$3.6m	21.8	26.5
Multiple of EBIT – FY17 forecast	\$5.3m	14.8	18.0
Multiple of EBIT – FY18 forecast	\$9.5m	8.3	10.0

An explanation regarding interpreting the above multiples is included at Appendix E.

### 7.4 Valuation of TeamTalk Mobile Radio

Grant Samuel has valued TeamTalk Mobile Radio on an ungeared basis in the range of NZ\$30.8 to NZ\$38.5 million. This range implies the following multiples:

#### TeamTalk Mobile Radio - Implied Multiples

	Amount \$m <sup>9</sup>	Valuation Range	
		Low	High
<b>Enterprise Value</b>		<b>30.8</b>	<b>38.5</b>
Multiple of EBITDA – FY16 actual	\$5.9m	5.2	6.5
Multiple of EBITDA – FY17 forecast	\$6.8m	4.5	5.7
Multiple of EBITDA – FY18 forecast	\$7.7m	4.0	5.0
Multiple of EBIT – FY16 actual	\$3.3m	9.3	11.7
Multiple of EBIT – FY17 forecast	\$4.6m	6.7	8.4
Multiple of EBIT – FY18 forecast	\$5.3m	5.8	7.3

The valuation of TeamTalk Mobile Radio has been determined using the capitalisation of earnings approach. Grant Samuel's valuation is based on a multiple of 4.0 to 5.0 times forecast FY18 EBITDA.

Grant Samuel has also valued TeamTalk Mobile Radio using the discounted cash flow (DCF) approach as a cross-check to its capitalisation of earnings valuation. TeamTalk Mobile Radio's projections through to the forecast financial year ended 30 June 2022 (FY22) were used as the basis for the DCF valuation. The key assumptions underlying the projections are outlined below:

- TeamTalk Mobile Radio's network is expanded to a complete national DMR network off the current partial digital network footprint. The total capital expenditure to complete the DMR has been forecast at approximately \$8 million;
- following completion of the DMR, TeamTalk Mobile Radio's revenue is forecast to grow from new services provided to existing and new customers. In TeamTalk Mobile Radio's existing markets revenue is forecast to grow at a compound annual growth rate (CAGR) of 4.6%;
- TeamTalk Mobile Radio's gross margins are forecast to increase only modestly from approximately 53% in FY17 to 55% by FY22; and

<sup>9</sup> The amounts shown exclude corporate costs which have been deducted for the purposes of calculating the implied multiples.

- TeamTalk Mobile Radio carries approximately \$1.9 million of corporate overhead costs. For the purposes of the valuation these costs have been added back to TeamTalk and the corporate overhead costs valued separately.

## 7.5 Valuation of CityLink

Grant Samuel has valued CityLink on an ungeared basis in the range of NZ\$44.6 to NZ\$52.7 million. This range implied the following multiples:

### CityLink - Implied Multiples

	Amount	Valuation Range	
	\$m	Low	High
<b>Enterprise value</b>		<b>44.6</b>	<b>52.7</b>
Multiple of EBITDA – FY16 actual	\$7.2m	6.2	7.3
Multiple of EBITDA – FY17 forecast	\$7.0m	6.4	7.5
Multiple of EBITDA – FY18 forecast	\$8.1m	5.5	6.5
Multiple of EBIT – FY16 actual	\$5.3m	8.4	9.9
Multiple of EBIT – FY17 forecast	\$5.1m	8.7	10.3
Multiple of EBIT – FY18 forecast	\$6.2m	7.2	8.5

The valuation of CityLink has been determined using the capitalisation of earnings approach. Grant Samuel's valuation is based on a multiple of 5.5 to 6.5 times forecast FY18 EBITDA.

Grant Samuel has also valued CityLink using a DCF approach as a cross-check to its capitalisation of earnings valuation. CityLink's projections through to FY22 were used as the basis for the DCF valuation. The key assumptions underlying the projections are outlined below:

- City Links revenue is forecast to grow at a CAGR of 3.4% p.a. between FY18-FY22 driven by:
  - new services comprising active management of access and value services at remote locations (Layer 3) and new Wi-Fi networks including enhancements and expansions to existing networks;
  - TaaS. Expanded access to providers and the addition of peering locations as Infrastructure as service locations is expanded;
  - provincial broadband. Providing high speed wireless services for business continuity applications, increased demand for low concentration, reliable high speed services to extend corporate WAN facilities and creating a business grade satellite service for remote locations; and
  - new markets including mobile radio customers.

## 7.6 Valuation of Farmside

Grant Samuel has valued Farmside on an ungeared basis in the range of NZ\$9.6 to NZ\$12.0 million. This range implies the following multiples:

### Farmside - Implied Multiples

	Amount	Valuation Range	
	\$m	Low	High
<b>Enterprise Value</b>		<b>9.6</b>	<b>12.0</b>
Multiple of EBITDA – FY16 actual	\$1.3m	7.4	9.2
Multiple of EBITDA – FY17 forecast	\$0.1m	n.m.	n.m.
Multiple of EBITDA – FY18 forecast	\$2.4m	4.0	5.0

The valuation of Farmside has been determined using the capitalisation of earnings approach. Grant Samuel's valuation is based on a multiple of 4.0 to 5.0 times forecast FY18 EBITDA.

Grant Samuel has also valued Farmside using a DCF approach as a cross-check to its capitalisation of earnings valuation. Farmside's projections through to FY22 were used as the basis for the DCF valuation. The key assumptions underlying the projections are outlined below:

- Farmside's revenue is forecast to grow at a CAGR of 0.5% p.a. through to FY22. The major growth drivers are:
  - RBI full-install customer growth of 5.5% p.a. driven by Vodafone partnering and increased coverage with RBI2. ARPU is forecast to remain flat. RBI up take is currently at just under 40% or 179,000 customers out of an addressable market of approximately 301,000. TeamTalk currently has a 5-6% market share, which it is maintaining;
  - RBI self-install customer numbers growing from 316 as at December 2016 to 4,180 by FY22, driven by more 4G Towers becoming available. The key enabler is the 4G coverage which will be provided by Vodafone. ARPU is forecast to remain flat;
  - residential satellite numbers are forecast to peak at approximately 2,110 and reduce through to circa 1,920 by January 2019. The reduction in customer numbers is forecast to be offset by ARPU increasing from \$139 to \$159 in January 2019 driven by completion of the migration promotion; and
  - corporate satellite is forecast to grow at a CAGR of 11.5%.
- for FY19 TeamTalk is forecasting further churn in the consumer market but larger growth in the corporate market producing a small increase in revenues;
- in FY20 Farmside has forecast a 35% fall in the satellite consumer business with projected gains in the corporate market mitigating some of this; and
- the move away from residential should result in the costs to serve reducing. Further optimisation and rightsizing of overheads will still be required.

## Transactions in the Telecommunications Industry

The valuation of TeamTalk has been considered having regard to the earnings multiples implied by the price at which broadly comparable companies and businesses have changed hands. A selection of relevant transactions is set out below:

### Recent Transaction Evidence

Date	Target	Acquirer	Implied Enterprise Value (millions)	EBITDA Multiple <sup>10</sup> (times)		EBIT Multiple <sup>11</sup> (times)	
				Historical	Forecast	Historical	Forecast
Feb 2017	TeamTalk	Spark	NZ\$56m	4.4	4.7	15.5 <sup>12</sup>	10.1
<b>Satellite</b>							
Nov 2012	Farmside	TeamTalk	NZ\$31m	5.3	-	14.8	-
<b>Mobile Radio</b>							
Sep 2011	ASTRID	Belgian Government	EUR143	8.4	7.5	n.m.	n.m.
Apr 2007	Airwave	Macquarie	£1,932	21.3	n.a.	n.a.	n.a.
<b>Fibre Networks</b>							
Jun 2016	Nextgen Networks	Vocus	A\$700	11.3	10.7	23.3	21.0
Dec 2014	Amcom Communications	Vocus	A\$678	14.5	13.6	19.2	18.8
Jul 2014	Pacnet	Telstra	US\$697	6.3	n.a.	n.a.	n.a.
Jul 2014	FX Networks	Vocus	NZ\$115	8.5	7.4	24.1	17.6
Dec 2013	AAPT	TPG Telecom	A\$450	8.2	6.4	n.a.	15.0
Mar 2013	Telecommunications assets of Leighton Holdings	Ontario Teachers' Pension Plan	A\$824	n.a.	6.4 <sup>13</sup>	n.a.	8.1
<b>Average (fibre networks only)</b>				<b>9.8</b>	<b>8.9</b>	<b>22.2</b>	<b>16.1</b>
<b>Median (fibre networks only)</b>				<b>8.5</b>	<b>7.4</b>	<b>23.3</b>	<b>17.6</b>

Source: Media reports, company announcements, annual reports and presentations.

The following comments are relevant when reviewing the table above:

- TeamTalk acquired Farmside in November 2012 for an upfront purchase price of \$31 million. The purchase price implied multiples of 5.3 times historical EBITDA and 14.8 times historical EBIT. TeamTalk did not provide forecast guidance for Farmside at the time the acquisition was announced;
- there have been a limited number of transactions involving mobile radio network assets where sufficient detail has been available to calculate implied multiples. Two transactions where sufficient detail was available was the Belgian Government's acquisition of a 40% stake in ASTRID, a TETRA network for first responder organisations in that country and Macquarie Communication Infrastructure Group's acquisition of the UK's TETRA network. The implied historical EBITDA multiple for the Airwave transaction of 21.3 times was high due to strong forecast growth in EBITDA as the network build had just been fully completed. The relatively high multiple is likely also attributable to the size and quality of the asset and the long-term contracted nature of Airwave's revenue base;
- there have been a range of transactions involving fibre network businesses, the most recent being Vocus Group Limited's (**Vocus**) acquisition of Australian business Nextgen Networks Group Pty Limited (**Nextgen**). The EBITDA multiples for transactions involving fibre network assets have varied substantially reflecting the strategic nature of many of the acquisitions to the purchasers and the substantial synergies available to the purchasers. In all of the transactions listed above, the target companies are significantly larger than CityLink; and

<sup>10</sup> Represents implied enterprise value divided by EBITDA.

<sup>11</sup> Represents implied enterprise value divided by EBITA.

<sup>12</sup> EBIT before impairments.

<sup>13</sup> Mid-point of estimate.

- descriptions of the transactions included above are provided in Appendix B. Each transaction has its own unique set of circumstances. As such it is often very difficult to identify trends or draw any meaningful conclusions.

### Share Market Evidence

The valuation of TeamTalk has been considered in the context of the share market ratings of listed Australasian companies with operations in the telecommunications industry. While none of these companies is precisely comparable to TeamTalk, the share market data provides some framework within which to assess the valuation of TeamTalk.

#### Share Market Ratings of Selected Listed Companies<sup>14</sup>

Company	Market Capitalisation (millions)	EBITDA Multiple <sup>15</sup> (times)		EBIT Multiple <sup>16</sup> (times)	
		Historic	Forecast	Historic	Forecast
<b>TeamTalk (pre-offer price)</b>	<b>NZ\$12.8</b>	<b>3.6</b>	<b>3.8</b>	<b>12.8</b>	<b>8.7</b>
<b>TeamTalk (Spark offer price)</b>	<b>NZ\$22.7</b>	<b>4.4</b>	<b>4.7</b>	<b>15.5</b>	<b>10.5</b>
<b>Integrated Carriers (Australasia)</b>					
Spark	NZ\$6,451	7.5	7.4	13.7	12.9
Telstra	A\$56,403	6.6	6.7	10.6	11.8
Vocus Group	A\$2,647	n.m.	8.4	n.m.	10.9
TPG Telecom	A\$5,566	8.7	8.1	11.3	11.5
<b>Average (integrated carriers only)</b>		<b>7.6</b>	<b>7.7</b>	<b>11.9</b>	<b>11.8</b>
<b>Wholesale Only Carriers</b>					
Chorus	NZ\$1,689	5.3	5.3	12.9	10.7
<b>Satellite</b>					
Sky Network Television	NZ\$1,467	5.3	6.0	7.6	9.4
<b>Average (all companies)</b>		<b>6.7</b>	<b>7.0</b>	<b>11.2</b>	<b>11.2</b>

Source: Grant Samuel analysis<sup>17</sup>

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

- the multiples are based on closing share prices as at 16 March 2017. The share prices, and therefore the multiples, do not include a premium for control. Shares in a listed company normally trade at a discount to the underlying value of the company as a whole;
- TeamTalk is significantly smaller than other listed telecommunication companies in Australasia. The current trading values of integrated carriers imply multiples in the range of 6.7 to 8.4 times forecast EBITDA and 10.9 to 12.9 times forecast EBIT. The Spark Offer implies multiples of 4.7 times forecast FY17 EBITDA and 10.5 times forecast FY17 EBIT;
- Chorus is the only wholesale-only carrier and is currently trading at multiples of 5.3 times forecast EBITDA and 10.7 times forecast EBIT. Grant Samuel's valuation of CityLink implies multiples of 6.4 - 7.5 times forecast FY17 EBITDA and 8.7- 10.3 times forecast EBIT.
- the companies selected have varying financial year ends. The data presented above is the most recent annual historical result plus the subsequent forecast year; and

<sup>14</sup> The companies selected have a variety of year ends. The financial information presented in the Historic column corresponds to the most recent actual annual result. The forecast column corresponds to the forecast for the subsequent year.

<sup>15</sup> Represents gross capitalisation (that is, the sum of the market capitalisation adjusted for minorities, plus borrowings less cash as at the latest balance date) divided by EBITDA.

<sup>16</sup> Represents gross capitalisation divided by EBIT.

<sup>17</sup> Grant Samuel analysis based on company announcements and, in the absence of company published financial forecasts, brokers' reports. Where company financial forecasts are not available, the median of the financial forecasts prepared by a range of brokers has generally been used to derive relevant forecast value parameters. The source, date and number of broker reports utilised for each company depends on analyst coverage, availability and recent corporate activity.

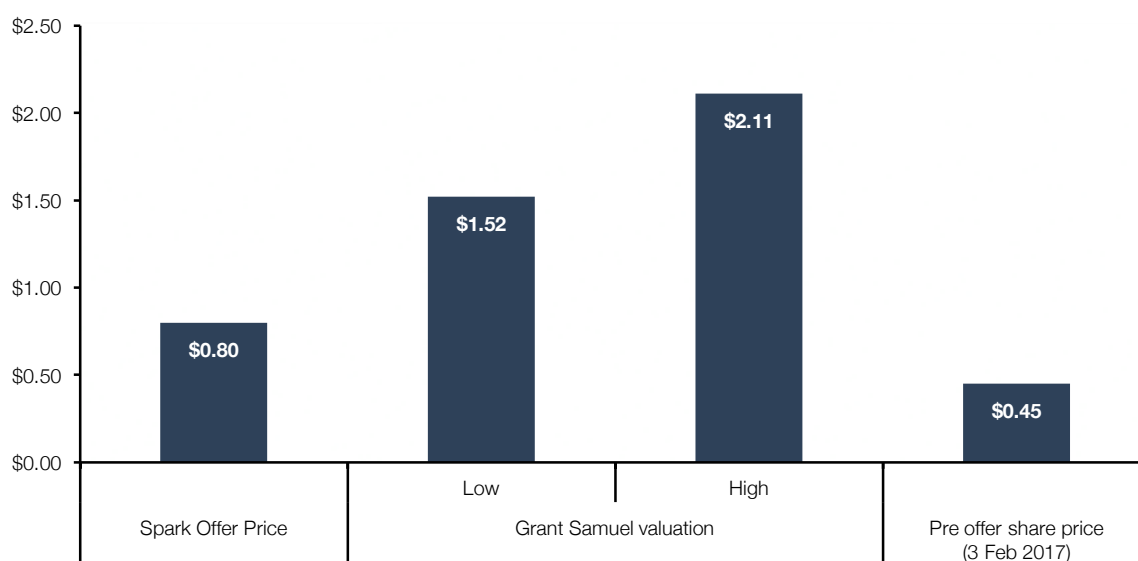
- there are considerable differences between the operations and scale of the comparable companies when compared with TeamTalk. In addition, care needs to be exercised when comparing multiples of New Zealand companies with internationally listed companies. Differences in regulatory environments, share market and broader economic conditions, taxation systems and accounting standards hinder comparisons.

