

20 August 2018

Adrian Smythe  
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20 Bridge Street  
SYDNEY NSW 2000

Email: [adrian.smythe@asx.com.au](mailto:adrian.smythe@asx.com.au)

Dear Mr Smythe,

**LETTER TO BENJAMIN HORNIGOLD LIMITED ("BHD") DATED 9 AUGUST 2018**

Benjamin Hornigold Limited notes your comments relating to the draft notice of general meeting and independent expert's report lodged with ASX on 23 July 2018 for the purpose of listing Rule 10.1. Hanrick Curran Corporate Finance Pty Ltd have provided their response to ASX's assertions in relation to their independent expert's report at Annexure A attached to this letter.

**Meeting materials**

You have suggested that the Notice of Meeting does not contain an adequate explanation of the commercial rationale for the transaction. In particular, you have queried JB Trading House's reasons for incurring debts to BHD in consideration for undertakings to trade exclusively with JB Trading House and its subsidiaries, with no minimum trading requirements and a discount to valuation if the notes are converted.

Firstly, it is important to remember that the Board of BHD is only able to address queries that relate to BHD's actions or operations. The BHD Board is not able to provide ASX with information regarding the rationale behind a third party making a decision to undertake a commercial transaction.

From BHD's perspective, the proposed transaction with JB Trading House offers several benefits, including the following:

- (a) The consideration for the Convertible Notes is the agreement by BHD to trade exclusively through JB Trading House and its subsidiaries. It does not require the outlay of cash from BHD;
- (b) JB Trading House is required to provide its trading services at market competitive rates for commissions and broking fees;
- (c) BHD is not required to commit to a minimum volume of trading;

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- (d) JB Trading House must provide minimum levels of service including priority in terms of execution of trading instructions;
- (e) During the term of the Convertible Note, BHD will receive payment of a coupon and the option to receive \$13.5 million face value of the Convertible Notes;
- (f) BHD is being offered registered security over JB Trading House to secure the above payment obligations;
- (g) BHD has the sole discretion to convert the notes into equity depending on the performance and growth of JB Trading House over time; and
- (h) BHD has leveraged its position as a key foundation client of JB Trading House to negotiate beneficial terms, including the ability to convert the notes into equity in JB Trading House at a discount to valuation at the time.

In addition, from a general market perspective, BHD believes that JB Trading House has four competitive advantages in terms of anticipated future growth:

1. It employs trading strategies that have longer holding periods than High Frequency Trading strategies.
2. It trades all markets including emerging markets.
3. All macro research is proprietary.
4. All technology and trading algorithms are proprietary.

These four strengths provide JB Trading House with the opportunity to take advantage of developments in the derivatives market. As established players such as commercial banks have exited the derivatives market in recent times, that space has largely been filled by new entrants that are highly profitable and growing rapidly. BHD believes JB Trading House will be able to utilise its competitive advantages to capture market share and increase scale and profitability. This would ultimately benefit BHD if it chooses to convert the notes into equity in JB Trading House at some future time.

The Board of BHD has previously identified market making and the provision of liquidity as a attractive opportunity. Industry reports indicate that, with major global commercial and major global investment banks exiting proprietary trading, liquidity in global markets is largely provided by either hedge funds or specialist proprietary trading firms which have emerged from hedge funds.<sup>1</sup>

The Board of BHD believes the largest opportunity is in foreign exchange, which has historically been dominated by the major banks. Today, however, there are six non-bank liquidity providers in the top 50 FX providers globally.<sup>2</sup> Further, the Board of BHD believes the medium term opportunity is in emerging market currencies particularly in Asia, where large population bases with fast growing economies are likely to see their currencies displace some of the traditional highly liquid developed world currencies over time.

While BHD is committed primarily to global macro trading, it has previously considered the opportunities associated with this market sector. The current proposal with JB Trading House provides BHD with the option, at its entire discretion, to consider

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<sup>1</sup> <https://www.fnlondon.com/articles/specialist-liquidity-provider-of-the-year-2018-the-nominees-20180327#>

<sup>2</sup> <https://www.euromoney.com/article/b18f5s6kqtcr6m/euromoney-fx-survey-2018-results-released>

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participating by way of taking a stake in JB Trading House if the performance of that company and its subsidiaries is attractive over time. If not, then BHD has the ability to elect to receive payment for the face value of the Convertible Notes in return for its commitment to trade exclusively through JB Trading House for the required period.

