AFFINITY EDUCATION
GROUP
ABN 37 163 864 195

24 August 2015

Company Announcements Office
Australian Securities Exchange Limited

Dear Sir / Madam

Takeover offers by G8 Education Group Limited (G8) for Affinity Education Group Limited (Affinity)

We **attach**, by way of service pursuant to item 14 of section 633(1) and item 10 of section 635(1) of the *Corporations Act 2001* (Cth) and the relief granted by ASIC on 10 August 2015 under ASIC Instrument [15-0746], a copy of the target's statement of Affinity in response to the off-market and market takeover offers by G8 for all the shares in Affinity that G8 does not already own.

Yours faithfully

Paul Cochrane
Company Secretary
Affinity Education Group Limited

About Affinity Education Group Limited
Affinity Education Group Limited has been established to be a leading provider in the Australian market of high quality education and care to children aged six weeks to 12 years. Provision of these services includes long day care, before and after school care and occasional care.

THIS IS AN IMPORTANT DOCUMENT AND REQUIRES YOUR IMMEDIATE ATTENTION.

IF YOU ARE IN ANY DOUBT AS TO HOW TO DEAL WITH THIS DOCUMENT, YOU SHOULD CONTACT YOUR BROKER, FINANCIAL ADVISER OR LEGAL ADVISER, OR CALL THE AFFINITY SHAREHOLDER INFORMATION LINE ON 1300 911 275.

AFFINITY EDUCATION
GROUP

REJECT

TARGET'S STATEMENT

AFFINITY EDUCATION GROUP LIMITED ABN 37 163 864 195

YOUR DIRECTORS UNANIMOUSLY RECOMMEND THAT YOU REJECT THE G8 CASH OFFER AND THE G8 SHARE OFFER

THIS DOCUMENT IS A TARGET'S STATEMENT IN RESPONSE TO THE G8 CASH OFFER AND THE G8 SHARE OFFER, BOTH MADE BY G8 EDUCATION LIMITED ABN 95 123 828 553 FOR ALL YOUR AFFINITY SHARES.

FINANCIAL ADVISER

LUMINIS PARTNERS
IN AFFILIATION WITH EVERCORE

LEGAL ADVISER

CORRS
CHAMBERS
WESTGARTH
lawyers

KEY DATES

Date of G8 Share Offer	21 August 2015
Date of G8 Cash Offer	26 August 2015
Date of this Target's Statement	24 August 2015
Date Your Directors will provide an update as to any alternative proposals	No later than the morning of 21 September 2015
G8 Share Offer closes (unless extended or withdrawn)	7 pm (Sydney time) 28 September 2015
G8 Cash Offer closes (unless extended or withdrawn)	7 pm (Sydney time) 28 September 2015

Affinity Shareholder Information Line

Affinity has established the Affinity Shareholder Information Line, which you may call if you have any queries in relation to the G8 Offers. The telephone number for the Affinity Shareholder Information Line is 1300 911 275.

Information relating to the G8 Offers can also be obtained from Affinity's website at www.affinityeducation.com.au.

Important information

This document (including the annexure) is dated 24 August 2015 and contains the target's statements issued by Affinity under Part 6.5 Division 3 of the Corporations Act, comprising:

- the target's statement in response to the G8 Share Offer and the G8 Share Offer Bidder's Statement, as required under item 10 of section 633(1) of the Corporations Act; and
- the target's statement in response to the G8 Cash Offer and the G8 Cash Offer Bidder's Statement, as required under item 9 of section 635(1) of the Corporations Act.

A copy of this Target's Statement was lodged with ASIC and released to ASX on 24 August 2015. None of ASIC, ASX, or any of their respective officers take any responsibility for the content of this Target's Statement.

No investment advice

This Target's Statement does not take into account your individual objectives, financial situation or particular needs. It does not contain personal advice. Your Directors encourage you to seek independent financial, legal and taxation advice before making a decision as to whether or not to accept either of the G8 Offers.

Forward looking statements

This Target's Statement contains forward looking statements. You should be aware that such statements are only predictions and are subject to inherent risks and uncertainties. Those risks and uncertainties include factors and risks specific to the industry in which Affinity operates as well as general economic conditions and conditions in the financial markets. Actual events or results may differ materially from the events or results expressed or implied in any forward looking statement and such deviations are both normal and to be expected. None of Affinity, any officer of Affinity, any other person named in this Target's Statement with their consent, or any person involved in the preparation of this Target's Statement makes any representation or warranty (either express or implied) as to the accuracy or likelihood of fulfilment of any forward looking statement, or any events or results expressed or implied in any forward looking statement, except to the extent required by law. You are cautioned not to place undue reliance on any forward looking statement. The forward looking statements in this Target's Statement reflect views held only as at the date of this Target's Statement.

Defined terms

A number of defined terms are used in this Target's Statement. These terms are defined in section 11 of this Target's Statement and in the Independent Expert's Report. Unless the contrary intention appears, the context requires otherwise or words are otherwise defined in section 11 of this Target's Statement or the Independent Expert's Report, words and phrases used in this Target's Statement have the same meaning and interpretation as in the Corporations Act.

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Contents of this Target's Statement

CHAIRMAN'S LETTER

24 August 2015

Dear Affinity Shareholder,

YOUR DIRECTORS UNANIMOUSLY RECOMMEND THAT YOU REJECT BOTH OF THE G8 OFFERS

G8 has made two separate takeover offers for your Affinity Shares:

- the G8 Share Offer - G8 is offering 1 G8 Share for every 4.25 Affinity Shares you own, which at 20 August 2015 was worth approximately $0.78 for each Affinity Share you own.[1] Between 4 August 2015 and 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), the value of the G8 Share Offer has not been worth more than $0.80[2] and has been worth as low as $0.725;[3] and
- the G8 Cash Offer - G8 is offering $0.80 for each Affinity Share you own.

G8 has declared that each of the G8 Offers is final and will not be increased.[4]

Your Directors unanimously recommend that you REJECT both of the G8 Offers.

Each of Your Directors intends to **REJECT** both of the G8 Offers in respect of the Affinity Shares which they own or control.[5]

The reasons for Your Directors' unanimous recommendation that you **REJECT** both of the G8 Offers include:

- your Affinity Shares are worth more than G8 is offering. The Independent Expert has concluded that the G8 Offers are **NEITHER FAIR NOR REASONABLE**; and
- Your Directors are currently in discussions with, and have received acquisition proposals from, other interested parties which may result in a superior proposal for Affinity Shareholders.

  Your Directors are continuing to negotiate these alternative proposals, with the aim of reaching agreement on a superior proposal that Affinity directors can recommend to Affinity Shareholders. Affinity will provide an update as to any alternative proposals by no later than the morning of 21 September 2015.[6] If you accept either of the G8 Offers before then, you will miss out on the chance for a higher value under any alternative proposals.

Detailed reasons for Your Directors' unanimous recommendation are set out in section 2 of this Target's Statement.

You have until 7pm (Sydney time) on 28 September 2015 (the scheduled closing date of the G8 Offers) to decide what to do in relation to the G8 Offers, which are unconditional and final. Your Directors recommend that you TAKE NO ACTION until Your Directors provide an update by no later than the morning of 21 September 2015.

To **REJECT** both of the G8 Offers, **DO NOT RESPOND** and **DO NOTHING** in relation to any of the documents sent to you by G8.

Please carefully read this Target's Statement and the Independent Expert's Report, which contain important information. You should also read the G8 Bidder's Statements.

If you are in any doubt as to how to deal with this document, you should contact your broker, financial adviser or legal adviser, or call the Affinity Shareholder Information Line on 1300 911 275.

On behalf of Your Directors, I thank you for your consideration and support.

Yours sincerely,

Stuart James
Chairman and fellow Affinity Shareholder

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1 On 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), the closing price of Affinity Shares was $0.81 and the closing price of G8 Shares was $3.32.
2 Based on the closing price of G8 Shares between 4 August 2015 and 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC).
3 On 18 August 2015, the closing price of G8 Shares was $3.08.
4 G8 Share Offer Bidder's Statement, letter from the Chairperson, page 6; G8 Cash Offer Bidder's Statement, letter from the Chairperson, page 5.
5 Details of each of Your Directors' interests in Affinity Shares are set out in section 10.5 of this Target's Statement.
6 Affinity will announce this update to ASX and on the Affinity website (www.affinityeducation.com.au) and will send this update by mail or email to all Affinity Shareholders.

1 YOUR DIRECTORS' UNANIMOUS RECOMMENDATION AND INTENTION TO REJECT THE G8 CASH OFFER AND THE G8 SHARE OFFER

1.1 What do Your Directors recommend?

Your Directors unanimously recommend that you REJECT both of the G8 Offers. The reasons for Your Directors' unanimous recommendation that you REJECT both of the G8 Offers include that the Independent Expert has concluded that the G8 Offers are NEITHER FAIR NOR REASONABLE. Detailed reasons for Your Directors' unanimous recommendation are set out in section 2 of this Target's Statement.

Your Directors encourage you to:

- read this Target's Statement, the Independent Expert's Report and the G8 Bidder's Statements; and
- have regard to your own risk profile, portfolio strategy, tax position and financial circumstances.

If you are in any doubt as to how to deal with this document, you should contact your broker, financial adviser or legal adviser, or call the Affinity Shareholder Information Line on 1300 911 275.

1.2 What do Your Directors intend to do with their Affinity Shares?

Each of Your Directors intends to REJECT both of the G8 Offers in respect of the Affinity Shares which they own or control.[7]

1.3 Are there any alternative proposals?

Your Directors are currently in discussions with, and have received acquisition proposals from, other interested parties which may result in a superior proposal for Affinity Shareholders.

Your Directors are continuing to negotiate these alternative proposals, with the aim of reaching agreement on a superior proposal that Affinity directors can recommend to Affinity Shareholders. Affinity will provide an update as to any alternative proposals by no later than the morning of 21 September 2015. If you accept either of the G8 Offers before then, you will miss out on the chance for a higher value under any alternative proposals.

7 Details of each of Your Directors' interests in Affinity Shares are set out in section 10.5 of this Target's Statement.

1.4 When will Your Directors provide an update?

Your Directors will provide an update as to any alternative proposals by no later than the morning of 21 September 2015.[8]

1.5 What should you do to follow Your Directors' recommendation?

To REJECT both of the G8 Offers, DO NOT RESPOND and DO NOTHING in relation to any of the documents sent to you by G8.

1.6 When do you need to make a decision?

You have until 7pm (Sydney time) on 28 September 2015 (the scheduled closing date of the G8 Offers) to decide what to do in relation to the G8 Offers. Your Directors will provide an update as to any alternative proposals by no later than the morning of 21 September 2015.[9] Your Directors recommend that you TAKE NO ACTION until Your Directors provide this update.

1.7 Will G8 improve either of the G8 Offers?

G8 has declared that the G8 Offers are final and will not be increased.[10]

G8 has not qualified these statements by reference to the emergence of a superior proposal. Therefore, if an alternative offer eventuates that is superior to the G8 Offers, G8 will not be entitled to increase either of the G8 Offers.

8 Affinity will announce this update to ASX and on the Affinity website (www.affinityeducation.com.au) and will send this update by mail or email to all Affinity Shareholders.
9 Affinity will announce this update to ASX and on the Affinity website (www.affinityeducation.com.au) and will send this update by mail or email to all Affinity Shareholders.
10 G8 Share Offer Bidder's Statement, letter from the Chairperson, page 6; G8 Cash Offer Bidder's Statement, letter from the Chairperson, page 5.

1 YOUR DIRECTORS' UNANIMOUS RECOMMENDATION AND INTENTION TO REJECT THE G8 CASH OFFER AND THE G8 SHARE OFFER (CONT)

1.8 Have Your Directors engaged with G8?

The Board received an approach from G8 wishing to discuss an indicative merger proposal in April 2015. The chairs and managing directors of G8 and Affinity met on 24 April 2015 to discuss a potential proposal that G8 wished to advance. At that meeting, G8 proposed a nil premium merger between G8 and Affinity (based on the closing price of Affinity Shares and G8 Shares on 23 April 2015, this would have involved an equivalent value for each Affinity Share of around $1.105). Affinity advised G8 that it would consider the proposal.

The chairs and managing directors of G8 and Affinity agreed to meet again on 24 June 2015. At that meeting, G8 again proposed a nil premium merger between G8 and Affinity, with Affinity Shareholders receiving consideration of G8 Shares at a ratio based on the market price of Affinity Shares on a spot or 30 day VWAP basis. Based on the closing price of Affinity Shares and G8 Shares on 23 June 2015, this would have involved an equivalent value for each Affinity Share of around $0.825 (**Previous Proposal**).

The Board met to consider the Previous Proposal on 25 June 2015. Affinity advised G8 that the Previous Proposal was not acceptable based on (among other things) the Board's view that an $0.825 offer undervalued Affinity. Affinity advised G8 that Affinity was prepared to continue to engage in discussion with G8 but only if G8 revised the Previous Proposal.

Affinity understood that G8 would respond to Affinity within 10 days (before 4 July 2015) but Affinity did not receive anything further from G8 before the G8 announcement on 3 July 2015 of its intention to make an unsolicited takeover offer *"valuing [Affinity] at $162 million (or $0.70 per [Affinity Share])"*.[11]

On 3 August 2015, G8 announced the G8 Share Offer and the G8 Cash Offer.

Your Directors do not see any reason to engage with G8 in relation to the G8 Offers as G8 cannot increase the consideration it is offering under either of the G8 Offers and the Independent Expert has determined that the G8 Offers are NEITHER FAIR NOR REASONABLE.

Further details about G8's various approaches to Affinity, including approaches made prior to the G8 Offers, is set out in section 4 of this Target's Statement.

1.9 Why has G8 made two offers?

Your Directors do not know why G8 has made two separate offers at the same time and G8 has not provided any explanation.

1.10 Why has Affinity established an independent board committee?

The husband of one of Your Directors, Ms Gabriel Giufre, is involved in a potential alternative proposal that Affinity is currently negotiating with interested parties.

Accordingly, Affinity has adopted protocols to ensure that Affinity's consideration of any alternative proposals is free from any influence from Ms Giufre and that any disclosure of sensitive information in relation to any potential alternative proposals is subject to appropriate oversight and control.

Affinity has established an independent board committee comprising Stuart James, Justin Laboo, Stephanie Daveson and Jeff Forbes to consider any alternative proposals and the G8 Offers, and to oversee the application of the protocols.

The independent board committee unanimously recommends that you REJECT the G8 Cash Offer and the G8 Share Offer.

Ms Giufre also recommends that you REJECT the G8 Cash Offer and the G8 Share Offer.

11 G8 "GEM to make a takeover offer of AFJ at a 29.6% premium" released on ASX on 3 July 2015, page 1.

2 KEY REASONS WHY YOU SHOULD REJECT THE G8 CASH OFFER AND THE G8 SHARE OFFER

1	THE INDEPENDENT EXPERT HAS CONCLUDED THAT THE G8 OFFERS ARE NEITHER FAIR NOR REASONABLE
2	IF YOU ACCEPT EITHER OF THE G8 OFFERS, YOU WILL MISS OUT ON THE CHANCE FOR A HIGHER VALUE UNDER ANY ALTERNATIVE PROPOSAL
3	THE G8 OFFERS DO NOT REFLECT AFFINITY'S LONG-TERM VALUE AND HAVE BEEN OPPORTUNISTICALLY TIMED TO EXPLOIT AFFINITY'S LOWEST EVER CLOSING PRICE
4	G8 IS NOT OFFERING AN ADEQUATE CONTROL PREMIUM
5	STAY WITH AFFINITY – $0.80 IS NOT ENOUGH
6	YOUR DIRECTORS BELIEVE THAT AFFINITY IS WORTH MORE TO G8 THAN G8 IS OFFERING TO AFFINITY SHAREHOLDERS
7	YOUR DIRECTORS ARE CONCERNED ABOUT THE G8 SHARE OFFER

1 THE INDEPENDENT EXPERT HAS CONCLUDED THAT THE G8 OFFERS ARE NEITHER FAIR NOR REASONABLE

The Independent Expert has concluded that the G8 Offers are NEITHER FAIR NOR REASONABLE.

THE G8 CASH OFFER IS NEITHER FAIR NOR REASONABLE

- The Independent Expert has assessed the control value of your Affinity Shares as being in the range of $0.92 to $1.00 for each Affinity Share.
- The value of the G8 Cash Offer Consideration is $0.80 for each Affinity Share you own and the Independent Expert's assessed mid-point value of Affinity on a 100% controlling interest basis is $0.96 for each Affinity Share.
- The Independent Expert has concluded:

> – *"As the Cash Offer consideration is less than our assessed value of 100% of the ordinary shares in Affinity, in our opinion the Cash Offer is not fair."*
>
> – *"In our opinion, an appropriate share of the value of these synergies is not reflected in… the Cash Offer consideration… Accordingly we have concluded that the Offers are also not reasonable."*

THE G8 SHARE OFFER IS NEITHER FAIR NOR REASONABLE

- Under the G8 Share Offer, G8 is offering 1 G8 Share for every 4.25 Affinity Shares you own. At 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), this implied a value of approximately $0.78 for each Affinity Share.
- The Independent Expert has assessed the control value of your Affinity Shares as being in the range of $0.92 to $1.00 for each Affinity Share.
- The mid-point of the Independent Expert's assessed value of the G8 Share Offer Consideration is $0.77 for each Affinity Share, which is below the Independent Expert's assessed mid-point value of Affinity of $0.96 for each Affinity Share on a 100% controlling interest basis.
- The Independent Expert has concluded:

> – *"As the Revised Scrip Offer consideration is less than our assessed value of 100% of the ordinary shares in Affinity, in our opinion, the Revised Scrip Offer is not fair."*
>
> – *"In our opinion, an appropriate share of the value of these synergies is not reflected in either the Revised Scrip Offer… Accordingly we have concluded that the Offers are also not reasonable."*

The Independent Expert's Report is contained in Annexure A of this Target's Statement and you are encouraged to read it in full.

Summary of the Independent Expert's Valuation

Source: Independent Expert's Report and IRESS. Implied value of G8 Share Offer based on G8 Share Offer of 1 G8 Share for every 4.25 Affinity Shares and the closing price of G8 Shares on 20 August 2015 (being the last practicable date prior to the lodgement of this Target's Statement with ASIC).

2 IF YOU ACCEPT EITHER OF THE G8 OFFERS, YOU WILL MISS OUT ON THE CHANCE FOR A HIGHER VALUE UNDER ANY ALTERNATIVE PROPOSAL

Your Directors are currently in discussions with, and have received proposals from, other interested parties which may result in a superior proposal for Affinity Shareholders.

Your Directors are continuing to negotiate these alternative proposals, with the aim of reaching agreement on a superior proposal that Affinity directors can recommend to Affinity Shareholders.

If you accept either of the G8 Offers, you will miss out on the chance for a higher value under any alternative proposals.

You have until 7pm (Sydney time) on 28 September 2015 (the scheduled closing date of the G8 Offers) to decide what to do in relation to the G8 Offers.

Your Directors will provide an update as to any alternative proposals by no later than the morning of 21 September 2015.[12]

YOUR DIRECTORS RECOMMEND THAT YOU TAKE NO ACTION UNTIL YOUR DIRECTORS PROVIDE THIS UPDATE.

12 Affinity will announce this update to ASX and on the Affinity website (www.affinityeducation.com.au) and will send this update by mail or email to all Affinity Shareholders.

3 THE G8 OFFERS DO NOT REFLECT AFFINITY'S LONG-TERM VALUE AND HAVE BEEN OPPORTUNISTICALLY TIMED TO EXPLOIT AFFINITY'S LOWEST EVER CLOSING PRICE

Your Directors consider that the G8 Offers have been opportunistically timed to exploit a short term weakness in the price of Affinity Shares.

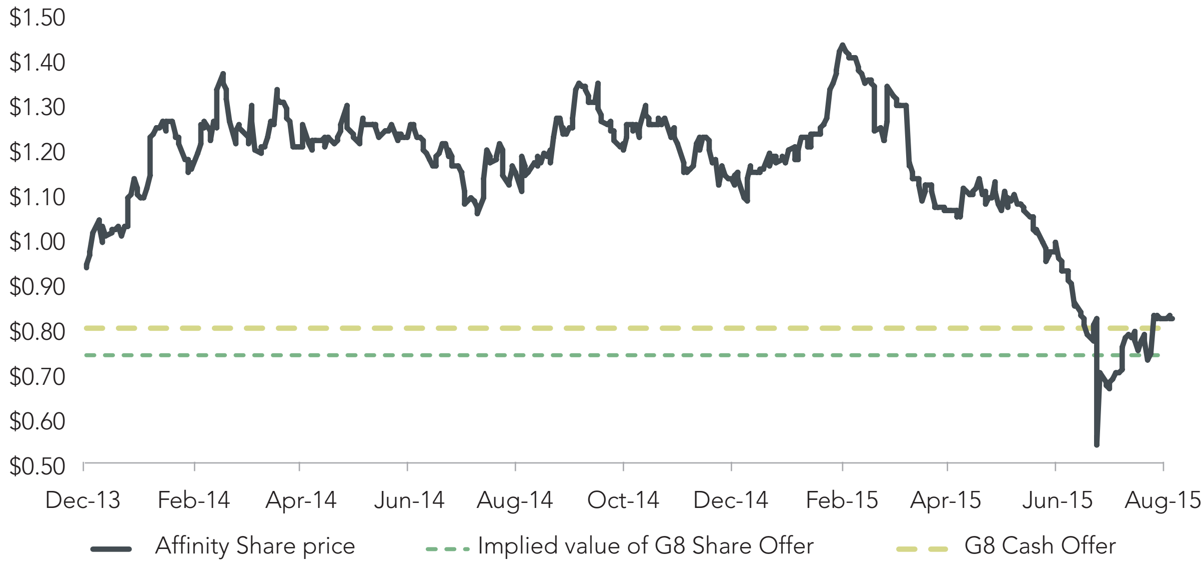
Your Directors note that G8 makes a number of statements in the G8 Bidder's Statements regarding the premium under the G8 Offers.[13] G8 has calculated the premium against Affinity's closing price of $0.54 on 2 July 2015.[14] This was the lowest ever closing price of Affinity Shares.

This sudden drop in the price of Affinity Shares was the immediate result of a market update by Affinity on 2 July 2015.[15] In that update, Affinity excluded future acquisitions in its earnings outlook. In doing so, Affinity was seeking to clarify to the market the earnings attributable to its existing operations.

The market reacted negatively to this earnings update, and on 2 July 2015 the price of Affinity Shares dropped by 34% to its lowest ever closing price, $0.54.

Affinity has since clarified that the earning guidance on 2 July 2015 was based on Affinity's current portfolio and that further acquisitions will increase its earnings.[16] In the Half Year Results lodged with ASX on 18 August 2015, Affinity reported an upgrade to the lower end of its full year guidance, with underlying EBITDA for the full year ending on 31 December 2015 expected to be in the range of $30 million to $32 million (excluding any contribution from further anticipated acquisitions).

Performance of Affinity Shares since listing



Source: IRESS. Implied value of G8 Share Offer based on G8 Share Offer of 1 G8 Share for every 4.25 Affinity Shares and the closing price of G8 Shares on 20 August 2015 (being the latest practicable date prior to lodgement of this Target's Statement with ASIC).

The Independent Expert has made this point in the Independent Expert's Report:

> *"We note that the VWAP of Affinity shares [subsequent to the announcement of the Offers on 3 August 2015] is marginally higher than the value of the consideration implied by the exchange ratio as per the Revised Scrip Offer as well as the $0.80 cash consideration per the Cash Offer. This suggests that the market consensus view is that the Revised Scrip Offer and Cash Offer are both too low."*

13 G8 Share Offer Bidder's Statement, pages 6, 8, 12 and 13; G8 Cash Offer Bidder's Statement, pages 6, 9 and 10.
14 G8 Share Offer Bidder's Statement, letter from the Chairperson, page 6.
15 Affinity "Earnings Guidance and Operational Update" released on ASX on 2 July 2015.
16 Affinity "Market Update Presentation" released on ASX on 7 July 2015.

4 G8 IS NOT OFFERING AN ADEQUATE CONTROL PREMIUM

G8 HAS BEEN SELECTIVE IN ITS COMPARISONS

Your Directors note that G8 makes a number of statements in the G8 Bidder's Statements regarding the premium under the G8 Offers.[17] Your Directors believe G8's statements regarding any premium are selective.

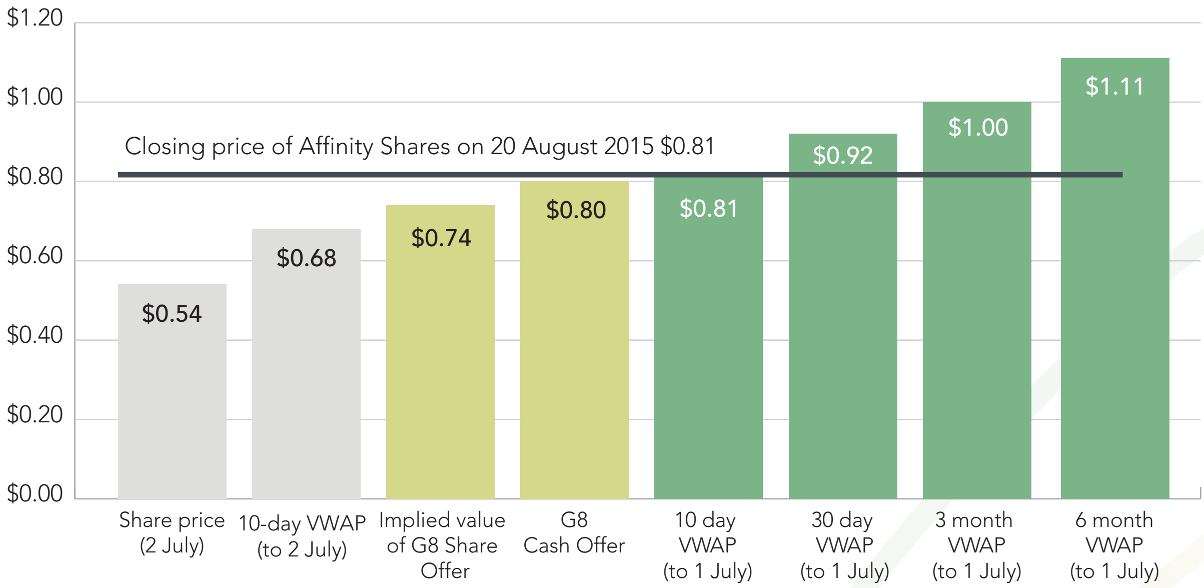
In addition to using the historic low one day share price benchmark for comparison, G8 has selectively chosen not to compare the value of the G8 Offers to Affinity's market performance prior to its market update on 2 July 2015. G8 has chosen only a narrow 10 day VWAP, which includes the decline of the price of Affinity Shares on 2 July 2015. This means that G8's calculations of premiums exclude significant periods where the price of Affinity Shares was well above the value of the G8 Offers.

In comparison, Affinity's VWAP benchmarks to 1 July are all over and above the G8 Cash Offer Consideration of $0.80 and the implied value of the G8 Share Offer Consideration of $0.78.[18] On 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), the closing price of Affinity Shares of $0.81 was above both the G8 Cash Offer Consideration and the implied value of the G8 Share Offer Consideration.

The Independent Expert has made this point in the Independent Expert's Report:

- *"…in our view, the recent listed market prices of Affinity shares prior to the announcement of G8 Education's intention to make a takeover offer for the Company are not a reliable reference point upon which to assess whether an appropriate control premium is being paid."*
- *"…in our view it is inappropriate to base the pre-bid market price upon very limited share trading that occurred between the Company's earnings announcement and the announcement of G8 Education's intention to make a takeover offer (i.e. one day of trading)."*
- *"…we do not consider the pre-bid share price to be an appropriate reference point."*

Pricing of G8 Offers relative to recent Affinity VWAP benchmarks



Source: IRESS. Implied value of G8 Share Offer based on G8 Share Offer of 1 G8 Share for every 4.25 Affinity Shares and the closing price of G8 Shares at 20 August 2015 (being the last practicable date prior to the lodgement of this Target's Statement with ASIC). VWAPs calculated as the VWAP of Affinity Shares in the period up to 1 July 2015 (being the day prior to Affinity's market update) and VWAPs calculated in the period up to and including 2 July 2015 (being the day of Affinity's market update).

17 G8 Share Offer Bidder's Statement, pages 6, 8, 12 and 13; G8 Cash Offer Bidder's Statement, pages 6, 9, and 10.
18 See figure titled "Pricing of G8 Offers relative to recent Affinity VWAP benchmarks".

4 G8 IS NOT OFFERING AN ADEQUATE CONTROL PREMIUM (CONT)

OTHER COMMENTS BY THE INDEPENDENT EXPERT

The Independent Expert has made a number of important comments in the Independent Expert's Report including:

- *"…the ratio reflected by the closing price of G8 Education shares divided by the closing price of Affinity shares [over the year prior to the announcement of G8 Education's intention to make a takeover offer for Affinity] was (generally) materially better than that offered by G8 Education under the Revised Scrip Offer (the observed average range was 1 G8 Education share for every 3.67 Affinity shares). Adjusting Affinity's share price for a theoretical control premium of say 30% further improves the observed ratio to 1 G8 Education share for every 2.82 Affinity shares."*
- *"We note that Affinity received a number of unsolicited approaches from G8 Education prior to the announcement of its intention to make a takeover offer for the Company (refer below). The exchange ratios implied by those approaches (of 3.17 and 4.01) were better than that proposed under the Revised Scrip Offer (and not inconsistent with the observed trading average...)."*
- *"…as both the Revised Scrip Offer and Cash Offer are materially below our valuation range, we do not consider that either offer provides Affinity shareholders with a sufficient premium for control."*

5 STAY WITH AFFINITY – $0.80 IS NOT ENOUGH

YOUR DIRECTORS BELIEVE YOU ARE BETTER OFF REMAINING AN AFFINITY SHAREHOLDER THAN ACCEPTING EITHER OF THE G8 OFFERS

Affinity has invested considerable capital and resources in becoming a fully integrated owner and operator of 161 childcare centres around Australia.

The Affinity business model provides many future benefits that Affinity expects to realise. Your Directors believe that Affinity will continue to improve margins and earnings growth through:

- its ability to attract high quality staff through its people development and training programs;
- well invested technology and systems which provide Affinity with an attractive opportunity for service innovation and increased market share; and
- cost control.

Your Directors believe that the synergies available to Affinity as it continues to consolidate and grow have not yet been realised and are not reflected in either of the G8 Offers.

ATTRACTIVE INDUSTRY OUTLOOK

Your Directors believe that the outlook for the childcare industry in Australia is attractive, driven by:

- growing female labour workforce participation rates;
- growing population of children in Australia aged 0-14 years; and
- positive Federal Government regulatory framework and funding model.

G8 has not reflected the attractive industry outlook in the value G8 is offering for your Affinity Shares.

AFFINITY'S FUTURE IS BRIGHT

The outlook for Affinity is positive with strong fundamentals leading to increases in demand for childcare services. Affinity has created a strong corporate platform that will drive further efficiencies with continued growth.

Affinity lodged the Half Year Results with ASX on 18 August 2015.

Affinity reported a positive outlook in the Half Year Results. Affinity reported significant growth, strong underlying cash flows and an upgrade to the lower end of its full year guidance, with underlying EBITDA for the full year ending on 31 December 2015 expected to be in the range of $30 million to $32 million (excluding any contribution from further anticipated acquisitions). Affinity also confirmed that it expects to pay its maiden dividend in February 2016.

Affinity reported strong revenue and earnings growth in comparison to the prior corresponding period, with:

- revenue growth of 128%;
- underlying EBITDA growth of 76%;
- an improvement in relation to statutory net loss of 58%;
- underlying operating cashflow up 311%; and
- portfolio growth up 29%.

Affinity also reported a significant improvement on occupancy rates. As at 18 August 2015, Affinity's occupancy across its entire portfolio was 81%, up from 77% as at 30 June 2015.

6 YOUR DIRECTORS BELIEVE THAT AFFINITY IS WORTH MORE TO G8 THAN G8 IS OFFERING TO AFFINITY SHAREHOLDERS

Your Directors believe that significant synergies and benefits would be available to G8 if G8 were to acquire Affinity and that these have not been adequately reflected in either of the G8 Offers.

COST SYNERGIES

If G8 were to acquire Affinity, there would be a significant amount of duplication between the G8 and Affinity head office functions. Removing the duplication would lead to cost savings and value creation for G8 Shareholders.

G8 is aware of the synergies that are available and has indicated that it believes that synergies in relation to head office costs could result in as much as a $6.5 million per annum benefit if G8 owns 100% of the total issued Affinity Shares.[19]

The value of these synergies is not adequately reflected in either of the G8 Offers.

Regarding the value offering to Affinity Shareholders for potential synergies, the Independent Expert has concluded:

- *"…we expect that G8 Education will be able to generate significant synergies as a result of acquiring 100% of Affinity. In our opinion, an appropriate share of the value of these synergies is not reflected in either the Revised Scrip Offer or Cash Offer consideration."*
- *"…as the assessed value of the consideration under both the Revised Scrip Offer and Cash Offer is below our assessed valuation range of Affinity shares, in our opinion, Affinity shareholders are not being offered an appropriate share of the expected synergies."*
- *"…in our view the exchange ratio (and implied sharing of the synergy benefits associated with the transaction) also favours G8 shareholders to the detriment of Affinity shareholders."*

OTHER SYNERGIES

G8 has indicated that it believes that the merged group is likely to have an increased profile within the investment community, increased research coverage and potentially greater liquidity than either G8 or Affinity currently experiences on a stand-alone basis.[20] The value of these synergies is not adequately reflected in either of the G8 Offers.

CONSOLIDATION BENEFITS

The childcare industry is highly fragmented with the majority of providers (83%) managing only one education and care service. Goodstart Early Learning is currently the largest not-for profit operator with approximately 640 centres nationally.

G8 is the largest for-profit operator in the industry, with 457 centres as at 30 June 2015, and Affinity has 161 centres as at 30 June 2015. Only 1% of the industry manages operations with 25 centres or more; the rest of the market (99%) is highly fragmented and represents a compelling consolidation opportunity for both G8 and Affinity.

Your Directors believe that Affinity has considerable opportunity to expand through acquisitions. G8 is seeking to acquire Affinity's growth prospects, which would reduce competition for its own expansion but has not factored the value of such benefits into the G8 Offers.

A key reason to REJECT both the G8 Offers is that Your Directors believe the value of the synergies available to G8 is not adequately reflected in either of the G8 Offers.

19 G8 Share Offer Bidder's Statement, page 15.

20 G8 Share Offer Bidder's Statement, page 14.

7 YOUR DIRECTORS ARE CONCERNED ABOUT THE G8 SHARE OFFER

One of the reasons for Your Directors' recommendation to **REJECT** the G8 Share Offer is that Your Directors have a number of concerns about G8 Shares:

- G8 is highly leveraged with risky Singaporean debt facilities;
- G8's disclosure of occupancy levels is selective and does not allow the market to accurately assess G8's performance;
- it is questionable as to whether G8's treatment of acquisition-related costs complies with the accounting standards; and
- unlike Your Directors, not all G8 Directors have "skin in the game".

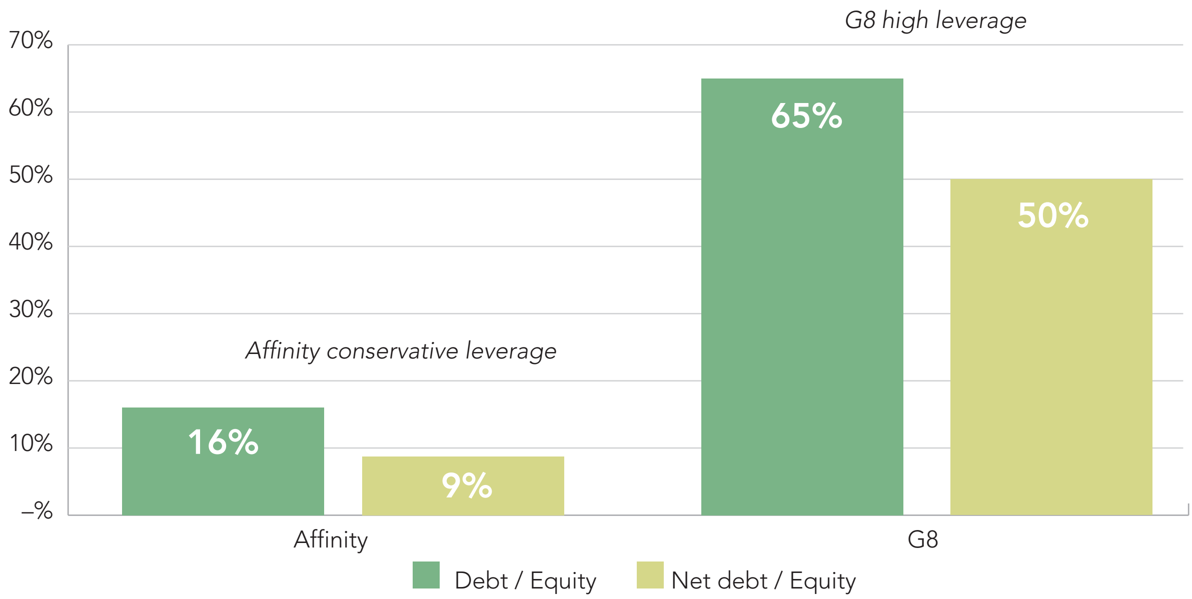
WHY DO YOUR DIRECTORS BELIEVE YOU ARE BETTER OFF WITH AFFINITY THAN ACCEPTING THE G8 SHARE OFFER?