## 8. Merits of the Spark Offer

### 8.1 The Value of the Spark Offer

- **Grant Samuel's assessment of the value of TeamTalk.** In Grant Samuel's opinion, the full underlying value of TeamTalk shares is in the range of \$1.52 to \$2.11 per share as set out in Section 7. The full underlying value is the price a person or entity would be expected to pay to acquire the company as a whole and, accordingly, includes a premium for control. In Grant Samuel's opinion, the offer price under which the offeror will gain control should be within or exceed the pro rated full underlying value range of the company. **As the Spark Offer of \$0.80 per share is below Grant Samuel's assessed value range for TeamTalk shares there is no compelling reason to accept the offer.** The diagram below compares the Spark Offer price with Grant Samuels assessed value range and the Team Talk share price immediately prior to the announcement by Spark of its intention to make a full takeover offer.

**TeamTalk Valuation versus Spark Offer price and pre Offer share price (NZ\$ per share)**



- **the premium implied by the Spark Offer.** The Spark Offer represents a premium of approximately 78% relative to the closing price of \$0.45 per share on 3 February 2017 being the trading day prior to the announcement of the Spark Offer and a premium of 71% over the volume weighted average share price (VWAP) over the 30 trading days prior to the announcement. Over the longer term the Spark Offer represents a 46% premium to the 6-month VWAP and a 46% premium to the 12-month VWAP. The premium for control implied by the offer price is higher than the premiums control implied by successful takeovers for other listed companies. Since the Spark Offer was announced, TeamTalk shares have traded in the range \$0.71 to \$0.80; and
- **comparable company and comparable transaction data.** The Spark Offer implies multiples of 4.4 times historical FY16 EBITDA and 4.7 times forecast FY17 EBITDA. Grant Samuel's analysis suggests the historical and forecast EBITDA multiples implied by the Proposed Transaction are below the multiples paid for controlling shareholdings in comparable companies and substantially less than the multiples implied by the share prices of comparable listed companies, although this should be qualified by the fact that TeamTalk is much smaller than any of the comparable companies selected.

### 8.2 The timing and circumstances surrounding the Offer

- TeamTalk has a relatively short but colourful history. Established initially as a radio telecommunications company, TeamTalk purchased Telecoms NZ's mobile radio business in 2001. The company then made a series of acquisitions culminating in the ill-fated purchase of Farmside in 2012. The acquisition of Farmside Group for an upfront payment of \$19 million in cash and \$12 million in TeamTalk shares (with an additional \$11 million of cash and shares tied to an earn out mechanism) increased the debt of TeamTalk by approximately \$20 million and placed the business under strain. As new technologies emerged Farmside suffered a progressive decline in an ability to attract and retain customers. Limited synergies were foreseen with the Farmside

acquisition and the business ultimately failed to deliver. The earn out was not paid as the minimum earnings performance targets were not met. In the years following the acquisition TeamTalk has incurred a series of write downs in the value of Farmside and its assets. Somewhat surprisingly, during this period of earnings contraction, TeamTalk continued to pay reasonably sizeable dividends. Dividends eventually ceased in 2016. In the same year, TeamTalk Managing Director David Ware resigned, and in a somewhat unique announcement stated that he had stayed on too long;

- TeamTalk at that time was in some disarray – a new management team was required, Farmside in particular was performing poorly, debt was high and provided under a facility that would shortly expire, the business units had limited communication or coordination between themselves and the company was missing earnings projections. These factors were collectively factored into a falling share price, that fell from a high of \$1.75 per share in 2015 to a low of \$0.38 per share in 2016. The Board of TeamTalk, many of whom had been on the journey, had to act;
- by September 2016, the Board had appointed new management including CEO (Andrew Miller) who then appointed his new leadership team including CFO (Jason Bull) and Chief Transformation Officer (John Fischer). In conjunction with the appointment of the new management team the board of TeamTalk commissioned a strategic review by an external advisory firm. The strategic review was in the initial review stages when the first approach was made by Spark to the company in June 2016. At that time, Spark made an indicative and conditional proposal to TeamTalk during 2016 at \$0.60 per share soon after TeamTalk's Managing Director departed. This was rejected by the TeamTalk board as opportunistic;
- the new management team, some of whom have worked together before, have moved efficiently to address the key issues facing TeamTalk. In a relatively short space of time the new management team have worked to provide a clear direction to the business units, which has included putting in place control and review mechanisms. A structured capital expenditure request and analysis format has been initiated, significantly assisting in prioritising requests for capital by the individual business units. Sales initiatives across the group have been coordinated and are now centrally controlled. At a group level, a major cultural change programme has been effected, seeking to involve key people as required and actively moving away from historical practices. In more recent weeks a five year plan has been formulated and the company's bank facilities renegotiated and extended. While a number of these steps could be argued as relatively basic, the new management team was clear that these steps needed to occur before any strategic initiatives with the business units were implemented;
- prior to the announcement of the Spark Offer TeamTalk had a market capitalisation of approximately \$12.8 million and had suffered a marked reduction in value as a consequence of a combination of factors including financial underperformance, management changes and fundamentally falling below or out of the investment market radar. Liquidity in TeamTalk shares was poor with low volumes traded, no analyst produced research on the company and any market commentary on the business was largely negative;
- Spark continued to pursue the company over the following seven months requesting various items to undertake more detailed due diligence investigations of TeamTalk. In January 2017 Spark approached TeamTalk again expressing a desire for further diligence with a view to potentially making an offer for the business of 80 cents per share. This was rejected by the Board on 3 February 2017. The due diligence materials provided to Spark comprised financial reports, a summary of TeamTalk's FY17 budget, the capital expenditure plan, contract information, statistics on CityLink and an organisation chart;
- on 7 February 2017 Spark announced to the market its intention to make a full takeover for TeamTalk. Given the short time the new management team have been in place, the board of TeamTalk described the timing of the Spark Offer as "opportunistic, hostile and woefully low"; and
- there are a number of likely reasons for Spark to be interested in TeamTalk, including:
  - Spark has stated that it wants to reduce its dependence on Chorus. To do this it will need to invest in 'last-mile' network infrastructure. CityLink owns and operates a significant last mile fibre network in Auckland and Wellington CBD's. This network is substantially undervalued in terms of the cost (in time and dollars) to replicate this network infrastructure based on TeamTalk's current share price;
  - as Farmside migrates more customers from its satellite based service to products based on wireless RBI infrastructure it will increasingly become a natural bolt-on for other RBI service providers. Spark could



readily integrate Farmside into its other retail activities and achieve some economies of scale particularly if it uses its own wireless broadband product to substitute for RBI and existing copper in rural areas;

- o mobile radio is a niche segment of the New Zealand telecommunications market. Owning both a cellular network and a radio network would allow a mobile network owner such as Spark the ability to offer large enterprises (e.g. New Zealand Police) a bundle of digital two-way radio and cellular mobile services, which may prove beneficial when tendering for this business. Given the size of the New Zealand market and competition from cellular networks it is unlikely that a new entrant would seek to replicate TeamTalk's network; and
- o based on the forecast earnings for FY18 the Spark offer appears opportunistic. Spark is able to remove costs from TeamTalk in relation to Farmside and Head Office and will achieve substantial benefits from ownership of the Wellington and Auckland fibre networks of CityLink and its ownership of the only nationwide mobile radio network. It would be unreasonable to expect Spark to share all or indeed any of the benefits with the vendors. Equally it is unusual when there are such benefits that the Offer price is substantially below the assessed full underlying value.

### **8.3 Possible Outcomes of the Offer**

#### ***Spark acquires 100% of TeamTalk***

Spark is seeking to acquire 100% of the shares in TeamTalk. The Offer is conditional on receiving sufficient acceptances to take its shareholding in TeamTalk to 90% or more of the shares on issue. If Spark receives acceptances that take its shareholding in TeamTalk to 90% or more the Offer will be unconditional and:

- Spark has stated that it intends to acquire the remaining shares in TeamTalk using the compulsory acquisition provisions of the Takeovers Code. The compulsory acquisition provisions give Spark the right to compulsorily acquire the remaining TeamTalk shares on issue upon the 90% acceptance threshold being reached; and
- TeamTalk will be de-listed from the NZX and become a wholly owned subsidiary of Spark.

#### ***Spark receives acceptances of more than 50% but less than 90% of TeamTalk***

The implications of Spark receiving sufficient acceptances to take its shareholding in TeamTalk to more than 50% but less than 90% by the date on which the Offer closes (as extended) are as follows:

- if Spark chooses not to waive its 90% minimum acceptance condition, Spark will not acquire any shares in TeamTalk and TeamTalk will remain a public company listed on the NZX;
- Spark has reserved the right to waive its 90% minimum acceptance condition and accept a lower percentage shareholding in TeamTalk, provided that percentage exceeds 50% as required by the Takeovers Code for all full takeover offers. If Spark chooses to waive its 90% minimum acceptance condition and declares the Offer unconditional then:
  - Spark must acquire all TeamTalk shares accepted into the Offer;
  - TeamTalk will continue to be listed on the NZX with Spark as a cornerstone majority shareholder with a shareholding of more than 50% but less than 90%;
  - Spark will have effective control over the day-to-day operations of TeamTalk. Remaining minority shareholders will have limited influence over the day-to-day operations of TeamTalk;
  - Spark will be entitled to appoint new directors to the board of TeamTalk;
  - by virtue of its majority shareholding Spark would control the outcome of any ordinary resolution put to shareholders;
  - once Spark has control of TeamTalk it can determine such matters as dividend policy, capital expenditure and funding mix. These may have an impact on the earnings of the business. At a shareholding of more than 50% but less than 90% Spark may prevent a dividend being paid preferring profits to be re-invested in expanding the business;
  - if Spark acquires a shareholding of 75% or more it will be able to control the outcome of special resolutions such as those required to change the constitution or approve a major transaction;

- it is possible that shares in TeamTalk will trade below the Offer price of \$0.80 per share. Even in the absence of a substantial shareholding being acquired by Spark, TeamTalk shares are relatively thinly traded. This may suppress the TeamTalk share price. The closer the Spark shareholding gets to 90% the lower the liquidity of TeamTalk shares will be. The forecast financial information included in the Target Company Statement (including this report) is likely to result in a better understanding by the market of TeamTalk, and potentially a re-rating of TeamTalk;
- if the Offer is declared unconditional at a shareholding of more than 50% but less than 90%, Spark cannot acquire any further shares in TeamTalk for a period of twelve months without making another formal takeover offer for all or some of the remaining shares in the company, or without shareholder approval. However, from twelve months after the Offer closes, Spark will be able to utilise the “creep” provisions of the Takeovers Code to purchase up to a further 5% of TeamTalk per annum.
- the Takeovers Code permits Spark to extend its Offer close date under certain conditions. If Spark chooses to waive the 90% minimum acceptance condition the Offer close date can be extended for a further 60 days to 21 June 2017 to allow further time for Spark to try and reach its 90% target. This has the effect of Spark being able to delay the close of its Offer for a period of up to 5 months, during which time no other takeover offers are likely to be forthcoming. The extension date of 21 June 2017 assumes that Spark would not have extended the offer to the full 90-day period allowable before waiving its minimum acceptance condition and that Spark declares the offer unconditional as at the level of acceptances on 22 April 2017.
- TeamTalk shareholders who choose not to accept the Offer have either decided they want to retain their investment in TeamTalk for the longer term, or are expecting that Spark will make another offer at a higher price. There is no certainty regarding the ongoing performance of TeamTalk or that a subsequent offer from Spark will be forthcoming if it does not acquire 100% of TeamTalk. The risks and benefits associated with an investment in TeamTalk are outlined at Section 8.6 below.

Spark has not provided any indication, and nor does it have to, as to whether or not it is likely to waive its 90% minimum acceptance threshold. If the minimum acceptance condition is waived in the last seven days of the Offer period, the offer period will automatically extend for a further 14 days.

#### ***Spark does not receive acceptances of more than 50% of TeamTalk***

If Spark receives acceptances of less than 50% of the shares in TeamTalk the Offer will lapse and no shares will be acquired by Spark.

#### **8.4 Factors that may affect the outcome of the Offer**

- Approximately 24% of the issued shares in TeamTalk are owned by the top 20 shareholders or custodians. The support or otherwise of the larger shareholders in relation to the Spark Offer will be material in determining whether or not Spark achieves the 90% acceptance threshold (or, if waived, the lower threshold of more than 50%);
- since the announcement of the Offer, TeamTalk shares have traded in a range of NZ\$0.71 to NZ\$0.80;
- in some takeovers there are factors that suggest that even if an offer is below the assessed value range shareholders should consider accepting the offer. In this instance there does not appear to be any compelling reason for shareholders to accept a takeover offer that is below the full underlying value range;
- there are only two permissible variations to the Offer:
  - Spark may choose to extend its Offer period. The Offer is due to close on 22 April 2017. Under the rules of the Takeovers Code the latest date to which the Offer may be extended is 90 days after the date on which the Offer opens, in this case 9 March 2017. However, if the offer is declared unconditional at any level above 50% acceptances, the Offer is able to be extended for a further 60 days from the date the Offer becomes unconditional as to the level of acceptances under rule 24B of the Takeovers Code;
  - Spark may choose to increase its Offer price. If Spark chooses to increase its Offer price while its current Offer is still open the increased price will be available to all TeamTalk shareholders even if they have already accepted the Offer at the lower price. However, if Spark later makes a further takeover offer at a higher

price after the current Offer has closed, the higher price would not be available to shareholders that accepted the current Offer;

- in Grant Samuel's opinion it is possible that, depending on the reaction of TeamTalk shareholders to the current Offer price, Spark may consider increasing its Offer price in order to secure a shareholding of more than 90% of the TeamTalk shares on issue. However, this is by no means certain;
- there is no need for shareholders to accept the Offer early. The closing date for the Offer is 22 April 2017. This date can be extended by Spark by giving no less than 14 days' notice of such an extension. Not accepting the Offer or holding out until near the time the Offer closes may cause the Offer price to be increased. However, there is no certainty that the Offer price will be increased;
- TeamTalk shareholders who choose not to accept the Offer have either decided they want to retain their investment in TeamTalk for the longer term, or are expecting that Spark will make another offer at a higher price. There is no certainty regarding the ongoing performance of TeamTalk or that a subsequent offer from Spark will be forthcoming if it is not successful in acquiring 90% of TeamTalk or declaring its offer unconditional at any lower level of acceptances. The risks and benefits associated with an investment in TeamTalk are outlined at Section 7.6 below; and
- TeamTalk has received approaches for some of its business units from credible parties in 2017. As at the date of this report these approaches were either unsatisfactory or inconclusive.