As to the commercial rationale for JB Trading House entering the transaction, as indicated above, it is not appropriate for the Board of BHD to assume to know the reasonings of a third party. However, based on its understanding of the industry, the Board of BHD assumes that these reasons may include:

- (a) By procuring an exclusive trading relationship with BHD, JB Trading House secures a valuable client. It is not unusual for service providers to enter into agreements to provide increased service levels to important clients in order to secure their client base.
- (b) As a result, JB Trading House is likely to benefit by increased trading volume, which will provide it with a stronger negotiating position with Exchanges in terms of rebates and fees.
- (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.
- (d) BHD trades all equity markets, currency pairs (including emerging markets), government bond markets and commodities, with a total annual notional contract value in excess of AUD\$57.5 billion in turnover. Because BHD trades all markets, including currencies, bonds, equities and commodities in size and consistently, this gives JB Trading House the ability to negotiate Exchange and platform discounts and consistent counterparty business.
- (e) BHD is committed primarily to global macro trading, and would therefore be anticipated to be a key revenue-producing client for JB Trading House.
- (f) BHD's investment portfolio is largely in cash. There is a strong likelihood that BHD will grow its capital and therefore increase its trading scale over time. The volume of trading from BHD is anticipated to be significant, and to grow further over time. This would benefit both BHD and JB Trading House.

## Queries

Separately, BHD's responses to each question set out in your letter of 9 August 2018 are set out below:

1. In negotiating the terms of the transaction with JB Trading House, BHD has ensured that it is able to respond to market conditions and either increase or decrease its trading activity appropriately, without incurring additional cost obligations during the exclusivity period. The transaction documents between BHD and JB Trading House do not require BHD to place a minimum amount of trading through JB Trading House. The transaction documents also require that brokerage fees are to be equal to or more competitive than market rates. Accordingly, the amount of brokerage or trading commissions payable to JB Trading House will fluctuate based on the volume of trading undertaken by BHD, the size and frequency of those

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trades, the market conditions at the time, and then current market rates for brokerage and commissions. For these reasons, BHD has refrained from forecasting the exact amount of trading and the amounts of brokerage or trading commissions that it expects to pay JB Trading House or its subsidiaries over the five year exclusivity period.

Currently, BHD trades all equity markets, currency pairs (including emerging markets), government bond markets and commodities, with a total annual notional contract value in excess of AUD\$57.5 billion in turnover. If BHD continues to do so, and/or increases its funds under management, trading volumes are also likely to increase. This would benefit both BHD and JB Trading House.

2. BHD has paid the following brokerage and exchange fees to JB Trading House or its subsidiaries for each financial year since incorporation:

	2017 2 months \$	2018 12 months \$	2019 1 month \$	Total \$
<b>Listed securities:</b>				
Purchase brokerage and exchange fees	108,732	1,238,242	71,734	1,418,708
Sales brokerage and exchange fees	108,732	1,237,642	69,234	1,415,608
<b>Total</b>	<b>217,464</b>	<b>2,475,884</b>	<b>140,968</b>	<b>2,834,316</b>

3. As part of its due diligence process, the Committee of Independent Directors of BHD made enquiries into the financial performance of the businesses within JB Trading House, namely, JB Markets Pty Ltd, JB Alpha Ltd and Genesis Proprietary Trading Pty Ltd, and sought information regarding the anticipated growth of JB Trading House over the next four years. In addition, the Committee required registered security over the entire JB Trading House group, as well as the right to convert the notes into shares, in order to provide security for JB Trading House's payment obligations under the proposed transaction.

In considering the current operations and anticipated growth of JB Trading House, the Committee was updated on the size of, and opportunities offered by, the global derivatives market to JB Trading House. It was noted that 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<sup>3</sup>. In respect of foreign exchange and interest rate derivatives in particular, those markets have achieved compound annual growth of 9.9% and 7.4% from 2001-2016 respectively. This growth is expected to continue, creating opportunities for the JB Trading House group to grow its client base and broaden its product and service offering to include market making and hedging strategies.

<sup>3</sup> Bank for International Settlements (Triennial Central Bank Survey, 2016)

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These strategies, combined with the commissions which JB Trading House would generate from increased derivatives trading and Exchange fee rebates could, if realised, provide lucrative income streams for JB Trading House.

The Committee noted the potential opportunity for BHD to participate in this growth if it later determined to convert the notes, at its discretion, into shares in JB Trading House subject to contractual and regulatory requirements.

Separately, the Committee engaged an Independent Expert to advise on the proposed transaction and provide an opinion on, amongst other things, a valuation of the shares in JB Trading House.