Concern	Affinity position	Observed G8 position
G8 is highly leveraged with risky Singaporean debt facilities	Affinity has a conservative balance sheet. As reported in the Half Year Results, Affinity has a conservative debt level of $33.9 million (or 9% net debt to equity). Your Directors remain committed to diligent financial governance and overseeing Affinity's ongoing capital position.	G8 is highly leveraged when compared to Affinity. These high debt levels are mostly denominated in Singapore dollars, which creates additional currency risk. The strengthening of the Singapore dollar against the Australian dollar recently has made the Singaporean denominated debt more expensive in Australian dollars. In the year ended 31 December 2014, G8 incurred an $18.6 million foreign exchange loss on its Singaporean dollar borrowing.[21] G8 incurred a further $7.3 million foreign exchange loss (tax effected) for the six months ended 30 June 2015.[22] Further, on 3 August 2015, G8 announced that it had undertaken an additional debt issuance under its Multicurrency Debt Issuance Program of a further $155 million in Singapore dollars.[23] <u>How much more will G8 Shareholders lose as a result of such exposure to currency risk?</u>

21 G8 "Preliminary Final Report and Annual Report" released on ASX on 16 February 2015, page 53.
22 G8 "Half Yearly Report and Accounts" released on ASX on 10 August 2015, page 2.
23 G8 "Debt Issuance" released on ASX on 3 August 2015, page 1.

7 YOUR DIRECTORS ARE CONCERNED ABOUT THE G8 SHARE OFFER (CONT)

Affinity vs. G8 leverage positions (30 June 2015)



Source: Half Year Results and G8's half year results[24]

G8's capital structure now consists of the following debt instruments:[25]

Class	Maturity	Issuance[26]	Cost
Senior Unsecured Note	7 August 2019	A$70 million	7.675%
Senior Unsecured Note	17 February 2018	A$50 million	BBSW + 3.90%
Senior Unsecured Note	19 May 2017	S$175 million	4.75%
Senior Unsecured Note	19 May 2017	S$85 million	4.75%
Senior Unsecured Note	3 August 2016	S$155 million	3.50%

24 G8 "Half Yearly Report and Accounts" released on ASX on 10 August 2015.
25 G8 "Half Yearly Report and Accounts" released on ASX on 10 August 2015, page 18; G8 "Debt Issuance" released on ASX on 3 August 2015.
26 References to "S$" are references to Singapore dollars.

7 YOUR DIRECTORS ARE CONCERNED ABOUT THE G8 SHARE OFFER (CONT)

Concern	Affinity position	Observed G8 position
Occupancy disclosure	Affinity fully discloses occupancy levels and trends for its entire portfolio on an up-to-date basis. Affinity's transparency in its disclosure of key performance drivers allows Affinity Shareholders to accurately assess Affinity's performance.	G8's disclosure of occupancy levels is selective and its practice has been only to disclose occupancy rates for a limited portion of the centres it owns. For the year ended 31 December 2014, G8 only disclosed the occupancy for 154 centres out of a portfolio of 455 centres in Australia (approximately 33.8% of its portfolio),[27] with similar limited disclosure in previous years.[28] The G8 Bidder's Statements refer to "average occupancy rates" but there is no reference to what the occupancy rates are measured against and for which portion of G8's portfolio.[29] In contrast with Affinity's transparent and extensive disclosure, G8's disclosure is selective and opaque. How can you judge how G8's business is really performing?
Does G8 comply with accounting standards?	Affinity's accounting policy for acquisition-related costs in relation to business combinations is that all costs are expensed as incurred to profit or loss.[30] Affinity expenses acquisition -related costs in compliance with AASB 3 Business Combinations, paragraph 53 of which requires acquisition-related costs to be expensed to profit or loss in the period to which they relate.	G8's accounting policy states that acquisition-related costs are capitalised as part of the assets and liabilities acquired.[31] If acquisition costs have in fact been capitalised in accordance with G8's accounting policy and G8 has not complied with the accounting standards, how can you accurately assess the value of G8 Shares?

27 G8 "Institutional Investor Presentation" released on ASX on 16 February 2015, page 6.
28 G8 "Preliminary Final Report and Annual Report" released on ASX on 17 February 2014, page 5 (occupancy of 126 centres of 252 total disclosed); G8 "Investor Presentation" released on ASX 15 May 2013, page 9 (occupancy of 118 centres of 185 total disclosed).
29 G8 Share Offer Bidder's Statement, page 26; G8 Cash Offer Bidder's Statement, page 20.
30 Affinity "Annual Report to shareholders" released on ASX on 27 February 2015, pages 44 – 46.
31 G8 "Preliminary Final Report and Annual Report" released on ASX on 16 February 2015, page 44.

7 YOUR DIRECTORS ARE CONCERNED ABOUT THE G8 SHARE OFFER (CONT)

Concern	Affinity position	Observed G8 position
Unlike Your Directors, not all G8 Directors have "skin in the game"	Your Directors believe in the future of Affinity and each of Your Directors holds Affinity Shares.	Only three G8 Directors hold G8 Shares.[32] G8 provided a loan of $5 million to Christopher Scott, the managing director of G8, to fund the acquisition of Mr Scott's G8 Shares, which is not repayable if the sale of Mr Scott's G8 Shares would not cover the balance of the loan outstanding.[33] G8 has issued loans of up to $5 million to the nominees of other G8 executives to fund the acquisition of G8 Shares on similar terms.[34] <u>Theses individuals share in the upside of an investment in G8 Shares, but unlike ordinary G8 Shareholders do not share the risk.</u> <u>What does it say about the confidence that the G8 Directors and senior G8 executives have in G8's future performance when their personal exposure to G8 Shares is so limited?</u>

THE INDEPENDENT EXPERT HAS RAISED CONCERNS ABOUT THE INHERENT RISKS OF INVESTING IN G8 SHARES

The Independent Expert makes the following comments in the Independent Expert's Report:

- *"Affinity shareholders that elect to accept the Revised Scrip Offer should also note that… G8 Education's financial gearing levels may increase significantly relative to its position at 30 June 2015 if a large proportion of Affinity shareholders elect to receive cash (rather than scrip) under the Offers."*
- *"Should G8 Education acquire less than 90% of Affinity:*
  – *G8 Education may not be able to realise all estimated synergy benefits*
  – *G8 Education will not have access to their pro-rata share of the full underlying cash flow generated by Affinity*
  – *Affinity shareholders will not be granted capital gains tax roll-over relief unless G8 Education acquires at least 80% of Affinity."*

32 G8 "Preliminary Final Report and Annual Report" released on ASX on 16 February 2015, page 20; G8 Appendix 3Y released on ASX on 17 June 2015.
33 G8 "Half Yearly Report and Accounts" released on ASX on 10 August 2015, page 19; G8 Share Offer Bidder's Statement, pages 76, 77 and 78.
34 G8 "Half Yearly Report and Accounts" released on ASX on 10 August 2015, page 19; G8 Share Offer Bidder's Statement, pages 76, 77 and 78.

3 YOUR CHOICES AS AN AFFINITY SHAREHOLDER

Your Directors unanimously recommend that you REJECT both of the G8 Offers. However, as an Affinity Shareholder you have three choices:

3.1 REJECT BOTH OF THE G8 OFFERS BY NOT RESPONDING AND DOING NOTHING

If you do not wish to accept the G8 Offers or sell your Affinity Shares on ASX, DO NOT RESPOND and DO NOTHING in relation to any of the documents sent to you by G8.

Section 7.3 of this Target's Statement sets out certain risks associated with retaining and holding Affinity Shares.

3.2 Sell your Affinity Shares on ASX / accept the G8 Cash Offer

You may elect to sell some or all of your Affinity Shares on ASX for the market price at the time. This may be above or below the value of the G8 Share Offer Consideration and the G8 Cash Offer Consideration.

On 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), the closing price of Affinity Shares was $0.81, which is higher than the value of the G8 Share Offer Consideration and the G8 Cash Offer Consideration. The latest price for Affinity Shares may be obtained from the ASX website at www.asx.com.au.

During the G8 Cash Offer Period, Canaccord Genuity will stand in the market to acquire, on behalf of G8, Affinity Shares at the G8 Cash Offer Consideration ($0.80) during normal trading on ASX.

If you sell your Affinity Shares on ASX:

- you may be liable for CGT or income tax on the sale (including under the CGT rules);
- you may incur a brokerage charge;
- you may be liable for GST on incidental costs associated with the sale (such as the brokerage charge);
- you will lose the ability to accept the G8 Share Offer;
- you will miss out on the chance for a higher value under any alternative proposals; and
- you may receive more or less for your Affinity Shares than the value of the G8 Share Offer Consideration and the G8 Cash Offer Consideration.

If you wish to sell your Affinity Shares on ASX, you should contact your broker.

The taxation consequences of selling your Affinity Shares on ASX depend on a number of factors and will vary according to your particular circumstances. For further information, see section 9 of this Target's Statement and section 8 of the G8 Cash Offer Bidder's Statement. You are encouraged to seek your own professional advice as to the taxation consequences applicable to your circumstances.

3.3 Accept the G8 Share Offer

You may elect to accept the G8 Share Offer in respect of some or all of your Affinity Shares.

If you accept the G8 Share Offer, you will lose the right to deal with your Affinity Shares, you will not be able to sell your Affinity Shares on ASX, and you will miss out on the chance for a higher value under any alternative proposals.

Details of how to accept the G8 Share Offer are set out in the section of the G8 Share Offer Bidder's Statement entitled 'How to Accept'.

The taxation consequences of accepting the G8 Share Offer depend on a number of factors and will vary according to your particular circumstances. For further information, see section 9 of this Target's Statement and section 11 of the G8 Share Offer Bidder's Statement. You are encouraged to seek your own professional advice as to the taxation consequences applicable to your circumstances.

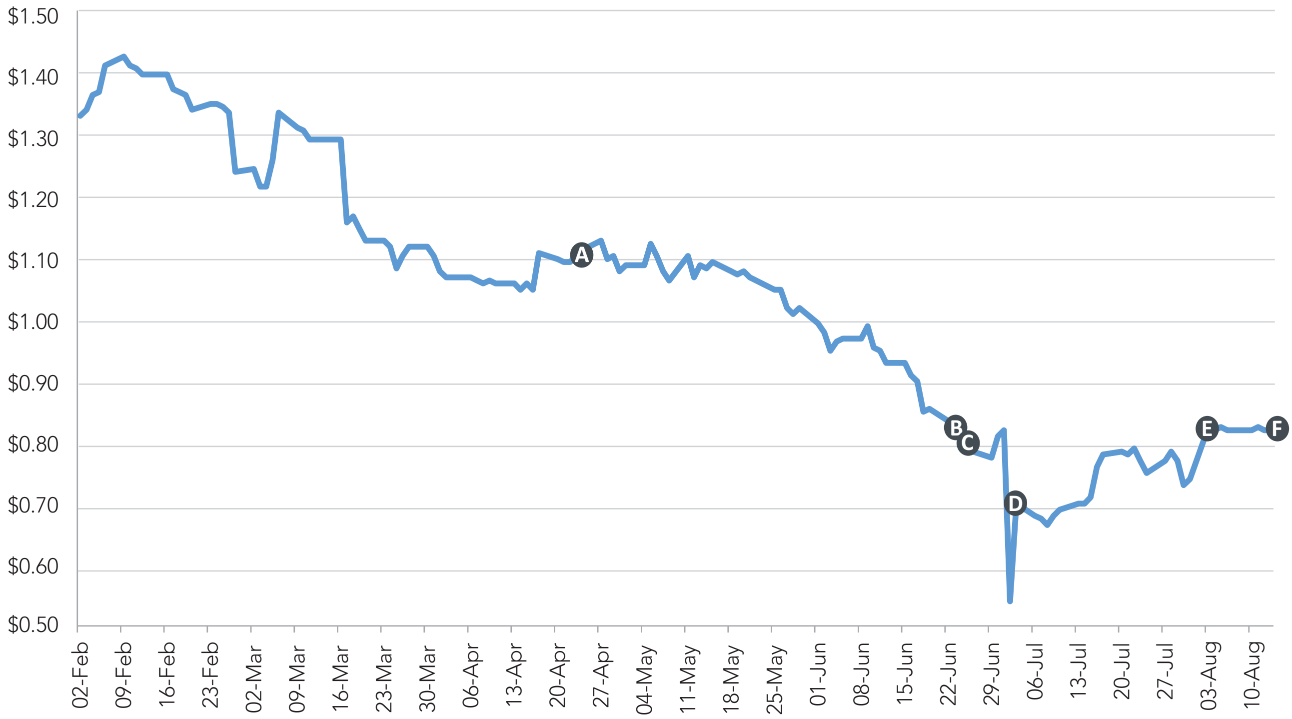
If you choose to accept the G8 Share Offer, Your Directors recommend that you consider exercising the cash alternative which may be available after the G8 Share Offer closes.

As noted in section 12.7 of the G8 Share Offer Bidder's Statement, if you accept the G8 Share Offer and G8 acquires Affinity Shares for cash outside the G8 Share Offer during the G8 Share Offer Period, you may elect to take cash in lieu of the G8 Shares. Notice of that right will be given to you within 14 days after the end of the G8 Share Offer Period in accordance with section 651A(4) of the Corporations Act. You will be able to exercise this right for one month after receiving this notice.

4 BACKGROUND TO THE G8 OFFERS

The following chart provides additional background to G8's various approaches to Affinity, including approaches made prior to the G8 Offers.

As outlined in section 1, Your Directors unanimously recommend that you **REJECT** both of the G8 Offers.



A ***First approach: 24 April***
G8 approached Affinity in April 2015 in relation to an indicative merger proposal. The chairs and managing directors of Affinity and G8 met on 24 April 2015 to discuss a nil premium merger between Affinity and G8. Based on the closing price of Affinity Shares and G8 Shares on 23 April 2015, this would have involved an equivalent value for each Affinity Share of around $1.105. Affinity advised G8 that it would consider the proposal.

B ***Second approach: 24 June***
The chairs and managing directors of Affinity and G8 met again on 24 June 2015. At that meeting, a further proposal in relation to a nil premium merger between Affinity and G8 was discussed. Based on the closing price of Affinity Shares and G8 Shares on 23 June 2015, this would have involved an equivalent value for each Affinity Share of around $0.825.

C ***Approach rejections: 25 June***
Affinity advised G8 that the further proposal was not acceptable based on (among other things) the Board's view that an $0.825 offer undervalued Affinity. Affinity advised G8 that Affinity was prepared to continue to engage in discussion with G8, but only if G8 revised this further proposal.

D ***Announcement of takeover bid: 3 July***
G8 announced that it intended to make a scrip takeover bid for all of the Affinity Shares which it did not already own for an implied value of $0.70 for each Affinity Share.

E ***Announcement of G8 Share Offer and the G8 Cash Offer: 3 August***
G8 announced the G8 Share Offer and the G8 Cash Offer. G8 also declared the G8 Offers final.

F ***Alternative proposals being investigated***
Your Directors do not see any reason to engage with G8 in relation to the G8 Offers as G8 cannot increase the consideration it is offering under either of the G8 Offers. Your Directors are currently engaged with other interested parties and are pursuing alternative proposals.

5 FREQUENTLY ASKED QUESTIONS – KEY FEATURES OF THE G8 OFFERS

This section answers some frequently asked questions about the G8 Offers. This section should be read together with all other parts of this Target's Statement. If you have any other questions, please contact the Affinity Shareholder Information Line on 1300 911 275.

GENERAL INFORMATION ABOUT THE G8 OFFERS

Who is G8?	G8 is the company making the G8 Offers. For further information on G8, see section 5 of the G8 Share Offer Bidder's Statement, section 4 of the G8 Cash Offer Bidder's Statement and section 8 of this Target's Statement.
What is the G8 Share Offer Bidder's Statement?	The G8 Share Offer Bidder's Statement was prepared by G8. The G8 Share Offer Bidder's Statement describes the terms of the G8 Share Offer and information relevant to your decision as to whether or not to accept the G8 Share Offer.
What is the G8 Cash Offer Bidder's Statement?	The G8 Cash Offer Bidder's Statement was prepared by G8. The G8 Cash Offer Bidder's Statement describes the terms of the G8 Cash Offer and information relevant to your decision as to whether or not to accept the G8 Cash Offer.
What is this Target's Statement?	This document contains the target's statements issued by Affinity under Part 6.5 Division 3 of the Corporations Act in response to the G8 Share Offer Bidder's Statement and the G8 Share Offer, and the G8 Cash Offer Bidder's Statement and the G8 Cash Offer. This document contains information that is relevant to your decision as to whether or not to accept the G8 Offers, including Your Directors' recommendation in relation to the G8 Offers.
What is the G8 Share Offer for my Affinity Shares?	If you accept the G8 Share Offer for all of your Affinity Shares, you will receive 1 G8 Share for every 4.25 Affinity Shares you hold. For further information on the G8 Share Offer, see the G8 Share Offer Bidder's Statement.
What is the G8 Cash Offer for my Affinity Shares?	If you accept the G8 Cash Offer for all of your Affinity Shares, you will receive $0.80 for every Affinity Share you hold. For further information on the G8 Cash Offer, see the G8 Cash Offer Bidder's Statement.
Will anyone else make a rival proposal or takeover offer for Affinity?	Your Directors are currently in discussions with, and have received proposals from, other interested parties which may result in a superior proposal for Affinity Shareholders. Your Directors are continuing to negotiate these alternative proposals, with the aim of reaching agreement on a superior proposal that Affinity directors can recommend to Affinity Shareholders. If you accept either of the G8 Offers, you will miss out on the chance for a higher value under any alternative proposals. You have until 7pm (Sydney time) on 28 September 2015 (the scheduled closing date of the G8 Offers) to decide what to do in relation to the G8 Offers. Your Directors will provide an update as to any alternative proposals by no later than the morning of 21 September 2015.[35] Your Directors recommend that you **TAKE NO ACTION** until Your Directors provide this update.

35 Affinity will announce this update to ASX and on the Affinity website (www.affinityeducation.com.au) and will send this update by mail or email to all Affinity Shareholders.

5 FREQUENTLY ASKED QUESTIONS – KEY FEATURES OF THE G8 OFFERS (CONT)

INFORMATION ABOUT YOUR CHOICES AND YOUR DIRECTORS' RECOMMENDATION TO REJECT BOTH OF THE G8 OFFERS

What choices do I have?	Your Directors unanimously recommend that you **REJECT** both of the G8 Offers. However, as an Affinity Shareholder, you have the following choices in respect of your Affinity Shares: • reject both of the G8 Offers by **NOT RESPONDING** and **DOING NOTHING**; • sell your Affinity Shares on ASX (unless you have previously accepted the G8 Share Offer); or • accept the G8 Share Offer. There are implications in relation to each of the above choices. For further information, see section 3 and this section 5 of this Target's Statement.
What should I do?	Your Directors unanimously recommend that you **REJECT** both of the G8 Offers. To follow Your Directors' recommendation to **REJECT** both of the G8 Offers, **DO NOT RESPOND** and **DO NOTHING** in relation to any of the documents sent to you by G8. If you are in any doubt as to what you should do, you should contact your broker, financial adviser or legal adviser, or call the Affinity Shareholder Information Line on 1300 911 275.
What does the Independent Expert say?	The Independent Expert has concluded that the G8 Offers are **NEITHER FAIR NOR REASONABLE**. For further information, see the Independent Expert's Report.
What are Your Directors recommending?	Your Directors unanimously recommend that you **REJECT** both of the G8 Offers. The key reasons why Your Directors unanimously recommend that you **REJECT** both of the G8 Offers are: 1. the Independent Expert has concluded that the G8 Offers are **NEITHER FAIR NOR REASONABLE**; 2. If you accept either of the G8 Offers, you will miss out on the chance for a higher value under any alternative proposal; 3. the G8 Offers do not reflect Affinity's long-term value and have been opportunistically timed to exploit Affinity's lowest ever closing price; 4. G8 is not offering an adequate control premium; 5. $0.80 is not enough; 6. Your Directors believe that Affinity is worth more to G8 than G8 is offering to Affinity Shareholders; and 7. Your Directors are concerned about the G8 Share Offer. For further information, see sections 1 and 2 of this Target's Statement.
What are Your Directors doing in relation to their Affinity Shares?	Each of Your Directors intends to **REJECT** both of the G8 Offers in respect of the Affinity Shares which they own or control. As at 20 August 2015 (being the latest practicable date prior to the lodgment of this Target's Statement with ASIC), Your Directors have a Relevant Interest in approximately 3.73% of the total issued Affinity Shares. For further information, see sections 1, 2 and 10.5 of this Target's Statement.
How do I reject both of the G8 Offers?	To **REJECT** both of the G8 Offers, **DO NOT RESPOND** and **DO NOTHING** in relation to any of the documents sent to you by G8.
If I reject both of the the G8 Offers, can I be forced to sell my Affinity Shares?	You cannot be forced to sell your Affinity Shares unless G8 compulsorily acquires your Affinity Shares. G8 will need to acquire a Relevant Interest in 90% or more of the total issued Affinity Shares in order to proceed to compulsory acquisition.

5 FREQUENTLY ASKED QUESTIONS – KEY FEATURES OF THE G8 OFFERS (CONT)

SPECIFIC INFORMATION ABOUT THE G8 SHARE OFFER

How do I reject the G8 Share Offer?	To **REJECT** the G8 Share Offer, **DO NOT RESPOND** and **DO NOTHING** in relation to any of the documents sent to you by G8.
How do I accept the G8 Share Offer?	Details of how to accept the G8 Share Offer are set out in the section of the G8 Share Offer Bidder's Statement entitled 'How to Accept'.
What are the consequences of accepting the G8 Share Offer now?	If you accept the G8 Share Offer, you will lose the right to deal with your Affinity Shares, you will not be able to sell your Affinity Shares on ASX and you will miss out on the chance for a higher value under any alternative proposals. Further information about the effect of acceptance of the G8 Share Offer is set out in section 3 of this Target's Statement and section 2 of the G8 Share Offer Bidder's Statement. If you choose to accept the G8 Share Offer, Your Directors recommend that you consider exercising the cash alternative which may be available after the G8 Share Offer closes. As noted in section 12.7 of the G8 Share Offer Bidder's Statement, if you accept the G8 Share Offer and G8 acquires Affinity Shares for cash outside the G8 Share Offer during the G8 Share Offer Period, you may elect to take cash in lieu of the G8 Shares. Notice of that right will be given to you within 14 days after the end of the G8 Share Offer Period in accordance with section 651A(4) of the Corporations Act. You will be able to exercise this right for one month after receiving this notice. Your Directors advise that you consider whether an investment in G8 is appropriate for you.
If I accept the G8 Share Offer, can I withdraw my acceptance?	If you accept the G8 Share Offer, unless the G8 Share Offer is withdrawn, you will not be able to withdraw your acceptance of the G8 Share Offer.
If I accept the G8 Share Offer, when will I receive the G8 Share Offer Consideration?	If you accept the G8 Share Offer, G8 will issue the G8 Share Offer Consideration on the earlier of: • one month after you accept the G8 Share Offer; and • 21 days after the end of the G8 Share Offer Period.
Why is G8 unable to increase the G8 Share Offer Consideration?	G8 indicated in the G8 Share Offer Bidder's Statement that the G8 Share Offer Consideration is final and will not be increased.[36] G8 has not qualified this by reference to the emergence of a superior proposal. Therefore if an alternative proposal were to eventuate that was superior to the G8 Share Offer, G8 would not be entitled to increase the G8 Share Offer Consideration.
When does the G8 Share Offer close?	The G8 Share Offer is currently scheduled to close at 7pm (Sydney time) on 28 September 2015, unless extended or withdrawn.

36 G8 Share Offer Bidder's Statement, page 6.

5 FREQUENTLY ASKED QUESTIONS – KEY FEATURES OF THE G8 OFFERS (CONT)

SPECIFIC INFORMATION ABOUT THE G8 SHARE OFFER (CONT)

In what circumstances may G8 extend the G8 Share Offer Period?	G8 may extend the G8 Share Offer Period at any time before the end of the G8 Share Offer Period.
In what circumstances may G8 withdraw the G8 Share Offer?	G8 may only withdraw the G8 Share Offer with the written consent of ASIC and subject to the conditions (if any) specified in such consent.
What are the taxation consequences of accepting the G8 Share Offer?	The taxation consequences of accepting the G8 Share Offer depend on a number of factors and will vary according to your particular circumstances. For further information, see section 9 of this Target's Statement and section 11 of the G8 Share Offer Bidder's Statement. You are encouraged to seek your own professional advice as to the taxation consequences applicable to your circumstances.
I am an overseas Affinity Shareholder. How does the G8 Share Offer affect me?	See page 3 of the G8 Share Offer Bidder's Statement.

SPECIFIC INFORMATION ABOUT THE G8 CASH OFFER

How do I reject the G8 Cash Offer?	To **REJECT** the G8 Cash Offer, **DO NOT RESPOND** and **DO NOTHING** in relation to any of the documents sent to you by G8.
How do I accept the G8 Cash Offer?	Details of how to accept the G8 Cash Offer are set out in the section of the G8 Cash Offer Bidder's Statement entitled 'How to Accept'.
What are the consequences of accepting the G8 Cash Offer now?	If you accept the G8 Cash Offer, you will lose the ability to accept the G8 Share Offer and you will miss out on the chance for a higher value under any alternative proposal. Further information about the effect of acceptance of the G8 Cash Offer is set out in section 3 of this Target's Statement and section 2 of the G8 Cash Offer Bidder's Statement.
If I accept the G8 Cash Offer, can I withdraw my acceptance?	If you accept the G8 Cash Offer, unless the G8 Cash Offer is withdrawn, you will not be able to withdraw your acceptance of the G8 Cash Offer.
If I accept the G8 Cash Offer, when will I receive the G8 Cash Offer Consideration?	If you accept the G8 Cash Offer, you will be paid the G8 Cash Offer Consideration on a T+3 basis.
Why is G8 unable to increase the G8 Cash Offer Consideration?	G8 indicated in the G8 Cash Offer Bidder's Statement that the G8 Cash Offer Consideration is final and will not be increased.[37] G8 has not qualified this by reference to the emergence of a superior proposal. Therefore if an alternative proposal were to eventuate that was superior to the G8 Cash Offer, G8 would not be entitled to increase the G8 Cash Offer Consideration.

37 G8 Cash Offer Bidder's Statement, letter from the Chairperson, pages 5 and 7.

5 FREQUENTLY ASKED QUESTIONS – KEY FEATURES OF THE G8 OFFERS (CONT)

SPECIFIC INFORMATION ABOUT THE G8 CASH OFFER (CONT)

When does the G8 Cash Offer close?	The G8 Cash Offer is scheduled to close at 7pm (Sydney time) on 28 September 2015, unless extended or withdrawn.
In what circumstances may G8 extend the G8 Cash Offer Period?	G8 may extend the G8 Cash Offer Period at any time up to five trading days before the end of the G8 Cash Offer Period and otherwise in accordance with section 649C of the Corporations Act.
In what circumstances may G8 withdraw the G8 Cash Offer?	G8 may only withdraw the G8 Cash Offer with the written consent of ASIC and subject to the conditions (if any) specified in such consent.
What are the taxation consequences of accepting the G8 Cash Offer?	The taxation consequences of accepting the G8 Cash Offer depend on a number of factors and will vary according to your particular circumstances. For further information, see section 9 of this Target's Statement and section 8 of the G8 Cash Offer Bidder's Statement. You are encouraged to seek your own professional advice as to the taxation consequences applicable to your circumstances.

6 RESPONSE TO THE G8 BIDDER'S STATEMENTS

G8 made a number of claims in the G8 Bidder's Statements which Your Directors **REJECT**.

6.1 Statements in the G8 Share Offer Bidder's Statement

G8's claim	Affinity's response
G8 says: "The [G8 Share Offer] provides [Affinity Shareholders] with the ability to exchange 4.25 [Affinity Shares] for 1 [G8 Share]. This is equivalent to $0.80 per [Affinity Share]…"[38]	By stating that the G8 Share Offer is "equivalent to $0.80 per [Affinity Share]", G8 implies that the value of the G8 Share Offer Consideration is fixed. This is not the case – in fact, the value of the G8 Share Offer Consideration will depend on the price of G8 Shares. Between 4 August 2015 and 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), the value of the G8 Share Offer Consideration has fluctuated widely: the G8 Share Offer has not been worth more than $0.80[39] and has been worth as low as $0.725.[40]

6.2 Statements in both G8 Bidder's Statements

G8's claim	Affinity's response
G8 suggests that, if G8 acquires a Relevant Interest in between 50% and 90% of the total issued Affinity Shares, G8 will apply to ASX to delist Affinity.[41]	Affinity believes that it is misleading to create an impression that Affinity Shareholders will realistically be exposed to a risk of delisting without also explaining the significant hurdles G8 would face, unless G8 was entitled to proceed to compulsory acquisition (which would only be the case if G8 acquired a Relevant Interest in 90% of the total issued Affinity Shares). The Listing Rules set out the circumstances in which Affinity may be delisted. Under the Listing Rules, it is not likely that Affinity will be delisted unless at the end of the G8 Share Offer Period and the G8 Cash Offer Period: • G8 proceeds to compulsory acquisition; or • G8 has a Relevant Interest in at least 75% of the total issued Affinity Shares, and certain other conditions are satisfied (including that the number of Affinity Shareholders having holdings with a value of at least $500 is fewer than 150 (excluding G8)).
G8 includes a table "illustrating average occupancy for the year".[42]	The implication from these tables is that they reflect overall occupancy rates for all G8 childcare centres. However, G8's previous practice has been only to disclose occupancy rates for a limited portion of the centres it owns. For example, in the disclosure of occupancy levels for the year ended 31 December 2014, G8 only disclosed the occupancy for 154 centres out of a portfolio of 455 centres in Australia (approximately 33.8% of its portfolio),[43] with similar limited disclosure in previous years.[44] It is not clear what metric the tables in the G8 Bidder's Statements are measured against – is this overall occupancy rates or selective occupancy rates?

38 G8 Share Offer Bidder's Statement, letter from the Chairperson, page 6
39 Based on the closing price of G8 Shares between 4 August 2015 and 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC).
40 On 18 August 2015, the closing price of G8 Shares was $3.08.
41 G8 Share Offer Bidder's Statement, pages 18 and 59; G8 Cash Offer Bidder's Statement, pages 12 and 38.
42 G8 Share Offer Bidder's Statement, page 26; G8 Cash Offer Bidder's Statement, page 20.
43 G8 "Institutional Investor Presentation" released on ASX on 16 February 2015, page 6.
44 G8 "Preliminary Final Report and Annual Report" released on ASX on 17 February 2014, page 5 (occupancy of 126 centres of 252 total disclosed); G8 "Investor Presentation" released on ASX 15 May 2013, page 9 (occupancy of 118 centres of 185 total disclosed).

6 RESPONSE TO THE G8 BIDDER'S STATEMENTS (CONT)

G8's claim	Affinity's response
G8 refers to Affinity's full consolidated financial accounts for the financial period ending 31 December 2014.[45]	Since Affinity's full consolidated financial accounts for the financial period ending 31 December 2014 were released, Affinity carried out the Entitlement Offer. In connection with the Entitlement Offer, Affinity released a pro-forma balance sheet reflecting the Entitlement Offer, which is publicly available on ASX.[46] The G8 Bidder's Statements do not include any information in relation to the Entitlement Offer. The omission of such information in the G8 Bidder's Statements: • means that Affinity's current net asset position is understated and creates an inaccurate impression of the value of Affinity Shares; and • is inconsistent with ASIC Regulatory Guide 228, which states that all events with a material effect since the date of the most recent financial statements should be noted.

45 G8 Share Offer Bidder's Statement, pages 45 and 55; G8 Cash Offer Bidder's Statement, page 31.
46 Retail Offer Booklet released to ASX on 17 March 2015.

7 INFORMATION ABOUT AFFINITY

This section provides an overview about Affinity.

7.1 Overview of Affinity

Affinity is a public company listed on ASX (ASX code: AFJ).

Affinity owns and operates 161 childcare centres and manages six childcare centres across Queensland, New South Wales, Victoria, Western Australia, the Northern Territory and the Australian Capital Territory, servicing over 15,000 children and families.

Affinity's business model is to identify, acquire, integrate and manage childcare centres and extract operational improvement through managing a portfolio of childcare centres. In the ordinary course of business, Affinity aims to increase its portfolio by approximately 20-25% per annum.

In 2014, Affinity acquired 68 childcare centres funded using proceeds from an entitlement offer, banking facilities, cash flows from operations and the issue of shares as approved at the 2014 annual general meeting.

In 2015, Affinity has acquired a further 36 childcare centres to 30 June 2015.

With this significant growth, Affinity has focussed on improving occupancy and optimising the cost base at the centre level.

The outlook for Affinity is positive with strong fundamentals leading to increases in demand for childcare services. Affinity has created a strong corporate platform that will drive further efficiencies with continued growth. Affinity's outlook for 2015 is to maintain a focus on delivering continued growth and better margins with multiple initiatives underway to increase profitability. Affinity has been in discussions to diversify domestic bank funding, has a strong acquisition pipeline and is continuing to work with the Federal Government on future industry opportunities.

Affinity reported a positive outlook in the Half Year Results.

Affinity reported significant growth, strong underlying cash flows and an upgrade to the lower end of its full year guidance, with underlying EBITDA for the full year ending on 31 December 2015 expected to be in the range of $30 million to $32 million (excluding any contribution from further anticipated acquisitions).

Affinity confirmed that it expects to pay its maiden dividend in February 2016.

Affinity reported strong revenue and earnings growth in comparison to the prior corresponding period, with:

- revenue growth of 128%;
- underlying EBITDA growth of 76%;
- an improvement in relation to statutory net loss of 58%;
- underlying operating cashflow up 311%; and
- portfolio growth up 29%

Affinity also reported a significant improvement on occupancy rates. As at 18 August 2015, Affinity's occupancy across its entire portfolio was 81%, up from 77% as at 30 June 2015.

7.2 Your Directors

As at the date of this Target's Statement, Your Directors are:

Name	Position
Stuart Bruce James	Chairman and Independent Non-Executive Director
Justin Michael Laboo	Chief Executive Officer and Managing Director
Stephanie Jane Daveson	Independent Non-Executive Director
Jeffrey Ian Forbes	Independent Non-Executive Director
Gabriel Anna Giufre	Chief Operating Officer and Executive Director

7.3 The childcare centre industry and the risks associated with holding shares in companies that operate within the industry

There are a number of risk factors which may affect the future operating and financial performance of companies that operate within the childcare industry.

This section 7.3 sets out some of the risks associated with holding Affinity Shares. The future level of dividends, the value of the assets of Affinity and the price at which Affinity Shares trade on ASX may be influenced by any of these risks.

7 INFORMATION ABOUT AFFINITY (CONT)

Additional risks and uncertainties not currently known to Affinity may also have a material adverse effect on the business of Affinity and the information set out in this section 7.3 does not purport to be, nor should it be construed as representing, an exhaustive list of the risks affecting Affinity. In particular, Affinity Shareholders should have regard to the disclosure regarding the risks associated with holding Affinity Shares set out in the first appendix of the Retail Offer Booklet. The Retail Offer Booklet was lodged by Affinity with ASX on 17 March 2015. Any Affinity Shareholder who would like to receive a copy of the Retail Offer Booklet should contact the Affinity Shareholder Information Line on 1300 911 275.