### 8.5 Likelihood of alternative offers

- the takeover offer was made by Spark on 9 March 2017. To date, no alternative takeover offers have been forthcoming. No other party has made a bid for TeamTalk. There is nothing to prevent another bid at a higher price being made;
- the use of "lock up agreements" is very common in the context of takeover Offers for Code companies. Lock up agreements that are put in place between the offeror and shareholders in the target company ensure that those shareholders will accept the offer when it is made in respect of the number of shares locked up. This mechanism allows offerors to launch takeover offers with a degree of pre-acceptances, which can assist in influencing the outcome of the offer and its likelihood of success. Recent successful takeover offers include Bapcor's Offer for Hellaby Holdings – 29.8% locked up and the RIFA offer for Airwork – 58.9% locked up. Whether Spark could not entice any TeamTalk shareholders to enter into lock up agreements or whether it elected not to employ that mechanism is not known. However, no shares in TeamTalk are subject to lock up agreements meaning alternative potential purchases are not currently disadvantaged by the existence of the Spark Offer;
- if Spark declares its Offer unconditional at a shareholding of more than 50% but less than 90%, the likelihood of a takeover offer from another party is substantially reduced. If at the conclusion of the Spark takeover offer Spark owns a controlling shareholding in TeamTalk, the chances of any other competing partial takeover offers are slim. Any alternative partial offer for over 20% of TeamTalk (should one be forthcoming) would require the approval of TeamTalk shareholders, which would therefore require the support of Spark. Any subsequent takeover offer for 100% of TeamTalk would require Spark to sell its shareholding in TeamTalk to the new offeror for an alternative full takeover offer to be successful; and
- there will be a time period between when the Offer is made and the dispatch of the Target Company Statement. TeamTalk has advised shareholders to not take any action until with they receive the Target Company Statement which is normal practice in similar circumstances. Spark has indicated that the Offer will close on 22 April 2017 although it can extend the period. There is no need for TeamTalk shareholders to accept the Offer immediately when it is received. Shareholders who do accept the Offer cannot withdraw it. They will receive any higher price subsequently offered by Spark under the current Offer.

### 8.6 An investment in TeamTalk

TeamTalk is a business in transition. The period following the purchase of Farmside was disruptive, culminating in a change in leadership and a reset of the business strategy, culture and way the business units cooperate. A key issue for shareholders is whether they have confidence in the new leadership and the new strategic direction of the

company. This is a difficult question to answer, given the very short time between appointment of the new management team at the end of 2016 and the announcement of the Spark Offer. Grant Samuel notes:

- on 28 February 2017, TeamTalk announced that it had agreed the essential terms of a new bank facility through until 31 March 2020 that would replace the existing facility which expires at the end of August 2017. The bank facilities include amortisation payments and a general reduction in exposure over time. Grant Samuel would expect that the new bank facility would be subject to a range of covenants that would require the business to continue to perform for the bank facility (current or new) to be continue to be provided. The five-year business plan projects debt to be approximately \$22 million by 2018;
- Grant Samuel has reviewed the forecast included in the five-year business plan. The forecasts appear achievable and are based on conservative assumptions as set out in sections 4.3, 5.3 and 6.3 of this report. As with any forecasts, the deliverability of the results is subject to a range of factors including market forces over the forecast period;
- Grant Samuel is satisfied that management have completed a number of straight forward but necessary changes to the way the TeamTalk business has been operated. These include improved capital expenditure discipline, improved communication, cooperation between the operating businesses, tighter and timely financial reporting, right sizing parts of the business. Collectively, these changes have assisted in creating a more collaborative culture; and
- the five-year business plan has been completed which includes strategic direction for each operating business as well as the Head Office.

Delivery of the business plan will present a number of challenges and opportunities. TeamTalk faces a number of business challenges including:

- migration to RBI and upgraded satellite services. RBI has created competition for TeamTalk's Farmside satellite broadband product. RBI solutions offer faster speeds and have a lower capital cost and as such TeamTalk has been forced to migrate customers to RBI solutions;
- migration off the trolley bus infrastructure for parts of its Wellington fibre network. City Link will need to migrate parts of its Wellington fibre networks off the city's trolley bus infrastructure by no later than 2021;
- the projected growth in the land mobile radio market may or may not eventuate or may eventuate at a lower rate;
- the market for satellite delivered communications has contracted as terrestrial communications networks have expanded and improved. While this trend is expected to continue it is not expected to be extinguished altogether. In the meantime, Farmside has morphed to become a significant reseller of RBI solutions in New Zealand.

### **8.7 Acceptance or Rejection of the Spark Offer**

Acceptance or rejection of the Spark Offer is a matter for individual shareholders based on their own view as to value and future market conditions, risk profile, liquidity preference, portfolio strategy, tax position and other factors. In particular, taxation consequences will vary widely across shareholders. Shareholders will need to consider these consequences and, if appropriate, consult their own professional adviser(s).

**GRANT SAMUEL & ASSOCIATES LIMITED**

**20 March 2017**

*Grant Samuel + Associates*

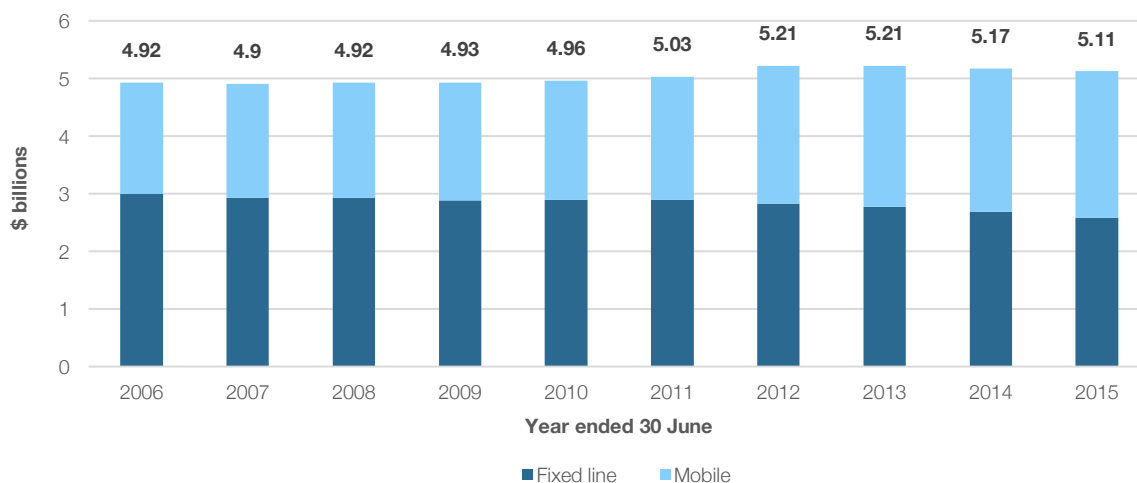
## New Zealand Telecommunications Industry

The New Zealand telecommunications industry has evolved significantly since the mid 1980s when New Zealand Post owned and ran the telecommunications system in New Zealand in a state protected monopoly. Telecom Corporation of New Zealand Limited (**Telecom NZ**) was formed as one of three new state-owned enterprises following the restructure of New Zealand Post in 1987 and was privatised in 1990. Telecom NZ was listed on the NZX, ASX and New York Stock Exchange in 1991.

The Telecommunications Act 1987 was put in place at the time of the creation of Telecom NZ and set out restrictions on the number, activities and foreign ownership of participants in the telecommunications market. Since 1987, the telecommunications market has been progressively deregulated and a number of new participants have entered the market. New entrants initially competed for traditional international and national toll revenues and more recently for internet-related and mobile services. The sector has been dramatically transformed in terms of the range of services offered and the technologies used to deliver these services, with consequent effects on the overall market structure. Rapid change continues today as users consume increasing amounts of video, data and other content through smartphones and tablets, and internet connectivity of devices such as home appliances and vehicles becomes increasingly widespread.

While substantially more network bandwidth is required to meet the ever increasing demand for data, revenue growth for the telecommunication sector is in overall decline, presenting challenges for providers. Revenue from telecommunications in New Zealand grew very slowly between 2006 and 2011. Following a year of strong revenue growth in 2012 reflecting increased growth in mobile and data, revenue has fallen marginally each year since. The decline in total revenue has been led by falling revenue from fixed line voice and business data (primarily the result of aggressive price based competition) partially offset by increasing revenue in mobile, broadband and internet services, as summarised in the chart below:

**New Zealand Telecommunications Industry Revenue (2006 to 2015)**



Source: Commerce Commission, Annual Telecommunications Monitoring Report 2015

In 2009 the New Zealand Government announced plans for the Ultra Fast Broadband (**UFB**) fibre network and the Rural Broadband Initiative (**RBI**). The initiatives are designed to deliver a fibre to the home network in most residential centres in New Zealand and high speed broadband using other technologies to rural locations. These initiatives led directly to the restructuring of Telecom NZ, which was separated in 2011 into two separate listed companies:

- **Chorus Limited (Chorus)**, a wholesale network provider that owns copper and fibre network assets, access electronics, telephone exchange buildings and transport radio towers; and

- **Spark New Zealand Limited (Spark)**, a telecommunications retailer that owns mobile network assets, the public switched telephone network (PSTN),<sup>18</sup> telecommunications network equipment, international submarine cables and spectrum associated with the supply of mobile services.

More detail on the UFB and the RBI is set out in Section 3.8.

## Market Segments and Products

The telecommunications market is typically segmented by customer type, as the products demanded and customer behaviour differ markedly between households, small businesses and large corporates. There is some commonality but also important differences in the infrastructure used to service these customer segments.

Telecommunications services are a key delivery channel for and, are commonly bundled with, media and entertainment products in the consumer segment and they are closely linked with information technology (IT) services in the corporate and enterprise sectors. As the telecommunications sector has evolved, these linkages have become deeper and more important and the distinction between telecommunications services and other sectors has become blurred in some areas. Generally, the telecommunications sector can be viewed as providing the infrastructure used by consumers and businesses to access data/content or enable upstream IT services, and can be summarised as follows:

### Telecommunications and Adjacent Sectors – Market Segments and Products

Segment	Key Products	
	Telecommunications Sector	Adjacent Sectors
<b>Consumer (Household)</b>	<ul style="list-style-type: none"> <li>▪ Broadband internet</li> <li>▪ Home phone</li> <li>▪ Mobile devices</li> </ul>	<ul style="list-style-type: none"> <li>▪ Pay television</li> <li>▪ Video and music streaming</li> <li>▪ Remote storage and back-up</li> </ul>
<b>Small to Medium Business</b>	<ul style="list-style-type: none"> <li>▪ Broadband internet</li> <li>▪ Phone services (PABX<sup>19</sup> and VoIP<sup>20</sup>)</li> <li>▪ Mobile devices</li> <li>▪ High speed data connections (Ethernet and IP-VPN<sup>21</sup>)</li> </ul>	<ul style="list-style-type: none"> <li>▪ Web hosting</li> <li>▪ Ecommerce services</li> <li>▪ IT services (e.g. storage, disaster recovery, cloud services<sup>22</sup>)</li> </ul>
<b>Corporate, Enterprise and Government</b>	<ul style="list-style-type: none"> <li>▪ High speed data connections (dark fibre<sup>23</sup>, Ethernet and IP-VPN)</li> <li>▪ Internet connection</li> <li>▪ Phone services (PABX and VoIP)</li> <li>▪ Mobile devices</li> <li>▪ Data centre space</li> </ul>	<ul style="list-style-type: none"> <li>▪ Outsourced IT and hosted services</li> <li>▪ IT consulting and integration services</li> <li>▪ Ecommerce services</li> <li>▪ Content delivery services</li> <li>▪ Internet security services</li> <li>▪ Mobile device management &amp; security</li> </ul>
<b>Wholesale</b>	<ul style="list-style-type: none"> <li>▪ Local access infrastructure (copper lines and DSL<sup>24</sup>)</li> <li>▪ High speed data connections (dark fibre, Ethernet)</li> <li>▪ Internet connection</li> <li>▪ Services to MVNOs<sup>25</sup></li> </ul>	

<sup>18</sup> PSTN (public switched telephone network) is the traditional telephone system.

<sup>19</sup> PABX is a traditional product that provides a phone system with multiple internal and/or external lines for a business.

<sup>20</sup> VoIP (voice over internet protocol) is a technology for delivering single or multi-line phone services to businesses and households more effectively over modern high speed data links.

<sup>21</sup> Ethernet and IP-VPN are types of private high speed data links commonly provided by carriers to medium and large businesses.

<sup>22</sup> A cloud service is an application, data processing or storage service operated remotely by a third party, allowing the customer to use a complex application with minimal hardware onsite, using a high speed data connection to the cloud service provider (e.g. accounting systems, inventory and stock management systems, customer relationship management systems).

<sup>23</sup> Dark fibre is a service provided by carriers to large businesses for high speed, private data links where the business is able to connect its own equipment directly to the carrier's optical fibre cable.

<sup>24</sup> DSL (digital subscriber line) refers to a family of technologies used to provide a broadband connection over a traditional copper phone line.

<sup>25</sup> MVNO (mobile virtual network operator) refers to a carrier that buys wholesale access to a mobile network.

Source: Grant Samuel

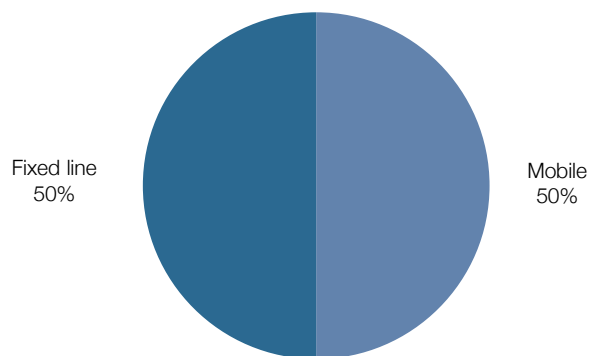
## Market Structure

Aggregate revenue for the New Zealand retail market is estimated at approximately \$5 billion per annum. The major participants are:

- the two large integrated carriers - Spark and Vodafone NZ;
- Chorus and three other local fibre companies (**LFCs**) providing wholesale only local access; and
- a number of mid-size carriers, including Two Degrees Mobile Limited (**2degrees**) (mobile and fixed line broadband), TrustPower (consumer and business segments), Vocus Communications Limited (**Vocus**) (intercity fibre and data centres and a consumer and small business reseller), Compass (consumer and business segments), TeamTalk (consumer and business segments) and Kordia (business segment). Of these businesses, 2degrees is the largest, with approximately 1.4 million mobile customers and estimated annual revenue of approximately \$570 million in the year to 31 December 2015<sup>26</sup>.

The market is split approximately 50/50 between mobile and fixed line services:

### New Zealand Telecommunications Industry Revenue by Product (FY2015)



Source: Commerce Commission, Annual Telecommunications Monitoring Report 2015

Following a proliferation of telecommunications service providers in the 1990s and early 2000s, mergers and acquisitions in the last ten years have significantly reduced the number of market participants. This consolidation is evident in the number of small to mid-tier carriers in New Zealand that have been acquired by competitors, including:

- telecommunications companies TelstraClear Limited (**TelstraClear**), Snap, Orcon, WorldxChange Communications Limited (**WorldxChange**), Woosh and Farmside; and
- fibre network and data centre companies FX Networks, Revera Limited (**Revera**), Computer Concepts (**CCL Group**), ICONZ and Maxnet.