Upon consideration of all circumstances, including the above, the Board of BHD satisfied itself of the ability of JB Trading House to satisfy its obligations under the Convertible Note transaction.

4. Any management or performance fee payable will be based on the formula set out in the Management Services Agreement entered into between BHD and John Bridgeman Limited. The fees payable are not solely attributable to any one transaction and are calculated based on the net tangible assets and investment return of BHD.

Assuming that the Transaction proceeds and the entire \$23 million valuation assessed by the Independent Expert increases the investment return of BHD, the maximum performance fee able to be earned over the term of the Transaction may be up to \$4.35 million (plus any applicable GST).

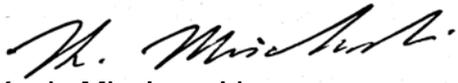
Management fees of up to \$480,000 (plus any applicable GST) may be payable on any increase in the net tangible assets of BHD as a result of the Transaction.

BHD has considered the likely timing of any management or performance fees that may become payable and notes that it is unlikely that the Transaction will immediately crystallise the entire amount of these fees. To the extent necessary, BHD expects to be able to pay these fees from working capital and if required may enter into an agreement to defer payment of fees to John Bridgeman Limited until sufficient liquid assets are available within BHD to discharge the performance fee.

5. In order to comply with ASX's direction under Listing Rule 10.9.1 to cancel or arrange for the cancellation of its acceptance of placement securities from JBL, BHD 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 BHD's knowledge, the securities were subsequently bought back as part of JBL's on-market buy-back. BHD is not aware of the contents of the NSX trading records.
6. BHD confirms that it is in compliance with the Listing Rules, in particular Listing Rule 3.1.
7. BHD'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.

Yours faithfully



**Kevin Mischewski**  
Company Secretary  
**Benjamin Hornigold Limited**

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**ANNEXURE A**

**Hanrick Curran Corporate Finance Pty Ltd re ASX Letter to Benjamin Hornigold Limited**

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16 August 2018

Mr Kevin Mischewski  
Company Secretary  
Benjamin Hornigold Ltd  
Level 9 Riverside Centre  
123 Eagle Street  
BRISBANE QLD 4000

By Email: [kmischewski@benjaminhornigold.com.au](mailto:kmischewski@benjaminhornigold.com.au)

Dear Mr Mischewski

RE: ASX LETTER TO BENJAMIN HORNIGOLD LIMITED ("BHD")

We refer to ASX's Letter to BHD dated 9 August 2018 ("Letter") which contains ASX's concerns in relation to the content of the Independent Expert's Report that we have prepared.

Our comments on the relevant items within the Letter are as follows:

1. Appendix 5 of the IER contains a list of 21 selected companies, said to be the most comparable to JBTH in terms of size and calculates the 19.9 times PER as the average PER of those 21 companies. This includes Aberdeen Asia-Pacific Income Investment Company Limited (TSX: FAP), which has a PER of 115.6. If this company is excluded, the average PER for the remaining companies is reduced from 19.90 times to 15.11 times. It's unclear to ASX why such an obvious outlier was not excluded from the calculation of the average PER for these companies.

#### Comment

In preparation of the IER, our analysis in relation to PER included a review of companies that may be comparable to JBTH, from public information available to us. As we were unable to identify a directly comparable company, we decided to include broadly comparable companies based on industry. We appreciate different companies have different operating structures and business models. However, we believe companies within the same industry share similar drivers thus are broadly relevant and comparable. At the start of the analysis process, our review included international companies which contained mostly US companies. The reason for this step was that JBTH's trading involves foreign currencies and instruments, and the Group's recent increasing involvement and partnership with international financial institutions. At that stage of our analysis, there were a number of companies with 100+ and 200+ times PER. The average US PER was approximately 75 times. We then focused on Australian companies only. At that stage, there were about 95 companies on the list and out of which, about 10 companies had a PER of 90+ times. Further shortlisting was done to

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filter companies that were most comparable in terms of size as stated in paragraph 4.4.1 in our report.

As explained above, the company which showed a PER of 115.6 times was, in our opinion, not truly an outlier as opposed to its appearance only because of our shortlisting process.

Further to the above, we did not view solely from a pure statistics perspective. High PERs can sometimes represent companies' growth prospects that a marginal investor has priced in. JBTH has three main business components which were recently acquired. We have reviewed business strategic plan documents and had various discussions with management. There were a number of key milestones achieved just prior to valuation date which could represent very high revenue growth for JBTH over the next few years. We were, on one hand, cautious of any aggressive future predictions, but also conscious of not eliminating such potential entirely, especially if other companies within the industry exist which the market is pricing as a growth prospect. As a proxy and in plain language, our rationale was that having 1-in-21 chance for JBTH having a high growth did not appear unreasonable to us having reviewed the documents and had those management discussions. Accordingly and in our opinion, it is reasonable to consider and include FAP in our analysis.

