



HENRY MORGAN LIMITED
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Henry Morgan

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20 August 2018

Ms Lisa Banh
Senior Advisor, Listings Compliance (Sydney)
ASX Compliance Pty Ltd
20 Bridge Street
SYDNEY NSW 2000

Email: lisa.banh@asx.com.au

Dear Ms Banh,

HENRY MORGAN LIMITED ("HML"): ASX QUERY

Henry Morgan Limited notes your comments relating to the draft Notice of Extraordinary General Meeting and Independent Expert's Report lodged with ASX on 20 July 2018 for the purpose of ASX Listing Rule 10.1.

ASX have indicated that the draft Notice of Meeting does not contain an adequate explanation of the commercial rationale for the Transaction from the perspective of JB Trading House and JB Financial Group. The Board of HML would like the ASX to understand that HML has been concerned only to focus only on HML's position in considering this Transaction in accordance with HML's directors' common law and statutory duties. The board of HML has not been, and is not, concerned with the motivations, objectives, perspectives, risks or anticipated financial returns of any other party.

However, based on its understanding of JB Trading House's industry and that company's commercial drivers, the Board of HML assumes that the reasons for JB Trading House entering into the Transaction may (but do not necessarily) include the following matters:

- (a) HML has the possibility to be a key revenue-producing client for JB Trading House over time. This is particularly the case as in the event of the exercise of the Put Option HML will be able to exchange its unlisted JB Financial Group shares for cash, thereby ultimately freeing up HML's funds to pursue other investment opportunities, including the undertaking of those investments which may provide an incidental collateral benefit to JB Trading House.
- (b) HML trades numerous equity markets, currency pairs (including emerging markets), government bond markets and commodities, with a total annual notional contract value in excess of AUD\$35.5 billion. Because HML tends to consistently trade numerous markets, including currencies, bonds, equities and commodities, in significant volumes, this gives JB Trading House the ability to negotiate favourable Exchange and platform discounts and consistent counterparty business.



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- (c) Trading houses are a 'scale' business. Scale enables the house to exploit the skills of internal staff, technology and trading platforms. As a general principle, the more trading volume, the lower the average cost and the greater the profit margin. JB Trading House is therefore more likely to benefit by having an exclusive trading arrangement with HML, particularly if HML's current trading volume is maintained or increases in frequency.
- (d) The derivatives market is the largest economic market in the world, with global average daily trading value of foreign exchange and interest rate instruments alone of approximately US\$12.9 trillion.¹ We note that in respect of foreign exchange and interest rate derivatives, these markets have achieved compound annual growth of 9.9% and 7.4% from 2001-2016, respectively. This is considered to be highly suggestive that this growth in trading volumes may be expected to continue, creating opportunities for the JB Trading House group to grow its client base and broaden its product and service offering.

HML's responses to each question as set out in your letter dated 16 August 2018 are as follows:

1. HML expects to pay JB Trading House or its subsidiaries no more than market rates determined on an arms-length basis for transactions of this type and volume in all the circumstances.

Currently, HML trades numerous equity markets, currency pairs (including emerging markets), government bond markets and commodities, with a total annual notional contract value in excess of AUD\$35.5 billion. In addition, if HML increases its funds under management, HML's trading volumes may be likely to increase.

However, it is not possible to reasonably determine the brokerage or other trading commission which HML may be expected to pay over the five year exclusivity period. The ultimate brokerage or other trading commission payable will clearly be influenced by the number and types of transactions that are actually undertaken.

2. JB Trading House trades exchange traded securities including foreign exchange and interest rate instruments on numerous markets worldwide. HML has paid the following brokerage and exchange fees to JB Trading House or its subsidiaries for each financial year since incorporation:

| | 2017 6 months \$ | 2018 12 months \$ | 2019 1 month \$ | Total \$ |
|--------------------------------------|------------------------|-------------------------|-----------------------|------------------|
| Exchange traded securities: | | | | |
| Purchase brokerage and exchange fees | 292,408 | 711,361 | 11,322 | 1,015,091 |
| Sales brokerage and exchange fees | 292,408 | 710,661 | 11,322 | 1,014,391 |
| Total | 584,816 | 1,422,022 | 22,644 | 2,029,482 |

