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Project Akersten

Synergies Review – Summary Report

March 2021

Deloitte.

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31 March 2021

Dear Nikki

Project Akersten: Review of Synergy Estimates – Summary Report

We enclose our summary report (the "Report") which summarises the synergies and our view on the potential achievability of the synergies based on our understanding of Project Akersten. This is a summary of our work only and is subject to the analysis contained in our detailed report and the disclaimers and restrictions contained in our detailed report and Engagement Letter. The analysis included in the detailed report, on which this summary report is prepared, was completed on 8 December and we have not updated our work since that date.

Our report is provided in accordance with our letter of engagement dated 26 November 2020 (the Engagement Letter).

This report has been prepared only for Nelson City Council (NCC) and their advisors. No party is entitled to rely on this report for any purpose whatsoever and we accept no responsibility or liability to any party in respect of the contents of this report.

We accept no duty of care or liability to anyone, other than NCC, who is shown or gains access to, or uses or relies on, the report.

Yours faithfully

S.McClay

Scott McClay
Partner
For Deloitte Limited (as trustee for the Deloitte Trading Trust)

Important Notice to the Review of Synergy Estimates Reader

- **This report summarises the output of the work that we performed in relation to reviewing the proposed synergies of Project Akersten. This is a summary of our work only and is subject to the analysis contained in our detailed report and the disclaimers and restrictions contained in our detailed report and Engagement Letter.**
- **NCC has asked for, and we consented to, the publication of this summary report (the Report) to allow for wider, and more transparent, consultation on Option 1 of the business case prepared by the project governance group (the Proposal). This Notice sets out the terms on which we are prepared to allow you access to the report. If you do not agree to the terms of this Notice you may not read the report.**
- We are prepared to allow you access to the Report on the following terms:
  - Our work was performed and the Report was prepared for NCC:
    - at its request, from information provided by NCC;
    - solely for its benefit and not for any other person; and
    - in accordance with our engagement letter dated 26 November 2020.
- You may only have access to and use the Report to consider whether you wish to provide consultation feedback on the Proposal (the Purpose) and not for any other purpose.
- Our work or the Report may not be sufficient or appropriate for your Purpose and the report does not constitute a recommendation from us regarding the Proposal. The Report may not address or reflect matters in which you may be interested or which may be material to you (Additional Matters).
- You are responsible for verifying the accuracy and completeness of the Report. We do not accept any responsibility to you in respect of any errors or omissions in the Report, of which you are aware or should be aware from your own knowledge and inquiries in relation to the Proposal.
- We have no responsibility to advise you of any Additional Matters and we are not responsible to you (whether for our negligence or otherwise) if any Additional Matters are not included in the Report.
- Significant events may have occurred since the date of the Report or the date detailed in the Report which may have a material effect on the Report. We have no responsibility to, and we will not monitor or advise you of any events or circumstances which may have become known or occurred after the date of the Report or the date detailed in the Report, including those which may impact on our work, the Report or the Proposal; or update our work or the Report.
- You may not rely on the Report. We are not responsible to you or anyone else for any loss (however caused, including as a result of our negligence) you or anyone else may suffer or incur in connection with your access to, or if you rely on the Report.
- You will not acquire any rights in connection with your access to the Report. We have no duty of care to you for the work we have performed or for the Report or anything in it. You are responsible for making your own enquiries as may be appropriate to your interests in providing consultation feedback. In providing you with a copy of the Report we do not accept any responsibility to you or anyone else in that regard.
- You must not name us in any Report or document which will be made publicly available or provided to any regulator without our consent.
- You will not make any claim or demand or bring any proceedings against us in connection with the report or your access to it.
- This Notice forms a binding agreement between Deloitte and any recipient of this report which is governed by the laws of New Zealand and in respect of which the Courts of New Zealand shall have exclusive jurisdiction.