Acquisition of smaller competitors has enabled the major carriers in New Zealand to achieve cost efficiencies through increased scale and national reach.

## The Mobile Market

The major participants in New Zealand's mobile market are Spark, Vodafone NZ, and 2degrees, which entered the market in 2009. Spark responded to the launch of 2degrees with the introduction of its own secondary brand, *Skinny*, to compete primarily in the prepaid market. However, Vodafone NZ remains the market leader with around 40% of connections while Spark (including *Skinny*) has around 36% of connections<sup>27</sup>. 2degrees has progressively captured market share and now accounts for approximately 24% of mobile connections, but a much lower share of

<sup>26</sup> Source: 2degrees Annual Report.

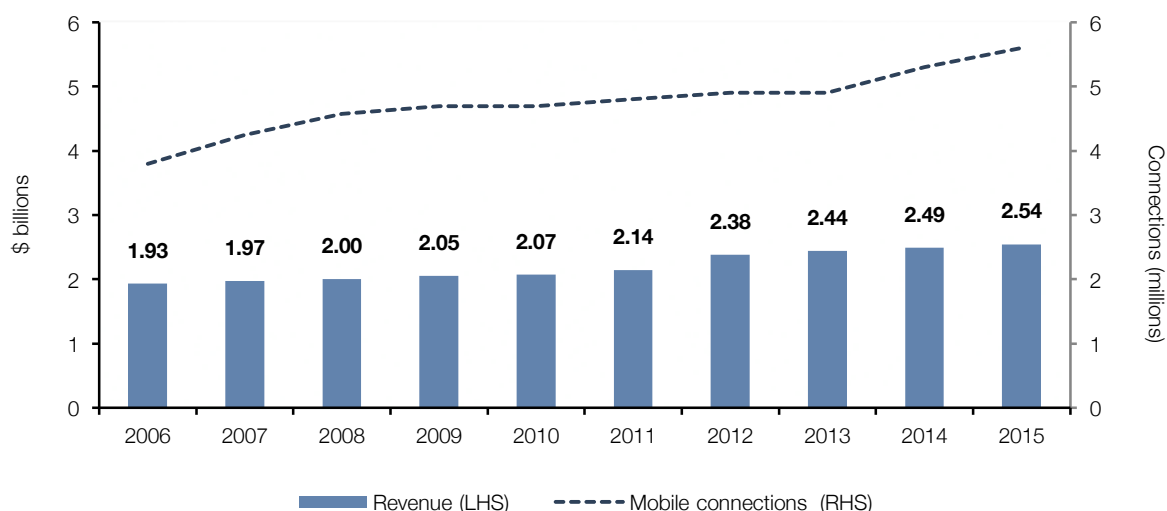
<sup>27</sup> Source: Commerce Commission, Annual Telecommunications Monitoring Report 2015

revenue. The relatively low share of market revenue for 2degrees reflects the large proportion of its revenue that it generates from the typically lower value consumer prepaid market.

Mobile virtual network operators (**MVNO**) represent a small proportion of the market in New Zealand, with only approximately 20,000-25,000 customers.

Since 2006, mobile revenues have continued to grow, primarily due to the continued increase in the number of connections. Recent data published by Vodafone NZ and Spark indicates that mobile revenues are coming under pressure due to the higher level of competition and consequent reduction in average revenue per user (**ARPU**).

#### New Zealand Telecommunications Sector – Mobile Radio and Connections (FY06 to FY15)



Source: Commerce Commission Annual Telecommunications Monitoring Report 2015

While the trend of fixed to mobile substitution (i.e. the abandoning by households of fixed phone and internet services for mobile services) is still evident, the physical constraints on mobile bandwidth (finite spectrum, cost of base stations, topography and buildings that block signals) mean that fixed broadband services are expected to continue to play a major role in delivering high speed data to households.

#### The Fixed Line Market

The fixed line market in New Zealand is more fragmented than the mobile market as small retailers are able to compete with larger incumbents by selling regulated services provided by wholesale providers. Spark is the dominant provider of fixed line services, with estimated retail market shares of 48%<sup>28</sup> measured by connections and 56%<sup>28</sup> measured by revenue. Vodafone NZ has around a 29%<sup>28</sup> share of connections with the balance split between Vocus, Trustpower and others.

The industry consolidation that has occurred over the past two years has primarily been in the fixed line market. Acquisitions of note include:

- the acquisition of Snap by 2degrees, creating another participant in the market able to deliver “triple play”<sup>29</sup> offerings with the support of its own mobile network. Market evidence suggests that providing an increased number of services on a “bundled” basis both increases ARPU and improves customer retention rates (the net of customers gained and lost is usually referred to as customer “churn”); and
- the acquisition of Orcon by M2 Group Ltd (**M2 Group**), now part of Vocus, which has positioned Vocus as the clear third player in the fixed line market.

<sup>28</sup> Source: Commerce Commission, Annual Telecommunications Monitoring Report 2015 (using ISP market share as a proxy for fixed line share).

<sup>29</sup> The sale of fixed voice, broadband and mobile in a bundle.



Increased competition has contributed to a progressive decline in fixed line revenue since 2010. This has reflected both lower overall market prices (primarily as a consequence of the proliferation of value bundles) and the replacement of traditional voice services by mobile services and messaging applications online (e.g. Skype).

Fixed line revenue has been supported by continued growth from broadband connections, primarily a result of the growth in fibre from the take up of the UFB, as can be seen on the chart below. The most recent quarterly report for the period January – March 2016 shows UFB connections grew by 131% over the previous 12 month period to 196,609 connections.<sup>30</sup>

## Infrastructure

Telecommunications infrastructure can be categorised as follows:

### Local Access Infrastructure (Fixed and Mobile)

Commonly known as the “last mile”, local access infrastructure is the immediate connection between the user’s device or premises and the carrier’s network. For households this can be:

- a twisted pair copper phone line to the local exchange or street cabinet, which can carry PSTN (traditional phone) and DSL (broadband internet) services. The copper network in New Zealand is owned by Chorus;
- a hybrid fibre-coaxial (**HFC**) cable to the nearest optical node, which can carry pay television, broadband internet and phone services. Vodafone NZ operates an HFC network in parts of New Zealand (Wellington, Kapiti Coast and Christchurch) that it inherited as part of the acquisition of TelstraClear; and
- a passive optical fibre to the nearest fibre access node to fibre networks, which can carry pay television, broadband internet and phone services. The fibre networks are primarily owned by Chorus and other LFCs under the UFB initiative.

For mobile services, the local access infrastructure comprises the antennas, radio spectrum licences and associated equipment at the carrier’s network of base stations. For businesses, local access infrastructure can be an optical fibre to the carrier’s nearest node or a legacy copper phone line to a local exchange. Businesses also have access to the UFB local access infrastructure.

### Core Network

A carrier’s core network comprises high capacity optical fibre cables connecting each element of the network to switches that route data around the network. Core networks can be categorised as:

- metropolitan networks – connections between business districts, local exchanges, data centres, mobile base stations and other network equipment within capital cities. The major metropolitan providers are Chorus and the LFCs that are building the UFB network; and
- long haul and inter-capital networks – connections between capital cities and regional cities. The major long haul and inter-capital fibre networks are owned by Chorus, Spark, Vodafone NZ and Vocus.

To provide customers with a connection to the internet, a carrier must connect its network both to other local carriers and also to global carriers offshore (typically known as **IP transit**). For New Zealand, this is done via a submarine optical fibre cable. The submarine cables connecting New Zealand to offshore locations form a critical element of telecommunications infrastructure. The submarine cables include:

- **Southern Cross Cable**, connecting Sydney, Auckland, Fiji and the United States (Hawaii, California and Oregon). The Southern Cross Cable is owned by Spark (50.01%), Singapore Telecommunications Group Limited (**SingTel**) (39.99%) and Verizon Communications Inc. (**Verizon**) (10%);
- **Tasman 2**, connecting Sydney and Auckland. Tasman 2 is owned by Telstra Corporation Limited (**Telstra**) (36.84%), Spark (32.87%) SingTel (through Optus) (11.91%), Vodafone NZ (10.0%) and AT&T Inc. (**AT&T**) (8.33%). This cable is low capacity and is primarily used for redundancy services (i.e. back up in the event of failure).

<sup>30</sup> Source: MBIE Broadband Deployment Update – March 2016.

The Tasman Global Access (**TGA**) cable connecting New Zealand and Australia is expected to be completed at the end of 2016. The TGA cable is owned by Spark, Vodafone NZ and Telstra.

While access to bandwidth on international cables remains a crucial asset for all New Zealand carriers, content providers such as Google (including YouTube), Netflix and Apple have deployed data storage locally to reduce lag times and international transit costs.

### Data Centres

Data centres allow corporate, enterprise and wholesale customers to locate network and storage equipment directly on a carrier's network, providing a secure environment, improved network performance and the ability to directly connect with other customers' equipment located at the same data centre. The limiting factors for a data centre's capacity are typically physical space, the amount of electrical power that can be delivered to the centre and the air-conditioning capacity of the centre.

A large number of local and international carriers and data centre specialists operate data centres in New Zealand including Spark, Vocus, Vodafone NZ, IBM, Hewlett Packard, Datacom and Plan B.

### Wholesale Access to Infrastructure

Most telecommunications carriers do not own all of the infrastructure required to deliver services to their customers. There is a well-developed wholesale market for access to most (but not all) of the telecommunications infrastructure in New Zealand, comprising regulated access and commercially negotiated arrangements:

- **Regulated Access:** Access to certain infrastructure elements is available at fixed maximum prices determined by the Commerce Commission, typically where the owner has a monopoly on that form of infrastructure. Regulated infrastructure includes the copper access network and duct space and fibre in certain locations. Chorus is the primary operator of regulated infrastructure and is subject to Commerce Commission regulation. It is also the single largest UFB network operator; and
- **Commercially Negotiated Access:** Wholesale access to infrastructure is available for mobile networks, metropolitan and inter-capital fibre, international transit and satellite services. Wholesale access to fibre, international transit and satellite services is often sold as an indefeasible right of use (**IRU**) which gives the buyer the right to use a maximum amount of bandwidth for a long term duration (typically 5-15 years). Wholesale access to mobile networks is more commonly charged on an ongoing basis depending on the bandwidth utilised or number of services in use.

Business models employed by telecommunications carriers vary from owning a portion of the infrastructure (e.g. Spark and Vodafone NZ) to owning minimal infrastructure and relying heavily on wholesale arrangements (i.e. a reseller).

The most contentious area of regulated pricing in recent years has been the wholesale price of consumer copper broadband products (e.g. DSL) and fibre input costs. These prices have now been fixed with a price path set to 2019. The wholesale copper prices are higher than entry level fibre costs which is intended to assist with the general migration of the market to the UFB network. There is no certainty regarding the pricing framework that will apply to fibre based products after 31 December 2019. The prices are likely to be regulated, but if that does not occur, the prices for fibre will be set by Chorus and the other LFCs.

The UFB network is to be unbundled in December 2019, which will allow retailers to invest in their own equipment and source layer 1 service from Chorus on a wholesale basis, and allow the other LFCs to deliver fibre services to the home. Chorus has made submissions to revisit the regulations. The Government is undertaking a review of telecommunications regulation to address the pricing and unbundling uncertainty associated with the UFB. The review is to be completed by 31 March 2019.

### UFB and RBI

The New Zealand Government has implemented policies and invested capital to provide improved broadband access for households and business through the UFB initiative and the RBI:

- **Ultra-Fast Broadband:** The UFB initiative was launched by the New Zealand government as a public-private-partnership tender in 2009 with the objective of connecting 75% of homes to a fibre to the premises network by 2019. In 2014, the target was increased to 80% of homes and the completion date extended to 2022. The UFB is an equal-access wholesale only network. While end users can elect to retain or reconnect their old copper connection, it is expected that over time the UFB network will become the primary local access network. The Government selected four partners to deliver the UFB network: Chorus (approximately 70% of premises), Enable Networks (15%), Ultrafast Fibre (14%) and Northpower Fibre (1.6%); and
- **The Rural Broadband Initiative:** The RBI was launched in 2011 to improve broadband access for premises in rural areas not covered by the UFB. The RBI will provide DSL services to 57% of rural households and fixed wireless access to a further 30% of rural households. The RBI is being delivered by Vodafone NZ and Chorus. Vodafone NZ is providing fixed wireless broadband to complement fixed line solutions and deliver peak downstream speeds of at least 5Mbps to circa 320,000 rural households.

As at 31 March 2016, there were 921,000 end users able to connect to the UFB network, with 63% of the UFB roll out complete, together with 285,000 premises able to connect to RBI services (89% complete).

### Market Trends and Outlook

Technology, products and customer preferences in the telecommunications sector continue to evolve rapidly, affecting the market structure and both influencing, and being influenced by, regulatory response. Overall, change in the sector reflects a rapid move to a more interconnected society characterised by pervasive technology and the universal availability of high speed data. The key trends features of the outlook included:

#### **Declining Revenue**

Revenue growth for the sector has been in overall decline in recent years due to a number of factors including:

- revenues from traditional services such as fixed voice revenues via PSTN continue to decline due to mobile substitution, pricing bundles and the use of online messenger applications (e.g. Skype, Facebook Messenger);
- the mobile market is widely believed to have reached or to be approaching maturity, characterised by high levels of penetration. While the number of connected devices continues to rise (e.g. entertainment devices, vehicles, machine-to-machine communications), these services typically add only a small amount of incremental revenue to an existing customer's account;
- the fixed broadband market is considered to be close to maturity; and
- cost reductions achieved by carriers have resulted in lower prices in a competitive environment. Cost reductions have been driven by:
  - lower prices for network equipment;
  - consolidation of carriers enabling efficiencies of scale; and
  - regulatory decisions that have reduced wholesale access prices for copper networks and mobile call termination.

Slowing market growth presents a challenge for carriers. Organic growth must come by taking market share from competitors or formulating new product bundles rather than implementing price rises or securing new customers. In this context, customer retention (i.e. reducing churn) is a key driver of future profitability.

#### **Increase in Data Volumes**

The volume of data downloaded by internet users has grown at dramatic rates since broadband connections became available in the early 2000s. Data demand has intensified in recent years, driven by the popularity of video streaming services such as subscription services (e.g. Netflix, NEON and Lightbox), catch-up services for broadcast television (e.g. TVNZ On Demand), video content on news websites, social media and user generated content. Mobile networks have also experienced dramatic growth in demand for mobile data services, particularly for video content.

The volume of data downloaded over fixed line broadband services in New Zealand rose at an average rate of 51% per annum in the five years to June 2015<sup>31</sup>. Cisco Systems Inc. (**Cisco**) predicts that this volume will continue to

<sup>31</sup> Source: Cisco Systems, Inc., Visual Networking Index Global IP Traffic Forecast, 2015- 2020, February 2016.

grow at an annual rate of 21% between 2014 and 2019 and that video data will represent 86% of all consumer traffic by 2019 (up from 74% in 2014)<sup>32</sup>. In 2015, New Zealand's mobile data grew 67% and Cisco predicts this volume will grow at an annual rate of 43% between 2015 and 2020<sup>33</sup>.