3. The board of HML has had regard to JB Trading House's current financial condition and, more particularly, the prospect of JB Trading House becoming a highly profitable undertaking based upon the revenue that it can derive from its trading operations in the course of its business. In particular, the board of HML considered the possibility and prospect of JB Trading House expanding its business and particularly as the derivatives market is the largest economic market in the world, with the global average daily trading value of foreign exchange and interest rate

¹ Bank for International Settlements (Triennial Central Bank Survey, 2016)

instruments alone of approximately US\$12.9 trillion.² The HML board noted that those latter markets have achieved compound annual growth of 9.9% and 7.4% from 2001-2016, respectively. The board of HML believes that this is highly suggestive of significant growth in revenue, profitability and cash flow for the JB Trading House group.

As a consequence of this anticipated growth in revenues and cash flows, the board of HML is of the opinion that JBTH should be able to satisfy its obligations to HML (and to BHD) under the convertible notes on a timely basis.

4. The board of HML considers that JB Financial Group will be able to satisfy its financial obligations if the Put Option is exercised given the two year time period which must elapse from the grant of issue of the Put Option prior to it being able to be exercised. In particular, the Board considers that JB Financial Group should be able to satisfy its financial obligations in light of the composition and anticipated growth of JB Financial Group's assets (including King's Currency Exchange).

In any event, the HML board notes that JB Financial Group has the right to nominate a party under the Put Option agreement to acquire HML's shareholdings in the event that HML gives notice of its exercise of this Put Option.

Finally, the HML board notes that, in the event of any material concern as to JB Financial Group's ability to satisfy its financial obligations, HML will be under no obligation to exercise the Put Option which has been granted to it. HML considers that it is commercially better off having the Put Option with the downside protection which it provides even if that downside protection may not be as financially secure as HML would otherwise desire. Please be aware that HML has a put option to put its shareholding to JB Financial Group or nominee. There is no obligation on HML to exercise this put option. This is not a case of JB Financial Group having a call option to acquire HML's shareholdings and then having the financial inability to complete the transaction having exercised that call option.

5. HML's obligation to pay any fee to JBL (be it a performance fee or otherwise) is strictly subject to the Management Services Agreement entered into by HML with JBL. As stated in the draft Notice of Meeting, if the Transaction proceeds and if the performance fee payable to JBL is considered on a standalone basis, this fee is estimated to be up to \$7.5 million.

As also indicated in the draft Notice of Meeting as revised and resubmitted on 6 August 2018, JBL has undertaken not to seek the discharge of any performance fee payable to it in connection with the Transaction unless and until sufficient liquid assets are available within HML to enable the payment of this performance fee. Accordingly, HML is expected to be in a position to be able to discharge the estimated performance fee which may be payable to JBL as a result of the Transaction.

Finally, with respect to this issue, we are unaware of what is implied by the ASX when it refers to "the highly unusual terms of the transaction." From HML's perspective, the Transaction taken as a whole is one which is perceived to be highly commercially advantageous to HML given its present business and anticipated future expansion of its business. The HML board has been concerned to focus only on HML's position in considering this Transaction in accordance with the common law

² Bank for International Settlements (Triennial Central bank Survey, 2016)



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and statutory duties of its directors. The board of HML has not been concerned with the motivations, objectives, perspectives, risks or anticipated financial returns of any other party.

6. In order to comply with ASX's direction under Listing Rule 10.9.1 to cancel or arrange for the cancellation of these securities, HML approached JBL. JBL agreed to arrange for the cancellation of the transaction by buying back the securities at the price at which they were issued within the scope of its 10/12 on-market buy-back. To HML's knowledge, the securities were subsequently bought back as part of JBL's on-market buy-back. HML is not aware of the contents of the NSX trading records.
7. Other than as noted by the Company and ASX in previous ASX announcements, HML confirms that it is in compliance with the Listing Rules and, in particular, Listing Rule 3.1.
8. HML's responses to the questions above have been authorised and approved in accordance with the Company's published continuous disclosure policies or otherwise by its board or an officer with delegated authority from the board to respond to ASX on disclosure matters.