Summary

Introduction

- Port Nelson Limited (PNL) and Nelson Airport Limited (NAL), along with their shareholders, are considering various options for restructuring the ownership and operations of PNL and NAL to leverage the synergies between their respective operations.
- A project governance group consisting of representatives from NAL, PNL and the Shareholders (Nelson City Council (NCC) and Tasman District Council (TDC)) have met regularly to consider the potential efficiencies and synergies from various restructuring options and have prepared a business case.
- One of the proposed restructure options ("Option 1") within the business case provided by the project governance group involves the establishment of a Holdings entity ("Holdco") which will acquire the shareholding of PNL and NAL. Holdco will be owned 50% by NCC and 50% by TDC.
- Resulting from the Option 1 restructure, the project governance group have estimated there are approximately $1.0m of synergy benefits (referred to as synergies in this report) mainly resulting from cost savings due to a reduction in effort across the group or from economy of scale gains.

Scope

- We have been engaged by NCC to provide our view as to whether the Option 1 synergies assumed are reasonable and to provide a level of diligence on the assumptions that have been utilised in the Option 1 analysis.
- More specifically, we have been engaged to provide the following services with respect to Option 1:
  - Understand the detailed assumptions which form the synergy estimates;
  - Discuss the assumptions with NAL and PNL management to confirm each respective management view;
  - Review the assumptions and provide our view as to the appropriateness of the assumptions applied and highlight any perceived risks; and
  - Prepare a detailed report that summarises the synergies, the synergy assumptions, and potential achievability of the synergies based on our understanding of the proposed restructure (collectively, the Services).
- The following matters are excluded from the scope of our Services:
  - The interest rate benefit from the use of LGFA funding is out of scope for this review; and
  - We will not assess the businesses resourcing, technical capability, or functionality requirements or if any restructuring of employees or other (i.e. IT equipment) is feasible.

Conclusion

- The project governance group identified savings of $992k, partially offset by transition costs resulting from the Option 1 restructure.
- In summary, $592k of the synergy benefits appear reasonable and likely; $54k of synergy benefits appear possible, albeit with risks of benefits not being able to be achieved; $250k of synergies identified have been assessed as possibly unlikely to the extent documented in the business case and $36k of synergy benefits appears unlikely.
- Additional synergy benefits relating to cost savings, revenue uplifts, and capital expenditure savings have also been identified but not included in the business case which highlights a level of conservatism displayed by the project governance group in preparing the synergy benefits.
- On balance, the Option 1 synergy benefits outlined appear mostly reasonable and achievable and should provide material benefit to a combined group, however, the reader should also note that quantitatively estimating synergies is difficult as the intricacies of merging two businesses are often not known until post-merger. In our experience:
  - Synergies are not effective immediately after the merger takes place. Typically, these synergies are realised two or three years after the transaction. This period is known as the "phase in" period, where operational efficiencies, cost savings, and incremental new revenues are slowly absorbed into the newly merged firm.
  - In the short term costs may actually go up as the integration incurs one-time expenses and a short-term inefficiency due to lack of history working together and culture clashes. If a culture clash is too great, synergies may never be realised.
  - Achievement of synergies requires focus from Management in order to ensure that the 'status quo' in each organisation is not maintained.
  - NAL is small relative to PNL (expenditure of ~10% of PNL) therefore in some cases the benefits from scale might be difficult as the merged entity will not be substantially larger than PNL in its current state.

Summary

- The table below summarises the project governance group's analysis of synergy benefits from Option 1 (as included the business case prepared by the project governance group) and our assessment of synergy achievability. The rationale for our assessments is set out in our detailed report.

Achievability: Likely Possible Unlikely

Cost Type				
Employee Benefit Expenses	$271k			
Governance Costs	$110k			
Audit Fees				$36k
Insurance Costs			$58k	
Computer Charges, Computer Software and Data, Contract Services		$22k $32k	 $43k $51k	
Electricity & Fuel			$98k	
Cleaning & R&M	$79k			
Accounting and Aeronautical Charges	N/A			
Consultancy Resource	$50k			
Other Synergies	$82k			
Total Savings	**$592k**	**$54k**	**$250k**	**$36k**

- Synergies benefits from reductions in Accounting and Aeronautical Charges were assessed as not be a result of the restructure therefore not applicable in the assessment.
- A number of identified but unquantified synergies have not been incorporated into the synergy assessment and may provide additional benefit.
- Transition costs of $385k have been identified, $335k as an upfront setup cost and $50k as a year 1 cost. These costs are not assessed within our scope.