

29 February 2012

## MARKET UPDATE

### PAPERLINX SPS TRUST

#### Fair Value determination for the purposes of the half-year financial report

- Fair value maintained at \$97M (\$34 per LLC preference share)
- Fair value assessed using a variety of scenarios and methodologies
- The Trust Company is committed to ensure rights of SPS Unitholders are appropriately recognised in any transaction

The Trust Company (RE Services) Limited is the independent responsible entity (**The Trust Company**) of the PaperlinX SPS Trust (the **Trust**). The Trust's financial report for the half-year ended 31 December 2011 has been released to the market today.

In its announcement of 21 February 2012, The Trust Company indicated that it would make an announcement at the time of releasing the Trust's half-year financial report providing further information about the results of the valuation process in determining fair value.

The Trust Company has considered that this is necessary given investor feedback and the general circumstances and uncertainties surrounding the Trust's investment in the PaperlinX SPS LLC which is a controlled entity of PaperlinX Limited (**PaperlinX**).

As part of the half-year financial report of the Trust, the directors of The Trust Company are required to make an assessment of the fair value of the Trust's preference share investment in PaperlinX SPS LLC.

The Australian Accounting Standards require that in circumstances where financial instruments (such as the preference shares of PaperlinX SPS LLC) are not traded in an active market, fair value is established based on a valuation technique or a number of techniques. This assessment involves taking into account a range of computational methodologies that are inherently subjective in nature. The objective of using a valuation technique is to establish what the transaction price would have been on the measurement date in an arm's length exchange motivated by normal business considerations, under the presumption of operating on a going concern basis.

The Trust Company is not privy to information in relation to PaperlinX other than that which is in the public domain. The Trust Company has considered the half-year financial reports of PaperlinX released on 22 February 2012 and related announcements it made in relation to its results and strategic direction. The Trust Company has also noted market commentaries, including broker commentaries and acknowledges investor feedback and their views on valuation, and has sought professional advice before determining the fair value of the Trust's investment in PaperlinX LLC preference shares.

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### **Approach to determining fair value**

PaperlinX, in its announcements to the market on the 22 February 2012, indicated that:

- Distributions to the SPS Trust are unlikely to occur until there was a significant improvement in trading conditions and in PaperlinX's financial position;
- Its largest debt facility (in Europe) has been amended to provide improved covenant headroom;
- It is in compliance with covenants on all its debt facilities;
- Any distribution to the SPS Trust would require financier consent under PaperlinX's amended facility terms;
- PaperlinX has also indicated that they have plans to reduce their operating cost base in their European operations and Corporate offices and that the costs of these restructure programs will be funded via asset sales;
- They have a clear and deliverable plan to restore profitability;
- A number of parties are interested in a whole of company transaction; and
- No decision has as yet been made in relation to the first periodic remarketing date of 30 June 2012 for the SPS Trust.

Fair value has historically been determined using a discounted present value model of expected future cash flows based on various assumptions and sense checked to a number of other valuation techniques.

However, given the change in circumstances as noted above the Responsible Entity is of the view that it should have due regard to a number of valuation techniques for different scenarios (including a DCF model).

#### *Valuation Techniques and Assumptions – 31 December 2011*

The Directors of the Responsible Entity have referenced multiple valuation methodologies in ultimately determining the fair value of the SPS Trust investment in PaperlinX LLC. The key assumptions implied in these methodologies are outlined in the table below for both the 31 December 2011 and 30 June 2011 fair value determination.

These assumptions have been determined by the Directors of the Responsible Entity based upon publicly available information such as:

- PaperlinX's published financial accounts for period ending 31 December 2011 and accompanying commentary on the results; and
- An announcement by PaperlinX on 23 December 2011 that it had received an incomplete, indicative, conditional and non-binding proposal to acquire all of the issued capital of PaperlinX and the SPS Trust via an inter conditional structure.



Valuation Date	Valuation Method used	Basic Assumptions
31/12/2011	Multiple valuation techniques	<ul style="list-style-type: none"> <li>The step up margin will apply from 01 July 2012;</li> <li>Distributions will resume from December 2015;</li> <li>A full redemption will be made December 2019 and;</li> <li>A risk adjusted discount rate of 20 to 25 percent;</li> <li>1 month VWAP of the SPS Trust's trading price;</li> <li>EBITDA multiples of PaperlinX;</li> <li>Full conversion in a change control event; and</li> <li>Net assets of PaperlinX as at 31 December 2011</li> </ul>
30/06/2011	DCF but with regard to other techniques	<ul style="list-style-type: none"> <li>PaperlinX SPS LLC will continue to pay half-yearly distributions into perpetuity and there will be no redemption in the foreseeable future;</li> <li>Distributions will be paid at the margin of 2.40% from 1 July 2011 to 30 June 2012 and thereafter at the step-up margin of 4.65%; and</li> <li>A risk adjusted discount rate of 27.5%. The discount rate reflects the uncertainty in future cash flows and includes an appropriate credit margin for PaperlinX Group for this type of investment.</li> </ul>

The Responsible Entity reiterates that there is uncertainty around future performance of PaperlinX and any assumptions made may or may not be realised in the future.