(a) General / industry

(i) Changes in law and government policy

The childcare industry in Australia is heavily regulated by each level of government. The state and territory governments are responsible for issuing licences to operate a childcare business and determining the standards that operators must meet in order to obtain and retain a licence. Any change or addition to the regulation imposed by any of the levels of government could negatively affect the operation of the centres and could negatively impact on the profitability of Affinity.

Changes in other laws (including tax and industrial relations laws) or their interpretation may affect the value of, and returns from, an investment in Affinity Shares. For instance, changes in the taxation treatment of companies may adversely affect the market price of Affinity Shares.

(ii) Changes to subsidies

Government subsidies through the Child Care Benefit and Child Care Rebate scheme represent a significant portion of Affinity's revenue. Any adverse changes to these childcare subsidies may have a significantly adverse impact on the operations and financial position of Affinity.

(iii) Regulatory risk and assessment and rating

The regulation and availability of the Child Care Benefit scheme is dependent upon individual childcare centres being registered with the National Quality Framework. The assessment and rating process and receipt of government subsidies involves regular review by representatives of the Australian Children's Education and Care Quality Authority, including inspections of childcare centres, the quality of services provided and facilities. Negative evaluations could result in loss of this registration, licences and the withdrawal of government subsidies. This would have a negative impact on Affinity's operations and financial position.

(iv) Economic

Changes in the general economic outlook both in Australia and globally may impact the performance of Affinity and its projects. Such changes may include: (a) contractions in the Australian economy or increases in the rate of inflation resulting from domestic or international conditions (including movements in domestic interest rates and reduced economy activity); (b) increases in expenses (including the cost of goods and services used by Affinity); (c) increase in unemployment rates; and (d) fluctuations in equity markets in Australia and internationally.

(v) Competition

Although there are barriers to entry in the childcare industry, increased competition from existing and new industry participants may reduce Affinity's revenues and profits. In addition, Affinity faces competition from other companies involved in the consolidation of childcare centres when seeking to acquire additional centres. This competition may increase the price that Affinity may be required to pay to acquire centres or limit the centres Affinity can acquire in the future.

7 INFORMATION ABOUT AFFINITY (CONT)

(vi) Reputation risk

Having a good reputation is an important factor in ensuring that Affinity maintains the occupancy rates and earnings of its childcare centres. Being an owner of a large number of childcare centres, there is a risk that an isolated incident occurring at one centre may impact on the reputation of Affinity and impact adversely on the profitability of all the other childcare centres.

(vii) Employee expense risk

Affinity's wage costs are the largest and most significant part of the group's total costs. Affinity has strategies in place to mitigate any wage increases and also assumes a commercial level of cost inflation per year. However, should circumstances arise through industry regulation or collective employee action that give rise to costs outside of the inflation indexation assumption, then this event would reduce the profitability of Affinity.

(b) Specific

(i) Integration risk

There is a risk that fully integrating centres (along with new centres) may take longer or cost more than anticipated by Affinity. This could impact the profitability of Affinity and occupy large amounts of management's time. There is also no guarantee these centres will operate as profitably after integration as they did prior to their acquisition by Affinity. Past and future acquisitions may subject Affinity to unanticipated risks and liabilities, or disrupt its operations and divert resources from Affinity's day-to-day operations.

(ii) Operational management

Management's ability to effectively monitor, maintain and improve centre performance is dependent on information/technology systems and centre management personnel who can identify and respond to local supply and demand factors. If Affinity is not able to maintain these systems and attract and employ such personnel (or if such personnel do not properly identify and respond to these local factors), this could adversely impact ongoing occupancy, cost control and profitability of individual centres and the financial performance of Affinity as a whole.

(iii) Managing expansion

Management's ability to successfully manage Affinity's expansion and growth as a result of acquisitions is critical to its success. A failure or inability to properly manage expansion and growth, including failing to control costs, may negatively impact profitability and prospects.

8 INFORMATION ABOUT G8

8.1 Disclaimer

The following information about G8 is based on publicly available information, including information in the G8 Bidder's Statements and has not been independently verified by Affinity. Affinity does not make any representation or warranty, express or implied, as to the accuracy or completeness of this information.

The information on G8 in this Target's Statement should not be considered comprehensive.

Further information about G8 is set out in the G8 Cash Offer Bidder's Statement, the G8 Share Offer Bidder's Statement, and G8's Half Year Results, which were lodged with ASX on 10 August 2015.

8.2 Overview of G8

G8 is a public company listed on ASX (ASX code: GEM). As at 30 June 2015, G8 owned 457 childcare centres in Australia and 18 childcare centres in Singapore.

8.3 G8 Directors

As at the date of this Target's Statement, the G8 Directors are:

Name	Position
Jennifer Joan Hutson	Chairperson and Independent Non-Executive Director
Christopher John Scott	Managing Director and Executive Director
Brian Hilton Bailison	Non-Executive Director
Susan Margaret Forrester	Non-Executive Director
Matthew Reynolds	Non-Executive Director

9 TAXATION CONSEQUENCES

9.1 Introduction

The following is a general outline of the main Australian income tax consequences for an Australian resident individual Affinity Shareholder resulting from accepting either of the G8 Offers.

The outline is not exhaustive of all income tax considerations which could apply in the circumstances of any given Affinity Shareholder and there are a number of limitations to the outline including that:

- it applies only to Australian resident individual taxpayers who do not hold their Affinity Shares in carrying on a business at or through a permanent establishment outside Australia. It does not cover the tax treatment for any other classes of taxpayers including persons who are non-residents of Australia for tax purposes, insurance organisations, trusts, taxpayers subject to a Division 230 financial arrangement, employees of Affinity or its associated companies who acquired their Affinity Shares in respect of their employment, or (unless otherwise expressly stated) superannuation entities or companies;
- it applies only where Affinity Shareholders hold their Affinity Shares on capital account. It does not apply where the Affinity Shares are held on revenue account (for example, Affinity Shares held by Affinity Shareholders who trade in shares or hold Affinity Shares as trading stock); and
- it is based on current Australian tax law. It does not take into account or anticipate any changes in the law (including changes to legislation, judicial authority or administrative practice).

This outline does not constitute, and should not be construed as, taxation advice. Affinity and its officers and advisers do not accept any liability or responsibility in respect of any statement concerning the taxation consequences of accepting either of the G8 Offers or in respect of the taxation consequences themselves.

All Affinity Shareholders, and particularly those Affinity Shareholders that are not specifically addressed by this outline as noted above (for example, non-resident Affinity Shareholders), should consult their own independent professional taxation advisers regarding the Australian and, if applicable, foreign income tax consequences of accepting either of the G8 Offers given the particular circumstances which apply to them.

9.2 Acceptance of either of the G8 Offers and disposal of Affinity Shares

(a) Capital gain or loss on Affinity Shares

The disposal of Affinity Shares pursuant to either of the G8 Offers will constitute a CGT event for Australian income tax purposes. Accordingly, if you choose to accept either of the G8 Offers either:

- a capital gain will arise to the extent the capital proceeds received from the disposal of your Affinity Shares exceed the cost base of those Affinity Shares; or
- a capital loss will be realised to the extent the capital proceeds received from the disposal of your Affinity Shares are less than the reduced cost base of those Affinity Shares.

Any capital gain realised from the disposal of your Affinity Shares must be included in your assessable income for the income year in which the G8 Cash Offer or G8 Share Offer is accepted (unless offset against other capital losses you may have).

Any capital loss may be offset against other capital gains you realise in the same year or, subject to the satisfaction of tax rules with respect to the utilisation of capital losses from prior years, may be carried forward to be offset against future capital gains.

(b) Capital proceeds

(i) If you accept the G8 Cash Offer

For the purpose of calculating a capital gain or capital loss on the disposal of the Affinity Shares, the capital proceeds received from accepting the G8 Cash Offer will include the G8 Cash Offer Consideration of $0.80 for each Affinity Share sold.

(ii) If you accept the G8 Share Offer

For the purpose of calculating a capital gain or capital loss on the disposal of the Affinity Shares, the capital proceeds will be the market value of Affinity Shares on the date the G8 Share Offer is accepted by the Affinity Shareholder.

It should be noted that the market value of Affinity Shares at the date the G8 Share Offer is accepted by the Affinity Shareholder may differ from the value placed on G8 Shares for the purposes of the G8 Share Offer.

9 TAXATION CONSEQUENCES (CONT)

(c) Cost base

The cost base and reduced cost base of Affinity Shares is generally equal to the amount paid by the Affinity Shareholder for the Affinity Shares plus certain incidental costs incurred (for example, brokerage fees).

(d) CGT discount

Affinity Shareholders may be entitled to a discount to any net capital gain realised on the disposal of Affinity Shares (after any capital losses have been applied). The amount of the discount is 50% for individuals and 33 1/3% for complying superannuation entities. Eligibility for the discount requires you to have held the Affinity Shares for at least 12 months prior to the date you accepted either of the G8 Offers. Companies are not eligible for the discount.

If you acquired new Affinity Shares as a result of participation in the Entitlement Offer for Affinity Shareholders (announced in March 2015), then you should not be eligible for the CGT discount in respect of the Affinity Shares acquired under that Entitlement Offer, as those new Affinity Shares will not have been held for at least 12 months.

9.3 Other tax consequences of accepting the G8 Share Offer and becoming an owner of G8 Shares

(a) Roll-over relief

If roll-over relief is available and is chosen, then any capital gain resulting from the disposal by you pursuant to the G8 Share Offer may be disregarded so that any capital gains tax implications are effectively deferred until the G8 Shares acquired pursuant to the G8 Share Offer are disposed of. The cost base of the G8 Shares will include an amount equal to the cost base of the Affinity Shares for which they were exchanged.

The availability of roll-over relief is dependent upon a number of factors. We note that the G8 Share Offer Bidder's Statement indicates that Affinity Shareholders may be able to choose roll-over relief in relation to the disposal of Affinity Shares as a consequence of acceptance of the G8 Share Offer. We recommend that Affinity Shareholders obtain their own tax advice as to whether or not the roll-over is available and the consequences of the roll-over for the particular shareholder.

In summary, roll-over relief may be available where:

- you accept the G8 Share Offer;
- the exchange of Affinity Shares for G8 Shares is in consequence of a single arrangement that results in G8 acquiring 80% or more of the voting shares in Affinity;
- you acquired the Affinity Shares on or after 20 September 1985 and, but for the roll-over, a capital gain would arise from the exchange;
- the arrangement must be one in which at least all owners of voting shares in Affinity could participate and such participation must be on substantially the same terms for all owners of interests of a particular type in Affinity;
- the relevant Affinity Shareholders are Australian residents or otherwise hold their shares as taxable Australian property; and
- the relevant Affinity Shareholder chooses that the roll-over applies.

If G8 does not acquire 80% or more of the voting shares in Affinity, then roll-over relief will not be available.

The G8 Share Offer Bidder's Statement notes that, in certain circumstances, it may be necessary for G8 to make a joint election with an Affinity Shareholder in order for CGT rollover relief to apply.

To choose CGT roll-over relief, an Affinity Shareholder must make a choice before lodging an income tax return for the tax year in which the G8 Share Offer is accepted. The manner in which the Affinity Shareholder prepares the income tax return will be evidence of the choice (ie no notice is required to be lodged with the Australian Taxation Office).

All Affinity Shareholders, and particularly those not covered by this outline as noted above, should obtain their own independent professional taxation advice as to whether and how a roll-over election should be made.

9 TAXATION CONSEQUENCES (CONT)

(b) Ownership of G8 Shares

The tax consequences of Affinity Shareholders owning G8 Shares should be substantially the same as the consequences of owning Affinity Shares.

(c) Dividends in relation to G8 Shares

If you accept the G8 Share Offer, during the period which you hold G8 Shares you may receive dividends which may be either franked or unfranked (subject to the terms of the G8 Shares in relation to the entitlement to receive dividends). The dividends, grossed up for any imputation (franking) credits, must be included in your assessable income and you will receive a tax offset (rebate) equal to the imputation credit included in their income. There are rules that limit the availability of imputation credits in certain circumstances (eg you are generally required to have held your G8 Shares at risk for at least 45 days). These rules are complex and you should consult your independent professional taxation adviser regarding their operation.

In some circumstances, to the extent that you have excess imputation credits (ie over and above the taxpayer's tax liability for the relevant tax year), you may be entitled to a refund of the excess amount. Again, you should consult your independent professional taxation adviser in this regard.

(d) Disposal of G8 Shares

The income tax consequences of any disposal of G8 Shares will generally be the same as for the disposal of Affinity Shares as described above, subject to the differences outlined below.

(i) G8 Shares acquired where roll-over election was made

Where a choice to apply roll-over relief was made by an Affinity Shareholder in respect of the disposal of Affinity Shares, the cost base of the G8 Shares issued to the Affinity Shareholder under the G8 Share Offer is equal to the cost base of the Affinity Shares that were exchanged for the G8 Shares which will be apportioned across the G8 Shares on a reasonable basis. Affinity Shareholders that are individuals or complying superannuation entities may determine whether the G8 Shares have been held for at least 12 months for the purpose of applying the CGT discount in relation to any capital gain as a result of disposing of the G8 Shares by reference to the date that they acquired the Affinity Shares. In such cases, if the combined period during which the Affinity Shareholder held the Affinity Shares and the G8 Shares is at least 12 months, the Affinity Shareholder may be entitled to apply the CGT discount in respect of the disposal of the G8 Shares.

(ii) G8 Shares acquired where roll-over relief does not apply

Where roll-over does not apply to the disposal of Affinity Shares, the cost base of the G8 Shares which are received in exchange for those Affinity Shares is the market value of Affinity Shares at the date of acceptance of the G8 Share Offer.

9.4 Transfer taxes on G8 Offers

No stamp duty or GST is payable on the transfer of Affinity Shares as a result of accepting either of the G8 Offers. You may, however, be charged GST by third parties on incidental costs incurred (for example, brokerage fees) if you decide to accept either of the G8 Offers.

10 OTHER MATERIAL INFORMATION

10.1 Continuous disclosure

Affinity is a disclosing entity under the Corporations Act and subject to regular reporting and disclosure obligations under the Corporations Act and the Listing Rules. These obligations require Affinity to notify ASX of information about specified matters and events as they occur for the purpose of making that information available to the market. In particular, Affinity has an obligation (subject to limited exceptions) to notify ASX immediately on becoming aware of any information which a reasonable person would expect to have a material effect on the price or value of Affinity Shares.

Copies of the documents filed with ASX are available from the ASX website at www.asx.com.au and Affinity's website at www.affinityeducation.com.au.

10.2 Latest financial results and change of position

Affinity's last published financial statements are the Half Year Results, which were lodged with ASX on 18 August 2015.

Except as disclosed in this Target's Statement, Your Directors are not aware of any material change to Affinity's financial position as disclosed in the Half Year Results.

10.3 Issued capital

As at 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), the issued capital of Affinity consisted of 231,451,639 Affinity Shares.

10.4 Substantial Holders

As at 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), based on disclosures made by Substantial Holders to Affinity under section 671B of the Corporations Act, there are four Substantial Holders in Affinity:

Substantial Holder	Number of Affinity Shares	Voting Power
G8	46,051,790	19.89%
Renaissance Smaller Companies Pty Limited	19,186,500	8.29%
Argo Investments Limited (and its Associate Mr Jason Beddow)	15,459,510	6.68%
Affinity[47]	12,443,305	5.38%

47 Affinity has the power to control the disposal of Affinity Shares the subject of voluntary restriction deeds entered into by Affinity and the parties set out in Annexure A of the substantial holding notice dated 15 June 2015, which gives rise to a Relevant Interest under section 608(1) of the Corporations Act. All voluntary restriction deeds are on the same terms other than the name of the shareholder and number of shares. Under the voluntary restriction deeds, for the 24-month period commencing on the date on which quotation of Affinity Shares on ASX commenced, the relevant Affinity Shareholders must not: sell, transfer or otherwise dispose of, or agree or offer to sell, transfer or otherwise dispose of, the restricted securities; or do, or omit to do, any act if the act or omission would have the effect of transferring effective ownership or control of the restricted securities. However, these restrictions cease to apply to the extent necessary to allow: the relevant Affinity Shareholders to accept a takeover bid where holders of at least 50% of the bid class securities that are not subject to escrow have accepted the takeover bid and the bid becomes unconditional; or the restricted securities to be transferred or cancelled as part of a scheme of arrangement.

OTHER MATERIAL INFORMATION (CONT)

10.5 Interests of Your Directors

(a) Interests of Your Directors in securities in Affinity

As at 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), Your Directors had made the following disclosures to ASX of their Relevant Interests in securities in Affinity:

Director	Number of Affinity Shares	Number of Affinity Performance Rights
Stuart Bruce James	4,473,525 Affinity Shares	Nil
Justin Michael Laboo	269,500 Affinity Shares	576,922 Affinity Performance Rights
Stephanie Jane Daveson	52,500 Affinity Shares	Nil
Jeffrey Ian Forbes	48,334 Affinity Shares	Nil
Gabriel Anna Giufre	3,799,759 Affinity Shares	335,462 Affinity Performance Rights
Total	8,643,618 Affinity Shares	912,384 Affinity Performance Rights

As at 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), Your Directors had a Relevant Interest in approximately 3.73% of the total issued Affinity Shares.

Each of Your Directors intends to **REJECT** both of the G8 Offers in respect of the Affinity Shares which they own or control.

(b) Dealings by Your Directors in Affinity Shares

None of Your Directors has acquired or disposed of a Relevant Interest in any Affinity Shares in the four month period ending on the date immediately before the date of this Target's Statement.

(c) Your Directors' interests or dealings in G8 securities

None of Your Directors or any of their respective Associates:

- has any Relevant Interest in the securities of G8 or any Related Body Corporate of G8; or
- has acquired or disposed of any securities of G8 or any Related Body Corporate of G8 in the four month period ending on the date immediately before the date of this Target's Statement.

(d) Benefits in connection with retirement from office

No person has been or will be given any benefit (other than a benefit which can be given without member approval under the Corporations Act) in connection with the retirement of that person, or someone else, from a board or managerial office of Affinity or any Related Body Corporate of Affinity, other than as follows:

Person	Benefit
Justin Michael Laboo	In the event of the termination of Mr Laboo's employment by Affinity, Mr Laboo will be entitled to a payment equivalent to 12 months salary.
Gabriel Anna Giufre	In the event of the termination of Ms Giufre's employment by Affinity, Ms Giufre will be entitled to a payment equivalent to 12 months salary.
Paul Cochrane	In the event of the termination of Mr Cochrane's employment by Affinity, Mr Cochrane will be entitled to a payment equivalent to 11 months salary.

(e) Agreements connected with or conditional on the G8 Offers

There are no agreements made between any of Your Directors and any other person in connection with, or conditional upon, the outcome of the G8 Offers other than in their capacity as an Affinity Shareholder.

(f) Interests of Your Directors in contracts with G8

None of Your Directors has any interests in any contracts with G8 or any Related Body Corporate of G8.

OTHER MATERIAL INFORMATION (CONT)

10.6 Impact of G8 Offers on financing arrangements and material contracts

(a) Financing arrangements

The Acquisition Facility contains a consent to change of control provision which, if not obtained, may result in a breach of the Acquisition Facility and allow CBA to terminate the Acquisition Facility. As at 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), Your Directors were not aware of any member of the Affinity Group receiving written notice from CBA indicating that CBA would not consent to any change of control resulting from the G8 Offers.

(b) Leases

Leases to which members of the Affinity Group are a party contain lessor consent to change of control provisions which, if not complied with, may result in a breach of the relevant lease and allow the lessor to terminate the lease. As at 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), Your Directors were not aware of any member of the Affinity Group receiving written notice from a lessor to any of these leases indicating that they would not consent to any change of control resulting from the G8 Offers.

(c) Provider and service approvals for childcare centres

Affinity has certain approvals under the Education and Care Services National Law to operate childcare centres. A change of control of itself is not expected to impact any of these approvals.

10.7 Impact of G8 Offers on employee incentive arrangements

The Affinity Equity Incentive Plan is a broad plan under which the Board can offer Affinity securities, including Affinity Performance Rights.

As at 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), the Board had issued a total of 1,327,141 Affinity Performance Rights. If G8 obtains Voting Power of more than 50% of the total issued Affinity Shares:

- the Affinity Performance Rights will be freed of any disposal restrictions or vesting conditions; and
- Affinity must issue to the holders of Affinity Performance Rights one Affinity Share for each Affinity Performance Right held.

10.8 Material litigation

As at 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), Your Directors were not aware of any current or potential litigation of a material nature against any member of the Affinity Group.

10.9 Related party transactions

The Half Year Results were lodged with ASX on 18 August 2015. The Half Year Results included disclosure in relation to transactions which had been entered into by Affinity with Related Parties. As at 20 August 2015 (being the latest practicable date prior to the lodgement of this Target's Statement with ASIC), except as disclosed in this Target's Statement, Your Directors were not aware of any material change in relation to this disclosure.

10.10 Alternatives to the G8 Offers

Your Directors are currently in discussions with, and have received proposals from, other interested parties which may result in a superior proposal for Affinity Shareholders.

Your Directors are continuing to negotiate these alternative proposals, with the aim of reaching agreement on a superior proposal that Affinity directors can recommend to Affinity Shareholders.

If you accept either of the G8 Offers, you will miss out on the chance for higher value under any alternative proposal.

You have until 7pm (Sydney time) on 28 September 2015 (the scheduled closing date of the G8 Offers) to decide what to do in relation to the G8 Offers.

Your Directors will provide an update as to any alternative proposals by no later than the morning of 21 September 2015.[48]

YOUR DIRECTORS RECOMMEND THAT YOU TAKE NO ACTION UNTIL YOUR DIRECTORS PROVIDE THIS UPDATE.

48 Affinity will announce this update to ASX and on the Affinity website (www.affinityeducation.com.au) and will send this update by mail or email to all Affinity Shareholders.

10 OTHER MATERIAL INFORMATION (CONT)

10.11 Compulsory acquisition

G8 has indicated in section 8 of its G8 Share Offer Bidder's Statement and section 6 of the G8 Cash Offer Bidder's Statement that if it satisfies the required thresholds, it intends to compulsorily acquire any outstanding Affinity Shares.

G8 will be entitled to compulsorily acquire any Affinity Shares in respect of which it has not received an acceptance on the same terms as the G8 Offers if, during or at the end of the G8 Offer Periods:

- G8 and its Associates have a Relevant Interest in at least 90% (by number) of the total issued Affinity Shares; and
- G8 and its Associates have acquired at least 75% (by number) of the Affinity Shares that G8 offered to acquire.

If these thresholds are met, G8 will be able to proceed to compulsory acquisition in accordance with the provisions of the Corporations Act. G8 will have one month after the end of the G8 Offer Periods within which to give compulsory acquisition notices to Affinity Shareholders who have not accepted the G8 Offers. Affinity Shareholders have statutory rights to challenge the compulsory acquisition, but a successful challenge will require the relevant Affinity Shareholder to establish to the satisfaction of a court that the terms of the compulsory acquisition do not represent 'fair value' for their Affinity Shares. If compulsory acquisition occurs, Affinity Shareholders who have their Affinity Shares compulsorily acquired are likely to be issued their consideration approximately five to six weeks after the compulsory acquisition notices are dispatched to them.

It is also possible that G8 will, at some time after the end of the G8 Offers, become the beneficial holder of 90% of the total issued Affinity Shares. G8 would then have rights to compulsorily acquire the Affinity Shares not owned by it within six months of becoming the holder of 90% of the total issued Affinity Shares. The price which G8 would have to pay to compulsorily acquire Affinity Shares under this procedure would have to be considered in a report of an independent expert nominated by ASIC.

10.12 Minority ownership consequences

If G8 acquires a Relevant Interest in more than 50% but less than 90% of the total issued Affinity Shares, G8 will become a majority Affinity Shareholder, and the Affinity Shareholders who do not accept the G8 Offers will become minority Affinity Shareholders. This will have a number of possible implications, including:

- G8 will be in a position to pass an ordinary resolution at a general meeting of Affinity. This would enable G8 to control the composition of the Board and senior management, determine Affinity's dividend policy and control the strategic direction of the businesses of Affinity and its subsidiaries;
- the Affinity Share price may fall following the end of the G8 Offer Periods;
- the liquidity of Affinity Shares may be lower than at present, and Affinity could be fully or partially removed from certain market indices due to a lack of free float or liquidity;
- G8 has indicated in the G8 Share Offer Bidder's Statement and the G8 Cash Offer Bidder's Statement that it will seek to have Affinity removed from the official list of ASX.[49] If this occurs, Affinity Shares would not be able to be bought or sold on the ASX; and
- if G8 acquires 75% or more of the total issued Affinity Shares, G8 will be in a position to pass a special resolution at a general meeting of Affinity. This would enable G8 to, among other things, change Affinity's constitution.

49 G8 Share Offer Bidder's Statement, page 18; and G8 Cash Offer Bidder's Statement, page 37.

10 OTHER MATERIAL INFORMATION (CONT)

10.13 Consents

Each of the following persons has given and has not, before the date of this Target's Statement, withdrawn their consent to be named in this Target's Statement in the form and context in which they are named:

- Luminis Partners Pty Ltd, as financial adviser; and
- Corrs Chambers Westgarth, as legal adviser.

Lonergan Edwards & Associates Limited has given and has not, before the date of this Target's Statement, withdrawn its consent to be named in this Target's Statement as Independent Expert, and to the inclusion of the Independent Expert's Report and statements said to be based on statements made in the Independent Expert's Report in the form and context in which the statements are included and to all references in this Target's Statement to those statements in the form and context in which they are included.

Each person named above as having given their consent to the inclusion of a statement or to being named in this Target's Statement:

- does not make, or purport to make, any statement in this Target's Statement or any statement on which a statement in this Target's Statement is based other than, in the case of a person referred to above as having given their consent to the inclusion of a statement, a statement included in this Target's Statement with the consent of that person; and
- to the maximum extent permitted by law, expressly disclaims and takes no responsibility for any part of this Target's Statement, other than a reference to their name and, in the case of a person referred to above as having given their consent to the inclusion of a statement, any statement or report which has been included in this Target's Statement with the consent of that person.

As permitted by ASIC Class Order 13/521, this Target's Statement contains fair representations of statements made, or based on statements made, in documents lodged with ASIC or ASX by G8 without G8's consent. Any Affinity Shareholder who would like to receive a copy of any of these documents should contact the Affinity Shareholder Information Line on 1300 911 275. Affinity, on request during the G8 Offer Periods, will provide within two Business Days of the request, a copy of the document free of charge to any Affinity Shareholder.

In addition, as permitted by ASIC Class Order 13/523, this Target's Statement contains certain statements:

- fairly representing a statement by an official person; or
- from a public official document or a published book, journal or comparable publication,

without the consent of the persons to whom such statements are attributed.

In addition, as permitted by ASIC Class Order 07/429, this Target's Statement contains security price trading data sourced from IRESS without IRESS's consent.

10 OTHER MATERIAL INFORMATION (CONT)

10.14 No other material information

This Target's Statement is required to include all the information that Affinity Shareholders and their professional advisers would reasonably require to make an informed assessment whether to accept the G8 Offers, but:

- only to the extent to which it is reasonable for investors and their professional advisers to expect to find this information in this Target's Statement; and
- only if the information is known to any of Your Directors.

Your Directors are of the opinion that the information that Affinity Shareholders and their professional advisers would reasonably require to make an informed assessment whether to accept the G8 Offers is:

- the information contained in the G8 Bidder's Statements (to the extent that the information is not inconsistent or superseded by information in this Target's Statement);
- the information contained in Affinity's releases to ASX, and in the documents lodged by Affinity with ASIC before the date of this Target's Statement; and
- the information contained in this Target's Statement.

Your Directors have assumed, for the purposes of preparing this Target's Statement, that the information in the G8 Bidder's Statements is accurate (unless they have expressly indicated otherwise in this Target's Statement). However, Your Directors do not take any responsibility for the contents of the G8 Bidder's Statements and are not to be taken as endorsing, in any way, any or all statements contained in it.

In deciding what information should be included in this Target's Statement, Your Directors have had regard to:

- the nature of Affinity Shares;
- the matters that Affinity Shareholders may reasonably be expected to know;
- the fact that certain matters may reasonably be expected to be known to Affinity Shareholders' professional advisers; and
- the time available to Affinity to prepare this Target's Statement.

11 GLOSSARY AND INTERPRETATION

11.1 Glossary

In this Target's Statement defined terms have the meanings set out below:

Term	Meaning
$	Australian dollar.
Acquisition Facility	the acquisition debt facility provided by CBA.
Affinity	Affinity Education Group Limited ABN 37 163 864 195.
Affinity Equity Incentive Plan	the equity incentive plan adopted by the Board, the terms and conditions of which are summarised in the notice of Affinity's 2015 annual general meeting dated 17 March 2015.
Affinity Group	Affinity and its Related Bodies Corporate.
Affinity Performance Right	a performance right issued under the Affinity Equity Incentive Plan.
Affinity Share	a fully paid ordinary share in the capital of Affinity.
Affinity Shareholder	a registered holder of one or more Affinity Shares.
Affinity Shareholder Information Line	the telephone line established by Affinity to answer Affinity Shareholders' questions regarding the G8 Offers. The telephone number is 1300 911 275.
ASIC	Australian Securities and Investments Commission.
Associate	has the meaning given in the Corporations Act.
ASX	ASX Limited ABN 98 008 624 691 or the securities exchange operated by it, as appropriate.
Board	the board of directors of Affinity.
Business Day	a day on which banks are open for business in Brisbane, excluding a Saturday, Sunday or public holiday.
Cannacord Genuity	has the meaning given in the G8 Cash Offer Bidder's Statement.
CBA	Commonwealth Bank of Australia.
CGT	capital gains tax.
Corporations Act	the *Corporations Act 2001* (Cth) (as modified or varied by ASIC).
Entitlement Offer	the entitlement offer announced by Affinity in March 2015.
G8	G8 Education Limited ABN 95 123 828 553.
G8 Bidder's Statements	the G8 Share Offer Bidder's Statement and the G8 Cash Offer Bidder's Statement.
G8 Board	the board of directors of G8.
G8 Cash Offer	the offer by G8 for the Affinity Shares, which offer is contained in the G8 Cash Offer Bidder's Statement.
G8 Cash Offer Bidder's Statement	the bidder's statement of G8 relating to the G8 Cash Offer dated 3 August 2015.
G8 Cash Offer Consideration	$0.80 for every Affinity Share.
G8 Cash Offer Period	the period during which the G8 Cash Offer will remain open for acceptance in accordance with the section titled "Key Dates" of the G8 Cash Offer Bidder's Statement (unless extended or withdrawn).
G8 Directors	a current director of G8.

11 GLOSSARY AND INTERPRETATION (CONT)

Term	Meaning
G8 Offer Periods	the G8 Cash Offer Period and the G8 Share Offer Period.
G8 Offers	the G8 Cash Offer and the G8 Share Offer.
G8 Share Offer	the offer by G8 for the Affinity Shares, which offer is contained in the G8 Share Offer Bidder's Statement.
G8 Share Offer Bidder's Statement	the bidder's statement of G8 relating to the G8 Share Offer dated 20 August 2015.
G8 Share Offer Consideration	1 G8 Share for every 4.25 Affinity Shares.
G8 Share Offer Period	the period during which the G8 Share Offer will remain open for acceptance in accordance with the section titled "Key Dates" of the G8 Share Offer Bidder's Statement (unless extended or withdrawn).
G8 Share	a fully paid ordinary share in the capital of G8.
G8 Shareholders	a registered holder of one or more G8 Shares.
GST	goods and services tax.
Half Year Results	Affinity's financial statements for the half year ended 30 June 2015, which were lodged by Affinity with ASX on 18 August 2015
Independent Expert	Lonergan Edwards & Associates Limited.
Independent Expert's Report	the report by the Independent Expert, a copy of which is contained in Annexure A.
Listing Rules	the listing rules of ASX.
Related Party	has the meaning given in the Corporations Act.
Related Body Corporate	has the meaning given in the Corporations Act.
Relevant Interest	has the meaning given in the Corporations Act.
Retail Offer Booklet	the retail offer booklet lodged by Affinity with ASX on 17 March 2015.
Substantial Holder	a person who has a Substantial Holding in Affinity.
Substantial Holding	has the meaning given in the Corporations Act.
Target's Statement	this document (including the annexure), being the target's statements issued by Affinity under Part 6.5 Division 3 of the Corporations Act, comprising: • the target's statement in response to the G8 Share Offer and the G8 Share Offer Bidder's Statement as required under item 10 of section 633(1) of the Corporations Act; and • the target's statement in response to the G8 Cash Offer and the G8 Cash Offer Bidder's Statement, as required under item 9 of section 635(1) of the Corporations Act.
Voting Power	has the meaning given in the Corporations Act.
VWAP	volume-weighted average price.
Your Directors	the current directors of Affinity, who at the date of this Target's Statement are Mr Stuart James, Mr Justin Laboo, Ms Gabriel Giufre, Mr Jeff Forbes and Ms Stephanie Daveson.

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GLOSSARY AND INTERPRETATION (CONT)

11.2 Interpretation

In this Target's Statement:

(a) Words of any gender include all genders.

(b) Words importing the singular include the plural and vice versa.

(c) An expression importing a person includes any company, partnership, joint venture, association, corporation or other body corporate and vice versa.

(d) A reference to a section, clause, annexure and schedule is a reference to a section of, clause of and an annexure and schedule to this Target's Statement as relevant.

(e) A reference to any legislation includes all delegated legislation made under it and amendments, consolidations, replacements or re-enactments of any of them.

(f) Headings and bold type are for convenience only and do not affect the interpretation of this Target's Statement.

(g) A reference to time is a reference to Sydney time (unless the context requires otherwise).

12 AUTHORISATION

This Target's Statement has been approved by a resolution passed by Your Directors on 21 August 2015.

Signed for and on behalf of Affinity:

Date

24 August 2015

ANNEXURE A
INDEPENDENT EXPERT'S REPORT

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The Independent Directors
Affinity Education Group Limited
Level 14, 100 Creek Street
Brisbane QLD 4000

20 August 2015

Subject: Takeover offers for Affinity Education Group Limited

Dear Independent Directors

Introduction

Overview of the Offers

1 On 3 July 2015, G8 Education Limited (G8 Education) announced its intention to make an off-market takeover offer for all the ordinary shares that it did not already own in Affinity Education Group Limited (Affinity or the Company)[1] at an offer price of one fully paid ordinary share in G8 Education for every 4.61 fully paid ordinary shares in Affinity (Scrip Offer).

2 On 3 August 2015, G8 Education increased its off-market takeover offer to one fully paid ordinary share in G8 Education for every 4.25 fully paid ordinary shares in Affinity (Revised Scrip Offer). Separately on 3 August 2015, G8 Education also announced an on-market takeover offer for all the Affinity shares that it did not already own for consideration of $0.80 per share (Cash Offer). The Cash Offer will be funded by G8 Education from SGD155 million[2] in newly issued unsecured notes and can only be accepted by Affinity shareholders by selling their Affinity shares on market at $0.80 per share.

3 It should be noted that pursuant to s651A of the *Corporations Act 2001 (Cth)* (Corporations Act), if (and only if) G8 Education acquires Affinity shares for cash outside of the Revised Scrip Offer during the offer period (e.g. under the Cash Offer or otherwise), it must also provide all Affinity shareholders that have accepted the Revised Scrip Offer with the opportunity to elect to receive a cash amount equal to the highest cash price paid in that offer period in lieu of G8 Education shares. G8 Education has until 14 days after the close of the Revised Scrip Offer to provide Affinity shareholders that accepted the Revised Scrip Offer with their right to make the election. Affinity shareholders will have one month from the date of the notice to make the election.

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1 On 2 and 3 July 2015, G8 Education acquired some 46.1 million fully paid shares in Affinity, representing approximately 19.89% of Affinity's ordinary shares on issue.

2 Singapore dollars (SGD).

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4 G8 Education has declared both the Revised Scrip Offer and Cash Offer unconditional and final. We collectively refer to the Revised Scrip Offer and Cash Offer in this document as the "Offers".

Affinity

5 Affinity is a provider of education and child care services in Australia to children aged six weeks to 12 years old. The Company provides long day care, before and after school care and occasional care. Affinity is the second largest Australian Securities Exchange (ASX) listed child care operator with some 161 centres and a daily licensed capacity of 12,682 children as at 30 June 2015. Its portfolio of child care centres is spread across Queensland (QLD), New South Wales (NSW), Victoria (VIC), Western Australia (WA), the Northern Territory (NT) and the Australian Capital Territory (ACT).

