Merchantec
capital

Tsogo Sun Hotels Limited
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13 July 2022

Dear Sirs

FAIRNESS OPINION IN RESPECT TO A RELATED PARTY TRANSACTION IN RELATION TO THE SEPARATION AND THE HOTEL SALE TRANSACTIONS

INTRODUCTION

Tsogo Sun Hotels Limited ("**TSH**" or the "**Company**") and its wholly owned subsidiaries, HPF Properties Proprietary Limited ("**HPF**") and Southern Sun Hotel Interests Proprietary Limited ("**SSHI**"), entered into a Hotel Sale Agreement with Tsogo Sun Gaming Limited ("**TSG**"), and its wholly owned subsidiaries, Listed Investments Proprietary Limited ("**Listed Investments**") and Tsogo Sun Casinos Proprietary Limited ("**TSC**") ("**TSG Subsidiaries**"), in terms of which, HPF will acquire the two hotel properties and business assets located thereon, currently trading as "Southern Sun Emnotweni" and "StayEasy Emnotweni" ("**Emnotweni Hotels**") in Mbombela, Mpumalanga province from Listed Investments and TSC for an aggregate purchase consideration of R141,599,000 (VAT exclusive) (the "**Hotel Sale Transaction**").

In addition, the Company and SSHI entered into the Separation Agreement with TSG and the TSG Subsidiaries, in terms of which the parties thereto agreed to the termination of the various Management Agreements and Licensing Agreements concluded between them in relation to the management by SSHI of fifteen hotels owned by TSG, subject to payment by such TSG Subsidiaries to SSHI of an aggregate termination fee of R398,802,000 (VAT exclusive) ("**Termination Fee**") ("**Separation Transaction**").

The Hotel Sale Transaction and the Separation Transaction are hereafter referred to as the "**Proposed Transactions**".

TSG is an associate of Hosken Consolidated Investments Limited ("**HCI**"), which in turn is a material shareholder of the Company and as such the Proposed Transactions are classified as related party transactions in terms of section 10.1 (a) and (b) of the Listings Requirements of the JSE ("**JSE Listings Requirements**").

In terms of section 10.4 (f) of the JSE Listings Requirements, each proposed transaction requires a fairness opinion ("**Fairness Opinion**") from an independent professional expert acceptable to the JSE ("**Independent Expert**"), confirming that the terms of the Proposed Transactions are fair as far as shareholders of TSH are concerned.

Merchantec Proprietary Limited ("**Merchantec Capital**") has been appointed by the board of TSH ("**TSH Board**") as the Independent Expert to independently determine whether, by using the information and assumptions available, the terms of Proposed Transactions are fair to TSH shareholders unrelated to the Transaction.

DEFINITION OF THE TERM "FAIR"

The assessment of fairness is primarily based on quantitative issues. A transaction will typically be considered fair to a company's shareholders if the benefits received by shareholders, as a result of a corporate action, are equal to or greater than the value ceded by a company.

For illustrative purposes, the Termination Fee of R398,802,000 received in connection with the Separation Transaction may be said to be fair if the Terminal Fee received is more than or equal to the fair value that can be attributed to Management Agreements or unfair if the Termination Fee received is less than the value attributed to Management Agreements.

The aggregate purchase consideration of R141,599,000 in connection with the Hotel Sale Transaction may be said to be fair if the purchase consideration paid is less than or equal to the fair value that can be attributed to the Emnotweni Hotels or unfair if the purchase consideration paid is more than the fair value attributed to the Emnotweni Hotels.

RESPONSIBILITY AND SCOPE

The responsibility of Merchantec Capital is to prepare a report in respect of the fairness of the Proposed Transactions and the report must at a minimum satisfy the requirements set out in schedule 5 of the JSE Listings Requirements.

Compliance with the JSE Listings Requirements is the responsibility of the directors of TSH. Our responsibility is to report on whether or not the terms and conditions of the Proposed Transactions, as they relate to the TSH shareholders not related to the Transaction, are fair.

FAIRNESS OPINION REQUIRED IN TERMS OF THE JSE LISTINGS REQUIREMENTS

In terms of paragraph 10.4 of the JSE Listings Requirements the TSH Board is required to obtain a fairness opinion, prepared in accordance with Schedule 5 of the JSE Listings Requirements, and include such fairness opinion in the circular to TSH shareholders.

INFORMATION AND SOURCES OF INFORMATION

In the course of our analysis, we relied upon financial and other information obtained from TSH, together with other information available in the public domain. Our conclusion is dependent on such information being accurate in all material respects. The information has, however, been tested for reasonableness to market related inputs at the date of the opinion.