The increasing demand for bandwidth favours infrastructure owners over resellers, as large upgrades to the capacity of an owned fibre network can be made for relatively little cost, while resellers are subject to wholesale arrangements priced per unit of capacity.

### **Bundling and Convergence with Content**

Telecommunications companies have been increasingly seeking to bundle services in a single package (and, ideally, through a unified interface with the customer to cover all the services provided on an integrated basis). Bundles are generally either "triple play" or "quad play" offerings combining some or all of fixed voice, fixed broadband, mobile (voice and data) and pay television. The objective of bundling is to enhance the overall value and attractions of the package and to protect revenue (in part by making direct comparisons more difficult). From a marketing perspective these bundled offerings have become a key plank in the strategies for both telecommunications companies and pay television operators.

Historically, the separate technologies used for pay television (analogue cables or satellite) meant that for a telecommunications company the bundling with pay television was achieved through partnerships or other commercial relationships (e.g. the relationship between AT&T and satellite operator DISH Network Corporation (**DISH**) in the United States). At the same time:

- some telecommunications companies developed their own pay television services. For example, in Australia, Telstra took a 50% interest in the FOXTEL Partnership (**FOXTEL**) when it started (which involved an HFC network separate to Telstra's own network) and Optus developed its own pay television business; and
- some pay television operators established their own voice and broadband (and, potentially, mobile) offerings utilising their own cable networks. Even satellite based broadcasters have moved down this path. The best example is Sky plc in the United Kingdom which is now one of the two largest retailers of broadband services, using third party open access cable networks.

More recently, the industry has seen:

- a blurring of the traditional boundaries as a result of digitisation. Pay television no longer requires separate delivery platforms and can be delivered over the internet;
- increased demand for video content on mobile devices and changing consumer viewing habits (fuelled by technology developments);
- mergers between telecommunications companies and pay television operators such as AT&T's acquisition of DIRECTV LLC (**DIRECTV**), the acquisition by Vodafone Group of Kabel Deutschland Holding AG (**Kabel Deutschland**) and the merger of Vodafone Group's business in the Netherlands with the Ziggo business owned by Liberty Global plc (**Liberty Global**); and
- acquisition of content rights by telecommunications companies directly, for example, the recent purchase by Optus of the Australian rights to the English Premier League (**EPL**) (and the earlier acquisitions by Telstra and Optus for non pay television digital broadcast rights for sports events). Content acquisition is driven by two key factors:
  - the attraction to customers and the anticipated benefits in terms of pricing, new customer acquisition and reduction in churn; and
  - greater ability to fully exploit the content across multiple platforms and delivery formats.

In short, access to exclusive quality video content has now become a fundamental strategy for, and differentiator between, telecommunications companies.

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<sup>32</sup> Source: Cisco Systems, Inc., Visual Networking Index Global IP Traffic Forecast, 2014-2019, May 2015.

<sup>33</sup> Source: Statistics New Zealand Internet Service Provider Survey 2015.

### ***Migration of Business and Consumer Services to the Cloud***

The use of external processing and storage has spread to large and small businesses and consumers and is often referred to as cloud services. Examples of cloud services include a document management system for an engineering firm, a photo storage library for a consumer, or a customer database and billing system for an insurance company. The increasing use of cloud services by businesses and consumers drives greater demand for data centre space and high speed network connections to those data centres.

### ***Expanding Internet Applications***

A rapidly increasing range and number of devices are becoming connected to the internet. These range from:

- consumer devices and appliances such as entertainment devices (e.g. tablets, televisions), air-conditioning systems and security systems;
- vehicles such as trains and buses (public safety, passenger internet access), cars (in-car entertainment, navigation, fault reporting) and commercial vehicles (tracking, fleet management);
- stationary devices such as gas and electricity meters, parking meters, vending machines and industrial equipment; and
- surveillance and security systems for businesses and public spaces.

As the number of devices proliferates, there will be increasing opportunities for carriers to provide broader coverage through wireless and fibre networks and managed services to activate and monitor fleets of network-connected devices.

Given the rapid rate of change in the sector and frequent development of new technologies, it is difficult to make accurate predictions for the telecommunications sector. Overall, it is expected that the sector will continue to experience:

- growth in demand for data, higher data rates and more connected devices;
- relatively low revenue growth in the absence of a major catalyst for price increases;
- a steady stream of new products, services and technologies;
- increasing levels of integration between services; and
- increasing demand for flexible access to video content across devices (anywhere, any time).

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## Appendix B – Recent Transaction Evidence

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A brief description of each of the transactions listed in Section 7 is outlined below:

### ***Transactions involving Satellite Telecommunications Businesses:***

#### ***The Farmside Group / TeamTalk***

On 2 November 2012 TeamTalk announced that it has entered into an agreement to acquire BayCity Communications Limited (trading as The Farmside Group) for an upfront purchase price of \$31 million plus an additional \$11.05 million in earn-out payments based on the achievement of future EBITDA targets. Farmside is a leading provider of wireless communications services and is New Zealand's largest satellite broadband provider. At the time of the acquisition Farmside had over 15,000 predominantly retail customers and 80 employees based in Timaru and Christchurch. The acquisition of Farmside built on TeamTalk's existing niche telco operations and strengthened its position in rural New Zealand. For the year to June 2012, Farmside generated EBITDA of \$5.8 million and EBIT of \$2.1 million. The purchase price (excluding earn-outs) implied multiples of 5.3 times historical EBITDA and 14.8 times historical EBIT. The transaction was funded through the issue of \$12 million in new TeamTalk shares and \$19 million in debt including the assumption of \$5.9 million of Farmside's borrowings.

### ***Transactions involving Fibre Networks Businesses:***

#### ***Nextgen Networks / Vocus***

On 29 June 2016 Vocus Communications Limited (**Vocus**) announced that it would acquire Nextgen Networks for A\$700 million and two development projects from the Nextgen Group for upfront consideration of US\$80 million (A\$107 million) plus deferred consideration of up to US\$40 million (A\$54 million). The acquisition of Nextgen Networks implied a multiple of approximately 10.7 times forecast FY16 normalised EBITDA (before synergies) and 7.3 times including expected synergies. Nextgen Networks has a 17,000km fibre backhaul network connecting Australia's mainland capital cities and major regional centres.

#### ***Amcom Communications Limited / Vocus Communications Limited***

On 17 December 2014, Vocus and Amcom Communications Limited (**Amcom**) announced that they had entered into a scheme implementation agreement under which Vocus would acquire the 90% of Amcom that it did not already own. The consideration under the scheme is 0.4614 Vocus shares for each Amcom share. Based on the Vocus share price on 24 October 2014 (the last trading day prior to announcement of Vocus' initial approach to Amcom), this exchange ratio represents a value of \$2.45 per Amcom share. Following completion of the transaction, former Amcom shareholders, in aggregate, held approximately 54% of the combined entity.

Amcom is a telecommunications and IT company that provides data, internet and unified communications services, cloud solutions and managed services primarily to the business segment. Amcom's business is based in Perth, Adelaide and Darwin where it owns approximately 2,300 kilometres of fibre network, seven data centres, deploys two unified communications platforms and provides a range of IT services. In November 2014, Amcom announced a significant expansion of its business on the east coast of Australia. This included the acquisition of 180 kilometres of fibre asset in Melbourne, Sydney and Brisbane from Megaport for \$15 million, execution of a 15 year fibre access agreement with Sydney based network and infrastructure owner, FirstPath, and the rollout of Ethernet in the First Mile infrastructure in 30 exchanges in Melbourne, Sydney and Brisbane. Amcom considered that this expansion would be earnings accretive in FY16 and had the potential to contribute up to 20% of earnings in FY17.

The terms of this transaction reflect premiums in the order of 30% over pre-announcement Amcom share prices. The multiples implied by the transaction are relatively high due to:

- the positive growth outlook for Amcom over the period to FY17 (the implied prospective multiples for FY16 are 12 times EBITDA and 16 times EBIT);

- Amcom primarily servicing the business segment, deriving higher margins (relative to consumer segment businesses); and
- the extent of synergy benefits available in the transaction. Vocus announced that cost savings in the order of \$13-15 million per annum were likely to be achieved by the end of FY17 and that there was the potential for significant revenue synergies. Allowing for \$14 million in cost savings (midpoint of estimate) reduces the prospective implied multiples to around 9.5-10.5 times EBITDA and 12-13.5 times EBIT.

It should also be noted that the multiples implied by the acquisition of Amcom reflect its range of activities and are therefore blended. In this context, Amcom's telecommunications business segment accounted for 58% of revenue and 83% of EBITDA (before corporate expenses) in FY14.

#### ***Pacnet Limited / Telstra Corporation Limited***

On 23 December 2014, Telstra announced that it would acquire Asian telecommunication services provider Pacnet Limited (**Pacnet**) for US\$697 million. Pacnet provides connectivity, managed services and data centre services to carriers, multi-national corporations and governments in the Asia-Pacific region. It owns a network of 29 interconnected data centres in 17 cities and Asia's largest privately owned submarine optical fibre cable network with 21 cable landing stations in China, Hong Kong, Japan, the Philippines, Singapore, South Korea and Taiwan. It also controls two of the five fibre pairs on the Unity Trans-Pacific submarine cable network connecting Japan to the United States. The acquisition also includes interests in a China joint venture, PBS, which is licensed to operate a domestic Internet Protocol Virtual Private Network and provide data centre services in most major provinces of China. Pacnet is headquartered in both Singapore and Hong Kong with approximately 815 employees across 25 offices. The acquisition is an important part of Telstra's offshore growth strategy and Telstra expects synergies of A\$65 million per annum (or around US\$45 million). As Pacnet was privately owned, financial information on the business is limited.

#### ***FX Networks Limited / Vocus Communications Limited***

On 2 July 2014, Vocus announced the acquisition of FX Networks Limited (**FX Networks**) for NZ\$115.8 million in cash and Vocus scrip. FX Networks owns and operates an inter city optical fibre network in New Zealand consisting of over 4,000 kilometres of ducted fibre cable covering both North and South Islands. It is one of only three inter-city network providers in New Zealand (behind Spark and Vodafone) and provides data backhaul and dark fibre services for telecommunications providers, networking and internet for enterprise and government and design and construction of fibre infrastructure for third parties. Its network is connected to 17 major data centres and 26 of 33 Ultra-Fast Broadband (**UFB**) areas.

#### ***Telecom New Zealand Australia Pty Limited / TPG Telecom Limited***

On 9 December 2013, TPG Telecom announced the acquisition of Telecom New Zealand Australia Pty Limited (known as **AAPT**) for \$450 million. AAPT offers voice, internet, data and cloud services for business and wholesale customers in Australia. It owns extensive telecommunications infrastructure including 11,000 kilometres of intercapital fibre across six states and territories, fibre access to 1,500 premises, 15 data centres and widespread mid-band Ethernet capability. The acquisition augments TPG Telecom's network and provides increased building coverage, additional data centre space and National Broadband Network (**NBN**) point of interconnect coverage.

#### ***Telecommunication assets of Leighton Holdings Limited / Ontario Teachers' Pension Plan***

On 28 March 2013, Leighton Holdings Limited (**Leighton**) announced that it had reached agreement with Ontario Teachers' Pension Plan for the sale of 70.1% of its non-core telecommunications assets (consisting of Nextgen Networks, Metronode and Infoplex) for \$885 million (subject to adjustments including net debt and working capital). Nextgen Networks owns and operates a 17,000 kilometre optical fibre network across mainland Australia linking capital cities and regional and remote areas. Metronode is a developer, owner and operator of data centres and Infoplex is a provider of private cloud services (hosting and management services) to medium-sized and large business and government customers.

Information in relation to the Leighton telecommunication assets and the transaction is limited. The multiples in the table are based on information in the annual report of Leighton Holdings Limited for FY13, which implies an enterprise value on completion of \$824 million (lower than the announced \$885 million). The earnings used to calculate the multiples are based on broker estimates. Furthermore, as the assets were sold into a joint venture arrangement with Leighton retaining a 29.9% interest, it is unclear whether the transaction reflects the fair value for 100% of the assets. Accordingly, these multiples for this transaction should be treated with caution.

#### ***PIPE Networks Limited / SP Telemedia Limited***

On 11 November 2009, SP Telemedia Limited (**SPT**) announced that it had entered into a merger implementation agreement with PIPE Networks Limited (**PIPE**) whereby it will acquire all of the outstanding shares in PIPE via a scheme of arrangement for \$6.30 cash per share, valuing PIPE at \$425 million. PIPE is a facilities based telecommunications service provider in Australia where it owns the third largest metropolitan optical fibre network. Its domestic business earns around 80% of revenue primarily from WAN/dark fibre services (with the network utilised to around 26%) with the remainder from telehousing, peering and managed Ethernet services. PIPE's key domestic customers include internet service providers and telecommunications providers, government agencies and corporate clients. At announcement of the transaction, PIPE had recently announced the completion of a submarine optical fibre cable linking Sydney to Guam, PIPE Pacific Cable 1 (**PPC-1**).

On 27 October 2009 (later affirmed in the scheme booklet dated 5 February 2010), PIPE provided earnings guidance for FY10. The multiples in the table are calculated by reference to that guidance. However, it should be noted that the earnings guidance includes international earnings which contain one-off sales of indefeasible rights of access (**IRUs**) on PPC-1 and PIPE provided guidance that FY11 EBITDA for its international business was expected to be \$15.4 million, \$9.6 million lower than FY10 guidance. If this amount is treated as non-recurring, the prospective EBITDA multiples implied by the transaction increase to 9.7-10.2 times.

#### ***Transactions involving Mobile Radio Network businesses:***

##### ***ASTRID / Belgian Government***

On 16 September 2011 the Belgian Government agreed to acquire a 39% stake in ASTRID SA (**ASTRID**) from Holding Communal NV for EUR 56 million. Under the terms of the transaction EUR 40 million was paid and an additional EUR 16 million transferred. ASTRID develops, manages and maintains mobile radio communications, paging and dispatching networks and control rooms for emergency and security services in Belgium. The ASTRID network was built by Nokia. The company also provides dispatching, local control room solutions and other related services including mobile and broadband data, GPS, automatic personal location. ASTRID generated EBITDA of EUR 14.1 million for its financial year ended 31 December 2010 EBITDA of EUR 15.7 million for its financial year ended 31 December 2011. The purchase price implies multiples of 8.4 times historical 2011 EBITDA and 7.5 times (forward actual) 2012 EBITDA.

##### ***Airwave / Macquarie***

On 18 April 2007 Macquarie Communications Infrastructure Group and Macquarie European Infrastructure Fund II entered into an agreement to acquire Airwave O2 Limited (**Airwave**) for GBP1,932 million. Airwave is the primary provider of secure digital radio communications to the UK police, fire and ambulance services as well as other public safety customers. Airwave is the world's largest purpose built TETRA public safety communication network. Airwave's network consists of 3,500 base station sites and a series of zone cluster switches and communication management centres. Approximately 39% of sites are owned, 43% are shared, and 18% are lead tenanted but not owned.

Significant EBITDA growth was expected in the near term based on contracted growth and potential additional revenue from both new and existing customers. The trailing acquisition multiple was 20.1 times historical pro-forma EBITDA to 31 December 2006. This declines quickly based on expected earnings growth.