2. Many of the companies in Appendix 5 do not appear to be genuinely comparable to JBTH and have very different businesses. For example, there are several listed investment companies such as WAM Research Limited, Clime Capital Limited, Century Australian Investments Limited and Pengana International Equities Limited amongst others. Not only are their business models completely different, their trading prices are more likely to reflect the current net tangible asset backing, rather than an earnings multiple.

#### Response

As stated in our response to Query 1 above, our review was based on a broadly comparable category by industry for the reason that companies within the same industry share similar business drivers. We were unable to find a directly comparable company which information was publicly available. We are aware that different companies may have different business structures and models.

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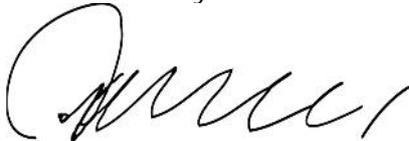
3. The IER includes no historical financial information for JBTH to compare against its FY2019 NPAT management forecast, nor is there any analysis to validate JBTH's FY2019 NPAT management forecast. For example, how does this forecast compare to JBTH's actual or forecast FY2018 NPAT? How has JBTH previously tracked against internal management profit forecasts? What are the assumptions underlying the increase in profit necessary for the forecast to be met? What are the events and risks that could lead to the forecast not being achieved?

Response

We will include the relevant historical information and analysis. However, as stated in paragraphs 4.1 and 4.3 of our report, the business components within JBTH were acquired fairly recently. Historical earnings from more than 12 months prior to valuation date represented historical performances under previous owners and management. Then there was period when the newly acquired units would need to go through a transition process including, to varying extents, management change, restructuring, business model changes and integration with other business units in the group both in terms of businesses and culture. We note JBTH itself was only formed very recently prior to valuation date. Prior to that, those business units were under a larger group which contains other business units which were not subject to our review for the purposes of the IER. For these reasons and as stated in the IER, we are of the opinion that the historical performance for these business units is of very little relevance in our assessment of what profit for a typical year is expected to be. As part of the IER, we discussed with senior management the forecast for FY2018 and actuals to April 2018, and general achievability of the forecast.

If you have any queries in relation to this please contact us.

Yours sincerely



Alex Fraser  
Alex.fraser@hanrickcurran.com.au

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9 August 2018

**Mr Kevin Mischewski**

Company Secretary  
Benjamin Hornigold Limited  
GPO Box 3112  
Brisbane QLD 4000

By email: kmischewski@benjaminhornigold.com.au

Dear Mr Mischewski,

**Benjamin Hornigold Limited ("BHD")**

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

- A. BHD's announcement titled "Proposed convertible note transaction" lodged on the ASX Market Announcements Platform ("MAP") on 6 June 2018, disclosing a proposal whereby JB Trading House Pty Ltd ("JBTH") will issue BHD a \$13.5 million convertible note ("Convertible Note") in return for BHD committing to trade exclusively through JBTH subsidiaries for a set period of time (the "Transaction").
- BHD may elect: (i) after 4 years to be paid \$13.5 million by JBTH (in 12 equal monthly instalments), or (ii) at any time within 4 years, to convert all or part of the Convertible Note into shares of JBTH at a 40% discount to the "pre-money valuation of JB Trading House (to be established either by IPO Pricing, trade sale price, other liquidity event or independent valuation if such valuation cannot be agreed)."
- B. The announcement by Henry Morgan Limited ("HML") titled "Update on JB Financial Group transaction" lodged on MAP on 9 July 2018, disclosing that JBTH also intends to issue a \$12 million convertible note to HML, on similar terms to the Convertible Note.
- C. The draft notice of general meeting ("NOM") and independent expert's report ("IER") prepared by Hanrick Curran Corporate Finance Pty Ltd ("Hanrick Curran") for the purposes of Listing Rule 10.1. The NOM states that pursuant to the Transaction, BHD has agreed to trade exclusively through JBTH and its subsidiaries for a period of five years.
- D. BHD's announcement entitled "Corrective action" lodged on MAP on 7 March 2018, advising that BHD is arranging for the cancellation of the acquisition of 539,585 shares and 539,585 options in its investment manager JBL acquired in breach of Listing Rule 10.1 (the "Corrective Action Announcement").
- E. The announcement by John Bridgeman Limited ("JBL"), the investment manager of both BHD and HML, lodged on NSX on 7 March 2018 indicating that its directors had provided their indicative agreement to undertake a selective buy-back of 536,585 [sic] shares and options issued to BHD on 23 November 2017.
- F. JBL's announcement lodged on the NSX on 6 August 2018 disclosing that JBL had bought back from BHD and cancelled 539,585 JBL shares for \$2.05 per share and 539,585 JBL options for \$0.00 per option, being in each case the original price received by JBL from BHD for the issue.