The principle sources of information used in formulating our opinion regarding the transaction which are relevant to TSH shareholders:

- License and Management Agreements made and entered into by and between SSHI and Silverstar Casino Proprietary Limited ("**Silverstar Casino**");
- First and Second Addendums to the Management Agreement made and entered into by and between SSHI and Silverstar Casino;
- License and Management Agreements made and entered into by and between SSHI and Akani Egoli Proprietary Limited ("**Akani Egoli**");
- First and Second Addendum to the Management Agreement made and entered into by and between SSHI and Akani Egoli;
- License and Management Agreements made and entered into by and between SSHI and Gold Reef City Theme Park Proprietary Limited ("**Gold Reef City Theme Park**");
- First and Second Addendums to the Management Agreement made and entered into by and between SSHI and Gold Reef City Theme Park;
- License and Management Agreements made and entered into by and between SSHI and Akani Msunduzi Proprietary Limited ("**Akani Msunduzi**");

- Addendum to the Management Agreement made and entered into by and between SSHI and Akani Msunduzi;
- License and Management Agreements made and entered into by and between SSHI and Tsogo Sun Newcastle Proprietary Limited ("**Tsogo Sun Newcastle**");
- First, Second and Third Addendums to the Management Agreement made and entered into by and between SSHI and Tsogo Sun Newcastle;
- License and Management Agreements made and entered into by and between SSHI and Tsogo Sun Caledon Proprietary Limited ("**Tsogo Sun Caledon**");
- First and Second Addendums to the Management Agreement made and entered into by and between SSHI and Tsogo Sun Caledon;
- License and Management Agreements made and entered into by and between SSHI and Garden Route Casino Proprietary Limited ("**Garden Route Casino**");
- First and Second Addendums to the Management Agreement made and entered into by and between SSHI and Garden Route Casino;
- All license and Management Agreements made and entered into by and between SSHI and TSC;
- All Addendums to the Management Agreements made and entered into by and between SSHI and TSC;
- Norman Griffiths valuation of the Emnotweni Hotels as at 31 March 2022;
- forecast financial information in relation to the Management Agreements of the seventeen TSG hotels for the financial years ending 31 March 2023 to 31 March 2028;
- discussions with the directors and management of TSH on the rationale for the Transaction;
- the circular and notice sent to TSH shareholders for the general meeting to be held on 18 August 2022 (the "**Circular**"); and
- publicly available information relating to TSH and the industry information that we deemed to be relevant.

PROCEDURES PERFORMED

In arriving at our opinion, amongst other things, we have undertaken the following procedures in evaluating the fairness of the Separation Transaction:

- Reviewed terms and conditions set out in the Separation Agreement and the Circular;
- Considered the underlying rationale for the Proposed Transactions;
- Analysed and reviewed all relevant financial information as set out above;
- Reviewed and obtained an understanding from management as to the assumptions in the forecast financial information of the management and licensing agreements and assessed the achievability thereof by considering historic information as well as macro-economic and sector-specific data;
- Based on the above, we utilised an income approach (discounted cash flow) valuation methodology to value the cash flows that relates to the Management Agreements; The income approach indicates the fair value of the Management Agreement based on the value of the expected future cash flows generated under the current Management Agreements;
- For the discounted cash flow ("**DCF**") we valued the cash flows of the management and licensing agreements using a 5 and half-year forecast period. We assessed the margins, occupancy and growth assumptions in relation to the historical information and the industry and these were flexed as per the results below. We considered the forecast operating expenditure ("**OPEX**") and discounted the Free Cash Flows ("**FCF**") using a weighted average cost of capital ("**WACC**") as the discount rate to capture the Company's risks;
- Sensitivity analyses were performed considering key assumptions, key internal and external valuation drivers in arriving at a valuation range;

- Key internal valuation drivers to the DCF valuation include average room rates, occupancy rates and operating margins. A 1% increase in the average room rates across all years will result in a 1.70% increase in the value. A 1% decrease in the average room rates across all years will result in a 1.67% decrease in the value. A 1% increase in the occupancy rates across all years will result in a 0.27% increase in the value. A 1% decrease in the occupancy rates across all years will result in a 0.30% decrease in the value. Another key sensitivity for the DCF valuation is the discount rate where a 1% increase in the discount rate results in a 12.51% decrease in the value. A 1% decrease in the discount rate results in a 16.87% increase in the value.
- Key external valuation drivers for the DCF valuation include consumer confidence, disposable income and unemployment rates; lower unemployment rates will lead to an increase consumer confidence and disposable income; which will lead to increase in the value of Management Agreements. Higher unemployment rates will lead to lower consumer confidence and disposable income; which will lead to a decrease in the value of Management Agreements; and
- We considered the effect of Covid-19 on the valuation and given the nature of the business we were comfortable that we have used prudent occupancy rates and average room rates over the forecast period.