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## Appendix C – Comparable Listed Companies

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A brief description of each of the companies listed in Section 7 is outlined below:

### **Integrated Carriers:**

#### **Spark**

Spark New Zealand Limited (**Spark**) (formerly Telecom Corporation of New Zealand Limited (**Telecom NZ**) was formed in 1987 from the telecommunications division of the New Zealand Post Office. In 2011, as a pre-requisite for participation in the New Zealand government's Ultra Fast Broadband (**UFB**) initiative, Telecom was required to structurally separate its retail business (now known as Spark) from the network services operator (now known as Chorus Limited (**Chorus**) which was demerged in November 2011. Spark's Home, Mobile & Business segment, which accounts for over half of total revenue, offers fixed voice, mobile and broadband services to residential households and small businesses. Spark Digital (35% of revenue) integrates telecommunication and information technology (**IT**) services to provide solutions for business, enterprise and government customers while Spark Connect develops and maintains Spark's telecommunications networks and IT systems, as well as offering services directly to wholesale customers. In recent years, Spark has divested a number of assets and businesses and invested in spectrum assets in order to pursue its strategy of focusing on the New Zealand market.

#### **Telstra**

Telstra Corporation Limited (**Telstra**) is Australia's largest telecommunications and information services company, offering a range of products, services and solutions across mobiles, fixed and mobile broadband, telephony, pay television, data and unified communications to households, businesses and governments. It operates the largest fixed network in Australia with 5,100 exchanges and over 225,000 kilometres of fibre. Telstra serves approximately 16.7 million domestic retail mobile services, 7.3 million fixed voice services and 3.1 million retail fixed broadband services in Australia. Its Telstra Retail business segment accounts for around two-thirds of revenue. During FY15 Telstra invested over A\$1 billion into the 4G mobile network to extend its coverage reach to 94% of the Australian population. The progressive rollout of the National Broadband Network (**NBN**) has commenced and will see Telstra's legacy copper and hybrid fibre-coaxial networks switched off over the next five years, with the loss of earnings partially offset by one-off Per Subscriber Address Amount payments each time a customer is disconnected from the copper network. In this context, on 9 October 2015, the Australian Competition & Consumer Commission announced a one-off 9.4% drop in the prices paid by operators to use Telstra's copper network with the new prices to apply from 1 November 2015 until 30 June 2019. Telstra has been strategically growing its offshore business, particularly in Asia.

#### **Vocus**

Vocus Communications Limited (**Vocus**) is a full service integrated trans-Tasman telecommunications company. It is the fourth largest integrated telecommunications company in Australia and the third largest in New Zealand. Vocus was formed following the nil-premium merger between Vocus and M2 Group Ltd (**M2 Group**) in February 2016. Vocus provided internet, fibre, data centre and unified communications services in Australia and New Zealand while M2 Group provided a range of telecommunications and other products and services to residential and small business customers across Australia and New Zealand. The combination of the two entities provided diversification, flexibility and strategic optionality to enable Vocus to take advantage of the opportunities represented by the progressive roll out of the NBN in Australia and the UFB in New Zealand. The merger is expected to result in A\$40 million per annum in cost synergies to be fully realised by the end of FY18 and significant revenue synergies available via the expanded product set and distribution capabilities.

Vocus' implied multiples of historical EBITDA and EBIT are not meaningful as the results do not reflect a full year of profitability of the merged group.

### **TPG Telecom**

TPG Telecom is an integrated telecommunications service provider to residential households, small and medium enterprises, government, large corporate enterprises and wholesale customers. It offers broadband products, telephony services, mobile services and business networking solutions. TPG Telecom owns and operates end-to-end network infrastructure including an extensive metropolitan and intercapital fibre network (over 17,000 kilometres), 400 DSLAM telephone exchanges across Australia and the international PPC-1 submarine cable between Australia and Guam. It is the second largest provider of broadband services in Australia with over 1.8 million subscribers. TPG Telecom has grown substantially since 2008 both organically and by acquisition. This growth is expected to continue over the short to medium term on the back of the September 2015:

- acquisition of iiNet Limited (**iiNet**) for which cost synergies of around \$70-80 million per annum are expected within three years as well as the potential for revenue or other synergies; and
- agreements with Vodafone Hutchison (the operating arm (50% owned) of Hutchison Australia) whereby TPG Telecom will provide dark fibre and network services to more than 3,000 Vodafone Hutchison sites over the next 15 years and will become a mobile virtual network operator (**MVNO**) migrating its mobile customer base to the Vodafone Hutchison network.

### **Wholesale Only Carriers:**

#### **Chorus**

Chorus is New Zealand's largest fixed line communications infrastructure company and was formed in 2011 as a consequence of the structural separation of Telecom NZ. Chorus offers phone and broadband services over both copper and fibre networks with approximately 1.8 million fixed line connections and 1.2 million broadband connections to homes and businesses throughout New Zealand. Chorus is prohibited from selling services directly to end-users and instead provides open access wholesale services to approximately 100 retail service providers. Chorus is contracted by the New Zealand Government to construct the network to over 830,000 properties in 24 deployment areas for the UFB initiative (around 70% of the program).

### **Satellite:**

#### **Sky TV**

Sky Network Television Limited (**Sky TV**) was established in 1987 to deliver a pay television service to the New Zealand market. It has continued to develop and grow since that time and is now well established as the market leading pay television company in New Zealand with approximately 816,000 subscribers. In June 2016 Sky TV entered into an agreement to merge with Vodafone New Zealand Limited (**Vodafone NZ**) through the issue of new Sky TV shares and cash. In February 2017 the New Zealand Commerce Commission declined to grant clearance for the merger.

### 1. Capitalisation of Earnings

Capitalisation of earnings or cash flows is most appropriate for businesses with a substantial operating history and a consistent earnings trend that is sufficiently stable to be indicative of ongoing earnings potential. This methodology is not particularly suitable for start-up businesses, businesses with an erratic earnings pattern or businesses that have unusual expenditure requirements. This methodology involves capitalising the earnings or cash flows of a business at a multiple that reflects the risks of the business and the stream of income that it generates. These multiples can be applied to a number of different earnings or cash flow measures including EBITDA, EBITA, EBIT or net profit after tax. These are referred to respectively as EBITDA multiples, EBITA multiples, EBIT multiples and price earnings multiples. Price earnings multiples are commonly used in the context of the share market. EBITDA, EBITA and EBIT multiples are more commonly used in valuing whole businesses for acquisition purposes where gearing is in the control of the acquirer.

Where an ongoing business with relatively stable and predictable earnings is being valued Grant Samuel uses capitalised earnings or operating cash flows as a primary reference point. Application of this valuation methodology involves:

- estimation of earnings or cash flow levels that a purchaser would utilise for valuation purposes having regard to historical and forecast operating results, non-recurring items of income and expenditure and known factors likely to impact on operating performance; and
- consideration of an appropriate capitalisation multiple having regard to the market rating of comparable businesses, the extent and nature of competition, the time period of earnings used, the quality of earnings, growth prospects and relative business risk.

The choice between the parameters is usually not critical and should give a similar result. All are commonly used in the valuation of industrial businesses. EBITDA can be preferable if depreciation or non-cash charges distort earnings or make comparisons between companies difficult but care needs to be exercised to ensure that proper account is taken of factors such as the level of capital expenditure needed for the business and whether or not any amortisation costs also relate to ongoing cash costs. EBITA avoids the distortions of goodwill amortisation. EBIT can better adjust for differences in relative capital intensity.

Determination of the appropriate earnings multiple is usually the most judgemental element of a valuation. Definitive or even indicative offers for a particular asset or business can provide the most reliable support for selection of an appropriate earnings multiple. In the absence of meaningful offers, it is necessary to infer the appropriate multiple from other evidence.

The usual approach is to determine the multiple that other buyers have been prepared to pay for similar businesses in the recent past. However, each transaction will be the product of a unique combination of factors. A pattern may emerge from transactions involving similar businesses with sales typically taking place at prices corresponding to earnings multiples within a particular range. This range will generally reflect the growth prospects and risks of those businesses. Mature, low growth businesses will, in the absence of other factors, attract lower multiples than those businesses with potential for significant growth in earnings.

An alternative approach used in valuing businesses is to review the multiples at which shares in listed companies in the same industry sector trade on the share market. This gives an indication of the price levels at which portfolio investors are prepared to invest in these businesses. Share prices reflect trades in small parcels of shares (portfolio interests) rather than whole companies and it is necessary to adjust for this factor.

The analysis of comparable transactions and share market prices for comparable companies will not always lead to an obvious conclusion as to which multiple or range of multiples will apply. There will often be a wide spread of multiples and the application of judgement becomes critical. Moreover, it is necessary to consider the particular attributes of the business being valued and decide whether it warrants a higher or lower multiple than the comparable companies. This assessment is essentially a judgement.

## **2. Discounted Cash Flow**

Discounting of projected cash flows has a strong theoretical basis. It is the most commonly used method for valuation in a number of industries, and for the valuation of start-up projects where earnings during the first few years can be negative. DCF valuations involve calculating the net present value of projected cash flows. This methodology is able to explicitly capture the effect of a turnaround in the business, the ramp up to maturity or significant changes expected in capital expenditure patterns. The cash flows are discounted using a discount rate, which reflects the risk associated with the cash flow stream. Considerable judgement is required in estimating future cash flows and it is generally necessary to place great reliance on medium to long-term projections prepared by management. The discount rate is also not an observable number and must be inferred from other data (usually only historical). None of this data is particularly reliable so estimates of the discount rate necessity involve a substantial element of judgment. In addition, even where cash flow forecasts are available the terminal or continuing value is usually a high proportion of value. Accordingly, the multiple used in assessing this terminal value becomes the critical determinant in the valuation (i.e. it is a “de facto” cash flow capitalisation valuation). The net present value is typically extremely sensitive to relatively small changes in underlying assumptions, few of which are capable of being predicted with accuracy, particularly beyond the first two or three years. The arbitrary assumptions that need to be made and the width of any value range mean the results are often not meaningful or reliable. Notwithstanding these limitations, DCF valuations are commonly used and can at least play a role in providing a check on alternative methodologies, not least because explicit and relatively detailed assumptions need to be made as to the expected future performance of the business operations.

## **3. Realisation of Assets**

Valuations based on an estimate of the aggregate proceeds from an orderly realisation of assets are commonly applied to businesses that are not going concerns. They effectively reflect liquidation values and typically attribute no value to any goodwill associated with ongoing trading. Such an approach is not appropriate in TeamTalk’s case.

## **4. Industry Rules of Thumb**

Industry rules of thumb are commonly used in some industries. These are generally used by a valuer as a “cross check” of the result determined by a capitalised earnings valuation or by discounting cash flows, but in some industries rules of thumb can be the primary basis on which buyers determine prices. Grant Samuel is not aware of any commonly used rules of thumb that would be appropriate to value TeamTalk. In any event, it should be recognised that rules of thumb are usually relatively crude and prone to misinterpretation.

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## Appendix E – Interpretation of Multiples

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Earnings multiples are normally benchmarked against two primary sets of reference points:

- the multiples implied by the share prices of listed peer group companies; and
- the multiples implied by the prices paid in acquisitions of other companies in the same industry.

In interpreting and evaluating such data it is necessary to recognise that:

- multiples based on listed company share prices do not include a premium for control and are therefore often (but not always) less than multiples that would apply to acquisitions of controlling interests in similar companies. However, while the premium paid to obtain control in takeovers is observable (typically in the range 20-35%) it is inappropriate to simply add a premium to listed multiples. The premium for control is an outcome of the valuation process, not a determinant of value. Premiums are paid for reasons that vary from case to case and may be substantial due to synergy or other benefits available to the acquirer. In other situations, premiums may be minimal or even zero. There are transactions where no corporate buyer is prepared to pay a price in excess of the prices paid by share market investors;
- acquisition multiples from comparable transactions are therefore usually seen as a better guide when valuing 100% of a business but the data tends to be less transparent and information on forecast earnings is often unavailable;
- the analysis will give a range of outcomes from which averages or medians can be determined but it is not appropriate to simply apply such measures to the company being valued. The most important part of valuation is to evaluate the attributes of the specific company being valued and to distinguish it from its peers so as to form a judgement as to where on the spectrum it belongs;
- acquisition multiples are a product of the economic and other circumstances at the time of the transaction. However, each transaction will be the product of a unique combination of factors, including:
  - economic factors (e.g. economic growth, inflation, interest rates) affecting the markets in which the company operates;
  - strategic attractions of the business – its particular strengths and weaknesses, market position of the business, strength of competition and barriers to entry;
  - the company's own performance and growth trajectory;
  - rationalisation or synergy benefits available to the acquirer;
  - the structural and regulatory framework;
  - investment and share market conditions at the time, and
  - the number of competing buyers for a business;
- acquisitions and listed companies in different countries can be analysed for comparative purposes, but it is necessary to give consideration to differences in overall share market levels and rating between countries, economic factors (economic growth, inflation, interest rates), market structure (competition etc.) and the regulatory framework. It is not appropriate to adjust multiples in a mechanistic way for differences in interest rates or share market levels;
- acquisition multiples are based on the target's earnings but the price paid normally reflects the fact that there were cost reduction opportunities or synergies available to the acquirer (at least if the acquirer is a "trade buyer" with existing businesses in the same or a related industry). If the target's earnings were adjusted for these cost reductions and/or synergies the effective multiple paid by the acquirer would be lower than that calculated on the target's earnings; and
- while EBITDA multiples are commonly used benchmarks they are an incomplete measure of cash flow. The appropriate multiple is affected by, among other things, the level of capital expenditure (and working capital investment) relative to EBITDA. In this respect:

- EBIT multiples can in some circumstances be a better guide because (assuming depreciation is a reasonable proxy for capital expenditure) they effectively adjust for relative capital intensity and present a better approximation of free cash flow. However, capital expenditure is lumpy and depreciation expense may not be a reliable guide. In addition, there can be differences between companies in the basis of calculation of depreciation; and
- businesses that generate higher EBITDA margins than their peer group companies will, all other things being equal, warrant higher EBITDA multiples because free cash flow will, in relative terms, be higher (as capital expenditure is a smaller proportion of earnings).

### 1. Qualifications

The Grant Samuel group of companies provides corporate advisory services in relation to mergers and acquisitions, capital raisings, corporate restructuring and financial matters generally. One of the primary activities of Grant Samuel is the preparation of corporate and business valuations and the provision of independent advice and expert's reports in connection with mergers and acquisitions, takeovers and capital reconstructions. Since inception in 1988, Grant Samuel and its related companies have prepared more than 400 public expert and appraisal reports.

The persons responsible for preparing this report on behalf of Grant Samuel are Michael Lorimer, BCA, Simon Cotter, BCom, MAppFin, F Fin, and Jake Sheehan, BCom (Hons). Each has a significant number of years of experience in relevant corporate advisory matters.

### 2. Limitations and Reliance on Information

Grant Samuel's opinion is based on economic, market and other conditions prevailing at the date of this report. Such conditions can change significantly over relatively short periods of time. The report is based upon financial and other information provided by the directors, management and advisers of TeamTalk. Grant Samuel has considered and relied upon this information. Grant Samuel 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 underlying value of TeamTalk. However in such assignments time is limited and Grant Samuel does not warrant that these inquiries have identified or verified all of the matters which an audit, extensive examination or "due diligence" investigation might disclose.