Yours faithfully

Kevin Mischewski
Company Secretary
Henry Morgan Limited

16 August 2018

Mr Kevin Mischewski
Company Secretary
Henry Morgan Limited
GPO Box 3112
Brisbane QLD 4000

By email: kmischewski@henrymorgan.com.au

Dear Mr Mischewski,

Henry Morgan Limited ("HML"): ASX Query

ASX Limited ("ASX") refers to the following:

- A. HML's announcement on 9 July 2018 titled "Update on JB Financial Group transaction", advising of changes to the proposal previously updated on 11 May 2018, whereby JBFG will acquire HML's stake in JBFG and BRL (the "Transaction"), to be implemented in part through a put option arrangement (the "Put Option"). The key terms of the Transaction were summarised (in part) as follows.
- 1) *Henry Morgan will enter into an exclusive trading agreement with JB Trading House Pty Ltd for a period of 5 years and can:*
 - a) *sell its shares in JB Financial Group Pty Ltd to JB Financial Group Pty Ltd or nominee; and*
 - b) *sell its shares in Bartholomew Roberts Pty Ltd to JB Financial Group Pty Ltd or nominee.*
 - 2) *JB Financial Group will grant a put option in respect of Henry Morgan's shareholding in Bartholomew Roberts and JB Financial Group, pursuant to which JB Financial Group will:*
 - a) *pay \$67.16 million in tranches in the event of exercise of the put option 2-5 years post grant; plus*
 - b) *provide security against all of the issued shares in King's Currency Exchange Pty Ltd and Harnewei Pty Ltd in a first priority position for the discharge of this debt.*
 - 3) *JB Trading House Pty Ltd will issue convertible notes to Henry Morgan with a total face value of \$12 million and a coupon of 4.1% per annum. The convertible notes are to be secured over JB Trading House Pty Ltd and its 100% owned subsidiaries.*

In respect of the convertible notes, Henry Morgan will have the right to elect to either:

 - i) *After four (4) years, be paid A\$12 million by JB Trading House, which shall then be paid in 12 equal monthly instalments from that date; or*
 - ii) *At any time within four (4) years, convert all or some of the convertible notes into shares in JB Trading House at a price which represents a 40% discount to the pre-money IPO or other valuation of JB Trading House.*
- B. The announcement by Benjamin Hornigold Limited ("BHD") on 6 June 2018 titled "Proposed convertible note transaction" lodged on 6 June 2018, disclosing that JB Trading House Pty Ltd ("JBTH") also intends to issue BHD a \$13.5 million convertible note, on similar terms to the convertible notes to be issued to HML.
- C. The draft notice of meeting ("NOM") and independent expert's report prepared by Leadenhall Pty Ltd ("IER") for the purposes of Listing Rule 10.1.
- D. HML's announcement entitled "Corrective Action" lodged on 13 March 2018, advising that HML is arranging for the cancellation of 1,398,573 shares and 1,398,573 options it acquired in its investment manager, John Bridgeman Limited ("JBL"), in breach of Listing rule 10.1.

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- E. HML's announcements entitled "Update on on-market buy-back" and "Update on placement securities" lodged on 20 July 2018 and 6 August 2018, respectively, advising that JBL has effectively bought back and cancelled its securities under an on-market buy-back from HML.
- F. JBL's announcement lodged on the NSX on 6 August 2018 disclosing that JBL had bought back from HML and cancelled 1,398,573 JBL shares for \$2.05 per share and 1,398,573 JBL options for \$0.00 per option, being in each case the original price received by JBL from HML for the issue.

ASX is concerned that the draft NOM does not contain an adequate explanation of the commercial rationale for what appears to be a highly unusual set of transactions from the perspective of all parties. In particular, it is not clear why JBTH would agree to incur substantial debts (\$25.5 million) to BHD and HML in consideration solely for undertakings from those companies to trade exclusively with JBTH and its subsidiaries, when there are no minimum trading requirements imposed on BHD or HML, nor why JBTH would agree to issue securities to BHD at a discount of 40% to an arm's length valuation. Additionally, it is unclear why JBFG would grant a put option to HML requiring the payment of \$67.16 million cash if exercised, when according to the IER as at 31 May 2018 JBFG only had \$16.8 million in cash, net assets of \$64.8 million (which includes \$60.8 million of intangible assets and \$6.2 million in deferred tax assets) and had lost \$3.2 million in the 11 months year to date.