ASX considers that the draft NOM and IER are not of an acceptable standard and do not provide shareholders with adequate information to make an informed decision in relation to the Transaction. ASX's concerns include:

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- The draft NOM does not contain an adequate explanation of the commercial rationale for what appears to be a highly unusual transaction 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.
- The IER places a value of between \$23.4 million and \$23.5 million on the Convertible Note, which is derived in part from the equity value attributed to JBTH. The equity value of JBTH is calculated by applying a price to earnings ratio ("PER") of 19.9 times (less a 15% discount for "lack of marketability" and a further 20% discount for "profit prediction risk") to JBTH's management forecast for FY2019 NPAT of \$9,032,983.
- Appendix 5 of the IER contains a list of 21 selected companies, said to be the most comparable to JBTH in terms of size and calculates the 19.9 times PER as the average PER of those 21 companies. This includes Aberdeen Asia-Pacific Income Investment Company Limited (TSX:FAP), which has a PER of 115.6. If this company is excluded, the average PER for the remaining companies is reduced from 19.90 times to 15.11 times. It's unclear to ASX why such an obvious outlier was not excluded from the calculation of the average PER for these companies.
- Many of the companies in Appendix 5 do not appear to be genuinely comparable to JBTH and have very different businesses. For example, there are several listed investment companies such as WAM Research Limited, Clime Capital Limited, Century Australian Investments Limited and Pengana International Equities Limited amongst others. Not only are their business models completely different, their trading prices are more likely to reflect the current net tangible asset backing, rather than an earnings multiple.
- The IER includes no historical financial information for JBTH to compare against its FY2019 NPAT management forecast, nor is there any analysis to validate JBTH's FY2019 NPAT management forecast. For example, how does this forecast compare to JBTH's actual or forecast FY2018 NPAT? How has JBTH previously tracked against internal management profit forecasts? What are the assumptions underlying the increase in profit necessary for the forecast to be met? What are the events and risks that could lead to the forecast not being achieved?
- The IER plainly does not accord with the expectations for an independent expert report set out in ASIC Regulatory Guide 111 *Content of expert reports*.

ASX requires BHD to submit updated documents addressing these issues.

Further, having regard to the above, ASX asks BHD under Listing Rule 18.7 to respond separately to each of the following questions and requests for information for the purposes of ASX being satisfied that BHD is in compliance with the Listing Rules:

1. What brokerage or other trading commissions does BHD 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 BHD paid JBTH or its subsidiaries in brokerage or other trading commissions since incorporation?
3. Please explain what analysis or other due diligence the board of BHD has undertaken to satisfy itself of the ability of JBTH to satisfy its obligations under the Convertible Note, particularly if JBTH is required to pay \$13.5 million cash to BHD and \$12 million cash to HML in 4 years' time?
4. If the Transaction proceeds, will it crystallise any management or performance fee payable to JBL? If so, what is the likely size of the management or performance fee and how does BHD propose to pay this fee?
5. Please explain whether JBL's buy back from BHD of 539,585 JBL shares for \$2.05 per share and 539,585 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 539,585 shares on-market from BHD 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 539,585 options on-market for nil consideration.

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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.

6. Please confirm that BHD is in compliance with the Listing Rules and, in particular, Listing Rule 3.1.
7. Please confirm that BHD's responses to the questions above have been authorised and approved in accordance with its published continuous disclosure policy or otherwise by its board or an officer of BHD 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 half an hour before the start of trading (ie before 9.30 a.m. AEST) on Thursday, 16 August 2018.

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. 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 BHD'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 BHD's obligation to disclose information under Listing Rule 3.1 is not confined to, nor is it necessarily satisfied by, providing the information requested in this letter.

Further, 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, BHD's obligation is to disclose the information "immediately". This may require the information to be disclosed before the deadline set out in this letter.

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

Yours sincerely

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**Adrian Smythe**

Manager Listings Compliance