The time constraints imposed by the Takeovers Code are tight. This timeframe restricts the ability to undertake a detailed investigation of TeamTalk. In any event, an analysis of the merits of the offer is in the nature of an overall opinion rather than an audit or detailed investigation. Grant Samuel has not undertaken a due diligence investigation of TeamTalk. In addition, preparation of this report does not imply that Grant Samuel has audited in any way the management accounts or other records of TeamTalk. It is understood that, where appropriate, the accounting information provided to Grant Samuel was prepared in accordance with generally accepted accounting practice and in a manner consistent with methods of accounting used in previous years.

An important part of the information base used in forming an opinion of the kind expressed in this report is the opinions and judgement of the management of the relevant enterprise. That information was also evaluated through analysis, enquiry and review to the extent practicable. However, it must be recognised that such information is not always capable of external verification or validation.

The information provided to Grant Samuel included projections of future revenues, expenditures, profits and cash flows of TeamTalk prepared by the management of TeamTalk. Grant Samuel has used these projections for the purpose of its analysis. Grant Samuel has assumed that these projections were prepared accurately, fairly and honestly based on information available to management at the time and within the practical constraints and limitations of such projections. It is assumed that the projections do not reflect any material bias, either positive or negative. Grant Samuel has no reason to believe otherwise.

However, Grant Samuel in no way guarantees or otherwise warrants the achievability of the projections of future profits and cash flows for TeamTalk. Projections are inherently uncertain. Projections are predictions of future events that cannot be assured and are necessarily based on assumptions, many of which are beyond the control of management. The actual future results may be significantly more or less favourable.

To the extent that there are legal issues relating to assets, properties, or business interests or issues relating to compliance with applicable laws, regulations, and policies, Grant Samuel assumes no responsibility and offers no

legal opinion or interpretation on any issue. In forming its opinion, Grant Samuel has assumed, except as specifically advised to it, that:

- the title to all such assets, properties, or business interests purportedly owned by TeamTalk is good and marketable in all material respects, and there are no material adverse interests, encumbrances, engineering, environmental, zoning, planning or related issues associated with these interests, and that the subject assets, properties, or business interests are free and clear of any and all material liens, encumbrances or encroachments;
- there is compliance in all material respects with all applicable national and local regulations and laws, as well as the policies of all applicable regulators other than as publicly disclosed, and that all required licences, rights, consents, or legislative or administrative authorities from any government, private entity, regulatory agency or organisation have been or can be obtained or renewed for the operation of the business of TeamTalk, other than as publicly disclosed;
- various contracts in place and their respective contractual terms will continue and will not be materially and adversely influenced by potential changes in control; and
- there are no material legal proceedings regarding the business, assets or affairs of TeamTalk, other than as publicly disclosed.

### **3. Disclaimers**

It is not intended that this report should be used or relied upon for any purpose other than as an expression of Grant Samuel's opinion as to the merits of the Spark Offer. Grant Samuel expressly disclaims any liability to any TeamTalk security holder who relies or purports to rely on the report for any other purpose and to any other party who relies or purports to rely on the report for any purpose whatsoever.

This report has been prepared by Grant Samuel with care and diligence and the statements and opinions given by Grant Samuel in this report are given in good faith and in the belief on reasonable grounds that such statements and opinions are correct and not misleading. However, no responsibility is accepted by Grant Samuel or any of its officers or employees for errors or omissions however arising in the preparation of this report, provided that this shall not absolve Grant Samuel from liability arising from an opinion expressed recklessly or in bad faith.

Grant Samuel has had no involvement in the preparation of the Target Company Statement issued by TeamTalk and has not verified or approved any of the contents of the Target Company Statement. Grant Samuel does not accept any responsibility for the contents of the Target Company Statement (except for this report).

### **4. Independence**

Grant Samuel and its related entities do not have any shareholding in or other relationship or conflict of interest with TeamTalk or Spark that could affect its ability to provide an unbiased opinion in relation to the Spark Offer. Grant Samuel had no part in the formulation of the Spark Offer. Its only role has been the preparation of this report. Grant Samuel will receive a fixed fee for the preparation of this report. This fee is not contingent on the outcome of the Spark Offer. Grant Samuel will receive no other benefit for the preparation of this report. Grant Samuel considers itself to be independent for the purposes of the Takeovers Code.

### **5. Information**

Grant Samuel has obtained all the information that it believes is desirable for the purposes of preparing this report, including all relevant information which is or should have been known to any Director of TeamTalk and made available to the Directors. Grant Samuel confirms that in its opinion the information provided by TeamTalk and contained within this report is sufficient to enable TeamTalk security holders to understand all relevant factors and make an informed decision in respect of the Spark Offer. The following information was used and relied upon in preparing this report:

#### **5.1 Publicly Available Information**

- TeamTalk Annual Reports for the years ended 30 June 2012-2016; and



- TeamTalk's recent announcement to the NZX including the financial results for the first half of the financial year through to 31 December 2018;

## **5.2 Non Public Information**

- TeamTalk's long-term financial projections by business division to 30 June 2022 including commentary regarding the key operating assumptions;
- TeamTalk's Bank and Business Plan dated February 2017;
- Materials provided to Spark as part of its limited due diligence of TeamTalk;
- Information regarding the key markets that TeamTalk operates in;
- TeamTalk's board approved budget for FY17;
- TeamTalk's monthly management accounts for FY16 and FY17 year to date;
- Information regarding the business plans of each of TeamTalk's business divisions;
- Detail regarding historical and forecast capital expenditure by division; and
- TeamTalk's Board Papers and Minutes for the past 12 months.

## **6. Declarations**

TeamTalk has agreed that it will indemnify Grant Samuel and its employees and officers in respect of any liability suffered or incurred as a result of or in connection with the preparation of the report. This indemnity will not apply in respect of the proportion of any liability found by a Court to be primarily caused by any conduct involving gross negligence or wilful misconduct by Grant Samuel. TeamTalk has also agreed to indemnify Grant Samuel and its employees and officers for time spent and reasonable legal costs and expenses incurred in relation to any inquiry or proceeding initiated by any person. Where Grant Samuel or its employees and officers are found to have been grossly negligent or engaged in wilful misconduct Grant Samuel shall bear the proportion of such costs caused by its action. Any claims by TeamTalk are limited to an amount equal to the fees paid to Grant Samuel.

Advance drafts of this report were provided to the directors and executive management of TeamTalk. Certain changes were made to the drafting of the report as a result of the circulation of the draft report. There was no alteration to the methodology, evaluation or conclusions as a result of issuing the drafts.

## **7. Consents**

Grant Samuel consents to the issuing of this report in the form and context in which it is to be included in the Target Company Statement to be sent to security holders of TeamTalk. Neither the whole nor any part of this report nor any reference thereto may be included in any other document without the prior written consent of Grant Samuel as to the form and context in which it appears.

## APPENDIX 2 – Half year results to 31 December 2016

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TeamTalk Limited

Condensed Interim  
Financial Statements  
For The  
Six Months Ended  
31 December 2016

# TeamTalk Limited

## Condensed Consolidated Statement of Comprehensive Income

For the six months ended 31 December 2016

	Note	Group		
		Six months ended 31 December 2016 (Unaudited) \$000's	2015 (Unaudited) \$000's	Year ended 30 June 2016 (Audited) \$000's
Revenue		28,547	28,693	57,295
Operating costs		(17,140)	(17,558)	(38,728)
<b>Gross profit</b>		<b>11,407</b>	<b>11,135</b>	<b>18,567</b>
Other income		393	397	786
Administrative expenses		(9,458)	(8,831)	(17,556)
<b>Results from operating activities</b>		<b>2,342</b>	<b>2,701</b>	<b>1,797</b>
Finance income	8	495	312	322
Finance expenses	8	(983)	(1,405)	(2,549)
<b>Net finance costs</b>		<b>(488)</b>	<b>(1,093)</b>	<b>(2,227)</b>
<b>Profit/(Loss) before income tax</b>		<b>1,854</b>	<b>1,608</b>	<b>(430)</b>
Goodwill impairment		-	-	(1,000)
<b>Profit/(Loss) before income tax</b>		<b>1,854</b>	<b>1,608</b>	<b>(1,430)</b>
Income tax (expense)/credit		(505)	(460)	120
<b>Profit for the period and total comprehensive income attributable to equity holders of the Company</b>		<b>1,349</b>	<b>1,148</b>	<b>(1,310)</b>
<b>Earnings per share</b>				
Basic earnings per share	9	\$0.048	\$0.040	(\$0.046)
Diluted earnings per share	9	\$0.048	\$0.040	(\$0.046)

# TeamTalk Limited

## Condensed Consolidated Statement of Changes in Equity

For the six months ended 31 December 2016

Group	Note	Share capital \$000's	Retained earnings \$000's	Other reserves \$000's	Total equity \$000's
<b>Balance at 1 July 2015</b>		<b>60,266</b>	<b>(36,344)</b>	<b>(119)</b>	<b>23,803</b>
Profit for the period		-	1,148	-	1,148
Total recognised income and expense for the period		-	1,148	-	1,148
Dividends to equity holders	7	-	(1,141)	-	(1,141)
Total transactions with owners		-	(1,141)	-	(1,141)
<b>Balance at 31 December 2015 (Unaudited)</b>		<b>60,266</b>	<b>(36,337)</b>	<b>(119)</b>	<b>23,810</b>
<b>Balance at 1 July 2015</b>		<b>60,266</b>	<b>(36,344)</b>	<b>(119)</b>	<b>23,803</b>
Profit for the period		-	(1,310)	-	(1,310)
Total recognised income and expense for the period		-	(1,310)	-	(1,310)
Dividends to equity holders	7	-	(2,284)	-	(2,284)
Total transactions with owners		-	(2,284)	-	(2,284)
<b>Balance at 30 June 2016 (Audited)</b>		<b>60,266</b>	<b>(39,938)</b>	<b>(119)</b>	<b>20,209</b>
<b>Balance at 1 July 2016</b>		<b>60,266</b>	<b>(39,938)</b>	<b>(119)</b>	<b>20,209</b>
Profit for the period		-	1,349	-	1,349
Total recognised income and expense for the period		-	1,349	-	1,349
Dividends to equity holders	7	-	-	-	-
Total transactions with owners		-	-	-	-
<b>Balance at 31 December 2016 (Unaudited)</b>		<b>60,266</b>	<b>(38,589)</b>	<b>(119)</b>	<b>21,558</b>

# TeamTalk Limited

## Condensed Consolidated Statement of Financial Position

As at 31 December 2016

	Group			
	As at 31 December 2016 (Unaudited) \$000's	As at 31 December 2015 (Unaudited) \$000's	As at 30 June 2016 (Audited) \$000's	
	Note			
<b>Non-current assets</b>				
Property, plant and equipment		39,227	39,903	36,962
Goodwill		19,796	20,796	19,796
Intangibles		1,404	2,660	1,529
Finance lease receivable		247	148	173
Prepayments		213	380	286
Deferred tax assets		1,420	-	1,228
<b>Total non-current assets</b>		<b>62,307</b>	<b>63,887</b>	<b>59,974</b>
<b>Current assets</b>				
Trade and other receivables		6,044	6,824	7,212
Current tax receivable		-	154	-
Finance lease receivable		181	165	161
Prepayments		1,076	992	974
Inventory		1,383	2,702	1,781
Cash and cash equivalents		1,340	899	522
<b>Total current assets</b>		<b>10,024</b>	<b>11,736</b>	<b>10,650</b>
<b>Total assets</b>		<b>72,331</b>	<b>75,623</b>	<b>70,624</b>
<b>Equity</b>				
Ordinary share capital	7	60,266	60,266	60,266
Retained earnings		(38,589)	(36,337)	(39,938)
Other reserves		(119)	(119)	(119)
<b>Total equity</b>		<b>21,558</b>	<b>23,810</b>	<b>20,209</b>
<b>Non-current liabilities</b>				
Loans and borrowings		-	35,473	33,593
Deferred income		1,088	1,611	1,299
Deferred tax liabilities		-	337	-
<b>Total non-current liabilities</b>		<b>1,088</b>	<b>37,421</b>	<b>34,892</b>

# TeamTalk Limited

## Condensed Consolidated Statement of Financial Position (continued)

	Note	Group		
		As at		As at
		2016 (Unaudited) \$000's	2015 (Unaudited) \$000's	2016 (Audited) \$000's
<b>Current liabilities</b>				
Loans and borrowings	13	33,893	-	93
Trade and other payables		10,177	8,714	8,934
Current Tax Payable		722	-	543
Deferred income		4,644	5,080	5,183
Derivatives		249	598	770
<b>Total current liabilities</b>		<b>49,685</b>	<b>14,392</b>	<b>15,523</b>
<b>Total liabilities</b>		<b>50,773</b>	<b>51,813</b>	<b>50,415</b>
<b>Total equity and liabilities</b>		<b>72,331</b>	<b>75,623</b>	<b>70,624</b>

On behalf of the Board of Directors



**Director**  
1 March 2017



**Director**  
1 March 2017

# TeamTalk Limited

## Condensed Consolidated Statement of Cash Flows

For the six months ended 31 December 2016

	Group		
	Six months ended 31 December 2016 (Unaudited) \$000's	2015 (Unaudited) \$000's	Year ended 30 June 2016 (Audited) \$000's
	Note		
<b>Cash flows from operating activities</b>			
<i>Cash provided from:</i>			
Receipts from customers		29,213	28,807
Net GST receipts/(payments)		99	(102)
		<u>29,311</u>	<u>28,705</u>
<i>Cash applied to:</i>			
Payments to suppliers and employees		(22,457)	(23,456)
Interest expense paid (net of realised FX (gain)/loss)		(983)	(780)
Income tax paid		(508)	(271)
		<u>(23,948)</u>	<u>(24,507)</u>
<b>Net cash flows from operating activities</b>	11	<u><b>5,363</b></u>	<u><b>4,198</b></u>
<b>Cash flows from investing activities</b>			
<i>Cash provided from:</i>			
Interest income received		5	8
Finance lease interest income received		34	29
Repayment of finance lease receivables		101	103
		<u>140</u>	<u>140</u>
<i>Cash applied to:</i>			
Acquisition of property, plant and equipment		(4,697)	(2,636)
Acquisition of goods provided on finance leases as lessor		(195)	(152)
		<u>(4,892)</u>	<u>(2,788)</u>
<b>Net cash flows from investing activities</b>		<u><b>(4,752)</b></u>	<u><b>(2,648)</b></u>
<b>Cash flows from financing activities</b>			
<i>Cash provided from:</i>			
Proceeds from borrowings		10,265	12,335
		<u>10,265</u>	<u>12,335</u>
<i>Cash applied to:</i>			
Repayment of borrowings		(10,058)	(12,269)
Dividends paid		-	(1,141)
		<u>(10,058)</u>	<u>(13,410)</u>
<b>Net cash flows from financing activities</b>		<u><b>207</b></u>	<u><b>(1,075)</b></u>
<b>Net increase/(decrease) in cash and cash equivalents</b>		<u><b>818</b></u>	<u><b>475</b></u>
<b>Cash and cash equivalents at beginning of period</b>		<u><b>522</b></u>	<u><b>424</b></u>
<b>Cash and cash equivalents at end of period</b>		<u><u><b>1,340</b></u></u>	<u><u><b>522</b></u></u>



# TeamTalk Limited

## Notes to the condensed consolidated interim financial statements

For the six months ended 31 December 2016

### 1 Reporting entity

TeamTalk Limited ("the Company") is a company domiciled in New Zealand, registered under the Companies Act 1993 and listed on the New Zealand Stock Exchange ("NZX"). The Company is a FMC Reporting Entity in terms of Part 7 of the Financial Markets Conduct Act 2013.