In arriving at our opinion, amongst other things, we have undertaken the following procedures in evaluating the fairness of the Hotel Sale Transaction:

- Reviewed and obtained an understanding from the Norman Griffiths Emnotweni Hotels Valuation Report as Fair Values of the Southern Sun Emnotweni and Stay Easy Emnotweni Hotels and assessed the reasonability of the assumptions used by considering historic information as well as macro-economic and sector-specific data;
- Critically assessed the assumptions used by the Norman Griffiths, especially in terms of the revenue and operating profits realised on properties, coupled with the discount and capitalisation rates used;
- Performed a sensitivity analysis relating to the significant assumptions used to evaluate the extent of the impact on the fair values; and
- Key internal valuation drivers to the fair value approach used to value the properties include the capitalisation rate, which is impacted by the location, property quality, star rating, long-term liability and interest rates. Other key internal valuation drivers include the discount rate and the deferred payment period.
- A 1% decrease in the capitalisation rate results in a 12.50% increase in the value of Emnotweni Hotels, while a 1% increase in the capitalisation rate results in a 10.00% decrease in the value of the Emnotweni Hotels. A 1% increase in the discount rate, results in a 0.88% decrease in the value of the Emnotweni Hotels, while a 1% decrease in the discount rate, results in a 0.90% increase in the value of the Emnotweni Hotels. A 6-month extension in the deferred payment period results in a 5.51% decrease in the value of the Emnotweni Hotels while shortening the deferred payment by 6-months results in a 5.83% increase in the value of the Emnotweni Hotels.

VALUATION RESULTS

In undertaking the valuation exercise of Separation Transaction above, we determined a valuation range of the Termination Fee of between R377,622,186.75 and R436,083,103.32, with a midpoint of R404,680,039.78.

In undertaking the valuation exercise of Hotel Sale Transaction above, we determined a valuation range of the Emnotweni Hotels of between R134,161,372.18 and R149,945,063.03, with a midpoint of R141,614,781.75.

ASSUMPTIONS

Our opinion is based on the following key assumptions:

- Current economic, regulatory and market conditions will not change materially;
- TSH is not involved in any other material legal proceedings other than what has been disclosed in the integrated annual report;
- There are no known undisclosed contingencies that could have a material effect on the value of management and licensing agreements or the Emnotweni Hotels;
- That the Proposed Transactions will have the legal, accounting and taxation consequences as described in discussions with, and materials furnished to us by the representatives and advisors of TSH; and
- Relied on the assumptions in the information available made by TSH's representatives during the course of forming this opinion.

LIMITING CONDITIONS

This report and opinion are provided to the board of directors of TSH in connection with and for the purposes of the Proposed Transactions. The opinion does not purport to cater for each individual shareholder's perspective, but rather that of the general body of TSH's shareholders. Should any shareholder be in doubt as to what action to take, he or she should consult an independent advisor.

We have relied upon and assumed the accuracy of the information used by us in deriving our opinion. While our work has involved an analysis of, *inter alia,* the historical financial information, financial forecasts and other information provided to us, our engagement does not constitute, nor does it include, an audit conducted in accordance with International Standards on Auditing, this information has, however, been tested for reasonableness.

Where relevant, forward-looking information on Management Agreements of the various TSG hotels relates to future events and is based on assumptions that may or may not remain valid for the whole of the forecast period. Consequently, such information cannot be relied upon to the same extent as that derived from audited financial statements for completed accounting periods. We accordingly express no opinion as to how closely actual results will correspond to those forecasted.

We have also assumed that the Proposed Transactions will have the legal, accounting and taxation consequences described in discussions with, and materials furnished to us by representatives of TSH and we express no opinion on such consequences. We have assumed that all agreements that have been entered into in regard to the Proposed Transactions will be legally enforceable.

None of the statements above invalidate the work done as per this opinion and the conclusion of the fairness opinions below.

INDEPENDENCE

In terms of Schedule 5.1(a) and 5.1(b) of the JSE Listings Requirements, we confirm that we have no material direct or indirect interest in the shares of TSH, TSG or the Proposed Transactions, nor do we have any relationship with any party involved in the Proposed Transactions.

Furthermore, we confirm that our professional fees are not contingent upon the success of the Proposed Transactions.

OPINION

Merchantec Capital has considered the terms and conditions of the Separation Transaction and, based upon and subject to the conditions set out herein, is of the opinion that the terms and conditions of the Separation Transaction are fair to TSH shareholders as the Consideration Received for the termination of the various management and licensing agreements being R398,802,000, is within our fair valuation range of between R377,622,186.75 and R436,083,103.32.

Merchantec Capital has considered the terms and conditions of the Hotel Sale Transaction and, based upon and subject to the conditions set out herein, is of the opinion that the terms and conditions of the Hotel Sale Transaction are fair to TSH shareholders as the Consideration Paid for the Emnotweni Hotels being R141,599,000, is within our fair valuation range of between R134,161,372.18 and R149,945,063.03.

Subsequent developments may affect this opinion, which we are under no obligation to update, revise or re-affirm.

CONSENT

We consent to the inclusion of this letter and reference to our opinion in the Circular to be issued to shareholders of TSH in the form and context in which it appears and in any required regulatory announcement or documentation.

Yours faithfully

Marcel Goncalves CA(SA)
Director

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