ASX requires HML to submit updated draft NOM addressing these issues.

Further, having regard to the above, ASX asks HML under Listing Rule 18.7 to respond separately to each of the following questions and requests for information:

1. What brokerage or other trading commissions does HML expect to pay to JBTH or its subsidiaries over the five year exclusivity period? Please explain how this figure has been calculated.
2. How much has HML paid JBTH or its subsidiaries in brokerage or other trading commissions since incorporation? Please provide a year by year breakdown showing the fees paid on purchases of listed securities, purchases of unlisted securities, sales of listed securities and sales of unlisted securities.
3. Please explain what analysis or other due diligence the board of HML has undertaken to satisfy itself of the ability of JBTH to satisfy its obligations under the convertible notes, particularly if JBTH is required to pay \$13.5 million cash to BHD and \$12 million cash to HML in 4 years' time?
4. Please explain what analysis or other due diligence the board of HML has undertaken to satisfy itself of the ability of JBFG to satisfy its obligations if the Put Option is exercised, given that as at 31 May 2018 JBFG only had \$16.8 million in cash, net assets of \$64.8 million (which includes \$60.8 million of intangible assets and \$6.2 million in deferred tax assets) and had lost \$3.2 million in the 11 months year to date.
5. If the Transaction proceeds, it will crystallise a performance fee payable to JBL estimated to be \$7.5 million. Please explain the basis on which the directors of HML consider that to be appropriate, given the highly unusual terms of the Transaction, and how HML proposes to pay this fee?
6. Please explain whether JBL's buy back from HML of 1,398,573 JBL shares for \$2.05 per share and 1,398,573 JBL options for \$0.00 per option announced on 6 August 2018 was conducted on-market or off-market.

If it was done on-market, please disclose how and when JBL was able to buy back 1,398,573 shares on-market from HML for \$2.05 per share when the trading records of NSX state that shares in JBL last traded on 14 February 2018, with 13,5000 shares being traded at \$2.00 per share. Please also explain how and when JBL was able to acquire 1,398,573 options on-market for nil consideration.

If it was done off-market please explain how JBL complied with the Corporations Act requirements for off-market buybacks and provide a copy of the buy-back agreement.

7. Please confirm that HML is in compliance with the Listing Rules and, in particular, Listing Rule 3.1.

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8. Please confirm that HML's responses to the questions above have been authorised and approved in accordance with its published continuous disclosure policies or otherwise by its board or an officer with delegated authority from the board to respond to ASX on disclosure matters.

When and where to send your response

This request is made under, and in accordance with, Listing Rule 18.7. Your response is required as soon as reasonably possible and, in any event, **by not later than 9.30am AEST on Friday, 24 August 2018.**

You should note that if the information requested by this letter is information required to be given to ASX under Listing Rule 3.1 and it does not fall within the exceptions mentioned in Listing Rule 3.1A, HML's obligation is to disclose the information "immediately". This may require the information to be disclosed before the deadline set out in the previous paragraph.

ASX reserves the right to release a copy of this letter and your response on the ASX Market Announcements Platform under Listing Rule 18.7A. Accordingly, your response should be in a form suitable for release to the market.

Your response should be sent to me by e-mail at lisa.banh@asx.com.au. It should not be sent directly to the ASX Market Announcements Office. This is to allow me to review your response to confirm that it is in a form appropriate for release to the market, before it is published on the ASX Market Announcements Platform.

Listing Rules 3.1 and 3.1A

In responding to this letter, you should have regard to HML's obligations under Listing Rules 3.1 and 3.1A and also to Guidance Note 8 *Continuous Disclosure: Listing Rules 3.1 – 3.1B*.

It should be noted that HML's obligation to disclose information under Listing Rule 3.1 is not confined to, nor is it necessarily satisfied by, answering the questions set out in this letter.

If you have any queries or concerns about any of the above, please contact me immediately.

Kind regards

[Sent electronically without signature]

Lisa Banh

Senior Adviser, Listings Compliance (Sydney)

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