G8 Education

6 G8 Education is a child care centre operator providing developmental and educational child care services in Australia and Singapore. The company provides a range of child care service activities and is the largest ASX listed child care operator. In Australia, G8 Education owns some 457 centres with a daily licensed capacity of 33,402 children as at 30 June 2015[3]. Its portfolio of child care centres is spread across NSW, VIC, QLD, WA, South Australia (SA), the ACT and Tasmania (TAS). In Singapore, G8 Education owns some 18 centres and has franchised a further 37 centres[4].

Purpose of report

7 While there is no statutory requirement for Affinity to obtain an independent expert's report (IER), the Independent Directors of Affinity have requested Lonergan Edwards & Associates Limited (LEA) to prepare an IER stating whether, in LEA's opinion, the Offers are "fair and reasonable".

8 LEA is independent of Affinity and G8 Education and has no other involvement or interest in the outcome of the Offers, other than the preparation of this report.

Summary of opinion

9 LEA has concluded that the Offers are neither fair nor reasonable. We have arrived at this conclusion for the reasons set out below.

Valuation of Affinity

10 LEA has valued 100% of the ordinary shares in Affinity at between \$0.92 and \$1.00 per share, as summarised below:

3 Source: Replacement Bidder's Statement dated 20 August 2015.

4 Source: Replacement Bidder's Statement dated 20 August 2015.

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Affinity – valuation summary	Paragraph	Low $m	High $m
EBITA for valuation purposes	194	37.1	37.1
EBITA multiple	217	6.5	7.0
Enterprise value		241.2	259.7
Other assets / (liabilities)	227	(0.3)	-
Net debt	229	(27.5)	(27.5)
Equity value – controlling interest basis		213.4	232.2
Number of shares on issue (million)(1)	232	232.8	232.8
Affinity value per share – controlling interest basis ($)		**0.92**	**1.00**

Note:
1 Assuming the exercise of 1.3 million executive performance rights.

Assessment of fairness

11 Pursuant to Australian Securities & Investments Commission (ASIC) Regulatory Guideline 111 – *Content of expert reports* (RG 111), an offer is "fair" if:

"The value of the offer price or consideration is equal to or greater than the value of the securities the subject of the offer."

12 In the case of Affinity, the value of the consideration to be received by Affinity shareholders is dependent on (and may vary according to) whether shareholders elect to accept the Revised Scrip Offer or the Cash Offer. We have therefore provided a comparison of each of these alternatives with our assessed value of Affinity shares on a 100% controlling interest basis.

13 The relevant comparison for Affinity shareholders electing to accept the Revised Scrip Offer is shown below:

Comparison of Revised Scrip Offer consideration and Affinity share value	Low $ per share	High $ per share	Mid-point $ per share
Value of Revised Scrip Offer consideration(1)	0.73	0.80	0.77
Value of 100% of ordinary shares in Affinity	0.92	1.00	0.96
Extent to which the Revised Scrip Offer consideration is less than the value of Affinity shares	(0.19)	(0.20)	(0.19)

Note:
1 It should be noted that, if (and only if) G8 Education acquires Affinity shares for cash outside of the Revised Scrip Offer during the offer period (e.g. under the Cash Offer or otherwise), it must also provide all Affinity shareholders that have accepted the Revised Scrip Offer with the opportunity (during a short period of time subsequent to the close of the Revised Scrip Offer) to elect to receive a cash payment equal to the highest cash price paid during the offer period in lieu of G8 Education shares.

14 As the Revised Scrip Offer consideration is less than our assessed value of 100% of the ordinary shares in Affinity, in our opinion, the Revised Scrip Offer is not fair.

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15 The relevant comparison for Affinity shareholders electing to accept the Cash Offer is shown below:

Comparison of Cash Offer consideration and Affinity share value	Low $ per share	High $ per share	Mid-point $ per share
Value of Cash Offer consideration[1]	0.80	0.80	0.80
Value of 100% of ordinary shares in Affinity	0.92	1.00	0.96
Extent to which the Cash Offer consideration is less than the value of Affinity shares	(0.12)	(0.20)	(0.16)

Note:
1 No allowance has been made for any brokerage costs that will be incurred as a result of selling Affinity shares on market pursuant to the Cash Offer.

16 As the Cash Offer consideration is less than our assessed value of 100% of the ordinary shares in Affinity, in our opinion, the Cash Offer is not fair.

Assessment of reasonableness

17 Pursuant to RG 111, an offer may be reasonable if, despite not being fair but after considering other significant factors, the expert is of the view that there are sufficient reasons for shareholders to accept the offer in the absence of any higher bid before the close of the offer.

18 In our opinion, there are a number of reasons why Affinity shareholders may wish to accept the Offers, as summarised below:

(a) in our opinion, the consideration offered under the Revised Scrip Offer and Cash Offer is likely to exceed the listed market price of Affinity shares in the absence of the Offers or a superior proposal (at least in the short-term). However, this is often the case with most takeovers as the listed market price generally reflects a portfolio rather than controlling interest value

(b) the Revised Scrip Offer provides Affinity shareholders with the opportunity to obtain an interest in a larger more diversified company in the child care sector. However, Affinity shareholders that elect to accept the Revised Scrip Offer should also note that:

(i) G8 Education's financial gearing levels may increase significantly relative to its position as at 30 June 2015 if a large proportion of Affinity shareholders elect to receive cash (rather than scrip) under the Offers.

(ii) should G8 Education acquire less than 90% of Affinity:

– G8 Education may not be able to realise all estimated synergy benefits

– G8 Education will not have access to their pro-rata share of the full underlying cash flow generated by Affinity

– Affinity shareholders will not be granted capital gains tax roll-over relief unless G8 Education acquires at least 80% of Affinity.

(c) the Cash Offer provides all Affinity shareholders with the ability to immediately realise their shareholdings for cash should they wish to do so

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(d) should G8 Education increase its ownership interest in Affinity to above 50% but less than 90% then G8 Education will control Affinity including its day-to-day management, strategic direction and level of dividend payments[5]. Depending on the level of shareholding obtained, G8 Education may also seek to delist Affinity from the ASX. That said, in our view, there is a reasonable prospect that G8 Education will make a further takeover offer at a later date in order to obtain 100% control of Affinity[6]. However, the prospect of a future takeover offer is inherently uncertain as to whether it arises, the timing thereof and the related offer price.

19 While we acknowledge these advantages (particularly for shareholders who expect to have to realise their Affinity shares in the short-term), in our opinion, they do not provide sufficient reasons for shareholders to accept the Revised Scrip Offer or the Cash Offer as the consideration provided under each is materially below our assessed valuation range:

Comparison of mid-points of the offer consideration and Affinity share value	Revised Scrip Offer $ per share	Cash Offer $ per share
Mid-point of assessed value of consideration	0.77	0.80
Mid-point of assessed value of Affinity shares	0.96	0.96
Discount of the Offers to assessed value of Affinity (%)	19.8	16.7

20 Furthermore, we expect that G8 Education will be able to generate significant synergies as a result of acquiring 100% of Affinity. In our opinion, an appropriate share of the value of these synergies is not reflected in either the Revised Scrip Offer or Cash Offer consideration.

21 Accordingly, we have concluded that the Offers are also not reasonable.

Likelihood of an alternative offer

22 Affinity shareholders should also note that G8 Education has declared its Offers final and accordingly they will not be increased.

23 Affinity's Independent Directors have advised that they are currently in discussions with, and have received indicative non-binding acquisition proposals from other interested parties which may result in a superior proposal for Affinity shareholders. Affinity has indicated that it will provide an update as to the status of these negotiations by no later than 21 September 2015 (i.e. prior to the close of the Revised Scrip Offer and the Cash Offer).

24 However, it should also be noted that G8 Education's 19.89% interest in Affinity may act as a deterrent to other bidders because:

(a) they will be unable to acquire 100% of Affinity, by way of a takeover offer, unless G8 Education agrees to sell its holding

5 Affinity announced on 17 April 2015 an intention to declare a maiden dividend for the financial year ending 31 December 2015. This intention was reaffirmed by Affinity on 18 August 2015.

6 We note that Affinity received a number of unsolicited approaches from G8 Education prior to the announcement of G8 Education's intention to make a takeover offer for the Company.

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(b) it would be difficult, from a practical perspective, to acquire 100% of Affinity, by way of a scheme of arrangement, given the size of G8 Education's current interest in Affinity.

25 In our opinion, it is therefore possible, but at this stage, highly uncertain as to whether any superior offer is likely to be made for Affinity prior to the close of the Offers.

General

26 In preparing this report we have considered the interests of Affinity shareholders as a whole. Accordingly, this report only contains general financial advice and does not consider the personal objectives, financial situations or requirements of individual shareholders.

27 The taxation consequences of accepting the Revised Scrip Offer or the Cash Offer depend on the individual circumstances of each investor. Shareholders should read the taxation advice set out in the Bidder's Statements and the Target's Statement and should consult their own professional adviser if in doubt as to the taxation consequences of the Revised Scrip Offer and the Cash Offer.

28 The ultimate decision whether to accept the Revised Scrip Offer or the Cash Offer should be based on each shareholders' assessment of their own circumstances, including their risk profile, liquidity preference, tax position and expectations as to value and future market conditions. Shareholders considering their response to the Revised Scrip Offer or the Cash Offer should be aware that our assessed value of Affinity shares has been determined having regard to their medium / longer term prospects. Given the current market conditions individual shareholders may have a different time horizon.

29 If shareholders are in doubt about the action they should take in relation to the Revised Scrip Offer or the Cash Offer or matters dealt with in this report, shareholders should seek independent professional advice.

30 For our full opinion on the Offers, and the reasoning behind our opinion, we recommend that Affinity shareholders read the remainder of our report.

Yours faithfully

Craig Edwards
Authorised Representative

Nathan Toscan
Authorised Representative

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I Outline of the Offers

31 On 3 July 2015, G8 Education announced its intention to make an off-market takeover offer for all the ordinary shares that it did not already own in Affinity[7] at an offer price of one fully paid ordinary share in G8 Education for every 4.61 fully paid ordinary shares in Affinity (Scrip Offer).

32 On 3 August 2015, G8 Education increased its off-market takeover offer to one fully paid ordinary share in G8 Education for every 4.25 fully paid ordinary shares in Affinity (Revised Scrip Offer). Separately on 3 August 2015, G8 Education also announced an on-market takeover offer for all the Affinity shares that it did not already own for consideration of $0.80 per share (Cash Offer). The Cash Offer will be funded by G8 Education from SGD155 million in newly issued unsecured notes and can only be accepted by Affinity shareholders by selling their Affinity shares on market at $0.80 per share.

33 It should be noted that pursuant to s651A of the Corporations Act, if (and only if) G8 Education acquires Affinity shares for cash outside of the Revised Scrip Offer during the offer period (e.g. under the Cash Offer or otherwise), it must also provide all Affinity shareholders that have accepted the Revised Scrip Offer with the opportunity to elect to receive a cash amount equal to the highest cash price paid in that offer period in lieu of G8 Education shares. G8 Education has until 14 days after the close of the Revised Scrip Offer to provide Affinity shareholders that accepted the Revised Scrip Offer with their right to make the election. Affinity shareholders will have one month from the date of the notice to make the election.

34 G8 Education has declared both the Revised Scrip Offer and Cash Offer unconditional and final. We collectively refer to the Revised Scrip Offer and Cash Offer in this document as the "Offers".

7 On 2 and 3 July 2015, G8 Education acquired some 46.1 million fully paid shares in Affinity, representing approximately 19.89% of Affinity's ordinary shares on issue.

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II Scope of our report

Purpose

35 While there is no statutory requirement for Affinity to obtain an IER, the Independent Directors of Affinity have requested LEA to prepare an IER stating whether, in LEA's opinion, the Offers are "fair and reasonable".

36 This report has been prepared to assist the Independent Directors of Affinity in making their recommendation to Affinity shareholders in relation to the Offers and to assist the shareholders of Affinity assess the merits of the Offers. The sole purpose of this report is to set out LEA's opinion as to whether the Offers are fair and reasonable. This report should not be used for any other purpose.

37 The ultimate decision whether to accept the Revised Scrip Offer or the Cash Offer should be based on each shareholders' assessment of their own circumstances, including their risk profile, liquidity preference, tax position and expectations as to value and future market conditions. If in doubt about the Revised Scrip Offer or Cash Offer or matters dealt with in this report, shareholders should seek independent professional advice.

Basis of assessment

38 Our report has been prepared as if it was required under s640 of the Corporations Act. Consequently, in preparing our report we have given due consideration to the Regulatory Guides issued by ASIC, particularly RG 111.

39 RG 111 distinguishes "fair" from "reasonable" and considers:

(a) an offer to be "fair" if the value of the offer price or consideration is equal to or greater than the value of the securities that are the subject of the offer. A comparison must be made assuming 100% ownership of the target company

(b) an offer to be "reasonable" if it is fair. An offer may also be "reasonable" if, despite not being "fair" but after considering other significant factors, shareholders should accept the offer in the absence of any higher bid before the close of the offer.

40 Our report has therefore considered:

Fairness

(a) the market value of 100% of the shares in Affinity

(b) the value of the consideration offered by G8 Education under both the Revised Scrip Offer and Cash Offer

(c) the extent to which (a) and (b) differ (in order to assess whether the Revised Scrip Offer and Cash Offer is fair under RG 111)

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Reasonableness

(d) the extent to which a control premium is being paid to Affinity shareholders

(e) the extent to which a share of the synergies likely to arise upon an acquisition of Affinity are being shared with Affinity shareholders

(f) the listed market price of Affinity shares both prior to the announcement of G8 Education's intention to make a takeover offer and during the offer period

(g) the likely market price of Affinity shares if the Offers are not successful

(h) the position of Affinity shareholders if G8 Education acquires at least 50.1% or more but less than 90% of the Affinity shares on issue

(i) G8 Education's current shareholding in Affinity

(j) the value of Affinity to an alternative acquirer and the likelihood of an alternative offer emerging, either prior to the close of the Offers, or sometime in the future

(k) the previous unsolicited approaches received by Affinity from G8 Education and the impact of intervening events on value

(l) other qualitative and strategic issues, risks, advantages and disadvantages associated with the Offers.

Limitations and reliance on information

41 Our opinions are based on the economic, sharemarket, financial and other conditions and expectations prevailing at the date of this report. Such conditions can change significantly over relatively short periods of time.

42 Our report is also based upon financial and other information provided by Affinity. We understand the accounting and other financial information that was provided to us has been prepared in accordance with the Australian equivalents to International Financial Reporting Standards. We have considered and relied upon this information and believe that the information provided is reliable, complete and not misleading and we have no reason to believe that material facts have been withheld.

43 The information provided was evaluated through analysis, enquiry and review to the extent considered appropriate for the purpose of forming an opinion on the Offers from the perspective of Affinity shareholders. However, we do not warrant that our enquiries have identified or verified all of the matters which an audit, extensive examination or "due diligence" investigation might disclose. Whilst LEA has made what it considers to be appropriate enquiries for the purpose of forming its opinion, "due diligence" of the type undertaken by companies and their advisers in relation to (for example) prospectuses or profit forecasts is beyond the scope of an IER.

44 Accordingly, this report and the opinions expressed therein should be considered more in the nature of an overall review of the anticipated commercial and financial implications of the proposed transaction, rather than a comprehensive audit or investigation of detailed matters.

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45 An important part of the information base used in forming an opinion of the kind expressed in this report is comprised of the opinions and judgement of management of the relevant companies. This type of information has also been evaluated through analysis, enquiry and review to the extent practical. However, it must be recognised that such information is not always capable of external verification or validation.

46 We in no way guarantee the achievability of budgets or forecasts of future profits. Budgets and forecasts are inherently uncertain. They are predictions by management of future events which cannot be assured and are necessarily based on assumptions of future events, many of which are beyond the control of management. Actual results may vary significantly from forecasts and budgets with consequential valuation impacts.

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III Profile of Affinity

Overview

47 Affinity is a provider of education and child care services in Australia to children aged six weeks to 12 years old. The Company provides long day care, before and after school care and occasional care. Affinity is the second largest ASX listed child care operator with some 161 centres and a daily licensed capacity of 12,682 children as at 30 June 2015. Its portfolio of child care centres is spread across QLD, NSW, VIC, WA, the NT and the ACT.

History and strategy

48 Affinity was incorporated on 21 May 2013 as Eternal Echoes Education Limited, with its name changed to Affinity Education Group Limited on 19 September 2013. The Company listed on the ASX on 5 December 2013, raising funds to acquire 57 established child care centres (located in QLD, NSW, VIC and the NT) and the management rights for a further 11 centres (located in QLD and NSW)[8].

49 Affinity's business model is to identify, acquire, integrate and then manage child care centres within a large corporatised portfolio. The Directors of the Company believe the acquisition and subsequent corporatisation of child care centres within a single portfolio has a number of benefits:

(a) economies of scale achieved via the operation of centralised management support functions (e.g. finance, payroll, human resources)

(b) improved wage control by grouping centres into geographic clusters which can benefit from efficiencies and greater staff flexibility

(c) enhanced ability to respond to ongoing regulatory and compliance changes

(d) increased staff retention as a result of improved career path training and progression

(e) targeted group wide capital expenditure programmes to improve operating efficiencies

(f) procurement synergies as a result of economies of scale.

50 Growth in the business is expected to be achieved through:

(a) improvements in occupancy levels and general efficiencies gained from managing a large portfolio of centres

(b) the acquisition of further centres that meet the Company's acquisition parameters. Affinity's current aim is to increase the size of its portfolio by 20% to 25% per annum.

[8] Two freehold properties were also acquired. Affinity does not generally intend to acquire freehold property nor intend to undertake the development of greenfield sites. Accordingly, at the time of the acquisition it was and remains management's intention to dispose of these two sites.

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51 The following table summarises the centres acquired by Affinity since listing (not all centre acquisitions had settled as at 30 June 2015):

Affinity – acquisition history	
Date	**Acquisition**
Mar 14	• Entered into agreements to acquire 7 child care centres for $8 million
Apr 14	• Announced a 3 for 4 entitlement offer to raise $75 million and fund the acquisition of 51 child care and education centres (which cost $80 million)
Sep 14	• Entered into agreements to acquire 20 child care centres for $19 million
Dec 14	• Entered into agreements to acquire a further 16 child care centres for $45 million
Feb 15	• Entered into an agreement to acquire 8 of the Affinity managed centres for $18 million
Mar 15	• Undertook an 8 for 21 entitlement offer to raise $75 million and fund the acquisition of 9 premium child care centres for $24 million

Source: Affinity ASX announcements.

Current operations

52 Affinity currently owns and operates 161 child care centres across Australia (and manages a further six individual centres). The Company provides a range of education and child care services including long day care, before and after school care and occasional care. Affinity operates a tiered management structure as follows:

(a) **centre level** – child care centre directors are responsible for the day-to-day management of an individual child care centre

(b) **regional** – regional area managers oversee a geographic cluster of centres. Area managers provide support to centre directors, manage the allocation of staff across the cluster and report to the corporate level

(c) **corporate** – corporate level includes executives, operations, marketing, human resources, finance and business development functions. A centralised corporate model is able to achieve economies of scale through the grouping of shared services and administration functions. This enables individual centres to focus upon providing high quality child care services.

53 The current portfolio of 161 owned centres and six managed centres, which are operated under a number of different brands[9], are located across Australia as follows:

Affinity – portfolio of owned centres
As at 30 June 2015

Source: Affinity.

54 The child care portfolio is balanced between metropolitan and non-metropolitan locations with a higher weighting towards areas where households have incomes of less than $160,000. It is estimated that Affinity's portfolio is some 50% regional, 40% suburban and 10% inner metro located[10].

9 Affinity generally retains the brand names of child care centres to maintain their existing presence and goodwill.

10 Moelis & Company, *Affinity Education Group Ltd: Scenario Analysis – Trading Below Scorched Earth Assumptions – BUY*, 2 July 2015.

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55 A breakdown of the child care portfolio by licensed and configured places is set out below:

Affinity – licensed and configured places[1]	Centres	Licensed places	Configured places
QLD	78	6,707	6,308
NSW	34	2,217	2,209
VIC	23	1,943	1,908
WA	19	1,263	1,071
NT	4	306	306
ACT	3	246	246
Total	**161**	**12,682**	**12,048**

Note:
1 As at 30 June 2015. Excludes the six managed centres.
Source: Affinity.

56 Each child care centre has a maximum number of places limited by regulatory requirements, which are referred to as licensed places. However, a centre's actual capacity is based on its number of configured places, which refers to the configuration of its floor space or room (a change to the configuration of a centre may have consequential capital expenditure impacts).

57 Since listing, Affinity has acquired over 100 child care centres and accordingly integration of acquisitions is an ongoing priority for Affinity. A key component is the implementation of financial reporting software to ensure that Affinity has the ability to produce accurate seven day reports for each centre, rolling up to consolidated reports for each cluster and ultimately to the corporate level.

Financial performance

58 The financial performance of Affinity for the year ended 31 December 2014 (FY14) (separated into half years) and 6 months to 30 June 2015 (1H15) is set out below:

Affinity – statement of financial performance[1]	1H14 Reviewed $m	2H14 Reviewed $m	FY14 Audited $m	1H15 Reviewed $m
Revenue from child care centres	37.4	72.9	110.4	86.9
Management fees	0.8	0.3	1.1	0.2
Total revenue[2]	**38.2**	**73.3**	**111.5**	**87.0**
Employee benefits	(24.2)	(44.8)	(69.0)	(55.4)
Occupancy costs	(5.4)	(9.4)	(14.8)	(12.8)
Direct costs of providing services	(2.8)	(4.0)	(6.8)	(9.0)
Administration expenses	(0.8)	(2.1)	(2.9)	(1.2)
Underlying EBITDA[3]	**4.9**	**13.0**	**17.8**	**8.6**
Depreciation and software amortisation	(0.5)	(0.8)	(1.2)	(1.0)
Underlying EBITA[4]	**4.4**	**12.2**	**16.6**	**7.6**
Amortisation of acquisition intangibles	-	-	-	-
Significant items[5]	(8.3)	(8.1)	(16.3)	(6.6)
Net finance costs	-	(0.4)	(0.4)	(1.1)[6]
Profit before tax (PBT)	**(3.8)**	**3.7**	**(0.1)**	**(0.1)**
Income tax expense	(1.2)	(2.8)	(4.0)	(1.9)

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Affinity – statement of financial performance[1]	1H14 Reviewed $m	2H14 Reviewed $m	FY14 Audited $m	1H15 Reviewed $m
Net profit after tax (NPAT) as reported	**(5.0)**	**0.9**	**(4.1)**	**(2.1)**
Employee benefits / revenue from child care (%)	*64.7*	*61.4*	*62.6*	*63.8*
EBITDA margin (%)	*12.8*	*17.7*	*16.0*	*9.9*
EBITA margin (%)	*11.6*	*16.6*	*14.9*	*8.7*

Note:
1 Rounding differences may exist.
2 Excluding interest income.
3 Earnings before interest, tax, depreciation and amortisation (EBITDA).
4 Earnings before interest, tax and amortisation of acquired intangibles (EBITA).
5 Significant items comprise acquisition and integration expenses.
6 Reported interest and finance charges include merchant fees of some $0.1 million which have been reclassified as administration expenses in 1H15 only.
Source: Affinity.

59 Affinity's revenue is influenced by three fundamental drivers; number of configured places, occupancy and fees. Affinity continues to increase their number of configured places, primarily via acquisition. A portion of fees are paid by the government with parents paying the gap between the amount paid by the government and the fee charged by the centre (Section V provides further information on government policy relating to child care).

60 The major expenses incurred are employee expenses and building occupancy expenses. The child care industry is labour intensive and typically wages for staff comprise the majority of expenses. To provide certainty over building occupancy expenses, Affinity aims to enter into long-term lease agreements with annual rent increases. Affinity's average lease tenure is some 21 years as at 30 June 2015.

61 More generally, Affinity's earnings are seasonal with a greater proportion of earnings being generated in the second half of the year. The seasonality is primarily a function of changing occupancy levels during the year which are influenced by the timing of the new school year. Occupancy is often at its highest around October / November before declining over summer and again rebuilding from around February.

62 Significant items relate to acquisition costs (including stamp duty, broker commission, due diligence costs and legal fees) which are expensed through the statement of financial performance. These expenses are largely non-deductible for tax purposes. Going forward, Affinity expects acquisition costs to represent less than 10% of acquisition value.

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FY15 guidance

63 On 2 July 2015, Affinity announced that it expects underlying EBITDA for FY15 to be between \$27 million and \$32 million. This was revised to \$30 million to \$32 million on 18 August 2015. The forecast excludes one off acquisition and integration costs and is based on the expected results from the current portfolio only. However, the forecast only reflects the results of recently acquired centres from their date of acquisition and therefore does not reflect the full year impact of centres acquired during 1H15.

64 Occupancy levels are expected to be higher in the second half of the year. Average occupancy was around 72% in January 2015, increased to around 77% as at 30 June 2015 and has further improved to 81% subsequent to 30 June 2015. However, the increase in occupancy post 31 March 2015 has not been as high as that experienced in 2014. The lower end of management's underlying EBITDA forecast for FY15 assumes a continuation of this lower first half occupancy trend compared to 2014.

65 Affinity management have stated that an increase in average occupancy levels in the second half to levels consistent with that achieved in 2H14 would result in underlying EBITDA at the higher end of management's guidance.

66 Affinity management's FY15 forecast also reflects a 3% fee increase across the portfolio, which was implemented on 6 July 2015, and ongoing improvements in the wage to revenue ratio and overhead efficiencies.

Financial position

67 The financial position of Affinity as at 31 December 2014 and 30 June 2015 is set out below. The financial position as at 31 December 2014 is shown on a pro forma basis and has been adjusted to reflect acquisitions announced but not settled as at 31 December 2014, the acquisition of nine centres announced in March 2015 and the eight for 21 entitlement offer which raised \$75 million (before transaction costs):

Affinity – statement of financial position[1]	31 Dec 14 Pro forma[2] \$m	30 Jun 15 Reviewed \$m
Cash and cash equivalents	3.3	13.2
Trade and other receivables	4.5	3.2
Prepayments	1.8	0.9
Other deposits	1.4	-
Assets held for sale	0.3	0.3
Total current assets	**11.2**	**17.6**
Property, plant and equipment	10.4	12.0
Intellectual property and software	0.7	1.3
Goodwill	250.0	252.8
Deferred tax assets	6.6	6.5
Total non-current assets	**267.7**	**272.5**
Total assets	**278.9**	**290.1**
Trade and other payables	9.8	11.0
Borrowings	0.7	0.4
Income tax payable	2.9	4.5

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Affinity – statement of financial position[1]	31 Dec 14 Pro forma[2] $m	30 Jun 15 Reviewed $m
Provisions	7.0	8.0
Retention payments (formerly titled deferred consideration)	0.2	0.2
Revenue received in advance	0.6	1.2
Centre enrolment bonds	2.4	2.7
Deferred government grant funding	-	3.9
Total current liabilities	**23.6**	**31.9**
Borrowings	38.5	33.9
Provisions	2.6	2.6
Lease straight line liability	1.4	2.4
Total non-current liabilities	**42.5**	**38.9**
Total liabilities	**66.1**	**70.7**
Net assets	**212.8**	**219.3**
Net tangible assets	**(44.5)**	**(41.2)**

Note:
1 Rounding differences may exist.
2 Adjusted to reflect acquisitions announced but not settled as at 31 December 2014, the acquisition of nine centres announced in March 2015 and the eight for 21 entitlement offer.
Source: Affinity.

68 In relation to the financial position, we note that:

(a) **assets held for sale** – represent land located at Ayr and Kelso in QLD which is expected to be sold during 2015

(b) **property, plant and equipment** – comprises furniture and fittings, motor vehicles, computer equipment and other equipment

(c) **goodwill** – arises from the acquisition of child care centres

(d) **trade and other payables** – comprises trade payables, accrued employee related expenses and other payables

(e) **borrowings** – mainly relate to drawn down amounts under bank facilities in place of $117 million provided by the Commonwealth Bank of Australia (CBA). This includes an acquisition facility of some $100 million, the maturity of which was recently extended to July 2018 (on 15 June 2015)

(f) **provisions** – primarily relate to annual and long service leave entitlements, but also include repairs and maintenance provisions

(g) **retention payments (formerly titled deferred consideration)** – consideration payable for the acquisition of child care centres that has been withheld until such time as settlement adjustments have been confirmed by Affinity as appropriate

(h) **revenue received in advance** – results from Affinity requiring child care fees to be settled two weeks in advance

(i) **centre enrolment bonds** – relate to deposits paid by parents to secure enrolment at the centre for their children and are held until the child leaves the child care centre

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(j) **deferred government grant funding** – funds received in advance from the government which is required to be spent on specific expenditure items (refer paragraphs 149 and 150)

(k) **lease straight line liability –** represents the difference between rent paid (for premises) and the expense charged in the Profit & Loss Statement. The liability arises (for accounting purposes only) because Affinity expenses the total cost of its lease obligations evenly over their term, notwithstanding that the amount of the expense recognised currently exceeds its cash rent costs.

Share capital and performance

69 As at 20 August 2015, Affinity had some 231.5 million fully paid ordinary shares on issue.

70 Affinity has a short and long-term incentive program in the form of a performance rights plan. In May 2015, 1.3 million performance rights were issued to executive directors and senior management under the scheme. The performance rights vest on 31 December 2017 and convert, subject to the achievement of specified performance benchmarks[11], on a one-for-one basis into ordinary shares for nil consideration.

Significant shareholders

71 As at 20 August 2015 the significant shareholders in Affinity (aside from itself[12]) were G8 Education, with a 19.89% interest[13], Renaissance Smaller Companies Pty Limited with a 8.29% interest[14] and Argo Investments with a 6.70% interest[15].

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11 Being earnings per share (EPS) and total shareholder return benchmarks.
12 Affinity is a party to voluntary initial public offering (IPO) escrow arrangements with certain Affinity shareholders.
13 Source: Affinity change in substantial holding dated 3 August 2015.
14 Source: Affinity change in substantial holding dated 20 August 2015.
15 Source: Affinity change in substantial holding dated 14 April 2015.

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Share price performance

72 The price of Affinity shares since listing on 9 December 2013 to 2 July 2015[16] is summarised below:

Affinity – share price performance	High $	Low $	Close $	Monthly volume 000
Quarter ended				
December 2013 (from 9 December 2013)	1.19	0.98	1.14	6,862
March 2014	1.56	1.14	1.45	8,766
June 2014	1.45	1.16	1.25	11,882
Month ended				
July 2014	1.28	1.07	1.24	11,284
August 2014	1.29	1.14	1.27	5,811
September 2014	1.43	1.27	1.31	16,025
October 2014	1.35	1.22	1.31	13,101
November 2014	1.31	1.15	1.22	9,730
December 2014	1.24	1.11	1.22	5,526
January 2015	1.33	1.20	1.31	3,455
February 2015	1.53	1.27	1.29	15,550
March 2015	1.39	1.07	1.11	31,146
April 2015	1.15	1.05	1.08	17,347
May 2015	1.15	1.01	1.02	15,253
June 2015	1.04	0.76	0.81	17,768
1 July 2015 to 2 July 2015	0.83	0.49	0.54	55,148

Source: Bloomberg.

73 The following chart illustrates the movement in the share price of Affinity since its listing on 9 December 2013 to 2 July 2015[17]:

[16] Being the date prior to the announcement of G8 Education's intention to make a takeover offer for Affinity.
[17] Being the date prior to the announcement of G8 Education's intention to make a takeover offer for Affinity.

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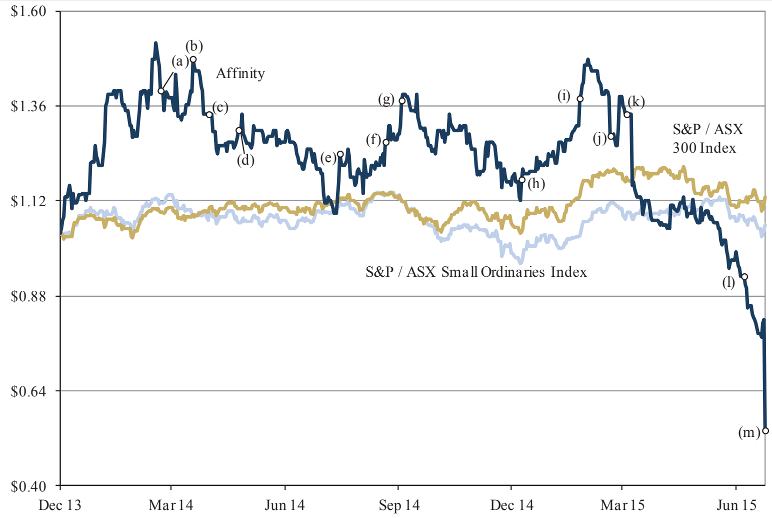
Affinity – share price history[1]
9 December 2013 to 2 July 2015



Note:
1 Based upon closing prices. The S&P / ASX 300 Index and the S&P / ASX Small Ordinaries Index have been rebased to Affinity's last traded price on 9 December 2013 ($1.04).
Source: Bloomberg.

74 Until recently, Affinity had (since listing) outperformed the S&P / ASX 300 Index and the S&P / ASX Small Ordinaries Index. Key market sensitive announcements are as follows:

(a) **28 February 2014** – announced results for the period from incorporation to December 2013. Revenue was $1.6 million with an earnings before interest and tax (EBIT) loss of $9.3 million

(b) **26 March 2014** – announced agreements to acquire seven child care centres

(c) **8 April 2014** – announced acquisition of 51 child care centres with funding through a combination of cash and a three for four accelerated renounceable entitlement offer to raise $75 million

(d) **2 May 2014** – announced increase in CBA debt facilities to $115 million, including an $80 million increase in the acquisition debt facility

(e) **23 July 2014** – announced completion of 35 of the 51 child care centre acquisitions as announced in April 2014

(f) **29 August 2014** – announced 1H14 underlying EBIT of $4 million representing a 30% increase over the prospectus forecast

(g) **11 September 2014** – announced agreements to acquire 20 child care centres

(h) **17 December 2014** – announced acquisition of 16 child care centres including a large group of premium centres in metropolitan areas for $45 million

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(i) **2 February 2015** – announced agreements to acquire eight of Affinity's managed centres

(j) **27 February 2015** – announced FY14 underlying EBIT of $16.6 million with a portfolio growth from 57 to 152 centres during the period

(k) **12 March 2015** – announced an eight for 21 accelerated renounceable entitlement offer to raise $75 million to fund the acquisition of nine premium child care centres and to reduce debt

(l) **15 June 2015** – announced improved pricing, increased size ($2 million) and term extension (by 12 months to July 2018) of its debt facilities with CBA

(m) **2 July 2015** – announced that the underlying EBITDA for 1H15 is likely to be between $7.5 million and $8.5 million and FY15 is likely to be between $27 million and $32 million (being less than the analyst consensus estimate at the time).

Liquidity in Affinity shares

75 The liquidity in Affinity shares based on trading on the ASX over the 12 month period to 1 July 2015[18] is set out below:

Affinity – liquidity in shares

Period	Start date	End date(1)	No of shares traded 000	WANOS(2) outstanding 000	Implied level of liquidity Period(3) %	Annual(4) %
1 month	2 Jun 15	1 Jul 15	17,705	231,452	7.6	91.8
3 months	2 Apr 15	1 Jul 15	50,090	231,452	21.6	86.6
6 months	2 Jan 15	1 Jul 15	101,114	206,934	48.9	97.7
1 year	2 Jul 15	1 Jul 15	161,789	186,958	86.5	86.5

Note:
1 Whilst 2 July 2015 was the last day prior to the announcement of G8 Education's intention to make a takeover offer for Affinity, an abnormally high percentage (i.e. 24%) of Affinity's shares were traded on that day in response to the Company's announcement of a lower than expected underlying FY15 EBITDA forecast.
2 Weighted average number of shares outstanding (WANOS) during relevant period.
3 Number of shares traded during the period divided by WANOS.
4 Implied annualised figure based upon implied level of liquidity for the period.
Source: Bloomberg and LEA analysis.

76 In each of the periods disclosed, total share turnover (on an annualised basis) has been close to 100% of the issued shares in Affinity, indicating a high level of market liquidity for a company of its size.