The condensed consolidated interim financial statements of the Company as at, and for the six months ended, 31 December 2016 are unaudited and comprise the Company and its subsidiaries (together referred to as "the Group").

The Group is a profit oriented entity primarily involved in the provision of mobile radio networks, high speed broadband services and ISP services in New Zealand.

### 2 Statement of compliance and basis of preparation

These condensed consolidated interim financial statements have been prepared in accordance with NZ IAS 34 Interim Financial Reporting. They do not include all of the information required for full financial statements and should be read in conjunction with the consolidated financial statements of the Group as at, and for the year ended, 30 June 2016.

These condensed consolidated interim financial statements of the Group have been prepared in accordance with the New Zealand Companies Act 1993 and the Financial Markets Conduct Act 2013.

These condensed consolidated interim financial statements were approved by the Board of Directors on 1 March 2017.

The condensed consolidated interim financial statements are presented in New Zealand dollars (NZD), which is the Group's functional currency and are rounded to the nearest thousand.

### 3 Significant accounting policies

The accounting policies applied by the Group in these condensed consolidated interim financial statements are the same as those applied by the Group in its annual financial statements as at, and for the year ended, 30 June 2016.

### 4 Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components, and for which discrete financial information is available. All operating segments' operating results are reviewed regularly by the Group's Chief Executive Officer to make decisions about resources to be allocated to the segment and assess its performance.

### 5 Estimates

The preparation of condensed consolidated interim financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

In preparing these condensed consolidated interim financial statements, the significant judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty were the same as those applied to the annual financial statements as at, and for the year ended, 30 June 2016.

# TeamTalk Limited

## Notes to the condensed consolidated interim financial statements

For the six months ended 31 December 2016

### 6 Operating Segments

Group for the six months ended 31 December 2016	Mobile radio	Broadband networks	ISP	Inter-Segment / Unallocated	Total
	\$000's	\$000's	\$000's	\$000's	\$000's
Operating revenue & other income					
- Sales to customers outside the Group	10,430	7,225	11,285	-	28,940
- Inter-segment sales	175	153	44	(372)	-
<b>Total revenue</b>	<b>10,605</b>	<b>7,378</b>	<b>11,329</b>	<b>(372)</b>	<b>28,940</b>
Costs					
- Costs paid to suppliers outside the Group	(8,279)	(3,386)	(11,208)	-	(22,873)
- Inter-segment costs	369	(374)	(367)	372	-
<b>Total costs</b>	<b>(7,910)</b>	<b>(3,760)</b>	<b>(11,575)</b>	<b>372</b>	<b>(22,873)</b>
EBITDA	2,151	3,839	77	-	6,067
Depreciation and amortisation	(1,225)	(973)	(1,527)	-	(3,725)
Impairment of fixed assets and inventory	-	-	-	-	-
<b>EBIT</b>	<b>926</b>	<b>2,866</b>	<b>(1,450)</b>	<b>-</b>	<b>2,342</b>
Finance income					495
Finance expense					(983)
Net interest					(488)
Profit before income tax					1,854
Income tax expense					(505)
<b>Profit for the period</b>					<b>1,349</b>
Capital expenditure	1,716	684	3,097	-	5,497
Total assets	22,062	35,090	15,179	-	72,331
Total liabilities	8,603	3,660	4,710	33,800	50,773
<b>Group for the six months ended 31 December 2015</b>	<b>Mobile radio</b>	<b>Broadband networks</b>	<b>ISP</b>	<b>Inter-Segment / Unallocated</b>	<b>Total</b>
	\$000's	\$000's	\$000's	\$000's	\$000's
Operating revenue & other income					
- Sales to customers outside the Group	9,983	6,828	12,279	-	29,090
- Inter-segment sales	226	64	19	(309)	-
<b>Total revenue</b>	<b>10,209</b>	<b>6,892</b>	<b>12,298</b>	<b>(309)</b>	<b>29,090</b>
Costs					
- Costs paid to suppliers outside the Group	(7,958)	(3,371)	(11,349)	-	(22,678)
- Inter-segment costs	301	(287)	(323)	309	-
<b>Total costs</b>	<b>(7,657)</b>	<b>(3,658)</b>	<b>(11,672)</b>	<b>309</b>	<b>(22,678)</b>
EBITDA	2,025	3,457	930	-	6,412
Depreciation and amortisation	(1,209)	(954)	(1,211)	-	(3,374)
Impairment of fixed assets and inventory	-	-	(337)	-	(337)
<b>EBIT</b>	<b>816</b>	<b>2,503</b>	<b>(618)</b>	<b>-</b>	<b>2,701</b>
Finance income					312
Finance expense					(1,405)
Net interest					(1,093)
Profit before income tax					1,608
Income tax expense					(460)
<b>Profit for the period</b>					<b>1,148</b>
Capital expenditure	855	929	852	-	2,636
Total assets	22,867	36,017	16,739	-	75,623
Total liabilities	8,913	5,219	2,301	35,380	51,813

# TeamTalk Limited

## Notes to the condensed consolidated interim financial statements

For the six months ended 31 December 2016  
6 Operating Segments (continued)

Group for the twelve months ended 30 June 2016	Mobile radio	Broadband networks	ISP	Inter-Segment / Unallocated	Total
	\$000's	\$000's	\$000's	\$000's	\$000's
Operating revenue & other income					
- Sales to customers outside the Group	19,808	13,810	24,463	-	58,081
- Inter-segment sales	455	127	52	(634)	-
<b>Total revenue</b>	<b>20,263</b>	<b>13,937</b>	<b>24,515</b>	<b>(634)</b>	<b>58,081</b>
Costs					
- Costs paid to suppliers outside the Group	(15,779)	(6,580)	(23,080)	-	(45,439)
- Inter-segment costs	595	(577)	(652)	634	-
<b>Total costs</b>	<b>(15,184)</b>	<b>(7,157)</b>	<b>(23,732)</b>	<b>634</b>	<b>(45,439)</b>
EBITDA	4,029	7,230	1,383	-	12,642
Depreciation and amortisation	(2,594)	(1,895)	(4,518)	-	(9,007)
Impairment of fixed assets and inventory	-	-	(2,838)	-	(2,838)
EBIT	1,435	5,335	(5,973)	-	797
Finance income					322
Finance expense					(2,549)
Net interest					(2,227)
Profit before income tax					(1,430)
Income tax expense					120
<b>Profit for the period</b>					<b>(1,310)</b>
Capital expenditure	1,985	1,659	2,053	-	5,697
Total assets	22,031	34,376	14,217	-	70,624
Total liabilities	8,898	3,890	4,127	33,500	50,415

### 7 Capital and reserves

#### Share capital

The Company has 28,368,994 fully paid no par value shares on issue at balance date (Interim Dec 2015: 28,368,994; Full Year Jun 2016: 28,368,994). All shares have equal rights and rank equally with regard to the Company's residual assets.

#### Dividends

The following dividends were declared and paid by the Group for the period ended 31 December 2016:

	Group		
	Six months ended		Year ended
	31 December		30 June
	2016	2015	2016
	\$000's	\$000's	\$000's
Nil Interim Dividend For 2016 financial year. Final dividend for prior year \$0.04 per qualifying ordinary share. Interim Dividend for 2015 financial year \$0.04 per qualifying ordinary share	-	1,141	1,142
	-	-	1,142
	-	1,141	2,284

### 8 Finance costs

	Group		
	Six months ended		Year ended
	31 December		30 June
	2016	2015	2016
	\$000's	\$000's	\$000's
Interest expense on external borrowings	(978)	(1,055)	(2,040)
Interest income	39	37	70
Net unrealised (loss)/gain on fair value of derivatives	456	(350)	(509)
Net realised (loss)/gain on foreign exchange/derivatives	(5)	275	252
<b>Net finance costs</b>	<b>(488)</b>	<b>(1,093)</b>	<b>(2,227)</b>

# TeamTalk Limited

## Notes to the condensed consolidated interim financial statements

For the six months ended 31 December 2016

### 9 Earnings per share

#### Basic and diluted earnings per share

The calculation of basic earnings per share at 31 December 2016 was based on the profit attributable to ordinary shareholders of \$1,349,000 and a weighted average number of ordinary shares outstanding of 28,368,994 calculated as follows:

	Group		
	Six months ended	Year ended	
	31 December	30 June	
	2016	2015	2016
	\$000's	\$000's	\$000's
Profit attributable to ordinary shareholders	1,349	1,148	(1,310)
	2016	2015	2016
	in shares	in shares	in shares
Weighted average number of ordinary shares			
Issued ordinary shares at start of period	28,368,994	28,368,994	28,368,994
Shares issued during the period	-	-	-
Issued ordinary shares at close of period	28,368,994	28,368,994	28,368,994
Weighted average number of ordinary shares for the period	28,368,994	28,368,994	28,368,994
Basic earnings per share (\$)	0.048	0.040	(0.046)
Diluted earnings per share (\$)	0.048	0.040	(0.046)

### 10 Commitments

	Group		
	Six months ended	Year ended	
	31 December	30 June	
	2016	2015	2016
	\$000's	\$000's	\$000's
(a) Operating lease commitments			
Leases as lessee			
Commitments under non cancellable operating leases are:			
Less than one year	1,018	941	1,165
Between one to two years	805	539	861
Between two to five years	742	615	815
	2,565	2,095	2,841

The Group leases a number of premises and vehicles under operating leases.

Premises leases operate under various differing terms, but typically are based around an initial lease period, with 1 or 2 further right of renewal periods. Some premises are leased on an annual basis and others are subject to monthly terms (storage units). Premises leases typically include rent uprates every 2-3 years with such increases reflecting revised valuations of the premises and changes in market conditions.

The vehicle leases typically run for a period of 3 years, with the vehicles returned to the lessor at the end of term.

#### (b) Capital commitments

At balance date the Group had capital commitments payable within one year of \$218,950 (Dec 2015: \$395,000, Jun 2016: \$2,807,000).

# TeamTalk Limited

## Notes to the condensed consolidated interim financial statements

For the six months ended 31 December 2016

### 11 Reconciliation of the profit for the period with the net cash flow from operating activities

	Group		
	Six months ended	Year ended	
	31 December	30 June	
	2016	2015	2016
	\$000's	\$000's	\$000's
<b>Profit for the period and total comprehensive income after tax</b>	1,349	1,148	(1,310)
<b>Adjustments for:</b>			
Depreciation, amortisation and impairment	3,725	3,711	11,844
(Decrease)/increase in bad debt provision	(11)	(110)	521
Loss/(Gain) on derivatives	(521)	349	(159)
Prepaid services utilisation/(additions)	17	(150)	(62)
Interest income received	(39)	(37)	(70)
Deferred income	(750)	(355)	(564)
Deferred tax movement	(161)	(98)	(1,663)
	2,260	3,310	9,847
Decrease/(increase) in prepayments	(51)	(94)	20
Decrease/(increase) in trade and other receivables	1,178	186	(251)
(Decrease)/increase in income tax payable	148	287	984
Decrease/(increase) in inventory	398	(409)	12
(Decrease)/ increase in trade and other payables	75	(236)	512
Decrease/(increase) in deferred expenses (prepaid IRU)	6	6	79
	1,754	(260)	1,356
<b>Net cash from operating activities</b>	<b>5,363</b>	<b>4,198</b>	<b>9,893</b>

### 12 Related party transactions

#### Transactions with key management personnel

##### Key management personnel compensation

Key Group management personnel compensation comprised short-term employee benefits of \$719,423 for the six months ended 31 December 2016 (Interim Dec 2015: \$740,769; Full Year Jun 2016: \$1,722,796). This excludes directors' fees of \$104,369 (Interim Dec 2015: \$89,167; Full Year Jun 2016: \$222,000).

##### Other transactions with key management personnel

Directors of Group Companies control 0.2% of the voting shares of the Company (Interim Dec 2015: 1.34%; Full Year Jun 2016: 0.2%).

##### Transactions and balances with related parties

The aggregate value of transactions relating to key management personnel and entities over which they have control or significant influence were as follows:

Reg Barrett and Tone Borren provided additional services following David Ware's resignation. During the period the fees for these services were \$48,000.

Directors of the subsidiary companies received no directors fees during the period (Interim Dec 2015: nil; Full Year Jun 2016: nil)

In April 2015 the Company entered into an agreement with Armillary Limited whereby Armillary provides the services of Geoff Davis as Finance Director. During the period the fees were \$44,467 (Full Year Jun 2016: \$132,000). This agreement has now concluded.

Elected directors conduct business with the Group in the normal course of their business activities.

There are no outstanding balances with key management personnel at 31 December 2016 (Interim Dec 2015: nil; Full Year Jun 2016: nil).

Group entities Significant subsidiaries	Country of incorporation	Ownership interest (%)	
		2016	2015
CityLink Limited	New Zealand	100%	100%
BayCity Communications Limited	New Zealand	100%	100%

# TeamTalk Limited

## Notes to the condensed consolidated interim financial statements

For the six months ended 31 December 2016

### 13 Subsequent Event

1. Subsequent to balance date TeamTalk Group has agreed a new banking facility with partners Westpac New Zealand Limited through to 31st March 2020.

2. On 7 February 2017 Spark New Zealand Limited (Spark NZ) filed a notice of its intention to make a full takeover offer for 100% of the fully paid ordinary shares of the group.

On 8 February the Board recommended that shareholders do not sell their shares pending further communication.

TeamTalk has allowed Spark NZ to undertake limited due diligence and no formal offer has been made.

# **TeamTalk Limited**

## **Financial Calendar**

<b>Full Year Result</b>	23 August 2017
<b>Annual Meeting</b>	25 October 2017

# TeamTalk Limited

## Corporate Directory

<b>Registered Office</b>	Level 6, 25-27 Cambridge Terrace, Wellington, New Zealand
<b>Head Office</b>	Level 6, 25-27 Cambridge Terrace, Wellington, New Zealand Phone: (04) 802 1470 Fax: (04) 802 1490 <a href="http://www.teamtalk.co.nz">www.teamtalk.co.nz</a>
<b>Branches</b>	<b><i>Auckland</i></b> 2 Robert Street, Ellerslie, Auckland Phone: (09) 580 9282  <b><i>Christchurch</i></b> Unit 2, 49 Sir William Pickering Drive, Burnside, Christchurch Phone: (03) 357 3005
<b>Subsidiaries</b>	<b>CityLink Limited</b> Level 6, 25-27 Cambridge Terrace, Wellington, New Zealand Phone: (04) 917 0200 Fax: (04) 385 9004 <a href="http://www.citylink.co.nz">www.citylink.co.nz</a>  <b>BayCity Communications Limited (trading as Farmside)</b> 8 Butler Street, Timaru, New Zealand Phone: (03) 687 9727 Fax: (03) 688 1557 <a href="http://www.farmside.co.nz">www.farmside.co.nz</a>
<b>Auditors</b>	KPMG 10 Customhouse Quay, Wellington, New Zealand
<b>Solicitors</b>	Crengle, Shreves & Ratner 105-109 The Terrace, Wellington, New Zealand
<b>Bankers</b>	Westpac Banking Corporation 10-14 Courtenay Place, Wellington, New Zealand
<b>Registrar</b>	Link Market Services Limited 138 Tancred Street, Ashburton, New Zealand