The valuation methodologies referenced were:

#### **1. Discounted cashflow model (DCF).**

The responsible entity does not have access to the internal cashflow projections of PaperlinX and has relied on market information and broker reports to access assumptions underpinning a DCF model for the SPS Trust's investment in the LLC preferences shares. The key assumptions are:

- the step up margin will apply from 01 July 2012;
- distributions will resume from December 2015;
- a full redemption in December 2019 and;
- a risk adjusted discount rate of 20 to 25 percent.

#### **2. Market Based Assessment.**

This involves a review of the historical ASX trading in the SPS Trust Units assuming a degree of "market efficiency", the implied discount rate/yield to maturity built into current trading, and the market's implicit assumptions regarding distributions, repayment and recoverability.

#### **3. Orderly realisation (going concern basis).**

This involves considerations around the theoretical break-up of PaperlinX based only on public information, considering asset pricing environment in the current market, the inherent enterprise value of PaperlinX and the implied residual value to cover SPS Trust after repaying secured and unsecured liabilities.

#### **4. Realisation via Change of Control Transaction.**

This involves considerations around what the implied value would be of a SPS unit in the event of a PaperlinX corporate transaction that triggers either a Change of Control conversion (as prescribed in the PaperlinX Step-up Preference Securities Product Disclosure Statement), a theoretical conversion at the next remarketing date of 30 June 2012, or payments made to SPS holders in priority to ordinary shareholders of PaperlinX, in accordance with PaperlinX's capital structure.



In this context we note that on 23 December 2011 PaperlinX announced that it had received an incomplete, indicative, conditional and non-binding proposal to acquire all of the issued capital of PaperlinX and the SPS Trust via an inter conditional structure, suggesting a cash price of \$0.09 per share for PaperlinX and \$21.85 for each SPS Trust Unit. The Responsible Entity has not been a party to the discussions in relation to this proposal but does not consider the share of value between the ordinary shareholders and SPS Unitholders holders (as per PaperlinX's ASX announcement of 23 December 2011) appropriately recognises the rights of SPS Unitholders set out in the Product Disclosure Statement and other relevant documents governing the SPS Trust.

#### **5. Net Assets Approach.**

This involves considerations around what value is implied by PaperlinX's 31 December 2011 audit reviewed accounts (noting the matters emphasised in PaperlinX's accounts), and noting off balance sheet items such as operating lease commitments (\$458 million at 30 June 2011) that may be required to be considered under this approach.

#### **Summary**

Given the range of inputs and assumptions, the range of values that can be derived using different valuation techniques, the uncertainties surrounding PaperlinX's operations and the fact that the Responsible Entity does not have access to the internal cash flow forecasts of PaperlinX, fair value estimates under such circumstances are very subjective in nature.

The Responsible Entity has considered the range of possible values arising out of the valuation techniques noted above and has determined that the fair value can be reasonably estimated to be \$96.9M (\$34 per LLC preference share) as at 31 December 2011 (30 June 2011: \$96.9M; \$34 per LLC preference share).

By way of additional information the valuation techniques set out in the table below gives the range of values that The Trust Company considered in its determination.

Fair value considerations for the Trust Dec 2011	Range (rounded)	
	Min	Max
Fair value technique		
DCF model	\$ 17	\$ 36
Market based assessment	\$ 17	\$ 23
Orderly realisation (going concern)	\$ -	\$ 17
Orderly realisation (change of control)	\$ 22	\$ 41
Net Assets Approach	N/A	\$ 100*

\* this figure does not have regard to the time value of money given the nature of the investment and other off balance items in relation to PaperlinX that may reduce any value that could actually be realised. For this reason the Directors of the Responsible Entity have had a lesser regard to this figure in its fair value assessment.

**The Trust Company is not privy to the financial and operational performance of PaperlinX and has relied on publically available information in its assessment of fair value. Any fair value estimate is highly subjective in nature and can differ greatly from results that may actually be obtained under any sale or change of control event of PaperlinX. The Trust Company notes that the assessment of fair value of the Trust's investment in PaperlinX SPS LLC preference shares does not otherwise impact on the rights of Trust unitholders, nor does the valuation affect the value that**



may be achieved for Trust unitholders should any proposal to acquire PaperlinX be advanced. If such a proposal is advanced, the responsible entity will be careful to ensure the rights of Trust unitholders are appropriately recognised.

The Trust Company reiterates that there is uncertainty around future performance and outcomes of PaperlinX and any assumptions made may or may not be realised in the future.

**ENDS**

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