18 Whilst 2 July 2015 was the last day prior to the announcement of G8 Education's intention to make a takeover offer for Affinity, an abnormally high percentage (i.e. 24%) of Affinity's shares were traded on that day in response to the Company's announcement of a lower than expected underlying FY15 EBITDA forecast.

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IV Profile of G8 Education

Overview

77 G8 Education is a child care centre operator providing developmental and educational child care services in Australia and Singapore. In Australia, G8 Education provides a range of child care service activities and is the largest ASX listed child care operator, owning some 457 centres with a daily licensed capacity of 33,402 children as at 30 June 2015[19]. Its portfolio of child care centres is spread across NSW, VIC, QLD, WA, SA, the ACT and TAS. In Singapore, G8 Education owns 18 centres and has franchised a further 37 centres[20].

History and strategy

78 G8 Education was founded in February 2007 as Early Learning Services Limited (ELS) and commenced trading on the ASX in December 2007. In March 2010, ELS merged with Payce Child Care Pty Limited and was renamed G8 Education Limited.

79 G8 Education's business model is to identify, acquire, integrate and manage child care centres. Once acquired, G8 Education focuses on a number of key operational metrics to drive performance. Efficiencies include achieving cost synergies in back office management and leveraging the education curriculum.

80 Since the merger, G8 Education has been highly acquisitive and has grown to become the largest for-profit provider of education and child care services in Australia:

G8 Education – number of centres acquired[1]

	FY11	FY12	FY13	FY14	1H15
Australia – opening balance	88	135	167	234	437
Additions	53	33	76	203	21
Disposals[2]	(6)	(1)	(9)[3]	-[3]	(1)[3]
Australia – closing balance	135	167	234	437	457
Singapore – closing balance	7	8	18	18	18
Total – closing balance	**142**	**175**	**252**	**455**	**475**

Note:
1 Based upon opening and closing balances and additions as reported in G8 Education's Annual Report and Appendix 4E / 4D.
2 Calculated as the difference between the reported opening and closing balance less additions.
3 Implied number of disposals differs from reported disposals as per Annual Report and Appendix 4E / 4D for the respective period.

Source: G8 Education Annual Reports and Appendix 4E for FY11, FY12, FY13 and FY14, Appendix 4D for 1H15 and LEA analysis.

19 Source: Replacement Bidder's Statement dated 20 August 2015.
20 Source: Replacement Bidder's Statement dated 20 August 2015.

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Current operations

81 The child care centres owned by G8 Education operate under a variety of brands with differing levels of service and cost depending on the location of the centre. The location and brands of the Company's owned centres are shown below. The diagram also includes the location of the 37 franchised centres:

G8 Education – portfolio of owned and franchised centres(1)
As at 30 June 2015

Source: Replacement Bidder's Statement dated 20 August 2015.

82 The majority of G8 Education's Australian centres are located in metropolitan areas with over 70% of centres located within 40 kilometres of a Central Business District (CBD)[21].

21 Source: Replacement Bidder's Statement dated 20 August 2015.

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Financial performance

83 The financial performance of G8 Education for the three years ended 31 December 2014 and six months to 30 June 2015 is set out below:

G8 Education – statement of financial performance[1]	FY12 Audited $m	FY13 Audited $m	FY14 Audited $m	1H15 Reviewed $m
Revenue from child care centres	174.8	270.7	476.9	304.2[2]
Royalty income from franchised centres	1.9	1.9	2.3	na
Other income[3]	-	-	-	0.6
Total revenue[4]	**176.7**	**272.6**	**479.2**	**304.8**
Employee benefits	(106.3)	(159.6)	(270.0)	(175.8)
Occupancy costs	(22.8)	(33.3)	(56.1)	(37.5)
Direct costs of providing services	(13.5)	(22.2)	(40.1)	(23.8)
Other expenses	(4.1)	(5.6)	(7.8)	(9.7)
Underlying EBITDA	**29.9**	**51.9**	**105.2**	**57.9**
Depreciation	(2.1)	(3.1)	(5.1)	(4.0)
Underlying EBITA[5]	**27.9**	**48.7**	**100.1**	**53.9**
Amortisation of acquisition intangibles	-	-	-	-
Significant items[6]	(0.1)	(1.0)	5.8	4.1
Net finance costs[7]	(0.9)	(3.1)	(14.8)	(9.9)
Foreign exchange translation loss	-	-	(18.6)	(10.5)
PBT	**26.9**	**44.6**	**72.5**	**37.6**
Income tax expense	(7.7)	(13.5)	(19.8)	(9.4)
NPAT	**19.2**	**31.1**	**52.7**	**28.2**
Employee benefits / revenue from child care (%)	*60.8*	*59.0*	*56.6*	*57.7*
EBITDA margin (%)	*16.9*	*19.0*	*22.0*	*19.0*
EBITA margin (%)	*15.8*	*17.9*	*20.9*	*17.7*
Dividend per share (cents)[8]	*7.0*	*12.0*	*19.0*	*12.0*
No. of child care centres owned at year end:[9]				
Australia	*167*	*234*	*437[9]*	*457*
Singapore	*8[9]*	*18*	*18*	*18*
Total	*175*	*252*	*455*	*475*
Average during year	*150*	*224*	*357*	*na*

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Note:
1 Rounding differences exist.
2 Revenue from continuing operations less interest received of $1.5 million as per statement of cash flows. Includes royalty income from franchised centres as this income is not separately disclosed in the 1H15 results.
3 Other income excludes deferred consideration not paid (which is treated as a significant item).
4 Excluding interest income.
5 Differs to that reported by G8 Education due to the differing treatment of interest income, share based payments expense and amortisation of facility fees.
6 Significant items comprise deferred consideration not payable and acquisition expenses only.
7 Net of interest income. Interest income for 1H15 assumed to be $1.5 million as per statement of cash flows.
8 Dividends declared in relation to reporting period. Dividends paid quarterly.
9 Closing balances for Singapore as at 31 December 2012 and Australia as at 31 December 2014 differ from those reported in the Replacement Bidder's Statement dated 20 August 2015 and G8 Education – overview 1H15 dated 10 August 2015 (being 18 and 436 respectively).
na – not available.
Source: G8 Education Annual Reports, Appendix 4E for FY12, FY13 and FY14, Appendix 4D for 1H15 and LEA analysis.

FY12 to FY14 and 1H15

84 Revenue and EBITA before significant items has increased significantly over recent years. This has principally been driven by the acquisition of child care centres.

85 However, average revenues per centre have also increased:

G8 Education – average revenue per centre[1]

	FY12 $m	FY13 $m	FY14 $m
Revenue from child care centres	174.8	270.7	476.9
Average number of child care centres during year (number)	150.0	224.0	357.0
Average revenue per centre	1.17	1.21	1.34

Note:
1 Rounding differences exist.
Source: G8 Education Annual Reports and Appendix 4E for FY12, FY13 and FY14.

86 EBITDA margins also appear to have benefited from increases in occupancy rates over recent years and economy of scale benefits, with head office costs per licensed place declining:

G8 Education – average occupancy rates and head office costs per licensed place

	FY11	FY12	FY13	FY14	1H15
Child care and education centre occupancy[1]	77%	80%	84%	84%	na
Number of licensed places (number)	9,868	12,661	17,597	32,782	33,402
Head office cost per licensed place ($)[2]	523	520	485	455	447

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Note:
1 It is unclear as to whether these percentages relate to the entire portfolio or just a segment thereof.
2 G8 Education does not disclose what expenses form part of head office costs.
na – not available.
Source: Replacement Bidder's Statement dated 20 August 2015 and G8 Education – overview 1H2015 dated 10 August 2015 (slide 9).

87 In FY14 and 1H15, G8 Education incurred an $18.6 million and $10.5 million foreign exchange loss respectively, arising from adverse movements in the AUD:SGD exchange rate on its Singapore dollar denominated borrowings. More information on this foreign currency exposure is set out at paragraph 106.

FY15 outlook

88 G8 Education has not provided any specific earnings guidance for FY15. However, the full year impact of child care centres opened during FY14 is expected to result in a further increase in EBITDA and EBITA in FY15. As noted above, the average number of child care centres operated by G8 Education in FY14 was 357, compared with 455 centres at year end[22].

89 G8 Education has also acquired a further 21 child care centres in 1H15, which are expected to be earnings accretive[23].

90 Analysts' forecasts for EBITDA for FY15 range between $150.0 million to $170.0 million, and average $160.9 million. EBIT forecasts range between $139.0 million to $160.0 million, and average $150.6 million[24].

Acquisition accounting

91 G8 Education has acquired 310 child care centres over the two and a half years ended 30 June 2015[25]. A summary of the purchase consideration and the assets and liabilities recognised by G8 Education for accounting purposes in relation to these acquisitions is shown below:

G8 Education – acquisition accounting[(1)(2)]

	FY13 $m	FY14 $m	1H15 $m	Total $m
Number of centres acquired (number)	86	203	21	310
Cash consideration	120.1	468.2	44.7	651.0
Contingent consideration	5.1	8.0	4.2	17.2
Purchase price adjustments	(4.3)	0.6	(3.1)	(6.9)
Total purchase consideration	**120.9**	**476.7**	**45.8**	**661.4**

22 Source: G8 Education Appendix 4E for FY14. We note that the Replacement Bidder's Statement dated 20 August 2015 and the G8 Education presentation of 10 August 2015 "Overview 1H2015" reports that there were 454 child care centres at year end.

23 Source: G8 Education Appendix 4D for 1H15 (note 10).

24 EBITDA and EBIT forecasts based on 11 analyst forecasts sourced from Bloomberg on 20 August 2015.

25 Source: G8 Education Annual Reports for FY13 (note 30), FY14 (note 28) and Appendix 4D for 1H15 (note 10). We note that in contrast, the Replacement Bidder's Statement dated 20 August 2015 and the G8 Education presentation of 10 August 2015 "Overview 1H2015" reports that there were 299 child care centres acquired over the two and a half years ended 31 December 2014.

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G8 Education – acquisition accounting[1][2]	FY13 $m	FY14 $m	1H15 $m	Total $m
Vehicles and furniture, fittings and equipment	0.3	1.9	-	2.2
Payables and employee liabilities	(4.9)	(7.9)	(1.0)	(13.8)
Net identifiable assets / (liabilities) acquired	**(4.6)**	**(6.0)**	**(0.9)**	**(11.6)**
Amounts held in trust pending final adjustment	0.3	-	(2.1)	(1.7)
Goodwill recognised[2]	125.2	482.8	48.8	656.7
Total assets and liabilities acquired	**120.9**	**476.7**	**45.8**	**643.4**

Note:
1 Rounding differences exist.
2 Amounts as reported in year of acquisition. We note that minor adjustments to the level of goodwill recognised are made in subsequent accounting periods.
Source: G8 Education Annual Reports for FY13 (note 30), FY14 (note 28) and Appendix 4D for 1H15 (note 10).

92 G8 Education has reported that the only tangible assets acquired in connection with the 310 child care centre acquisitions were vehicles and furniture, fittings and equipment. The value attributed to these assets upon acquisition was only $2.2 million, representing (on average) only $7,187 per child care centre.

93 In contrast, some $656.7 million has been attributed to goodwill arising from the acquisitions of the child care centres. This goodwill is tested annually for impairment but is not amortised under current accounting standards. Accordingly, G8 Education's acquisition accounting over recent years has not resulted in any material charges in the group's statement of financial performance.

94 In particular, the low level of value attributed to fixed assets upon acquisition results in low annual depreciation charges. In this regard we note that annual depreciation charges in recent years have been well below payments made for property, plant and equipment:

G8 Education – depreciation charges[1]	FY12 $m	FY13 $m	FY14 $m	1H15 $m
Depreciation charges	2.1	3.1	5.1	4.0
Payments for property, plant and equipment	4.8	10.5	16.5	6.8
Depreciation / payments (%)	43.1	29.8	30.7	58.8

Note:
1 Rounding differences exist.
Source: G8 Education Annual Reports, Appendix 4E for FY13 and FY14 and Appendix 4D for 1H15.

95 Given the above, in our view, G8 Education's current depreciation charges may materially understate sustainable capital expenditure levels.

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Contingent consideration

96 At the date of acquisition G8 Education recognises the fair value of any deferred contingent consideration payable where it expects the earn-out target to be met. Due to the low level of net assets acquired this increases the level of goodwill recognised in G8 Education's financial statements at the date of acquisition.

97 In circumstances where the earn-out target is subsequently not met, the amount of the deferred contingent consideration which has not been paid is eliminated and recognised as a profit in G8 Education's Consolidated Income Statement. Whilst this accounting treatment is consistent with the Australian equivalent of International Financial Reporting Standards, in our view it would be more appropriate to reduce the level of goodwill recognised (reflecting the reduction in the purchase price) rather than recognise it as income through the Consolidated Income Statement. In our view, the recognition of profit is also inconsistent with the failure to achieve the earn-out target.

98 The level of profits recognised by G8 Education in recent years from deferred consideration not paid is summarised below:

G8 Education – deferred consideration	FY12 $m	FY13 $m	FY14 $m	1H15 $m
Profit recognised due to deferred consideration not paid	1.0	0.6	9.2	4.6

Source: G8 Education Annual Reports, Appendix 4E for FY12, FY13 and FY14 and Appendix 4D for 1H15.

99 In the statement of financial performance as set out in paragraph 83, we have treated the above profits arising from deferred consideration not payable as a significant item.

Seasonality

100 The child care industry has a distinct seasonal pattern and G8 Education (like Affinity) generates significantly more of its annual profit in the second half of the year. This arises because a large group of children leave child care late in the year to commence school at the beginning of the following year. Revenue increases with new enrolments as the new calendar year progresses.

101 In FY13 and FY14 G8 Education generated 65% and 69% respectively of its underlying EBIT in the second half of the year[26].

[26] Based on underlying EBIT as reported in Appendix 4E / 4D for the respective period. We note that EBIT calculated by management differs marginally to EBITA presented at paragraph 83.

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Financial position

102 The financial position of G8 Education as at 31 December 2014 and 30 June 2015 is set out below:

G8 Education – statement of financial position[1]	31 Dec 14 Audited $m	30 Jun 15 Reviewed $m
Cash and cash equivalents	120.8	83.2
Trade and other receivables	14.2	13.5
Deposits on acquisitions (yet to settle)	8.8	19.0
Current tax assets	-	3.8
Other current assets	4.8	4.6
Total current assets	**148.6**	**124.1**
Property, plant and equipment	29.6	32.6
Deferred tax assets	15.4	17.8
Goodwill	809.2	856.5
Total non-current assets	**854.2**	**906.9**
Total assets	**1,002.8**	**1,031.0**
Trade and other payables	37.1	62.3[2]
Dividends payable	21.2	21.9[3]
Centre enrolment advances	8.0	na
Income received in advance	9.3	na
Employee entitlements	18.1	19.1
Derivative financial instruments	0.2	0.2
Current tax liabilities	9.7	na
Total current liabilities	**103.6**	**103.5**
Borrowings	352.9	364.7
Other payables	0.7	0.7
Provisions	3.6	3.5
Total non-current liabilities	**357.2**	368.9
Total liabilities	**460.8**	**472.4**
Net assets	**542.0**	**558.6**
Net tangible assets	**(282.6)**	**(315.8)**

Note:
1 Rounding differences exist.
2 Includes centre enrolment advances, income received in advance and current tax liabilities which were not separately disclosed in 1H15.
3 Estimate based on 365.1 million shares outstanding as at 26 June 2015 and declared dividend of six cents per share.
na – not available.
Source: G8 Education Annual Report for FY14 and Appendix 4D for 1H15.

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103 In relation to the financial position as at 30 June 2015, we note that:

(a) other current assets relate to prepayments ($3.5 million) and rental and utility security deposits ($1.1 million)

(b) property, plant and equipment comprises buildings ($4.6 million), vehicles ($0.6 million) and furniture, fittings and equipment ($27.4 million)

(c) goodwill arises from the acquisition of child care centres

(d) the properties at which G8 Education's child care centres are located are leased (mostly) from individual landlords on standard contract terms. The average lease tenure is 19 years[27]

(e) the increase in trade and other payables of $8.7 million is largely due to the Long Day Care Professional Development Funding received in advanced as well as an increase in parent fees paid in advance[28]

(f) borrowings comprise the following corporate notes:

G8 Education – borrowings as at 30 June 2015

Issue date		Face value in issue currency $m	Issue currency	Maturity	Interest rate %
7 Aug 13	Fixed	70	AUD	7 Aug 19	7.65
3 Mar 14	Floating	50	AUD	3 Mar 18	90 day BBSW + 390 bps[(1)]
12 May 14	Fixed	175	SGD	19 May 17	4.75
25 Aug 14	Fixed	85	SGD	19 May 17	4.75

Note:
1 Basis points (bps). Bank bill swap rate (BBSW).
Source: G8 Education Appendix 4D for 1H15.

On 31 July 2015, G8 Education raised a further SGD155 million from unlisted unsecured notes which were issued at a fixed rate of 3.5% per annum and a maturity date of 2 August 2016. The proceeds from these notes are intended to be used to fund the Cash Offer consideration (or elections to receive cash under the Revised Scrip Offer)[29]. On 3 August 2015, G8 Education announced a variation of its existing finance arrangements with the Bank of Western Australia which includes a new $50 million undrawn senior debt facility available for the purpose of refinancing Affinity's existing debt arrangements with the CBA.

Acquisition of interest in Affinity

104 On 2 and 3 July 2015, G8 Education acquired a 19.89% interest in Affinity (46.052 million shares). The total cost of the Affinity shares acquired was $32.2 million, representing an average cost of $0.70 per Affinity share acquired[30].

27 Source: Replacement Bidder's Statement dated 20 August 2015.
28 Source: G8 Education – overview 1H2015 dated 10 August 2015 (slide 14).
29 Source: Replacement Bidder's Statement dated 20 August 2015.
30 Source: Replacement Bidder's Statement dated 20 August 2015.

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105 As these shares were acquired post the above balance date, G8 Education's investment in Affinity (nor the cash cost thereof) is shown in the above financial position.

Foreign currency exposure

106 G8 Education has significant borrowings denominated in Singapore dollars. This exposure will increase to the extent to which the new SGD155 million facility is required to cash fund the acquisition of Affinity shares (under either the Cash Offer or Revised Scrip Offer). Whilst the group operates 18 child care centres in Singapore[31], its operations in the country are modest compared to its Australian operations. The high level of Singapore denominated debt (the majority of which is unhedged[32]) therefore exposes the group to significant foreign exchange risk.

107 Adverse foreign exchange movements resulted in G8 Education incurring an A$18.6 million and A$10.5 million foreign exchange translation loss in FY14 and 1H15 respectively. We note that since 30 June 2015, the Australian dollar has declined by a further 0.9% against the Singapore dollar[33] (implying a further foreign exchange translation loss).

Share capital and performance

108 As at 20 August 2015, G8 Education had some 367.8 million fully paid ordinary shares on issue[34].

109 3.1 million of the fully paid ordinary shares on issue have been allocated to members of the senior management team in accordance with the incentive plan approved by shareholders at the annual general meeting on 21 May 2015[35]. Shares were issued on 16 June 2015 at a price of $5 per share and will vest in accordance with the following conditions[36]:

(a) one third of the shares will vest on 31 December 2015 if the fully diluted EPS for FY15 is 40% more than the previous year

(b) one third of the shares will vest on 31 December 2016 if the fully diluted EPS for FY16 is 40% more than the previous year

(c) one third of the shares will vest on 31 December 2017 if the fully diluted EPS for FY17 is 40% more than the previous year.

110 Interest free, limited recourse loans have been provided to the senior management team to facilitate the purchase of these shares[37].

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31 G8 Education also receives royalties from a further 37 franchised centres.

32 G8 Education has announced that it intends to hedge the amounts owing under the SGD155 million facility for a period of four months. Source: Replacement Bidder's Statement dated 20 August 2015, Section 5.13.

33 Source: based upon Bloomberg AUD:SGD exchange rates of 1.0385 as at 30 June 2015 and 1.0291 as at 20 August 2015.

34 Source: Appendix 3B dated 13 July 2015. Excludes shares that may be issued to Affinity shareholders under the Revised Scrip Offer.

35 Source: G8 Education results of annual general meeting dated 21 May 2015.

36 Source: G8 Education notice of annual general meeting dated 21 April 2015.

37 In the event that the shares are required to be sold to repay the loan and the sale proceeds are insufficient to cover the amount of the loan that is outstanding, the company cannot recover the remaining amount.

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Significant shareholders

111 As at 20 August 2015, the significant shareholders in G8 Education were UBS Group AG with 31.8 million shares (or 8.6% of the total shares on issue)[38], Greencape Capital Pty Limited with 23.1 million shares (or 6.3% of the total shares on issue)[39], National Australia Bank Limited with 23.0 million shares (or 6.2% of the total shares on issue)[40] and Challenger Limited with 22.2 million shares (or 6.0% of the total shares on issue)[41].

Share price performance

112 The price of G8 Education shares from 1 January 2014 to 2 July 2015[42] is summarised below:

G8 Education – share price performance

	High $	Low $	Close $	Monthly volume 000
Quarter ended				
March 2014	5.10	2.97	5.07	40,993
June 2014	5.09	4.18	4.60	42,116
Month ended				
July 2014	5.01	4.38	4.99	48,459
August 2014	5.46	4.72	5.38	47,431
September 2014	5.63	4.96	5.12	48,031
October 2014	5.25	4.73	4.99	49,154
November 2014	5.06	4.33	4.45	54,983
December 2014	4.83	4.04	4.17	58,573
January 2015	4.31	3.54	4.20	56,598
February 2015	4.87	3.92	4.36	85,797
March 2015	4.37	3.25	3.36	126,922
April 2015	3.79	3.21	3.61	98,257
May 2015	4.15	3.54	3.75	89,165
June 2015	3.86	3.21	3.26	80,188
1 July 2015 to 2 July 2015	3.28	3.09	3.25	8,056

Source: Bloomberg.

113 The following chart illustrates the movement in the share price of G8 Education from 1 January 2014 to 2 July 2015[43]:

38 Source: G8 Education change in substantial holding dated 20 August 2015.
39 Source: G8 Education change in substantial holding dated 13 July 2015.
40 Source: G8 Education change in substantial holding dated 22 July 2015.
41 Source: G8 Education change in substantial holding dated 8 July 2015.
42 Being the date prior to the announcement of G8 Education's intention to make a takeover offer for Affinity.
43 Being the date prior to the announcement of G8 Education's intention to make a takeover offer for Affinity.

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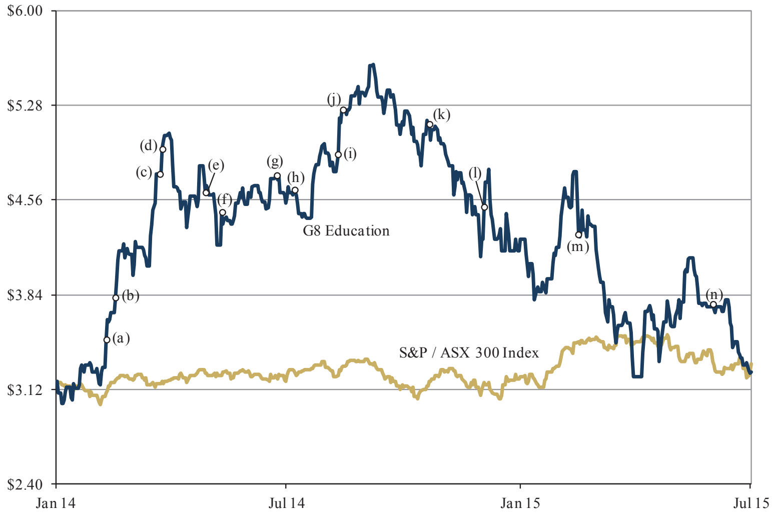
G8 Education – share price history
1 January 2014 to 2 July 2015



Note:
1 Based upon closing prices. The S&P / ASX 300 Index has been rebased to G8 Education's last traded price on 1 January 2014 ($3.18).
Source: Bloomberg.

114 Over the above period, G8 Education performed largely in line with the S&P / ASX 300 Index (having significantly outperformed in the first half and significantly underperformed in the second half). Key market sensitive announcements are summarised below:

(a) **10 February 2014** – announced agreements to acquire 63 child care centres

(b) **17 February 2014** – announced FY13 adjusted NPAT of $32.3 million, a 64% increase compared to the prior corresponding period

(c) **24 March 2014** – announced agreements to acquire 91 child care centres and all the shares in Sterling Early Education Limited (Sterling Early Education) with an aggregate purchase price of $228 million

(d) **26 March 2014** – announced a capital raising of $4.60 per share to raise $100 million to fund the acquisition of Sterling Early Education and the 91 child care centres

(e) **29 April 2014** – announced agreement to acquire seven child care centres

(f) **12 May 2014** – announced completion of an unsecured note offering to raise SGD175 million at 4.75% per annum for a three year term

(g) **24 June 2014** – announced repayment of debt facility provided by Bank of Western Australia

(h) **8 July 2014** – announced agreements to acquire 19 child care centres

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(i) **11 August 2014** – announced 1H14 NPAT of $16.3 million, a 48% increase compared to the prior corresponding period. Also announced agreements to acquire 25 child care centres

(j) **15 August 2014** – announced completion of a further tranche of unsecured notes to raise SGD85 million at 4.75 % per annum for a three year term

(k) **22 October 2014** – announced agreements to acquire 20 child care centres to be funded by a placement to institutions at a price of $4.91 per share to raise $100 million

(l) **4 December 2014** – announced expected EBIT for FY14 to be $101 million (being greater than the analyst consensus estimate at the time)

(m) **16 February 2015** – announced FY14 adjusted NPAT of $60.6 million, an 88% increase compared to the prior corresponding period. Also announced agreements to acquire 12 child care centres

(n) **2 June 2015** – announced agreements to acquire eight child care centres.

Liquidity in G8 Education shares

115 The liquidity in G8 Education shares based on trading on the ASX over the 12 month period to 2 July 2015[44] is set out below:

G8 Education – liquidity in shares

Period	Start date	End date	No of shares traded 000	WANOS[(1)] outstanding 000	Implied level of liquidity Period[(2)] %	Implied level of liquidity Annual[(3)] %
1 month	3 Jun 15	2 Jul 15	82,308	363,717	22.6	271.6
3 months	3 Apr 15	2 Jul 15	260,682	362,312	71.9	287.8
6 months	3 Jan 15	2 Jul 15	543,667	360,195	150.9	301.9
1 year	3 Jul 15	2 Jul 15	847,655	349,846	242.3	242.3

Note:
1 WANOS during relevant period.
2 Number of shares traded during the period divided by WANOS.
3 Implied annualised figure based upon implied level of liquidity for the period.
Source: Bloomberg and LEA analysis.

116 In each of the periods disclosed, total share turnover (on an annualised basis) has been substantially in excess of 100% of the issued shares in G8 Education, indicating a high level of market liquidity.

44 Being the date prior to the announcement of G8 Education's intention to make a takeover offer for Affinity.

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V Industry overview

Introduction

117 The child care industry in Australia principally provides care and early stage education to children from birth to 12 years old. The services offered by the child care industry include long day care, outside school-hours care, family day care and occasional care. In 2013, long day care services accounted for around 56% of industry revenue, outside school hours care 32%, family day care 9% and occasional care just 3%[45]

118 The industry is highly regulated and centres operate under the National Quality Framework (NQF), which is discussed in more detail below.

119 The industry has experienced strong growth in the last decade. Since 2004, the total numbers of children and families using child care have grown significantly. In 2014 there were over 1.16 million children attending child care, double the number in 2004, and the number of families with at least one child in approved care grew by 45% over the same period[46].

120 In March 2015, there were 14,827 approved child care services provided (13,908 centre-based services and 919 family day care services), an increase of 48% from 10,023 in 2004[47]. The industry was expected to generate revenue of $7.8 billion in FY14[48], and around $9 billion in FY15, with an overall profit of $495 million in that year[49].

Long day care

121 Long day care centres represent the largest contributor to industry revenue. These centres are set up to primarily offer care to below school age children with working parents. The care can be both full and part time. In 2014, there were 631,400 children in long day care, compared to 441,240 in 2004, an increase of 43%[50].

122 For long day care centres, compliance with the NQF means that 50% of staff must have or be working towards a diploma qualification or higher and the remaining 50% must have or be working towards a Certificate III level education and care qualification (or higher). Depending on the size of the service, it must be attended by, or have access to an early childhood teacher (ECT) who has completed 50% of the degree[51,52].

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45 Source: Affinity Education Group (2013) Prospectus.

46 Source: Department of Education, Employment and Workplace Relations (DEEWR) (2013) *Child Care in Australia*, and Department of Social Services (DSS) (2014) *Early Childhood and Child Care in Summary: June quarter 2014*.

47 Source: Australian Children's Education and Care Quality Authority (ACECAQ) (May 2015) *NQF Snapshot Q1 2015*.

48 Source: Think Childcare & Education (2014) *Prospectus*.

49 Source: Franchise Business website, accessed 8 July 2015.

50 Source: DEEWR (2013) *Child Care in Australia* and DSS (2014) *Early Childhood and Child Care in Summary June quarter 2014*.

51 Source: Australian National Audit Office (ANAO) (2015) *Administration of the Early Years Quality Fund.*

52 Certificate III courses typically require 12 months of full-time study, diplomas require 18-24 months of full-time study (or 2-3 years for an advanced diploma) and a Bachelor Degree requires 3-4 years full time study.

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123 ACECQA publishes a list of approved qualifications for each qualification level. Educators with a qualification that does not appear on the list can apply to ACECQA for individual recognition. Early childhood teaching students are able to be counted as diploma level educators for ratio purposes.

Outside school-hours care

124 Outside school-hours care refers to before and after school short-term care to children of primary school age. Vacation care is also considered part of this segment, providing child care services to parents during school holidays. In 2014, there were 367,940 children in outside school-hours care, compared to 235,550 in 2004, an increase of 56%[53].

Family day care

125 Family day care is the only area of child care that takes place outside of a centre, with care provided in the home of an approved educator. This type of care can be all day, part time, occasional or outside school hours. In 2014, there were 192,510 children in family day care, compared to 117,670 in 2004, an increase of 64%[54]. Family day care is a capped program, with a limited number of places available in a given time period.

126 All family day care educators must hold or be working towards an approved Certificate III level education and care qualification (or higher).

Occasional care

127 Occasional care offers child care services for children on a casual basis. Centres offering occasional services are primarily set up to provide flexibility to parents with irregular working hours or short-term needs. The number of children accessing the service fell from 11,240 in 2004 to 7,430 in 2014 (a decrease of 34%)[55], due to the Labor Government cutting all federal funding to neighbourhood-based occasional child care as a part of its FY11 budget[56]. State governments had to pick up the federal government's share of funding. However, the Coalition Government this year allocated $12.6 million over four years to reinstate Neighbourhood Model Occasional Care for emergency or late-notice situations[57].

Industry drivers

128 We set out below (in no particular order) the primary industry drivers being: female participation in the workforce; population trends; real household disposable income; and government financial support.

Females in the labour force

129 The workforce participation rate of women with dependent children drives the demand for child care services and can be affected by factors including out-of-pocket costs, accessibility of suitable child care services, the support of partners and the availability of employers offering flexible work and other family-friendly arrangements.

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53 Source: DEEWR (2013) *Child Care in Australia.*
54 Source: DEEWR (2013) *Child Care in Australia.*
55 Source: DEEWR (2013) *Child Care in Australia.*
56 For the reason that funding was not tied to service delivery and services were not subject to quality controls or learning outcomes.
57 Source: *Budget Review 2014-15: Early Childhood* on www.aph.gov.au accessed 14 July 2015.

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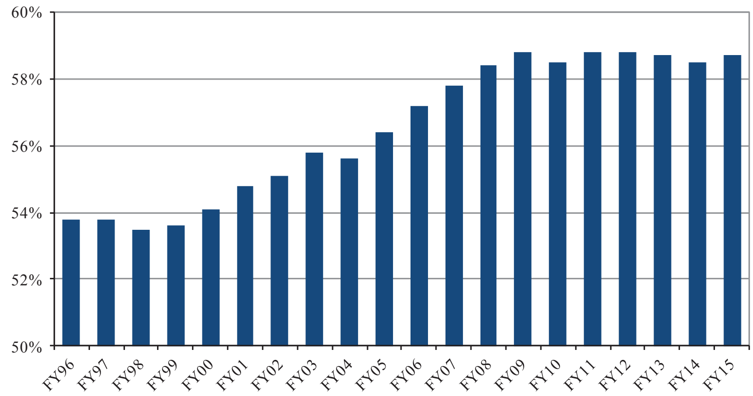
130 Over the last few decades, there has been an increase in overall female participation in the workforce, from 54% in FY96 to 59% in FY15[58]. Using the most recent comparable data, Australia's maternal employment rate in 2009 (62%) was below the Organisation of Economic Co-operation and Development (OECD) average (66%)[59].

Female participation in the workforce



Source: ABS 6202.0 *Labour Force, Australia* Table 03.

131 Surveys of parents not in the workforce due to caring for children have found that around half of those who stay home with their children do so because they prefer it to sending them to day care, or because they believe their child is too young for day care. The other half, however, is out of the workforce due to child care issues, indicating that increased availability of suitable child care services may improve female workforce numbers.

58 Source: ABS 6202.0 *Labour Force, Australia*.

59 Source: Productivity Commission (2014) *Childcare and Early Childhood Learning*.

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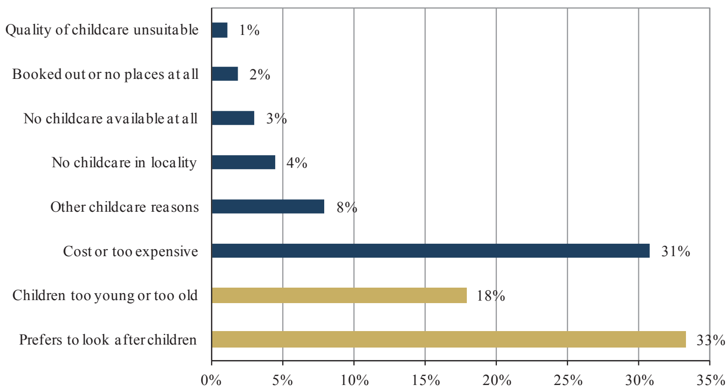
Main reason not working due to caring for children: February 2014

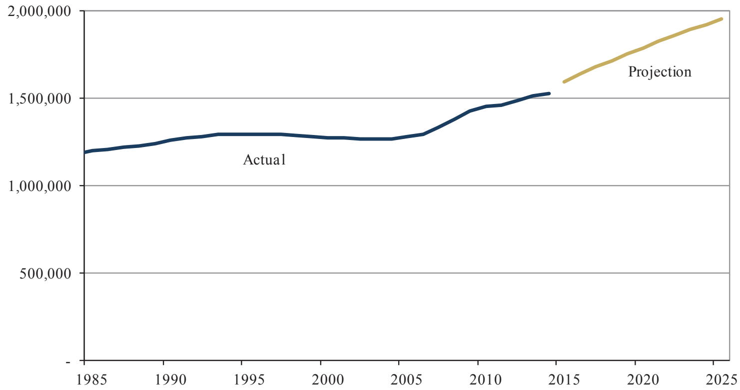


Source: ABS 6226 *Persons not in the labour force*

Population trends

132 Child care centre occupancy is driven in part by the population of eligible children. There has been an accelerated increase in the number of children aged 0-4 years in recent years. The number of children from birth to 4 years increased 20% in the 10 years to June 2014, and is forecast to increase by a further 23% between 2015 and 2025[60], representing annual compound growth of around 2%.

Australian population growth: Children aged 0-4 years



Source: ABS 3222.0 *Population Projections, Australia* and ABS 3101.0 *Australian Demographic Statistics.*

60 Source: ABS 3222.0 *Population Projections, Australia* and ABS 3101.0 *Australian Demographic Statistics*.

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Real household disposable income

133 Household disposable income has an effect on the demand for child care services. In 2010 more than 50% of children whose parents had a combined weekly income in excess of $2,000 accessed child care services, in contrast to just 25% accessing the services when combined weekly parental income was $800[61].

Government financial support with child care fees

134 As Australia's population ages, labour force participation becomes increasingly important if Australia is to maintain its standard of living. Government assistance with child care fees plays an important role in encouraging participation in the workforce as the cost of child care can present a major disincentive for parents to return to the workforce.

135 The Australian Government has provided increasing levels of funding to assist families to access early childhood education and care since 1972. Government expenditure on child care services doubled for FY04 to FY07, and again from FY08 to FY11[62]. While the Coalition Government's 2015 budget included a $3.5 billion increase over the next four years, cuts in other areas, such as paid parental leave and family tax benefit payments[63], will largely offset the increased benefit for some families. Consequently, the overall benefit to the industry is not yet clear.

136 The Coalition Government's proposed changes may not go ahead unchanged as they are tied to the Senate passing cuts to family tax benefits. The Labor Government has said it will not support the move to tie child care reforms to changes to the family tax benefit[64].

137 Currently, the Australian Government provides assistance to eligible families through three schemes, the Child Care Benefit (CCB), the Child Care Rebate (CCR) and a gap fee[65]:

(a) the CCB is means tested and eligible families currently receive support for between 24 to 50 hours of child care per week, depending on whether the parents are working, studying, or training. The CCB is paid to the service provider

(b) the CCR is not means tested and is paid to either parents or the service provider. In 2008, the rate of the CCR was increased from 30% to 50% of out-of-pocket expenses, and the annual maximum rebate was increased from $4,354 to $7,500 per child. Although previously increased annually to match inflation the rebate cap was frozen from 2011 to 2014 at $7,500 per child

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61 Source: Affinity Education Group (2013) *Prospectus*.

62 Source: DEEWR (2013) *Child Care in Australia*.

63 More than half a million households stand to lose the Family Tax Benefit Part B when their youngest child turns six under plans stalled in parliament. Source: www.sbs.com.au *Govt committed to family tax benefit cut* published 10 June 2015.

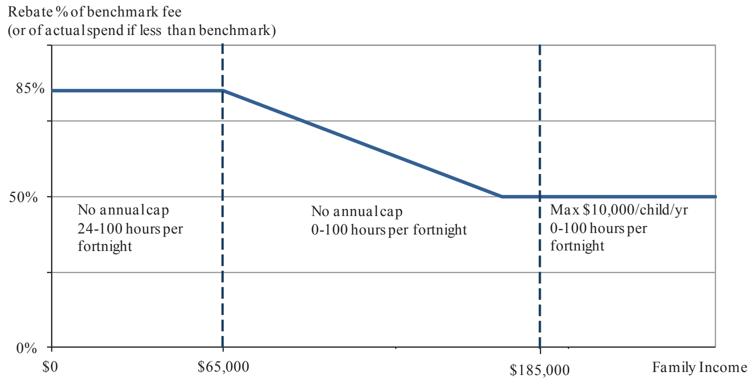
64 Source: www.news.com.au accessed 14 July 2015, *Federal Budget 2015: Government unveils jobs for families package* published 11 May 2015.

65 Known as Jobs, Education and Training Child Care Fee Assistance (JETCCFA), it provides assistance to eligible parents who qualify for the maximum rate of CCB. It pays most of the gap in out-of-pocket expenses while a parent is working, studying or training.

(c) eligible parents also receive help to pay the gap between the CCB and hours of care needed for approved activities such as job search, work, study or training.

138 The Coalition Government is proposing to replace these schemes from 1 July 2017 with a single, means tested payment made directly to the service provider. The new single payment will not be subject to a cap for families with incomes under $185,000, but will be capped at $10,000 per child for families with incomes over $185,000. Families with incomes of up to $65,000 will be able to access subsidies of 85% of the actual fee or a benchmark price. The level of support will gradually reduce to 50% for families with incomes of $170,000 and above.

Rebates for child care under the new system



Source: McKell Report (2015) Baby steps or giant strides?

Industry structure and competition

139 The child care industry is highly fragmented with the majority of providers (83%) managing only one education and care service, 16% managing services with 2–24 centres and only 1% managing operations with 25 centres or more[66].

Major operators

140 The main participants in child care services in Australia compete on a national level. A summary of the major operators is as follows[67]:

(a) Goodstart Early Learning is the largest not-for-profit operator with approximately 640 centres nationally and spaces for some 73,000 children

66 Source: ACECQA (May 2015) *NQF Snapshot Q1 2015*.

67 Source: Think Childcare and Education (2014) Prospectus, www.goodstart.org.au accessed 14 July 2015 and www.ku.com.au accessed 14 July 2015.

(b) G8 Education is the largest for-profit operator in the industry, with 457 centres and 33,402 licensed places as at 30 June 2015

(c) Affinity has 161 centres and 12,682 licensed places as at 30 June 2015

(d) other not-for-profit operators include KU Children's Services (150 centres) and the YMCA Australia (23 early learning centres, 28 family day care programs and 233 out of school hours care centres)

(e) Guardian Early Learning is a privately held for-profit business, with around 90 centres.

141 Barriers to entry for new centre-based services are significant and include:

(a) obtaining local government planning approval

(b) capital costs

(c) increasing compliance requirements and quality standards, such as caregiver qualifications and minimum staff-to-child ratios.

142 In contrast to centre-based services, home-based care arrangements face lower barriers to entry, particularly with respect to capital costs as home-based care operations are generally located within an existing residence.

Fees

143 Child care fee increases are generally annual however bi-annual increases are becoming more common practice in the industry. Increasing demand in the face of rising fees suggests that parents are willing to pay for quality, flexible care that suits their needs.

144 Average fees charged in 2014, and 12 month increases, for the main service types are shown below:

Average hourly fee per child		
Service type	**Jun 14 quarter**	**Increase on previous year**
Long day care	$7.95	6.0%
Family day care and in-home care	$7.95	5.3%
Occasional care	$9.25	4.5%
Outside school hours care	$6.35	5.0%

Source: DSS *Early Childhood and Child Care in Summary June quarter 2014.*

145 From the introduction of the new single payment on 1 July 2017, the hourly benchmark price for long day care will be $11.55 per hour, per child. For children at centres that charge less than this rate, the families will receive the same percentage of support based on the rate they pay. For children at more expensive centres the families will receive support set as a percentage of the maximum rate and will pay the difference (i.e. the gap) themselves. The introduction benchmark fee for family day care will be $10.10 per hour, per child, and for out of school hours care the benchmark will be $7.00 per hour, per child[68].

68 Source: Media release dated 10 May 2015 from www.pm.gov.au, accessed 9 July 2015.

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Key costs

146 Employee expenses are the most significant cost in the child care industry. Due to the implementation of the NQF, the industry is experiencing chronic staffing shortages[69] and wages continue to trend upwards as workers and educators become more skilled.

147 Implementation of the NQF has involved a transition from state and territory set educator-to-child ratios to new national ratios.[70] In some cases the new ratios are much higher than in the past and will significantly increase employee costs. The final changes will be introduced on 1 January 2016.

148 The previous Australian Government committed to establish the Early Years Quality Fund (EYQF) in March 2013, a $300 million fund to help early child care services to attract and retain qualified staff and in the process keep costs from being passed on to parents in the form of higher fees. The *Early Years Quality Fund Special Account Act 2013* came into effect on 1 July 2013 however, the level of funding was estimated to cover only around 30% of all long day care workers and the program was oversubscribed[71].

149 Following the 2013 Federal election, the Coalition Government reviewed the EYQF and decided to replace it with a new professional development program for child care educators, using uncommitted funds from the EYQF. Funding agreements already in place were renegotiated with funding levels reduced. As at 30 June 2014, $62.5 million of the EYQF had been paid to industry service providers[72].

150 The new program is directed towards assisting educators in long day care services to meet the qualification requirements under the NQF and improving practice to ensure quality outcomes for children.

Government regulation and policy

Overview of the NQF

151 On 1 January 2012, the NQF introduced a new integrated national approach to the regulation and quality assessment processes for child care services.

152 The framework created a uniform national approach to the regulation and quality assessment of early childhood education and care services. It replaced existing separate state and territory licensing and quality assurance processes. The national legislative framework consists of the *Education and Care Services National Law Act 2010* (National Law) and the *Education and Care Services National Regulations 2011*, as amended (National Regulations).

153 The National Regulations prescribe the minimum number of educators required to educate and care for children at an education and care service, and the minimum qualifications for educators. The following table shows the educator-to-child ratios required under the National Regulations and the current ratios. No national ratio has been set for over preschool age children, however state and territory ratios may apply.

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69 Source: The Coalition's Policy for Better Child Care and Early Learning September 2013.

70 Refer to paragraph 153 for details.

71 Source: Australian National Audit Office (ANAO) (2015) *Administration of the Early Years Quality Fund.*

72 Source: ANAO (2015) *Administration of the Early Years Quality Fund.*

44

Educator-to-child ratios for centre based services				
		0 – 2 year old[(1)]	**2 – 3 year old**	**3 – 5 year old**
Current:	QLD	1 : 4	1 : 6	1 : 12
	NSW	1 : 4	1 : 8	1 : 10
	VIC	1 : 4	1 : 4	1 : 15
	SA	1 : 4	1 : 10	1 : 10
	WA	1 : 4	1 : 5	1 : 10
National Regulations:	from 1 Jan 2016	1 : 4	1 : 5	1 : 11

Note:
1 All states and territories were required to comply with the ratio of 1:4 for 0 – 2 year olds from 2012.
Source: National Regulations, Part 4.4 and Chapter 7 and ACECQA website.

154 Some states have ratios that are lower than the National Regulations. These states will not be required to change their ratios on 1 January 2016.

155 For family day care services the National Regulations have been in force in all states and territories since 2014. The educator-to-child ratio required for family day care services is 1:7, with no more than four preschool age or younger children.

156 The Australian Government is in full cooperation with state and territory governments to take responsibility for both implementing these standards, and measuring child care institutions against the standards. This joint action between local and national governments aims to establish the standards to ensure quality services have a consistent approach in the industry.

157 Key aspects of the NQF include:

(a) **National Quality Standard** – all services will be assessed against the National Quality Standard (NQS) which will assess services in seven quality areas as well as providing an overall service assessment

(b) **National Quality Rating System** – this system consists of five rating levels for seven key quality areas, detailed as follows:

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National Quality Rating System

Source: ACECQA (May 2015) NQF *Snapshot Q1 2015.*

As at 31 March 2015, 8,287 or 56% of services had received a quality rating, of which 66% were meeting or exceeding the NQS. The remaining 44% were classified as Working Towards NQS[73]

(c) **Early Years Learning Framework** – this national framework for early childhood educators aims to ensure delivery of nationally consistent and quality education from birth to five years and through the transition to school

(d) **new national body** – ACECQA now monitors national consistency and assures quality implementation of the NQF

(e) **each state and territory as a regulatory authority** – regulatory authorities in each state and territory manage the NQF locally. These authorities have a quality assessment role under the NQF and responsibility for granting approvals, assessing and rating services and monitoring compliance with the legislation.

Outlook

Females in the labour force

158 The workforce participation rate of women has plateaued, with no growth in the last five years, however, Australia still has one the lowest rates of female workforce participation of any industrialised nation suggesting that higher participation rates can be achieved.

73 Source: ACECQA (May 2015) *NQF Snapshot Q1 2015.*

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159 The Productivity Commission's finding that roughly 165,000 parents (on a full-time equivalent basis) with children aged under 13 years would like to work, or work more hours (most of them part time), but are not able to do so because they are experiencing difficulties with the affordability and accessibility of suitable child care services[74], also suggests that Australia's maternal workforce participation rate will increase if child care affordability and availability improve.

160 The government's introduction of a stricter activity test related to child care benefits is aimed at ensuring that government funding of child care results in an increased female workforce participation rate. Under the current structure there are no minimum hours of work / training / study for the CCR as long as both parents, or the sole parent, work at some point during the week while the child is in care. The CCB provides for up to 24 hours care per week for those not working, and up to 50 hours for those with 15 hours of work / study / training per week (or 30 hours per fortnight). The new activity test will apply to families with incomes over $65,000 as follows:

Activity test for families with income over $65,000

Hours of work / study / training per fortnight	Maximum hours of child care subsidy per fortnight Current system	New system
0 – 8	48	0
8 – 16	100	36
17 – 48	100	72
49	100	100

Source: McKell Institute (June 2015) *Baby steps or giant strides?*

Other government funding changes

Nanny Pilot Program

161 In April 2015, the government announced $246 million in funding over two years for the Interim Home Based Carer Subsidy Program.

162 From January 2016 the interim program will subsidise the cost of child care for over 10,000 children delivered in the family home by approximately 4,000 nannies. To be eligible for the subsidy, nannies will be required to be attached to an approved service.

163 The interim program will extend fee assistance to participating families who are having difficulty obtaining child care, particularly those with irregular working hours, families in rural or remote locations or families with other accessibility issues. Care will be provided for up to 50 hours per week, with families meeting the program guideline requirements and earning less than $250,000 per year, are eligible to apply.

164 As the program targets families who are generally not using child care services at present this is likely to be a positive outcome for service providers.

74 Source: Productivity Commission (2014) *Childcare and Early Childhood Learning* Inquiry report No. 73.

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Child Care Safety Net

165 The government will provide additional funding of $327.7 million over four years from 2015-16 to provide targeted support to disadvantaged or vulnerable families through a new Child Care Safety Net. The funding will target disadvantaged or vulnerable children, whether they are children with disabilities, children at risk of abuse, children from families on incomes under $60,000 or families facing financial risk. Existing programs that support disadvantaged and vulnerable families will be wound down along with the current Budget Based Funding programs so the impact on service providers is not clear.

Inclusion Support Program

166 The new $409 million Inclusion Support Program, beginning in July 2016, will provide more funding for services to get the necessary skilled staff and equipment to support children with special needs. This will include a significant increase in the inclusion support subsidy, meaning centre-based services will no longer have to pay a 'gap fee' to engage a Certificate III qualified staff member to assist with children with additional needs. Family day care providers will also be assisted to include children with additional needs.

167 The program will ensure that families with children who have special needs will have more access to child care services in mainstream facilities. The program will provide support to an estimated 11,300 services and is a positive initiative for the industry.

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VI Valuation methodology

Valuation approaches

168 RG 111 outlines the appropriate methodologies that a valuer should consider when valuing assets or securities for the purposes of, amongst other things, share buy-backs, selective capital reductions, schemes of arrangement, takeovers and prospectuses. These include:

(a) the discounted cash flow (DCF) methodology

(b) the application of earnings multiples appropriate to the businesses or industries in which the company or its profit centres are engaged, to the estimated future maintainable earnings or cash flows of the company, added to the estimated realisable value of any surplus assets

(c) the amount that would be available for distribution to shareholders in an orderly realisation of assets

(d) the quoted price of listed securities, when there is a liquid and active market and allowing for the fact that the quoted market price may not reflect their value on a 100% controlling interest basis

(e) any recent genuine offers received by the target for any business units or assets as a basis for valuation of those business units or assets.

169 Under the DCF methodology the value of the business is equal to the net present value (NPV) of the estimated future cash flows including a terminal value. In order to arrive at the NPV the future cash flows are discounted using a discount rate which reflects the risks associated with the cash flow stream.

170 Methodologies using capitalisation multiples of earnings or cash flows are commonly applied when valuing businesses where a future "maintainable" earnings stream can be established with a degree of confidence. Generally, this applies in circumstances where the business is relatively mature, has a proven track record and expectations of future profitability and has relatively steady growth prospects. Such a methodology is generally not applicable where a business is in start-up phase, has a finite life, or is likely to experience a significant change in growth prospects and risks in the future.

171 Capitalisation multiples can be applied to either estimates of future maintainable operating cash flow, earnings before interest, tax, depreciation and amortisation (EBITDA), earnings before interest, tax and amortisation of acquired intangibles (EBITA), earnings before interest and tax (EBIT) or net profit after tax. The appropriate multiple to be applied to such earnings is usually derived from stock market trading in shares in comparable companies which provide some guidance as to value and from precedent transactions within the industry. The multiples derived from these sources need to be reviewed in the context of the differing profiles and growth prospects between the company being valued and those considered comparable. When valuing controlling interests in a business an adjustment is also required to incorporate a premium for control. The earnings from any non-trading or surplus assets are excluded from the estimate of the maintainable earnings and the value of such assets is separately added to the value of the business in order to derive the total value of the company.

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172 An asset based methodology is applicable in circumstances where neither a capitalisation of earnings nor a DCF methodology is appropriate. It can also be applied where a business is no longer a going concern or where an orderly realisation of assets and distribution of the proceeds is proposed. Using this methodology, the value of the net assets of the company are adjusted for the time, cost and taxation consequences of realising the company's assets.

Methodology selected

Value of Affinity

173 The market value of Affinity has been assessed by aggregating the market value of the business operations, together with the realisable value of any surplus assets and deducting net borrowings.

174 The valuation of the business has been made on the basis of market value as a going concern. The primary valuation method used to value Affinity's business is the capitalisation of future maintainable earnings approach (using EBITA). Under this methodology the value of the business is represented by its core underlying maintainable EBITA capitalised at a rate (or EBITA multiple) reflecting the risk inherent in those earnings.

175 We have adopted this method when valuing Affinity for several reasons:

(a) the child care industry is a relatively mature industry (albeit fragmented, thus providing growth opportunities for acquirers) and Affinity's business is made up of individual centres that have long established histories of profitability

(b) we do not have long-term cash flow projections which we regard as sufficiently robust to enable a DCF valuation to be undertaken[75]

(c) EBITA multiples for listed companies operating in the sector can be derived from publicly available information

(d) transaction evidence in the sector is generally expressed in terms of EBITA multiples.

176 The following methods have been used to cross-check our valuation:

Methods used to cross-check valuation range	
Method	**Reason**
Capitalisation of earnings after tax (Price earnings (PE) multiple approach)	• Demonstrated history of profits and expectation of on-going profitability • Listed company PE multiples for 'comparable' companies are readily available • IPO evidence includes, inter alia, PE multiples
Listed market price adjusted for a premium for control	• Consideration given to whether the pre-bid share price is an appropriate reference point upon which to derive the value of Affinity shares on a 100% controlling interest basis

[75] We note that Affinity has prepared cash flow projections for financial reporting / impairment testing purposes. However, the objective of impairment tests is to opine on whether the carrying values of assets are appropriate rather than to assess market value of 100% of the equity of the entity.

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Value of Revised Scrip Offer consideration

177 For the purpose of assessing the value of the Revised Scrip Offer consideration we have had primary regard to the recent listed market prices of G8 Education shares. This is principally because the listed market prices of G8 Education shares are likely to represent a reasonable proxy for the amount that Affinity shareholders could expect to realise if they sold any G8 Education shares received as consideration either immediately or in the short-term.

178 We have also cross-checked the reasonableness of our assessed value of G8 Education shares being offered as consideration under the Revised Scrip Offer by reference to implied earnings multiples.

VII Valuation of 100% of Affinity

Overview

179 As stated in Section VI, the market value of Affinity has been assessed on a going concern basis by aggregating the market value of the business operations, together with the realisable value of any surplus assets and deducting net borrowings.

180 We have adopted the capitalisation of EBITA as our primary valuation method. Under this methodology the value of the business is represented by its core underlying EBITA capitalised at a rate (or EBITA multiple) reflecting the risk inherent in those earnings.

181 The resulting value has been cross-checked for reasonableness by reference to the PE multiples implied by our valuation. We have also given consideration to whether the pre-bid share price is an appropriate reference point for a further cross-check of our valuation.

Assessment of underlying EBITA

182 In order to assess the appropriate level of EBITA for valuation purposes we have had regard to the historic and forecast results of the business, and discussed the business' financial performance, operating environment and prospects with Affinity management.

183 In undertaking our analysis, we have separately considered:

(a) **the underlying profitability of individual centres** – we have reviewed the profitability of the centres at the underlying EBITDA level on an individual basis (i.e. the revenue and expenses directly incurred by the individual centres on a day-to-day basis excluding shared services and centralised costs such as regional managers, insurance etc)

(b) **costs incurred by head office** – we have reviewed the costs incurred by head office (before depreciation and amortisation) as part of the centralised corporate model that it operates (i.e. all other remaining expenses not directly incurred by the individual centres and not captured within (a))

(c) **depreciation and software amortisation charges** – we have reviewed management's forecast depreciation and software amortisation charges for FY15 and adjusted them to reflect the full year impact of recently acquired centres.

184 We have separately valued the management service fee income received by Affinity as a part of Other assets / (liabilities) (refer to paragraph 222).

Individual centres

185 We set out below a summary of the historic financial performance of the individual centres. As new centres have been acquired by Affinity throughout each reporting period, we have, for comparative purposes, grouped the Company's 161 centres according to their period of acquisition (i.e. by vintage):

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Affinity – underlying EBITDA by centre[1][2]

Centre groups by acquisition date	No of centres	Configured places[3]	1H14A $m	2H14A $m	1H15A $m	LTM[4] $m
Group 1 – Pre 1 Jan 14	**58[5]**	**4,216**				
Revenue			34.1	40.1	33.7	73.9
Underlying EBITDA			6.8	10.1	6.0	16.1
EBITDA margin			*19.8%*	*25.0%*	*17.9%*	*21.8%*
Group 2 – 1 Jan 14 to 30 Jun 14	**33[5]**	**2,587**				
Revenue			2.3	22.5	19.9	42.4
Underlying EBITDA			0.3	4.8	3.1	7.9
EBITDA margin			*15.0%*	*21.2%*	*15.3%*	*18.5%*
Group 3 – 1 Jul 14 to 31 Dec 14	**34[5]**	**2,383**				
Revenue				11.1	21.5	32.6
Underlying EBITDA				2.7	4.2	6.9
EBITDA margin				*24.0%*	*19.6%*	*21.2%*
Group 4 – 1 Jan 15 to 30 Jun 15	**36**	**2,862**				
Revenue					11.2	11.2
Underlying EBITDA					2.7	2.7
EBITDA margin					*23.7%*	*23.7%*
Total revenue			**36.4**	**73.7**	**86.4**	**160.1**
Total underlying EBITDA			**7.1**	**17.5**	**16.0**	**33.5**
EBITDA margin			***19.5%***	***23.7%***	***18.5%***	***20.9%***

Note:
1 Rounding differences may exist.
2 Underlying EBITDA excludes one-off transaction and integration expenses.
3 As at 30 June 2015.
4 Last 12 months (LTM).
5 As a result of centres either being split or consolidated post acquisition, the centre numbers set out above marginally differ to those previously reported by Affinity in its prospectus, 1H14 Appendix 4D and FY14 annual report.
Source: Affinity and LEA analysis.

186 In assessing the underlying aggregate EBITDA of Affinity's individual centres we note the following:

(a) revenue and underlying EBITDA contributions for Groups 2, 3 and 4 are only part period contributions for 1H14, 2H14 and 1H15 respectively. We estimate that the Group 4 centres would have generated revenue of approximately $27.0 million in 1H15 had they been acquired on 1 January 2015

(b) as previously discussed, Affinity's revenue and earnings are seasonal. On a like-with-like basis revenue for the first half (i.e. 1 January to 30 June) generally represents around 46% of revenue for any given 12 month period

(c) a 3.0% fee increase across the portfolio was implemented on 6 July 2015 (the benefits of which are therefore not reflected in the historic results)

(d) the revenue and underlying EBITDA achieved by the Group 1 centres for 1H15 was below that achieved in 1H14 (on lower revenue and margins)

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(e) the underlying EBITDA margin achieved by the Group 2 centres for 1H15 were relatively consistent with that achieved in 1H14 (notwithstanding 1H14 reflected a part period contribution)

(f) Affinity has acquired one further centre subsequent to 30 June 2015 and has entered into a contract to acquire another centre which is expected to settle in 2H15. The earnings of these centres are not reflected in any of the Groups set out above.

187 On 2 July 2015, Affinity announced that it expects underlying EBITDA for FY15 to be between $27 million and $32 million. This was revised to $30 million to $32 million on 18 August 2015. After adding back the costs incurred by head office (excluding depreciation and software amortisation) and a small amount of other income, this forecast reflects underlying forecast EBITDA for the individual centres for FY15 of between $45 million and $47 million. In relation to management's forecast, we note that:

(a) the lower end (i.e. $44 million) principally reflects a continuation of the lower 1H15 occupancy trend compared to 2014 and slight improvement in the ratio of employee expenses to revenue compared to 2H14 (due primarily to the benefit of the 3.0% increase in fees)

(b) the higher end (i.e. $47 million) principally reflects an increase in average occupancy levels in 2H15 to levels consistent with that achieved in 2H14 and a related improvement in the ratio of employee expenses to revenue compared to 2H14 (due to the 3.0% fee increase and assumed efficiency savings)

(c) neither the low nor high end of the range reflects the full year EBITDA contribution from centres acquired in 1H15 or post 30 June 2015.

188 Having regard to the above and the estimated full year impact of recently acquired centres, we have adopted aggregate underlying EBITDA for Affinity's individual centres of $48.0 million.

Costs incurred by head office

189 The categories of expense incurred by Affinity's head office are as follows:

(a) **Corporate Charges** – corporate head office expenses including costs associated with being a publicly listed company (e.g. listing and registry fees, shareholder communication costs etc), CEO and CFO (and other head office staff member) salaries, head office lease charges and general consultancy fees

(b) **Straight line lease expenses** – a non-cash accounting entry to spread the cost of lease obligations evenly over the lease term

(c) a number of costs which are paid by Affinity's head office but relate to the operation of the individual centres:

(i) **Shared Services** – costs associated with the direct oversight of the individual centres (operational managers, regional managers and facilities management) as well as shared services being human resources, payroll, accounts processing and finance

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(ii) **Centralised Costs** – costs directly attributable to the individual centres but centrally controlled as part of Affinity's centralised corporate model. Costs include marketing, IT, insurance and procurement.

190 The FY14 and forecast FY15 costs incurred by Affinity's head office (excluding depreciation and amortisation) are set out below. We note that Affinity has implemented various cost saving initiatives in 1H15 and early 2H15[76]. The estimated full year benefit of these initiatives is reflected in the FY15 pro forma forecast:

Affinity – costs incurred by head office(1)	**FY14 Actual $m**	**FY15 Forecast $m**	**FY15 Pro forma(2) $m**
Public company costs(3)		(0.9)	(0.9)
Head office employees(4)		(2.6)	(2.6)
Ad-hoc consultancy costs		(0.1)	(0.1)
Accounting, tax and external audit costs		(0.3)	(0.3)
Other(5)		(0.5)	(0.2)
Corporate Charges		**(4.4)**	**(4.1)**
Straight line lease expenses (non-cash)		**(2.2)**	**-**
Shared Services and Centralised Costs		**(9.3)**	**(8.1)**
Total excluding depreciation and amortisation	**(11.9)**	**(15.9)**	**(12.2)**

Note:
1 Rounding differences may exist.
2 Ongoing estimated full run-rate cash costs.
3 Listing fees, shareholder communication costs, Board of director costs etc.
4 Chief Executive Officer, Chief Financial Officer, Chief Operations Officer, Financial Controller and associated support staff.
5 An allocation based on head count of (inter alia) rent, insurance, travel, IT, recruitment, training.
Source: Affinity and LEA analysis.

191 A proportion of the Corporate Charges would be saved in the event that Affinity was acquired and delisted from the ASX. Based upon discussions with management and our analysis of the individual cost items incurred, savings are estimated to be approximately $2.9 million per annum. In addition, there are likely to be further Shared Services and Centralised Cost savings available to a purchaser with a large existing portfolio of child care centres.

192 Having regard to the above, we have adopted head office costs of $8.6 million per annum (net of a share of synergy benefits).

Depreciation and software amortisation

193 Management have provided us their forecast depreciation and software amortisation charges for FY15. We have reviewed the forecast and adjusted it to reflect the full year impact of the centres acquired in 1H15 (as well as the two centres acquired post 30 June 2015[77]). For the purposes of this report we have adopted depreciation and software amortisation charges of $2.3 million.

76 For example, employee headcount reductions.
77 We note that one of these centres is yet to settle.

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Conclusion on EBITA for valuation purposes

194 Based on the above, we have adopted EBITA for valuation purposes as follows:

Affinity – EBITA for valuation purposes	Paragraph	$m
EBITDA of individual centres	188	48.0
Costs incurred by head office	192	(8.6)
EBITDA for valuation purposes		39.4
Depreciation and software amortisation	193	(2.3)
EBITA for valuation purposes		**37.1**

EBITA multiple

195 The selection of the appropriate EBITA multiple to apply is a matter of judgement but normally involves consideration of a number of factors including, but not limited to:

- The stability and quality of earnings
- The quality of the management and the likely continuity of management
- The nature and size of the business
- The spread and financial standing of customers
- The financial structure of the company and gearing level
- The multiples attributed by share market investors to listed companies involved in similar activities or exposed to the same broad industry sectors
- The multiples that have been paid in recent acquisitions of businesses involved in similar activities or exposed to the same broad industry sectors
- The future prospects of the business including the growth potential of the industry in which it is engaged, strength of competitors, barriers to entry, etc
- The cyclical nature of the industry
- Expected changes in interest rates
- The asset backing of the underlying business of the company and the quality of the assets
- The extent to which a premium for control is appropriate
- Whether the assessment is consistent with historical and prospective earnings

196 We discuss below specific factors taken into consideration when assessing the appropriate EBITA multiple range for Affinity.

197 We note that EBITA adopted for valuation purposes reflects the full year earnings contribution from recently acquired centres. We have taken this into consideration in our assessment of the appropriate EBITA multiple range.

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Listed company multiples

198 The EBITA multiples of Australian listed companies operating in the child care sector are set out below:

Listed company multiples[(1)(2)]	Enterprise Value $m	EV / EBITA multiples FY15 Forecast x	FY16 Forecast x
G8 Education	1,461	9.3	7.8
Affinity:			
Based on 2 July 2015 close	161	6.2	5.2
Based on 2 July 2015 VWAP[(3)]	187	7.3	6.1
Evolve Education Group Limited (Evolve Education)	156	6.0	5.9
Think Childcare Limited (Think Childcare)	38	5.7	4.8

Note:
1 A brief description of each company's operations are summarised at Appendix C.
2 G8 Education and Affinity as at 2 July 2015 (i.e. the date prior to the announcement of G8 Education's intention to make a takeover offer for Affinity). Evolve Education and Think Childcare as at 20 August 2015. Multiples based upon latest publicly available information at the date of calculation.
3 Volume weighted average price (VWAP).

199 In relation to the above we note that:

(a) the EBITA multiples for G8 Education and Affinity have been calculated based on their closing share prices on 2 July 2015 (i.e. prior to the announcement of G8 Education's intention to make a takeover offer for Affinity).

On 2 July 2015 the price of Affinity shares fell sharply in response to the updated earnings guidance provided by the Company prior to the commencement of trading on that day. At the end of trading on 2 July 2015 Affinity shares closed down 34%[78], having traded in a wide range between 49.0 cents and 74.5 cents per share. On the day G8 Education acquired approximately 38 million shares (16.4%) at a price of 70 cents per share (this was not announced until the following day). Including G8 Education's purchase, the VWAP on 2 July 2015 was 65.5 cents per share. Given the volatility in the Affinity share price in response to the updated earnings guidance, we have also set out above the EBITA multiples for Affinity using the VWAP on 2 July 2015

(b) Evolve Education, although listed in Australia, operates in the New Zealand (not Australian) child care sector

(c) all four companies (particularly G8 Education and Affinity) have made acquisitions in calendar 2015. Thus, only the FY16 EBITA multiples above reflect the full year impact of these acquisitions and therefore provide a better indicator of their respective EBITA multiples

(d) with the exception of the Affinity multiples based on the VWAP on 2 July 2015 (which reflect, in part, the acquisition of a pre-bid stake by G8 Education and are therefore

78 Compared to the last traded price on 1 July 2015.

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impacted by corporate activity), the above multiples do not reflect a takeover (i.e. control) premium

(e) the multiples are based upon closing share prices (and VWAP) on specific days and are not necessarily representative of the range of multiples that the companies trade on over time (which are shown further below).

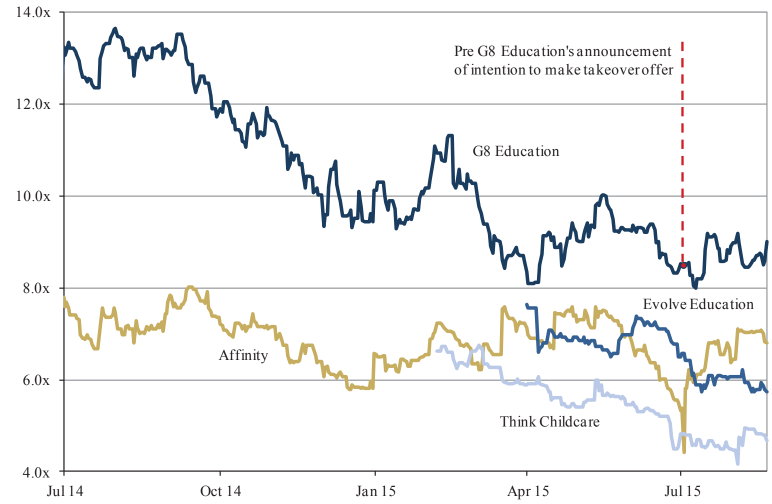
200 Empirical evidence undertaken by LEA indicates that the average premium paid above the listed market price in successful takeovers in Australia ranges between 30% and 35% (assuming the pre-bid market price does not reflect any speculation of the takeover). This broadly translates to a premium of 20% to 25% at the EBITA multiple or enterprise value level, although this varies depending on the level of debt funding employed in each company.

201 However, we note that the above listed companies have generally traded above the multiples implied by recent transaction evidence in the child care sector, which indicates that higher values (and EBITA multiples) can generally by achieved by aggregating large child care centre portfolios and listing them on the ASX. Accordingly, in our opinion, it is not appropriate to apply a significant control premium. Furthermore, we note that observed control premiums incorporate an element which is attributable to synergy value and that our assessment of Affinity's EBITA (for valuation purposes) already incorporates an allowance for synergy benefits arising (predominately) from public company cost savings.

Listed company multiples over time

202 We set out below the one year forward EBITA multiples (based on average analyst forecasts) for the above listed child care companies from 1 July 2014 to 20 August 2015:

One year forward EBITA multiples
1 July 2014 to 20 August 2015(1)



58

Note:
1 Think Childcare and Evolve Education multiples from 2 February 2015 and 30 March 2015 respectively, being the respective dates the companies were covered by more than one analyst. Affinity's enterprise value is based upon pro forma net debt from 17 April 2015 to 30 June 2015. The multiples for G8 Education and Affinity post 2 July 2015 are affected by the announcement of G8 Education's intention to make a takeover offer for Affinity.
Source: Bloomberg and LEA analysis.

203 As evidenced from the above:

(a) G8 Education has consistently traded on higher EBITA multiples than Affinity. In our view this reflects, inter-alia, the significant size differences between the companies (as evidenced by their respective market capitalisations[79]) and the fact that G8 Education's child care centre portfolio is more heavily weighted toward metropolitan regions which tend to exhibit higher and less volatile child care centre occupancy ratios

(b) both G8 Education and Affinity have generally traded on higher EBITA multiples to Think Childcare due to, inter alia, their greater size and the acquisitive growth strategies pursued since listing by both companies[80]

(c) the EBITA multiples for each company have declined over the period (as have their share prices) due to, inter alia, increasing concerns about the ability of the companies to achieve organic growth as a result of softer industry conditions[81] and regulatory changes[82]. Further, we note that it has become more difficult for the companies to maintain their high rates of acquisitive growth due to:

(i) the much larger and ever increasing size of the businesses, and in turn the decreasing relative marginal contribution to earnings achieved from acquisitions[83]

(ii) the diminishing number of opportunities to acquire a large number of centres in a single transaction, and

(iii) increased competition for the acquisition of centres which, all else being equal, is likely to lead to higher prices being paid (on an earnings multiple basis).

Transaction evidence

204 There have been a number of recent transactions in the child care industry.

IPO evidence

205 A summary of the EBITA multiples implied by recent IPO transactions is shown below:

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79 The respective market capitalisations on 2 July 2015 were $1.2 billion (G8 Education) and $125 million (Affinity based on closing price of 54 cents per share).

80 In contrast the level of acquisitive growth achieved by Think Childcare has been more modest in the short period since its listing.

81 For example, as noted in Section III, Affinity has indicated that increases in occupancy levels post 31 March 2015 have not been as high as experienced in 2014.

82 For example, the NQF introduced changes to the educator-child ratios which will increase in many states from 1 January 2016 and potentially increase the wage costs of the centre operators in those states.

83 This is particularly relevant for G8 Education which enjoyed first-mover advantage and was able to significantly increase the size of its centre portfolio in a very short period of time.

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Transaction evidence – IPOs					
Date[1]	IPO	No. of centres	No. of managed centres	Enterprise value $m	EV / EBITA Forecast[2] x
5 Dec 14	Evolve Education	85[3]	-	173.1[4]	7.8
24 Oct 14	Think Childcare	30	17	46.1	6.9
9 Dec 13	Affinity	57	11	88.4	7.3

Note:
1 Date of listing. Brief descriptions of each IPO are set out at Appendix D.
2 Based upon one year forward earnings.
3 Evolve Education also held 91 home based education licences at the time of listing.
4 Converted to AUD at the AUD:NZD exchange rate prevailing on date of listing.
Source: Company announcements, press commentary and LEA analysis.

206 The multiples implied by recent IPOs do not reflect a control premium and are based on the full year earnings from the portfolio of centres owned by the companies at their date of listing. In our opinion, the higher multiples attributable to them (compared to the multiples implied by the centre transactions below) principally relate to the economies of scale that can be achieved from owning a large portfolio of centres and the ability to utilise those economies of scale (and superior access to debt and equity markets) to drive future earnings growth from acquisitions.

207 Notwithstanding the above, we note that as at 20 August 2015 Evolve Education and Think Childcare were trading below their respective IPO issue prices and IPO multiples. Affinity was also trading below its IPO issue price and IPO multiples prior to the announcement of G8 Education's intention to make a takeover offer for the Company.

Centre transaction evidence

208 The EBITA multiples implied by recent centre acquisitions (as reported by the acquirers at the time of announcement of the acquisition) have ranged between 3.9 times and 7.0 times, with most transactions occurring in the range of 4.0 to 5.0 times EBITA[84].

209 In respect of the transaction evidence, we note:

(a) the centre transaction announcements generally relate to the aggregate purchase price and average multiple paid for a group of centres that have been acquired via separately negotiated transactions with different vendors (as opposed to the purchase of a group of centres from a single vendor or multiple vendors in a single negotiated transaction). The multiples paid for the individual centres (or portfolios of centres) may be higher or lower than the average reported multiple

(b) the largest of the transactions, being G8 Education's acquisition of Sterling Early Education's 91 centres on 24 March 2014, was reported as occurring at 5.8 times annualised centre based EBIT for the year ending 31 December 2015

(c) G8 Education and Affinity are generally trading on higher EBITA multiples than the transaction evidence. We have attributed this listed company premium to:

(i) the larger size of G8 Education and Affinity

84 Brief descriptions of each transaction are set out at Appendix D.

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(ii) the economies of scale that can be achieved from owning large portfolios of centres

(iii) G8 Education's and Affinity's superior access to debt and equity capital (as a result of their listed public company status), which has enabled both companies to pursue value accretive acquisitions[85].

Other transaction evidence

210 In addition to the above, we note that in January 2010 the independent expert appointed to opine on the merger of Early Learning Services Limited (ELS) and Payce Child Care Pty Limited (which was renamed G8 Education) valued ELS and the merged entity on a one year forward EBITA multiple of 7 to 8 times.

211 We also note that Affinity received a number of unsolicited approaches from G8 Education prior to the announcement of G8 Education's intention to make a takeover offer for the Company. The EBITA multiples implied by those approaches (which were rejected by Affinity) are as follows:

Previous G8 Education approaches for Affinity – implied EBITA multiples[1]

		EV / EBITA multiples		
	Enterprise Value $m	FY15 Forecast x	FY16 Forecast x	1 year forward x
24 April 2015 approach	256	8.2	6.2	7.4
24 June 2015 approach	191	6.7	5.1	5.8

Note:
1 Based upon listed market price on the date, pro forma 31December 2014 balance sheet and analyst consensus forecasts.
Source: Affinity ASX announcement dated 6 April 2015, Bloomberg and LEA analysis.

212 However, it should be noted that both approaches occurred prior to Affinity providing the market with its underlying FY15 EBITDA earnings guidance on 2 July 2015. This guidance was less than the then current consensus EBITDA estimate. Had G8 Education had the benefit of this information prior to the approaches, then the proposed terms (under both approaches) may have been less favourable to Affinity shareholders.

Potential synergies

213 In its Replacement Bidder's Statement dated 20 August 2015, G8 Education has indicated that it expects to generate significant synergies of around $6.5 million per annum from the acquisition of Affinity, as follows:

"G8 Education anticipates that, following integration and assuming G8 education is entitled to proceed to compulsory acquisition and does so, it will be able to operate the 12,000 Affinity Education licensed childcare places, at a cost of $455 per licensed place. This would see a reduction in costs for the Affinity Education licensed places from $1,000 per place to $455 per place, a saving of $545 per licensed place or $6.5 million per annum. G8 Education

85 For example, Affinity has a $100 million acquisition facility from the CBA which can be used for acquisitions.

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expects that the duplication in administrative and corporate functions, including head office positions at Affinity Education and related head office costs, will be a primary source of those cost savings. By way of example, G8 Education expects that certain head office positions associated with Affinity Education's company secretarial, financial management and board will no longer be required. Similarly, costs associated with Affinity Education's ASX listing will no longer be incurred in the event that Affinity Education is delisted from ASX (refer to sections 8.2 and 8.3 for more information of G8 Education's intentions in respect of the Affinity Education's ASX listing).

Given the presentation of expenses in Affinity Education's income statement does not separately identify the head office and related functions, including those identified above, G8 Education is unable to identify from a review of public information that exact amount of likely cost synergies. However, the Board considers a marginal cost of $455 per place an achievable target, consistent with G8 Education's previous experience with the integration of child care centres that it has acquired."[86]

214 As set out in RG 111, synergies that are not available to other potential bidders should not be taken into account in the valuation of the target company when assessing whether an offer is fair. While some of the synergies identified by G8 Education will be unique to them, in our opinion, a proportion of these annual synergies could be generated by other acquirers and have been reflected in our assessment of Affinity's EBITA (for valuation purposes).

215 Accordingly, in our opinion, it is inappropriate (in the circumstances of Affinity) to incorporate a separate value for synergies arising from public company cost savings in our multiple.

Other factors

216 In order to assess the appropriate EBITA multiple for Affinity we have also had regard to:

(a) **Macro-economic environment** – Australia is presently experiencing relatively soft economic conditions with unemployment at levels not seen since the early 2000s[87]

(b) **Industry drivers** – demand for child care centre places is expected to continue to increase over time due to factors such as increasing female participation in the workforce and general population trends. The industry is also expected to continue to benefit from favourable government policy (e.g. child care rebates / subsidies)

(c) **Consolidation opportunities** – the child care industry is highly fragmented and there remains significant opportunity for future acquisition growth. However, the ability to acquire a large number of centres in a single transaction is diminishing (and competition for assets appears to be intensifying)

(d) **Competitive landscape** – in recent history, G8 Education and Affinity have been the principal drivers of consolidation in the industry[88]. Should G8 Education be successful in acquiring Affinity it will remove one of its key consolidation competitors.

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86 Replacement Bidder's Statement dated 20 August 2015, pages 15 and 16.

87 Australian Financial Review, *Jobless rate matches 13-year high of 6.3pc*, 7 August 2015.

88 To date, Think Childcare has been much less active in this regard.

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Conclusion on appropriate EBITA multiple

217 Based on the above, in our opinion, an EBITA multiple range of 6.5 times to 7.0 times is appropriate when applied to the level of underlying EBITA adopted for valuation purposes.

Valuation of Affinity's business

218 Given the above, we have assessed the value of Affinity's business as follows:

Affinity – value of business	Paragraph	Low $m	High $m
EBITA for valuation purposes	194	37.1	37.1
EBITA multiple	217	6.5	7.0
Enterprise value		**241.2**	**259.7**

Other assets / (liabilities)

219 Affinity has a number of non-core or surplus assets / (liabilities) that are not reflected in our abovementioned business valuation and for which an allowance must be made.

Assets held for sale

220 Affinity holds two freehold properties located at Ayr and Kelso in QLD. Both properties were acquired as part of the IPO acquisition of the initial portfolio of centres and management rights. At the time of acquisition it was and today, remains management's intention to dispose of these two assets.

221 Both properties are carried on balance sheet at $250,000. We have adopted this value for the purposes of this report.

Management rights

222 Affinity currently provides management services to six child care centres in return for the payment of a monthly management fee.

223 Although we are not permitted to disclose the terms of the individual arrangements, as they are commercially sensitive, we note that total revenue (per half year) received from the contracts is expected to be marginally less than the reported amount in 1H15 and that the contracts have an average weighted expiry date of approximately two years. We have discounted the cash flows from the contracts through to their respective dates of expiry at an after tax cost of equity of between 12% and 13%. We have then added an allowance for the probability of renewal.

224 Given the above, for the purposes of this report, we have attributed a value of between $500,000 and $750,000 to the management rights.

Implementation costs associated with realising head office cost savings

225 Our assessment of underlying EBITA on a 100% controlling interest basis assumes that a proportion of public company related costs incurred by head office would be saved.

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226 Based upon discussions with management the implementation costs needed to be incurred in order to achieve the savings are estimated at approximately $1.0 million (net of assumed corporate tax savings of 30%).

Summary of other assets / (liabilities)

227 Based upon the above, we have assessed the value of Affinity's other assets / (liabilities) as follows:

Affinity – other assets / (liabilities)	Paragraph	Low $000	High $000
Assets held for sale	221	250	250
Management rights	224	500	750
Implementation costs – head office cost savings	226	(1,000)	(1,000)
Total other assets / (liabilities)		**(250)**	**-**

Net cash / (debt)

228 As at 30 June 2015, Affinity had net debt of $21.1 million, this has reduced to $19.6 million as at 31 July 2015. In addition, we note that:

(a) Affinity has $0.2 million in retention payment liabilities relating to centres acquired prior to 30 June 2015 (refer to paragraph 68)

(b) as at 31 July 2015, Affinity had received $3.9 million in advance payments from the Federal government in connection with the Long Day Care Professional Development program (refer paragraphs 68, 149 and 150). The monies can only be used for the purposes of the program and any unused cash must be returned

(c) Affinity is contracted to settle upon one further centre

(d) the 31 July 2015 net debt position does not reflect the costs of responding to the Offers.

229 Based upon the above, we have concluded that net debt of $27.5 million is appropriate for valuation purposes.

Share capital outstanding

230 Affinity has some 231.5 million fully paid ordinary shares on issue.

231 In addition there are 1.3 million performance rights that were issued to executive directors and senior management in May 2015. These performance rights vest on 31 December 2017 and convert, subject to the achievement of specified performance benchmarks, on a one-for-one basis into ordinary shares for nil consideration. However, in the event of a takeover:

(a) the rights automatically vest and convert to ordinary shares if the offer becomes unconditional and results in the acquirer obtaining an interest of more than 50%

(b) the Affinity Board has the discretion to allow the rights to vest and convert to ordinary shares if, in its opinion, (a) is likely to occur.

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232 Accordingly, when valuing 100% of the shares in Affinity, in our opinion, it is appropriate to assume that these additional shares will be issued. For valuation purposes we have therefore assumed 232.8 million fully diluted shares on issue.

Valuation summary

233 Given the above, the value of 100% of Affinity on a controlling interest basis is as follows:

Affinity – valuation summary	Paragraph	Low $m	High $m
Enterprise value	218	241.2	259.7
Other assets / (liabilities)	227	(0.3)	-
Net debt	229	(27.5)	(27.5)
Equity value – controlling interest basis		213.4	232.2
Number of shares on issue (million)[1]	232	232.8	232.8
Affinity value per share – controlling interest basis ($)		**0.92**	**1.00**

Note:
1 Assuming the exercise of 1.3 million executive performance rights.

234 We have cross-checked our valuation of Affinity's business for reasonableness by reference to the capitalisation of earnings after tax (i.e. PE multiple) approach. We have also given consideration to whether the pre-bid share price is an appropriate reference point for a further cross-check of our valuation.

Implied PE multiples

235 We have calculated the PE multiples implied by our valuation range. For comparative purposes we have calculated the implied PE multiple based on stand-alone earnings of Affinity (i.e. pre-synergies):

Affinity – implied PE multiples based on stand-alone (i.e. pre-synergy) earnings[1]	Paragraph	Low $m	High $m
Enterprise value	218	241.2	259.7
Net debt	229	(27.5)	(27.5)
Implied equity value excluding other assets / (liabilities)		213.7	232.2
Assessed EBITA for valuation purposes	194	37.1	37.1
Deduct synergy benefits implicit within EBITA above		(3.6)	(3.6)
Stand-alone EBITA (i.e. pre synergies)		33.5	33.5
Less net interest expense at 5.0% per annum[2]		(1.4)	(1.4)
PBT		32.1	32.1
Notional company tax at 30%		(9.6)	(9.6)
NPAT		22.5	22.5
Implied PE multiple (times)		**9.5**	**10.3**

Note:
1 Rounding differences may exist.
2 Broadly based upon Affinity's cost of debt.
Source: Affinity and LEA analysis.

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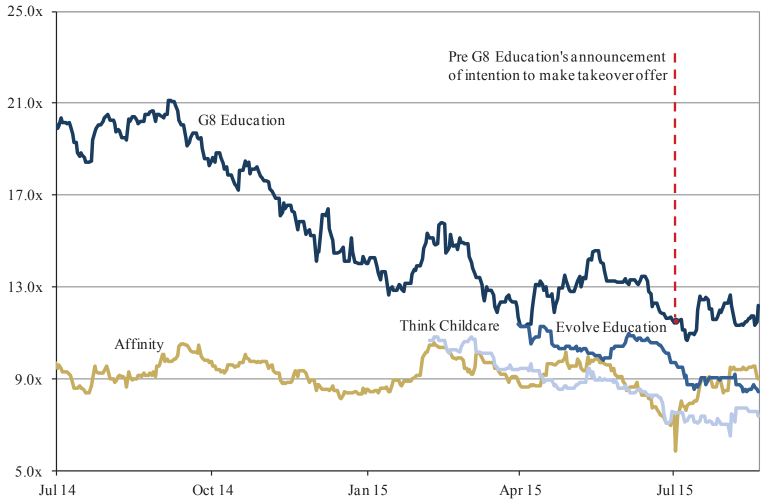
236 We set out below the one year forward PE multiples (based on average analyst forecasts) for the listed child care companies from 1 July 2014 to 20 August 2015:

One year forward PE multiples
1 July 2014 to 20 August 2015(1)



Note:
1 Think Childcare and Evolve Education multiples from 2 February 2015 and 30 March 2015 respectively, being the respective dates the companies were covered by more than one analyst. The multiples for G8 Education and Affinity post 2 July 2015 are affected by the announcement of G8 Education's intention to make a takeover offer for Affinity.
Source: Bloomberg and LEA analysis.

237 We consider the (stand-alone) PE multiples implied by our valuation range to be reasonable in comparison to the listed multiples shown above, noting that:

(a) our assessed valuation range reflects a 100% controlling interest value. In comparison, the listed company multiples, with the exception of Affinity post 3 July 2015, reflect portfolio interest multiples

(b) whilst Affinity has consistently traded at around 9.0 times (on a portfolio basis), its PE multiple deteriorated significantly in the period leading up to the announcement of G8 Education's intention to make a takeover offer for the Company

(c) Affinity, Evolve Education and Think Childcare listed on (portfolio) PE multiples of 10.8, 10.7 and 9.0 times forecast earnings

(d) the listed companies already trade at multiples above that implied by recent 'centre' transaction evidence.

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Comparison with listed market price

238 In our view, the recent listed market prices of Affinity shares prior to the announcement of G8 Education's intention to make a takeover offer for the Company are not a reliable reference point upon which to derive an indicative value of Affinity shares on a 100% controlling interest basis. This is because:

(a) on 2 July 2015, the price of Affinity shares fell sharply (on high volumes) in response to the updated earnings guidance provided by the Company prior to the commencement of trading on that day. Observed share price trading prior to 2 July 2015 did not reflect this new market sensitive information

(b) in our view it is inappropriate to base the pre-bid market price upon the very limited share trading that occurred between the Company's earnings announcement and the announcement of G8 Education's intention to make a takeover offer (i.e. one day of trading). This is because, in our opinion:

(i) it increases the risk of distortion brought about by short-term price volatility

(ii) the market did not have sufficient time to absorb and appropriately adjust to the new information. For example, many analyst reports containing updated earnings estimates and buy / sell / hold recommendations were not published until after the close of trading on 2 July 2015 and this information was therefore not reflected in the intra-day or closing prices

(c) subsequent to 2 July 2015, Affinity released its results for the six months to 30 June 2015. The announcement contained revised underlying EBITDA guidance for FY15 of between $30 million and $32 million as well as further information on the Company's performance subsequent to 30 June 2015. This information which is reflected in our valuation was not known to the market prior to the announcement of G8 Education's intention to make a takeover offer for the Company.

239 Given the above, we do not consider the pre-bid share price to be an appropriate reference point for a further cross-check of our valuation.

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VIII Valuation of Revised Scrip Offer consideration

Approach

240 Pursuant to the Revised Scrip Offer G8 Education is offering Affinity shareholders one fully paid ordinary share in G8 Education for every 4.25 fully paid ordinary shares held in Affinity.

241 As stated in Section VI, it is customary in transactions where scrip is offered as consideration to rely upon the listed market price of the bidder's shares[89] (in this case G8 Education) as the reference point for estimating the realisable value of the consideration offered. This is principally because:

(a) the listed market prices of G8 Education shares are likely to represent a reasonable proxy for the amount that Affinity shareholders could expect to realise if they sold any G8 Education shares received as consideration either immediately, or in the short-term

(b) any decision to continue to hold G8 Education shares beyond the immediate to short-term is a separate investment decision which should be made by shareholders having regard to their risk profile, liquidity preference, tax position and expectations as to value and future market conditions. It is also not possible to accurately predict future share price movements

(c) whilst there may be a future opportunity for Affinity shareholders to share in a control premium in the event G8 Education was acquired, this is not a scenario that we consider likely in the short-term.

242 Accordingly, in our opinion, the recent market prices of G8 Education shares are the appropriate reference point for estimating the value of the Revised Scrip Offer consideration. In doing so, we have also considered the depth of the market for those securities and the volatility of the share price.

243 We have also cross-checked the reasonableness of our assessed value of G8 Education shares being offered as consideration under the Revised Scrip Offer by reference to implied earnings multiples.

Recent share prices

Recent share trading history

244 The historical share prices for G8 Education are set out in Section IV. More recent trading in G8 Education shares (together with the S&P / ASX 300 Index) is shown below:

[89] Provided there is sufficient liquidity in the bidder's shares.

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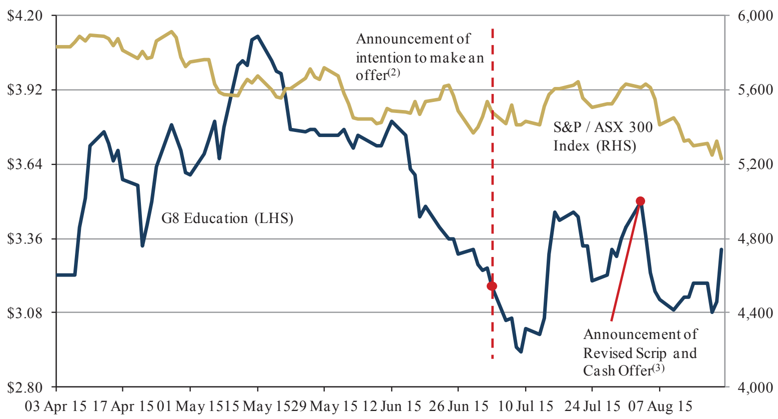
G8 Education – recent share price history
3 April 2015 to 20 August 2015 [(1)]



Period	Low[(4)] $	High[(4)] $	VWAP $	Shares traded 000	Value traded $m
Pre announcement of intention to make an offer[(2)]					
1 month to 2 Jul 15	3.09	3.86	3.49	82,308	287.3
3 months to 2 Jul 15	3.09	4.15	3.64	260,682	949.7
Post announcement of intention to make an offer[(2)]					
3 Jul 15 to 2 Aug 15 (inclusive)[(3)]	2.86	3.65	3.21	64,536	207.4
3 Jul 15 to 20 Aug 15 (inclusive)	2.86	3.65	3.22	116,366	374.2
Post announcement of the Revised Scrip Offer and Cash Offer[(3)]					
3 Aug 15 to 20 Aug 15 (inclusive)	3.05	3.65	3.22	51,830	166.8

Note:
1 Based upon closing prices.
2 G8 Education announced its intention to make a takeover offer for Affinity on 3 July 2015.
3 G8 Education announced the Revised Scrip Offer and Cash Offer on 3 August 2015.
4 Based upon intraday trading.
Source: Bloomberg and LEA analysis.

245 As indicated above, whilst the listed market price of G8 Education shares has traded within a fairly wide range ($2.86 to $4.15), the observed VWAPs subsequent to the announcement of G8 Education's intention to make a takeover offer for Affinity have remained more consistent at $3.21 to $3.22.

246 In our view, the listed market prices of G8 Education shares following the announcement of its intention to make an offer for Affinity and in particular, the announcement of the Revised Scrip and Cash Offer (on the morning of 3 August 2015) are more relevant when assessing the value of the Revised Scrip Offer consideration as they reflect the market's view[90] of the

90 Albeit probability weighted for the chance of successful completion of the Offers.

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combined value of the two entities based on the terms of the Offers, as well as the significant synergies that are expected to be realised.

Share trading restrictions and liquidity

247 There are no significant restrictions on trading in G8 Education which would prevent sufficient trading (on a day-to-day basis) to produce an unbiased share price.

248 Further, in our view, the liquidity in G8 Education shares over the previous 12 months has been high (refer to Section IV). In particular, since the G8 Education's announcement of the intention to make a takeover offer on 3 July 2015 to 20 August 2015, the total value of G8 Education shares traded was $374.2 million.

Information disclosures

249 G8 Education is well researched and analysed by share broking firms and institutional investors. As at 20 August 2015, earnings forecasts for G8 Education (for FY15 and FY16) were provided on Bloomberg from 11 securities / brokerage firms.

250 Significant information in relation to the operations of G8 Education has also been disclosed in its financial reports and ASX announcements. Further, G8 Education has an obligation under the ASX Listing Rules (subject to certain exemptions) to notify the ASX immediately of any information that it becomes aware of concerning G8 Education which a reasonable person would expect to have a material effect on the price or value of G8 Education shares.

Number of G8 Education shares to be issued as consideration

251 Pursuant to the Revised Scrip Offer G8 Education is offering Affinity shareholders one fully paid ordinary share in G8 Education for every 4.25 fully paid ordinary shares held in Affinity. As at 20 August 2015 Affinity had 231.5 million ordinary shares on issue plus a further 1.3 performance rights which, for the purposes of this report, we have assumed will vest and covert to ordinary shares. Should all Affinity shareholders (other than G8 Education) accept the Revised Scrip Offer then a maximum number of some 43.9 million new G8 Education shares will be issued[91].

252 The maximum number of shares to be issued by G8 Education as consideration under the Revised Scrip Offer will therefore represent only 10.7% of the enlarged capital base of G8 Education, as follows:

91 As at 20 August 2015 G8 Education held 46.1 million Affinity shares.

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Maximum Revised Scrip Offer consideration as a % of enlarged capital base[1]		
		million
Number of ordinary G8 Education shares outstanding[2]		367.8
Maximum number of shares to be issued pursuant to the Revised Scrip Offer[3]	(A)	43.9
Implied total shares outstanding in G8 Education	(B)	411.8
Affinity shareholders' maximum interest in G8 Education post transaction	(A) / (B)	10.7%

Note:
1 Rounding differences exist.
2 As at 20 August 2015 G8 Education had 367.8 million ordinary shares on issue (this includes 3.1 million shares issued to management on 16 June 2015).
3 Being 231.5 million Affinity shares, plus 1.3 million performance rights, less 46.1 million shares held by G8 Education, converted to G8 Education shares at the exchange ratio of 1 G8 Education share for every 4.25 Affinity shares held.

253 Based on the above, if a large number of Affinity shareholders elect to accept the Revised Scrip Offer and subsequently decide to sell their G8 Education shares on market, this could result in a short-term adverse price impact caused by the potential oversupply of G8 Education shares.

254 However, this short-term adverse price risk is arguably mitigated because Affinity shareholders wishing to realise their investment in Affinity are more likely to sell their Affinity shares on-market either at, or above the Cash Offer price of $0.80 per share. Further those Affinity shareholders that do accept the Revised Scrip Offer may also have the ability to elect to receive cash per share in lieu of G8 Education shares following the close of the Revised Scrip Offer[92].

Dilution and synergies

255 To the extent that G8 Education is paying a control premium (above the listed market price) for Affinity there will be a dilutive effect on the value of G8 Education shares should the Offers be successful. This is because the listed market price of G8 Education shares will reflect a portfolio rather than a controlling interest in the enlarged entity. In the absence of synergies this dilution often results in a fall in the share price of the bidder.

256 However, G8 Education has indicated that synergies of $6.5 million per annum are likely to be realised from combining the two businesses. In particular, many analysts that cover G8 Education have also highlighted that the proposed acquisition of Affinity under the Offers is significantly EPS accretive for G8 Education shareholders (prior to the amortisation of acquired intangibles)[93].

92 It should be noted that this option will only arise, if (and only if) G8 Education acquires Affinity shares for cash outside of the Revised Scrip Offer during the offer period (e.g. under the Cash Offer or otherwise). G8 Education has until 14 days after the close of the Revised Scrip Offer to provide Affinity shareholders that accepted the Revised Scrip Offer with their right to make the election. Affinity shareholders will have one month from the date of the notice to make the election.

93 For example, UBS, *G8 Education Ltd: All in*, 3 August 2015 and Ord Minnett, *Childcare Sector: GEM increases offer for AFJ to $0.80*, 3 August 2015 and Deutsche Bank, *G8 Education Limited: AFJ bid sweetened with cash and higher scrip offer*, 4 August 2015.

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257 Given the size of expected synergies relative to the stand-alone earnings of Affinity, in our opinion, it is reasonable to conclude that the value of expected synergies would exceed the dilutive effect discussed above.

Conclusion

258 In summary, in assessing the value of the G8 Education shares offered as consideration under the Revised Scrip Offer we have had regard to:

(a) the recent trading range of G8 Education shares, particularly subsequent to the announcement of the Revised Scrip Offer and Cash Offer on 3 August 2015

(b) the maximum number of shares to be issued by G8 Education under the Revised Scrip Offer, which is low compared to the enlarged (maximum) number of G8 Education shares on issue

(c) the likely level of on-market trading in G8 Education shares should the Offers be successful, having regard to factors including:

(i) the modest risk of a potential oversupply of G8 Education shares from those shareholders in Affinity that elect to accept the Revised Scrip Offer and subsequently decide they do not wish to retain the G8 Education shares received as consideration[94]

(ii) the dilution effect implicit in any control premium being paid by G8 Education

(iii) the level of synergies relative to the size of G8 Education should the Offers be successful

(d) recent stock market conditions

(e) the earnings multiples implied by our adopted range (see below).

259 Based on the above we have assessed the realisable value of the G8 Education shares offered as consideration under the Revised Scrip Offer at between $3.10 and $3.40 per share.

Assessed value of Revised Scrip Offer consideration

260 We have therefore assessed the value of the Revised Scrip Offer consideration to be received by Affinity shareholders at the amounts below:

Value of Revised Scrip Offer consideration	Low $ per share	High $ per share
Assessed realisable value of G8 Education shares	3.10	3.40
Divide by exchange ratio (times)	4.25	4.25
Assessed value of Revised Scrip Offer consideration	**0.73**	**0.80**

94 We note that Affinity shareholders that accept the Revised Scrip Offer may be offered the opportunity to elect to receive cash in lieu of G8 Education shares if (and only if) G8 Education acquires Affinity shares for cash outside of the Revised Scrip Offer during the offer period (e.g. under the Cash Offer or otherwise).

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261 Affinity shareholders should note that the listed market price of G8 Education shares is subject to daily fluctuation. The price at which G8 Education shares may be sold may therefore be greater or less than our assessed realisable value of G8 Education shares of $3.10 to $3.40 per share.

262 However, it should be noted that, if (and only if) G8 Education acquires Affinity shares for cash outside of the Revised Scrip Offer during the offer period (e.g. under the Cash Offer or otherwise), it must also provide all Affinity shareholders that have accepted the Revised Scrip Offer with the opportunity (during a short period of time subsequent to the close of the Revised Scrip Offer) to elect to receive a cash payment equal to the highest cash price paid during the offer period in lieu of G8 Education shares[95].

263 Affinity shareholders should also note that any decision to hold G8 Education shares beyond the short-term is a separate investment decision and as noted below, the multiples on which G8 Education has been trading are higher than other sector comparables and have been declining. The extent to which that decline comes to an end or is reversed, if at all, as a result of the acquisition of Affinity is inherently uncertain. Further, should a large proportion of Affinity shareholders elect to accept cash under the Offers, then the financial gearing of G8 Education will be significantly increased. As it is not possible to accurately predict future share price movements, any decision to hold G8 Education shares should be made by shareholders having regard to their risk profile, liquidity preference, tax position and expectations as to value and future market conditions.

Implied EBITDA multiple

264 As stated above, we have cross-checked our assessment of the realisable value of G8 Education shares by considering the EBITDA multiple implied for the core business of the enlarged entity should the Offers be successful.

Estimated market capitalisation

265 The market capitalisation of G8 Education based on our assessed value of G8 Education shares in the event the Offers are successful and the maximum number of G8 Education shares are issued pursuant to the Revised Scrip Offer is shown below:

95 G8 Education has until 14 days after the close of the Revised Scrip Offer to provide Affinity shareholders that accepted the Revised Scrip Offer with their right to make the election. Affinity shareholders will have one month from the date of the notice to make the election.

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G8 Education – estimated market capitalisation of enlarged entity[1] [2]	Low	High
Number of ordinary G8 Education shares outstanding[3]	367.8	367.8
Maximum number of shares to be issued pursuant to the Revised Scrip Offer[4]	43.9	43.9
Shares on issue should the Offers be successful (million)[2]	411.8	411.8
Assessed realisable value of G8 Education shares ($ per share)	3.10	3.40
Market capitalisation should Offers be successful ($m)[2]	**1,276.5**	**1,400.0**

Note:
1 Rounding differences exist.
2 Assuming maximum number of G8 Education shares are issued pursuant to the Revised Scrip Offer.
3 As at 20 August 2015 G8 Education had 367.8 million ordinary shares on issue (this includes 3.1 million shares issued to management on 16 June 2015).
4 Being 231.5 million Affinity shares, plus 1.3 million performance rights, less 46.1 million shares held by G8 Education, converted to G8 Education shares at the exchange ratio of 1 G8 Education share for every 4.25 Affinity shares held.

Estimated net debt

266 Based upon the latest reported balance sheet for G8 Education, we estimate that the enlarged entity will have the following net debt position (assuming that all Affinity shareholders accept the Revised Scrip Offer and the maximum number of G8 Education shares are issued)[96]:

G8 Education – estimated net debt should the Offers be successful[1]	G8 Education $m	Affinity $m	Total $m
Net debt[2]	(281.7)	(27.5)	(309.2)
Long day professional development program[3]	(8.7)	-	(8.7)
Mark to market on Singapore debt[4]	-	n/a	-
Estimated cash costs of 2Q15 7 July 2015 dividend[5]	(13.1)	n/a	(13.1)
Acquisition of pre-bid stake in Affinity[6]	(32.2)	n/a	(32.2)
Transaction costs[7]	-	-	-
Implementation costs associated with synergy benefits[8]	-	(1.0)	(1.0)
Net debt should the Offers be successful	(335.7)	(28.5)	(364.2)

96 Should any Affinity shareholders elect to receive cash under the Offers, then the estimated net debt position of G8 Education will be higher.

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Note:
1 Assuming maximum number of G8 Education shares are issued pursuant to the Revised Scrip Offer.
2 G8 Education based upon reported cash and cash equivalents, derivative financial instruments and borrowings as at 30 June 2015. Affinity based upon net debt for valuation purposes.
3 Estimate based upon statement within G8 Education's announcement "Overview – 1H2015" slide 14. Affinity allowance already captured within net debt.
4 Further foreign exchange translation loss between 30 June 2015 and date of this report (on the unhedged SGD debt) is considered immaterial (relative to the enterprise value of the enlarged entity).
5 Estimate based on 365.1 million shares outstanding as at 26 June 2015 and declared dividend of six cents per share less the value of shares issued pursuant to the dividend reinvestment program (as disclosed in the G8 Education Appendix 3B dated 13 July 2015).
6 G8 Education acquired 46.052 million shares in Affinity subsequent to 30 June 2015 at an issue price of $0.70 per share.
7 Transaction costs not provided by G8 Education. Estimated transaction costs for Affinity are already included within net debt.
8 Post tax as estimated per Section VII.
n/a – not applicable
Source: G8 Education Appendix 4D for 1H15, G8 Education – overview 1H2015 dated 10 August 2015 (slide 14), G8 Education Appendix 3B dated 13 July 2015, Replacement Bidder's Statement dated 20 August 2015 and LEA analysis.

Estimated enterprise value

267 The following table sets out the estimated enterprise value of G8 Education should the Offers be successful (and assuming the maximum number of G8 Education shares are issued pursuant to the Revised Scrip Offer):

G8 Education – estimated enterprise value should the Offers be successful(1) (2)

	Low $m	High $m
Estimated market capitalisation(2)	1,276.5	1,400.0
Add estimated net debt(2)	364.2	364.2
Less market value of other assets(3)	(0.9)	(0.9)
Enterprise value should the Offers be successful(2)	**1,639.8**	**1,763.3**

Note:
1 Rounding differences exist.
2 Assuming maximum number of G8 Education shares are issued pursuant to the Revised Scrip Offer.
3 Being the mid-point of the two freehold properties and management rights to six child care centres held by Affinity (refer Section VII).

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Implied EBITDA multiple

268 For the purpose of calculating the EBITDA multiple implied by the above enterprise value we have adopted underlying EBITDA of $217.0 million. This reflects:

(a) one year forward underlying EBITDA of $176.1 million for G8 Education on a stand-alone basis[97]; plus

(b) the level of EBITA for Affinity adopted for valuation purposes in Section VII of $37.1 million plus assumed depreciation and software amortisation of $2.3 million; plus

(c) $1.5 million in additional estimated synergy benefits that are not already reflected in the EBITA we have adopted for Affinity for valuation purposes (this broadly represents the difference between G8 Education's estimated synergies of $6.5 million[98] and that which we have allowed for in our valuation of Affinity[99]).

269 On this basis, the EBITDA multiple incorporating the benefit of expected synergies (which are expected to be achieved in full over three years) is as follows:

G8 Education – implied EBITDA multiple should the Offers be successful[(1)]

	Low $m	High $m
Estimated enterprise value should the Offers be successful	1,639.8	1,763.3
Underlying EBITDA (including expected synergies)	217.0	217.0
Implied EBITDA multiple should the Offers be successful (times)[(2)]	**7.6**	**8.1**

Note:
1 Assuming maximum number of G8 Education shares are issued pursuant to the Revised Scrip Offer.
2 The implied EBITDA multiple is broadly similar if it is assumed that no G8 Education shares are issued pursuant to the Revised Scrip Offer (i.e. all Affinity shareholders accept $0.80 cash).

270 G8 Education has consistently traded at a significant premium in terms of forward EBITDA multiples to Affinity, Evolve Education and Think Childcare (as shown below).

97 As at 20 August 2015, based upon the FY15 and FY16 consensus estimates of those analysts that have revised their estimates subsequent to the announcement of G8 Education's 1H15 results on 10 August 2015.
98 Source: Replacement Bidder's Statement dated 20 August 2015, page 15.
99 Being synergies of $3.6 million plus run-rate cost savings relating to costs incurred by head office of $1.5 million.

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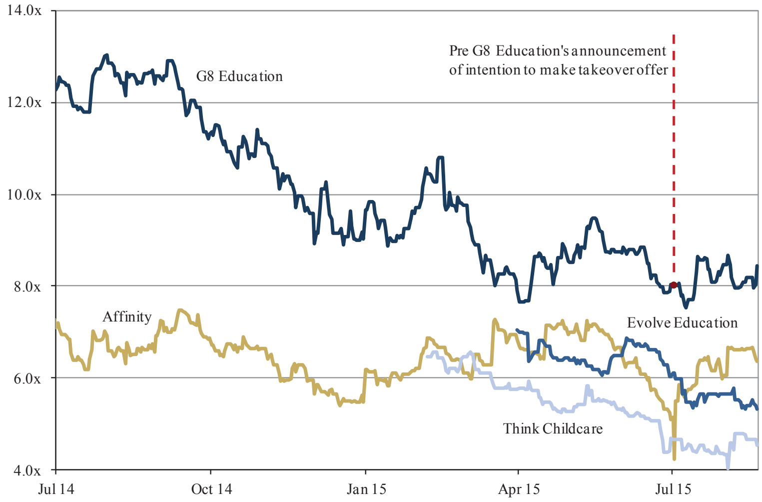
One year forward EBITDA multiples
1 July 2014 to 20 August 2015[1]



Note:
1 Think Childcare and Evolve Education multiples from 2 February 2015 and 30 March 2015 respectively, being the respective dates the companies were covered by more than one analyst. Affinity's enterprise value is based upon pro forma net debt from 17 April 2015 to 30 June 2015. The multiples for G8 Education and Affinity post 2 July 2015 are affected by the announcement of G8 Education's intention to make a takeover offer for Affinity.
Source: Bloomberg and LEA analysis.

271 The implied EBITDA multiples calculated above[100] are broadly consistent with the forward EBITDA multiples implied by recent trading in G8 Education shares. Consequently, we consider our assessed range of realisable values for G8 Education shares to be reasonable and appropriate.

272 However, we note that the forward EBITDA multiples upon which G8 Education has been trading are high relative to other sector comparables and that the forward EBITDA multiples of each of the three companies have been declining. Although, the acquisition of Affinity by G8 Education may reduce certain market concerns about its future performance, the extent to which the current decline in its multiples may be reversed (if at all) and its ability to continue to trade at a premium to the other sector participants is inherently uncertain. Further, should a large proportion of Affinity shareholders elect to accept cash under the Offers, then the financial gearing of G8 Education will be significantly increased.

100 Assuming 100% acceptance of scrip under the Offers as well as 100% acceptance of cash under the Offers.

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IX Evaluation of the Offers

Summary of opinion

273 LEA has concluded that the Offers are neither fair nor reasonable. We have arrived at this conclusion for the reasons set out below.

Assessment of fairness

274 Pursuant to RG 111 an offer is "fair" if:

"The value of the offer price or consideration is equal to or greater than the value of the securities the subject of the offer."

275 In the case of Affinity, the value of the consideration to be received by Affinity shareholders is dependent on (and may vary according to) whether shareholders elect to accept the Revised Scrip Offer or the Cash Offer. We have therefore provided a comparison of each of these alternatives with our assessed value of Affinity shares on a 100% controlling interest basis.

276 The relevant comparison for Affinity shareholders electing to accept the Revised Scrip Offer is shown below:

Comparison of Revised Scrip Offer consideration and Affinity share value

	Low $ per share	High $ per share	Mid-point $ per share
Value of Revised Scrip Offer consideration(1)	0.73	0.80	0.77
Value of 100% of ordinary shares in Affinity	0.92	1.00	0.96
Extent to which the Revised Scrip Offer consideration is less than the value of Affinity shares	(0.19)	(0.20)	(0.19)

Note:

1 It should be noted that, if (and only if) G8 Education acquires Affinity shares for cash outside of the Revised Scrip Offer during the offer period (e.g. under the Cash Offer or otherwise), it must also provide all Affinity shareholders that have accepted the Revised Scrip Offer with the opportunity (during a short period of time subsequent to the close of the Revised Scrip Offer) to elect to receive a cash payment equal to the highest cash price paid during the offer period in lieu of G8 Education shares.

277 As the Revised Scrip Offer consideration is less than our assessed value of 100% of the ordinary shares in Affinity, in our opinion, the Revised Scrip Offer is not fair.

278 The relevant comparison for Affinity shareholders electing to accept the Cash Offer is shown below:

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Comparison of Cash Offer consideration and Affinity share value	Low $ per share	High $ per share	Mid-point $ per share
Value of Cash Offer consideration(1)	0.80	0.80	0.80
Value of 100% of ordinary shares in Affinity	0.92	1.00	0.96
Extent to which the Cash Offer consideration is less than the value of Affinity shares	(0.12)	(0.20)	(0.16)

Note:
1 No allowance has been made for any brokerage costs that will be incurred as a result of selling Affinity shares on market pursuant to the Cash Offer.

279 As the Cash Offer consideration is less than our assessed value of 100% of the ordinary shares in Affinity, in our opinion, the Cash Offer is not fair.

Assessment of reasonableness

280 Pursuant to RG 111, an offer may be reasonable if, despite not being fair but after considering other significant factors, the expert is of the view that there are sufficient reasons for shareholders to accept the offer in the absence of any higher bid before the close of the offer.

281 In our opinion, there are a number of reasons why Affinity shareholders may wish to accept the Offers, as summarised below:

(a) in our opinion, the consideration offered under the Revised Scrip Offer and Cash Offer is likely to exceed the listed market price of Affinity shares in the absence of the Offers or a superior proposal (at least in the short-term). However, this is often the case with most takeovers as the listed market price generally reflects a portfolio rather than controlling interest value

(b) the Revised Scrip Offer provides Affinity shareholders with the opportunity to obtain an interest in a larger more diversified company in the child care sector. However, Affinity shareholders that elect to accept the Revised Scrip Offer should also note that:

(i) G8 Education's financial gearing levels may increase significantly relative to its position as at 30 June 2015 if a large proportion of Affinity shareholders elect to receive cash (rather than scrip) under the Offers

(ii) should G8 Education acquire less than 90% of Affinity:

– G8 Education may not be able to realise all estimated synergy benefits

– G8 Education will not have access to their pro-rata share of the full underlying cash flow generated by Affinity

– Affinity shareholders will not be granted capital gains tax roll-over relief unless G8 Education acquires at least 80% of Affinity.

(c) the Cash Offer provides all Affinity shareholders with the ability to immediately realise their shareholdings for cash should they wish to do so

(d) should G8 Education increase its ownership interest in Affinity to above 50% but less than 90% then G8 Education will control Affinity including its day-to-day management,

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strategic direction and level of dividend payments[101]. Depending on the level of shareholding obtained, G8 Education may also seek to delist Affinity from the ASX. That said, in our view, there is a reasonable prospect that G8 Education will make a further takeover offer at a later date in order to obtain 100% control of Affinity[102]. However, the prospect of a future takeover offer is inherently uncertain as to whether it arises, the timing thereof and the related offer price.

282 While we acknowledge these advantages (particularly for shareholders who expect to have to realise their Affinity shares in the short-term), in our opinion, they do not provide sufficient reasons for shareholders to accept the Revised Scrip Offer or the Cash Offer as the consideration provided under each is materially below our assessed valuation range:

Comparison of mid-points of the offer consideration and Affinity share value	Revised Scrip Offer $ per share	Cash Offer $ per share
Mid-point of assessed value of consideration	0.77	0.80
Mid-point of assessed value of Affinity shares	0.96	0.96
Discount of the Offers to assessed value of Affinity (%)	19.8	16.7

283 Furthermore, we expect that G8 Education will be able to generate significant synergies as a result of acquiring 100% of Affinity. In our opinion, an appropriate share of the value of these synergies is not reflected in either the Revised Scrip Offer or Cash Offer consideration.

284 Accordingly, we have concluded that the Offers are also not reasonable. However, Affinity shareholders should note that G8 Education has stated that its Revised Scrip Offer and Cash Offer are final and will not be increased.

285 Further commentary relevant to our assessment of the reasonableness of the Offers follows.

Extent to which a control premium is being paid

286 It is customary when assessing the merits of a proposed change of control transaction to assess the extent of the premium offered under the proposal by comparing the offer to the pre-bid market prices of the target company's shares. Empirical evidence indicates that average premiums paid in successful takeovers in Australia generally range between 30% and 35% above the listed market price of the target company's shares three months prior to the announcement of the bid (assuming no speculation of the takeover is reflected in the pre-bid price).

287 For the reasons set out in Section VII, in our view, the recent listed market prices of Affinity shares prior to the announcement of the G8 Education's intention to make a takeover offer for the Company are not a reliable reference point upon which to assess whether an appropriate control premium is being paid.

101 Affinity announced on 17 April 2015 an intention to declare a maiden dividend for the financial year ending 31 December 2015. This intention was reaffirmed by Affinity on 18 August 2015.

102 We note that Affinity received a number of unsolicited approaches from G8 Education prior to the announcement of G8 Education's intention to make a takeover offer for the Company.

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288 However, as both the Revised Scrip Offer and Cash Offer are materially below our valuation range, we do not consider that either offer provides Affinity shareholders with a sufficient premium for control.

Extent to which shareholders are being paid a share of synergies

289 Should the Offers be successful, Affinity will be delisted from the ASX resulting in the elimination of listed public company costs (e.g. Director fees, listing fees, share registry fees, shareholder communication costs etc). In addition, G8 Education has indicated that it expects to rationalise various administrative, management and corporate functions, the IT systems and duplicate services. G8 Education has estimated the synergies arising from an acquisition of Affinity to be some $6.5 million per annum (refer to Section VII of this report and the Replacement Bidder's Statement dated 20 August 2015).

290 However, as the assessed value of the consideration under both the Revised Scrip Offer and Cash Offer is below our assessed valuation range of Affinity shares, in our opinion, Affinity shareholders are not being offered an appropriate share of the expected synergies. In addition, as noted below, in our view the exchange ratio (and implied sharing of the synergy benefits associated with the transaction) also favours G8 Education shareholders to the detriment of Affinity shareholders.

Listed market prices of Affinity prior to 2 July 2015

291 The relative value of Affinity and G8 Education based on share market trading from 3 July 2014 to 2 July 2015 (being the last day of trading prior to the announcement of G8 Education's intention to make a takeover offer for Affinity) in comparison to the Revised Scrip Offer exchange ratio is shown below:

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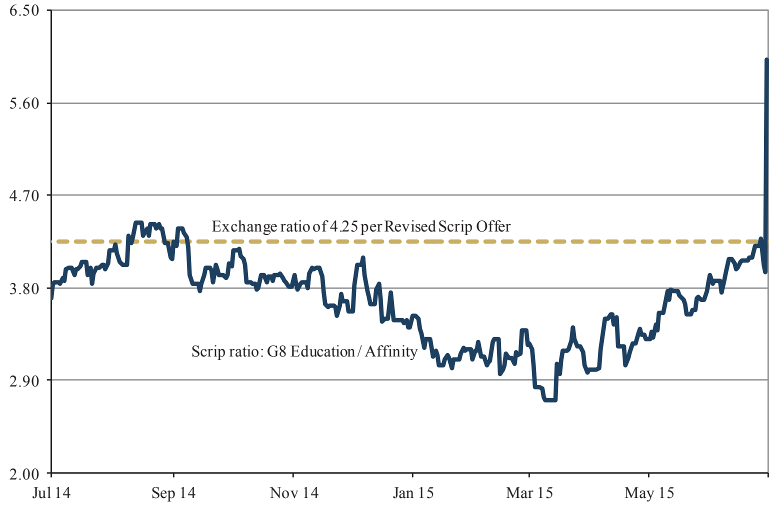
Relative share prices – Affinity and G8 Education[1]
3 July 2014 to 2 July 2015



Note:
1 Based upon closing prices.
Source: Bloomberg.

292 As indicated above, the ratio reflected by the closing price of G8 Education shares divided by the closing price of Affinity shares was (generally) materially better than that offered by G8 Education under the Revised Scrip Offer (the observed average was 1 G8 Education share for every 3.67 Affinity shares). Adjusting Affinity's share price for a theoretical control premium of say 30%, further improves the observed ratio to 1 G8 Education share for every 2.82 Affinity shares.

293 We note that Affinity received a number of unsolicited approaches from G8 Education prior to the announcement of its intention to make a takeover offer for the Company (refer below). The exchange ratios implied by those approaches (of 3.17 and 4.01) were better than that proposed under the Revised Scrip Offer (and not inconsistent with the observed trading average set out above).

294 However, we note that Affinity provided the market with underlying FY15 EBITDA earnings guidance on 2 July 2015 and that this new market sensitive information had a material impact on the share price (with Affinity shares closing down some 34% on the prior day's close). This information was not reflected in Affinity's share price trading prior to this date. We further note that the relative share price trading leading up to the 2 July 2015 announcement was (before adjusting for a theoretical control premium) materially closer to that being offered under the Revised Scrip Offer.

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Recent share prices subsequent to the Offers

295 The VWAPs of Affinity shares and G8 Education shares for the period 3 August 2015 to 20 August 2015 are $0.82 and $3.22 per share respectively (with a traded range of between $0.81 and $0.84 per share and $3.05 and $3.65 per share respectively).

296 We note that the VWAP of Affinity shares is marginally higher than the value of the consideration implied by the exchange ratio as per the Revised Scrip Offer as well as the $0.80 cash consideration per the Cash Offer. This suggests that the market consensus view is that the Revised Scrip Offer and Cash Offer are both too low.

Likely price of Affinity shares if the Offers lapse

297 In our opinion, if the Offers lapse and no higher offer or alternative proposal emerges, it is likely (at least in the short-term) that Affinity shares will trade at a discount to our valuation (consistent with the difference between the value of Affinity on a portfolio basis and the value on a 100% controlling interest basis) and may trade at a discount to our assessed value of the Revised Scrip Offer and Cash Offer of $0.92 to $1.00 per share and $0.80 per share respectively.

G8 Education acquires at least 50.1% or more but less than 90% of Affinity

298 Affinity shareholders should note that both the Revised Scrip Offer and Cash Offer are unconditional and all Affinity shares tendered by shareholders into either the Revised Scrip Offer or Cash Offer will be accepted. Implicitly therefore, there is the realistic potential for G8 Education to acquire more than 50.0% of Affinity shares.

299 Should G8 Education acquire 50.1% but less than 90% of Affinity, G8 Education will control Affinity[103] including its day-to-day management, strategic direction and level of dividend payments[104]. Should this occur, the liquidity of Affinity shares may be diminished and this may result in a fall in the price of Affinity shares. It should also be noted that G8 Education may, depending on the level of shareholding obtained, seek to remove Affinity from the official list of the ASX[105].

300 Notwithstanding the above, should G8 Education acquire at least 50.1% but less than 90% of Affinity shares, in our opinion, there is a reasonable prospect that G8 Education will make a further takeover offer at a later date in order to obtain 100% control of Affinity[106]. However, the prospect of a future takeover offer is inherently uncertain as to whether it arises, the timing thereof and the related offer price.

G8 Education's current shareholding in Affinity

301 As at 20 August 2015, G8 Education had a relevant interest in 19.89% of the shares on issue in Affinity. Whilst G8 Education could therefore prevent a competing bidder from proceeding to compulsory acquisition of Affinity, it does not control Affinity and, in our opinion, should therefore pay an appropriate premium for control.

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103 In our opinion, the Offers in their current form do not offer Affinity shareholders a full premium for control.

104 Affinity announced on 17 April 2015 an intention to declare a maiden dividend for the financial year ending 31 December 2015.

105 Replacement Bidder's Statement dated 20 August 2015, Section 8.3.

106 We note that Affinity received a number of unsolicited approaches from G8 Education prior to the announcement of G8 Education's intention to make a takeover offer for the Company.

Likelihood of an alternative offer

302 Affinity shareholders should note that G8 Education has declared its Offers final and accordingly they will not be increased.

303 Affinity's Independent Directors have advised that they are currently in discussions with, and have received indicative non-binding acquisition proposals from other interested parties which may result in a superior proposal for Affinity shareholders. Affinity has indicated that it will provide an update as to the status of these negotiations by no later than 21 September 2015 (i.e. prior to the close of the Revised Scrip Offer and the Cash Offer).

304 However, it should also be noted that G8 Education's 19.89% interest in Affinity may act as a deterrent to other bidders because:

(a) they will be unable to acquire 100% of Affinity, by way of a takeover offer, unless G8 Education agrees to sell its holding

(b) it would be difficult, from a practical perspective, to acquire 100% of Affinity, by way of a scheme of arrangement, given the size of G8 Education's current interest in Affinity.

305 In our opinion, it is therefore possible, but at this stage, highly uncertain as to whether any superior offer is likely to be made for Affinity prior to the close of the Offers.

Previous unsolicited approaches

306 On 6 July 2015, Affinity made an announcement containing the following comments about previous unsolicited approaches received by Affinity from G8 Education:

"Affinity advises its shareholders that the Affinity Board received an approach from G8 wishing to discuss an indicative merger proposal in April 2015. The chairs and managing directors of G8 and Affinity met on 24 April 2015 to discuss a potential proposal that G8 wished to advance. At that meeting, G8 proposed a nil premium merger between G8 and Affinity (based on the closing price of Affinity and G8 shares on 23 April 2015, this would have involved an equivalent value for each Affinity share of around $1.105). Affinity advised G8 that it would consider the proposal.

The chairs and managing directors of G8 and Affinity agreed to meet again on 24 June 2015. At that meeting, G8 again proposed a nil premium merger between G8 and Affinity, with Affinity shareholders receiving consideration of G8 shares at a ratio based on the market price of Affinity shares on a spot or 30 day VWAP basis. Based on the closing price of Affinity and G8 shares on 23 June 2015, this would have involved an equivalent value for each Affinity share of around $0.825 (Previous Proposal).

The Affinity Board met to consider the Previous Proposal on 25 June 2015. Affinity advised G8 that the Previous Proposal was not acceptable based on (among other things) the Affinity Board's view that an $0.825 offer undervalued Affinity. Affinity advised G8 that Affinity was prepared to continue to engage in discussion with G8 but only if G8 revised the Previous

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Proposal."[107]

307 The exchange ratios implied by the 24 April 2015 and 24 June 2015 approaches were 3.17[108] and 4.01 respectively[109]. We note that both implied exchange ratios are better than that proposed under the Revised Scrip Offer. We also note that implied values of $1.105 per Affinity share and $0.825 per Affinity share are also greater than the $0.80 per share consideration offered under the Cash Offer.

308 However, both approaches occurred prior to Affinity providing the market with underlying FY15 EBITDA earnings guidance on 2 July 2015. This guidance was less than the then current consensus EBITDA estimate. Had G8 Education had the benefit of this information prior to the approaches, then the proposed terms (under both approaches) may have been less favourable to Affinity shareholders.

Other matters

309 The taxation consequences of accepting the Revised Scrip Offer or the Cash Offer depend on the individual circumstances of each investor. Shareholders should read the taxation advice set out in the Bidder's Statements the Target's Statement and should consult their own professional adviser if in doubt as to the taxation consequences of the Revised Scrip Offer and Cash Offer.

310 The ultimate decision whether to accept the Revised Scrip Offer or the Cash Offer should be based on each shareholders' assessment of their own circumstances, including their risk profile, liquidity preference, tax position and expectations as to value and future market conditions. If shareholders are in doubt about the action they should take in relation to the Revised Scrip Offer or the Cash Offer or matters dealt with in this report, shareholders should seek independent professional advice.

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107 Affinity ASX announcement dated 6 July 2015.

108 Based upon a closing share prices on 23 April 2015 for Affinity and G8 Education of $1.105 and $3.50 respectively.

109 Based upon a closing share prices on 23 June 2015 for Affinity and G8 Education of $0.825 and $3.38 respectively.

LONERGAN EDWARDS & ASSOCIATES LIMITED

Appendix A

Financial Services Guide

Lonergan Edwards & Associates Limited

1 Lonergan Edwards & Associates Limited (ABN 53 095 445 560) (LEA) is a specialist valuation firm which provides valuation advice, valuation reports and independent expert's reports (IER) in relation to takeovers and mergers, commercial litigation, tax and stamp duty matters, assessments of economic loss, commercial and regulatory disputes.

2 LEA holds Australian Financial Services Licence No. 246532.

Financial Services Guide

3 The *Corporations Act 2001 (Cth)* (Corporations Act) authorises LEA to provide this Financial Services Guide (FSG) in connection with its preparation of an IER to accompany the Target's Statement to be sent to Affinity shareholders in connection with the Offers.

4 This FSG is designed to assist retail clients in their use of any general financial product advice contained in the IER. This FSG contains information about LEA generally, the financial services we are licensed to provide, the remuneration we may receive in connection with the preparation of the IER, and if complaints against us ever arise how they will be dealt with.

Financial services we are licensed to provide

5 Our Australian Financial Services Licence allows us to provide a broad range of services to retail and wholesale clients, including providing financial product advice in relation to various financial products such as securities, derivatives, interests in managed investment schemes, superannuation products, debentures, stocks and bonds.

General financial product advice

6 The IER contains only general financial product advice. It was prepared without taking into account your personal objectives, financial situation or needs.

7 You should consider your own objectives, financial situation and needs when assessing the suitability of the IER to your situation. You may wish to obtain personal financial product advice from the holder of an Australian Financial Services Licence to assist you in this assessment.

Fees, commissions and other benefits we may receive

8 LEA charges fees to produce reports, including this IER. These fees are negotiated and agreed with the entity who engages LEA to provide a report. Fees are charged on an hourly basis or as a fixed amount depending on the terms of the agreement with the entity who engages us. In the preparation of this IER, LEA is entitled to receive a fee estimated at $225,000 plus GST.

9 Neither LEA nor its directors and officers receives any commissions or other benefits, except for the fees for services referred to above.

LONERGAN EDWARDS & ASSOCIATES LIMITED

Appendix A

10 All of our employees receive a salary. Our employees are eligible for bonuses based on overall performance and the firm's profitability, and do not receive any commissions or other benefits arising directly from services provided to our clients. The remuneration paid to our directors reflects their individual contribution to the company and covers all aspects of performance. Our directors do not receive any commissions or other benefits arising directly from services provided to our clients.

11 We do not pay commissions or provide other benefits to other parties for referring prospective clients to us.

Complaints

12 If you have a complaint, please raise it with us first, using the contact details listed below. We will endeavour to satisfactorily resolve your complaint in a timely manner.

13 If we are not able to resolve your complaint to your satisfaction within 45 days of your written notification, you are entitled to have your matter referred to the Financial Ombudsman Services Limited (FOS), an external complaints resolution service. You will not be charged for using the FOS service.

Contact details

14 LEA can be contacted by sending a letter to the following address:

Level 7
64 Castlereagh Street
Sydney NSW 2000
(or GPO Box 1640, Sydney NSW 2001)

LONERGAN EDWARDS & ASSOCIATES LIMITED

Appendix B

Qualifications, declarations and consents

Qualifications

1 LEA is a licensed investment adviser under the Corporations Act. LEA's authorised representatives have extensive experience in the field of corporate finance, particularly in relation to the valuation of shares and businesses and have prepared hundreds of IERs.

2 This report was prepared by Mr Edwards and Mr Toscan, who are each authorised representatives of LEA. Mr Edwards and Mr Toscan have over 20 years and 11 years experience respectively in the provision of valuation advice (and related advisory services).

Declarations

3 This report has been prepared at the request of the Independent Directors of Affinity to accompany the Target's Statement to be sent to Affinity shareholders. It is not intended that this report should serve any purpose other than as an expression of our opinion as to whether or not the Offers are fair and reasonable to the shareholders of Affinity.

Interests

4 At the date of this report, neither LEA, Mr Edwards nor Mr Toscan have any interest in the outcome of the Offers. With the exception of the fee shown in Appendix A, LEA will not receive any other benefits, either directly or indirectly, for or in connection with the preparation of this report.

5 LEA has had no prior business or professional relationship with Affinity or G8 Education prior to the preparation of this report.

Indemnification

6 As a condition of LEA's agreement to prepare this report, Affinity agrees to indemnify LEA in relation to any claim arising from or in connection with its reliance on information or documentation provided by or on behalf of Affinity which is false or misleading or omits material particulars or arising from any failure to supply relevant documents or information.

Consents

7 LEA consents to the inclusion of this report in the form and context in which it is included in the Target's Statement.

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Appendix C

Trading evidence

1 The following table summarises the key trading metrics of ASX listed companies operating in the child care sector:

Trading evidence – ASX listed child care operators[1]

	Market Cap $m	Enterprise Value[3] $m	EBITA multiple[2] FY15 x	EBITA multiple[2] FY16 x	PE multiple[2] FY15 x	PE multiple[2] FY16 x
G8 Education	1,195	1,461	9.3	7.8	12.4	10.7
Affinity:[4]						
Based on 2 July 2015 close	125	161	6.2	5.2	6.9	6.3
Based on 2 July 2015 VWAP	152	187	7.3	6.1	8.4	7.6
Evolve Education	161	156	6.0	5.9	8.2	7.5
Think Childcare	35	38	5.7	4.8	8.3	6.9

Note:
1 G8 Education and Affinity as at 2 July 2015 (i.e. the date prior to the announcement of G8 Education's intention to make a takeover offer for Affinity). Evolve Education and Think Childcare as at 20 August 2015.
2 Forecast earnings are based on Bloomberg broker average analyst forecasts (excluding outliers and outdated forecasts).
3 Enterprise value includes net debt (interest bearing liabilities), convertible notes, net derivative liabilities, net pension liabilities, market capitalisation adjusted for material option dilution, share placements (for the purpose of reducing debt) and excludes surplus assets. Based upon latest publicly available information at the date of calculation.
4 Affinity forecasts as at 7 July 2015 to allow for analyst revisions on Bloomberg. Affinity's enterprise value based on pro forma 31 December 2014 balance sheet.
Source: Company announcements, Bloomberg and LEA analysis.

2 Brief descriptions of each of the above companies follow.

G8 Education

3 Refer to the profile of G8 Education in Section IV.

Affinity

4 Refer to the profile of Affinity in Section III.

Evolve Education

5 Evolve Education is a provider of early childhood education services in New Zealand offering both centre-based and home-based services. The company was established in 2014 and listed on the NZX and ASX on 5 December 2014. On listing, Evolve Education acquired 85 child care centres and a provider of home-based care and education. Currently, Evolve Education owns a total of 95 child care centres.

Think Childcare

6 Think Childcare owns, manages and operates child care facilities in Australia. The company listed on 24 October 2014 acquiring a portfolio of 30 child care centres. Currently, the company owns a total of 37 child care centres.

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Appendix D

Transaction evidence

1 There have been a number of recent transactions involving the acquisition of child care centres in recent years. Those transactions which disclosed sufficient financial information to enable the calculation of implied transaction multiples are summarised within the transaction tables set out in Section VII.

2 Brief descriptions of each of the above transactions (grouped by company) follow.

G8 Education

2 June 2015

3 Announced the acquisition of eight child care and education centres (855 licensed places) from a number of different vendors for some \$12.1 million at a multiple of 4.0 times anticipated EBIT for the 12 months post settlement.

16 February 2015

4 Announced the acquisition of 12 child care and education centres (1,003 licensed places) from a number of different vendors for some \$36.0 million (\$29.9 million payable at settlement and a further \$6.1 million conditional upon EBIT targets) at a multiple of 4.0 times anticipated EBIT for the 12 months post settlement.

22 October 2014

5 Announced the acquisition of 20 child care and education centres from a number of different vendors. Seventeen centres (1,134 licensed places) were acquired for some \$24.4 million at a multiple of 4.0 times anticipated EBIT for the 12 months post settlement.

6 A further three centres (209 licensed places) were acquired for some \$12.4 million at a multiple of 6.2 times anticipated EBIT for the 12 months post settlement. Sterling Early Education (acquired by G8 Education, refer to paragraph 10 of this Appendix), held options to purchase these centres.

11 August 2014

7 Announced the acquisition of 25 child care and education centres from a number of different vendors for some \$82.7 million (\$72.7 million payable at settlement and a further \$10.0 million conditional upon EBIT targets) at a multiple of 4.0 times anticipated EBIT for the 12 months post settlement.

8 July 2014

8 Announced the acquisition of 19 child care and education centres (1,213 licensed places) from a number of different vendors for some \$25.7 million (\$24.3 million payable at settlement and a further \$1.4 million conditional upon EBIT targets) at a multiple of 3.9 times anticipated EBIT for the 12 months post settlement.

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29 April 2014

9 Announced the acquisition of seven child care centres (495 licensed places) from a number of different vendors for some \$16.3 million at a multiple of 4.0 times anticipated EBIT for the 12 months post settlement.

24 March 2014

10 Announced the acquisition of 91 child care and education centres (6,203 licensed places) from Sterling Early Education for some \$228.0 million (consisting of \$2.5 million payable in G8 Education shares, \$215.0 million payable in cash at settlement and \$10.5 million payable in cash conditional upon EBIT targets) at a multiple of 5.8 times annualised centre based EBIT for the year ending 31 December 2015.

10 February 2014

11 Announced the acquisition of 63 child care and education centres (4,254 licensed places) from a number of different vendors for some \$104.7 million (\$103.9 million payable at settlement with \$0.8 million conditional upon EBIT targets) at a multiple of 4.0 times anticipated EBIT for the 12 months post settlement.

27 September 2013

12 Announced the acquisition of 29 child care and education centres (2,338 licensed places) located across NSW, TAS and VIC from a number of different vendors for some \$42.6 million (\$39.8 million payable at settlement with \$2.8 million conditional upon EBIT targets) at a multiple of 4.0 times anticipated EBIT for the 12 months post settlement.

26 August 2013

13 Announced the acquisition of five child care and education centres (397 licensed places) located across QLD, SA and VIC from a number of different vendors for some \$4.6 million (\$4.25 million payable at settlement with \$0.35 million conditional upon EBIT targets) at a multiple of 4.0 times anticipated EBIT for the 12 months post settlement.

Affinity

12 March 2015

14 Announced the acquisition of nine premium child care centres for a purchase price of some \$24.0 million, funded by a fully underwritten pro-rata accelerated renounceable entitlement offer.

2 February 2015

15 Announced the acquisition of eight child care centres previously managed by the Company for some \$17.8 million. The acquisition will be funded from operating cashflows and the Company's \$100 million acquisition facility.

17 December 2014

16 Announced the acquisition of 16 child care centres, including a large group of premium centres in metropolitan areas for some \$45 million which will be funded from surplus operating cashflows and the Company's \$100 million acquisition facility.

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Appendix D

11 September 2014

17 Announced the acquisition of 20 child care centres for some $19 million which will be funded from the Company's $100 million acquisition facility.

8 April 2014

18 Announced the acquisition of 51 child care centres for some $80.0 million ($65.0 million in cash and approximately $15 million in shares) at a multiple of 5.2 times anticipated 12 month forward centre based EBIT.

26 March 2014

19 Announced the acquisition of seven child care centres for some $8.0 million at a multiple of 4.3 times anticipated 12 month forward centre based EBIT.

9 December 2013 and 1 October 2013

20 Affinity listed on the ASX on 9 December 2013 at an offer price of $1.00 per share which represented a forecast EBITDA multiple of 6.9 times, forecast EBIT multiple of 7.3 times and forecast PE multiple of 10.8 times based on pro forma earnings for the company (after head office costs) for the year ended 31 December 2014.

21 Funds from listing were used, amongst other things, to acquire 57 child care centres (4,729 configured places) and the management rights for a further 11 centres located across QLD, NSW and VIC. These pre IPO centres were acquired by Affinity for some $68.2 million at a multiple of 4.1 times forecast EBIT.

Evolve Education (New Zealand)

2 April 2015

22 Announced the acquisition of nine centres in New Zealand for some $11.1 million with an average acquisition multiple of 4.9 times based on the child care centres current run-rate EBITDA.

5 December 2014 and 14 November 2014

23 Evolve Education listed on the NZX and ASX on 5 December 2014 at an offer price of $0.93[110] which represented a forecast EBITDA multiple of 7.3 times, forecast EBIT multiple of 7.8 times and forecast PE multiple of 10.7 times based on pro forma earnings for the company (after head office costs) for the year ended 31 March 2016. On listing, the company acquired 85 child care centres in New Zealand (5,954 licensed places) and the PORSE group companies, a provider of home-based care and education (7,280 licensed places).

[110] NZD1.00 converted to AUD at the AUD:NZD exchange rate of 1.0782 on 5 December 2014.

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Appendix D

24 Thirty of the 85 child care centres were acquired from Lollipops Educare Holdings Limited for $61.9 million[111] at a multiple of 7.0 time forecast EBITDA[112] on 14 November 2014. The remaining 55 child care centres were acquired from 39 separate vendors for $81.8 million[113] at a multiple of 4.9 times forecast EBITDA with settlement to occur during the period from December 2014 to March 2015.

Think Childcare

18 June 2015

25 Announced the acquisition of two child care centres (157 licensed places) in Australia for consideration of some $3.1 million at a multiple of 4.1 times forecast EBIT.

24 October 2014 and 2 October 2014

26 Think Childcare listed on 24 October 2014 at an offer price of $1.00 per share which represented a forecast EBITDA multiple of 6.7 times, forecast EBIT multiple of 6.9 times and forecast PE multiple of 9.0 times based on pro forma earnings for the company (after head office costs) for the year ended 31 December 2015.

27 Funds from the listing were used, amongst other things, to acquire a portfolio of 30 child care centres (2,244 licensed places) in Australia for some $37.9 million at multiple of 5.7 times forecast EBIT.

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111 NZD66.7 million converted to AUD at the AUD:NZD exchange rate of 1.0782 on 5 December 2014.

112 Indicative implied multiple based upon information disclosed in Evolved Education's prospectus and 2 April 2015 ASX announcement.

113 NZD88.2 million converted to AUD at the AUD:NZD exchange rate of 1.0782 on 5 December 2014.

LONERGAN EDWARDS & ASSOCIATES LIMITED

Appendix E

Glossary

Term	Meaning
ACECAQ	Australian Children's Education and Care Quality Authority
ACT	Australian Capital Territory
Affinity or the Company	Affinity Education Group Limited
ANAO	Australian National Audit Office
ASIC	Australian Securities & Investments Commission
ASX	Australian Securities Exchange
BBSW	Bank bill swap rate
bps	Basis points
Cash Offer	The on-market bid made by G8 Education for all the Affinity shares that it does not already own for consideration of $0.80 cash per Affinity share
CBA	Commonwealth Bank of Australia
CBD	Central Business District
CCB	Child Care Benefit scheme
CCR	Child Care Rebate scheme
Centralised Costs	Costs include marketing, IT, insurance and procurement. These costs relate to the operation of the individual centres but are paid by Affinity's head office
Corporate Charges	Affinity corporate head office expenses including costs associated with being a publicly listed company (e.g. listing and registry fees, shareholder communication costs etc), CEO and CFO (and other head office staff member) salaries, head office lease charges and general consultancy fees
Corporations Act	*Corporations Act 2001 (Cth)*
DCF	Discounted cash flow
DEEWR	Department of Education, Employment and Workplace Relations
DSS	Department of Social Services
EBIT	Earnings before interest and tax
EBITA	Earnings before interest, tax and amortisation of acquired intangibles
EBITDA	Earnings before interest, tax, depreciation and amortisation
ECT	Early childhood teacher
ELS	Early Learning Services Limited
EPS	Earnings per share
EV	Enterprise value
Evolve Education	Evolve Education Group Limited
EYQF	Early Years Quality Fund
FOS	Financial Ombudsman Services Limited
FSG	Financial Services Guide
FY	Financial year
G8 Education	G8 Education Limited
IER	Independent expert's report
IPO	Initial public offering
LEA	Lonergan Edwards & Associates Limited
National Law	*Education and Care Services National Law Act 2010*
National Regulations	*Education and Care Services National Regulations*
NPAT	Net profit after tax
NPV	Net present value
NQF	National Quality Framework
NQS	National Quality Standard
NSW	New South Wales

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Appendix E

Term	Meaning
NT	Northern Territory
OECD	Organisation of Economic Co-operation and Development
Offers	The collective reference to both the Revised Scrip Offer and Cash Offer
PBT	Profit before tax
PE	Price earnings
QLD	Queensland
Revised Scrip Offer	The off-market bid made by G8 Education for all the Affinity shares that it does not already own for consideration of one fully paid ordinary share in G8 Education for every 4.25 fully paid ordinary shares in Affinity
RG 111	Regulatory Guideline 111 – *Content of expert reports*
SA	South Australia
Scrip Offer	The former off-market bid made by G8 Education for all the Affinity shares that it does not already own for consideration of one fully paid ordinary share in G8 Education for every 4.61 fully paid ordinary shares in Affinity (this off-market bid has been superseded by the Revised Scrip Offer).
SGD	Singapore dollars
Shared Services	Costs associated with the direct oversight of the individual centres as well as shared services (such as human resources, payroll, accounts processing). These costs relate to the operation of the individual centres but are paid by Affinity's head office
Sterling Early Education	Sterling Early Education Limited
TAS	Tasmania
Think Childcare	Think Childcare Limited
VIC	Victoria
VWAP	Volume weighted average price
WA	Western Australia
WANOS	Weighted average number of shares outstanding

Affinity Education
Group