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Group Introduction

RHL International is one of the pioneering professional valuation and real estate consultants in Asia. Established since 1972, our group offers high quality professional services on Corporate Valuation & Advisory and Real Estate Solution & Surveying Practice. As an active participant in exchanging ideas and experience with regulators, government institutions and corporations, our group maintains vigilant to the dynamic changes in the market. Leveraging our extensive track record, technical resources and market intelligence, we are dedicated to provide tailored services to meet with the unique needs of our clients.

Editor's Message

Welcome to the Asset Valuation Bulletin issued by RHL Appraisal Limited. In this knowledge-based economy, a successful corporate management and investor need to be versatile to capture business opportunities, whilst understanding in accounting and finance is imperative to deal with the dynamic market. In response we launch this bulletin with the aim to share with you a wide range of useful knowledge and information, including but not limited to insight on current rules, and regulations, technical knowledge, market news and practical experience relating to asset valuation. We hope this bulletin could become one of your preferred knowledge update platforms.

Topics

- Understanding Preferred Shares (Part III)
- China's Overseas Mergers and Acquisitions Surge in 2016



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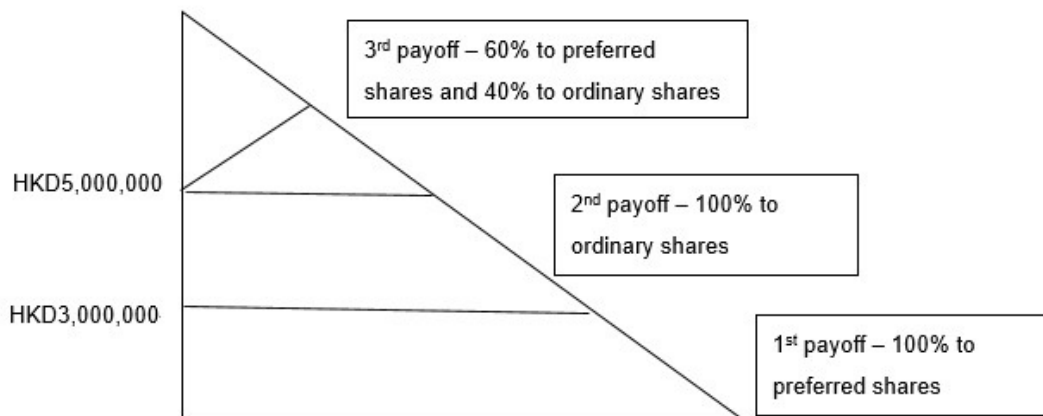
Understanding Preferred Shares (Part III)

In the previous bulletin, we had briefly described the types and terms of preferred shares. Following on, we shall now look into the valuation issues in related to preferred shares.

Valuation methodology of preferred shares

In order to evaluate the value of preferred shares, several key inputs need to be taken into consideration first, including the subscription price, liquidation preference, terms of early redemption and terms of conversion into ordinary shares. Given these information valuation models can be applied to determine its value.

One of the primary method is by equity allocation using Black-Scholes model, which requires an understanding on capital structure of the underlying company. If the company issued ordinary and preferred shares, and equity-like instruments such as options, warrants at the same time, holders of preferred shares received liquidation proceed prior to holders of ordinary shares. The preferred share and all other instruments in the capital structure can be modelled as call options on the residual value of the company (i.e. the value after debts) that provides holders the right to claim on the residual value of the company at a predetermined exercise price. For example, company A issued par amount of HKD 3,000,000 participating preferred shares and par amount of HKD 2,000,000 ordinary shares, the diagram for liquidation preference is as below:



In this case, if the equity value is not greater than HKD 3,000,000 at the liquidation, all of the liquidation proceeds will be assigned to holder of preferred share. When the equity value is between HKD 3,000,000 and HKD 5,000,000, once the portion of proceed of HKD 3,000,000 is assigned to holder of preferred share, the remaining proceed is assigned to holder of ordinary share. If the equity value is greater than HKD 5,000,000, the total amount of equity value is proportionally allocated to holders of ordinary and preference shares.

Another valuation model is lattice tree model. When using the lattice tree (binomial or trinomial model), one of the main focus is to evaluate the components of the preferred shares. Because of the possible debt nature of the preferred share in repaying the preferred shares, part of the preferred shares could be valued as the liability component, which can be evaluated by the discounted cash flow method. Decision rule of early redemption and conversion into ordinary shares can be taken into account in the lattice model and that is the reason that the lattice model can be used. The shortfall is that when lattice model is used, the maturity/expiry date of the shares is needed to be put in the model. In this case, assumptions of maturity date, depending on the assumed holding period made by the issuer or investor, is needed to be taken into consideration.

In summary, the preferred shares can be valued by using option pricing models. Given the terms of the preferred share (terms can be quantified including liquidation preference, dividend schedule, redemption feature, etc.), the value of the preferred share can be evaluated by equity allocation in conjunction with Black-Scholes model or binomial model.

China's Overseas Mergers and Acquisitions Surge in 2016

According to the regular press conference of the Ministry of Commerce on 15 December 2016, the Chinese investors made non-financial direct investment overseas in 7,500 enterprises of 164 countries and regions with amount of approximately USD161.7 billion, up 55.3% year on year. The previous statistics shows that the non-financial overseas direct investment hit a new record of USD134.22 billion during the first nine months of 2016, more than that of the whole of last year USD121.42 billion.

Overseas mergers and acquisitions (M&A) is the efficient and effective way for the Chinese investors to establish brand name, access the latest technology and expand sales channels in recent years when China's economic was restructuring. The developed countries in North America and Europe with leading technology, platform, brand name and mature consumer groups is the first choice for Chinese investors. The Brexit in 2016 caused the British pound to depreciate and attracted Chinese enterprises' investments in the property sector. Recently, the slowdown in China's economic growth and the depreciation of Renminbi has triggered Chinese investors' outbound deals.

In the past, most of the overseas M&A were paid in cash by the Chinese investors. As RMB against the USD depreciated and the Chinese Government started to tighten controls amid capital outflow, it is expected that the overseas M&A by Chinese investments will be settled by different ways such as issuance of convertible bonds and preference shares through its related parties, stock-for-stock or issuance of new shares.

Although the Chinese Government tried to tighten control on enterprise looking to invest abroad in an effort to slow surging outflow, the continued deprecation in RMB and Chinese Government's encouragement to develop "One Belt, One Road" project will boost Chinese investors' overseas M&A.

This year, RHL has cooperated with overseas professional parties to provide professional valuation service for our clients on their business acquisitions in the USA and the UK.

About Us

Professional Team

Our team comprises of professionals who have finance and/or real estate related academic background and internationally recognized qualifications, such as CPA, FRM, registered professional surveyors, and with diverse experience and up-to-date knowledge of the current market environment. We committed to provide our clients with high standard services.

The Group is committed to provide high standard of professional services in compliance with international standard and Government Statutory requirements.

Corporate Advisor

Our experience in operating businesses in the mainland China and cooperating with overseas parties has become our competitive advantage in offering comprehensive client solution to overseas as well as mainland clients. We cover real estate as well as other industries such as natural resources, green energy and finance area.

- Industry Market Research & Analysis
- Project Feasibility Study and Advisory
- Financial Analysis
- Investment Advisory
- Due Diligence
- Valuation (including Real Estate, Business Valuation, Plant & Machinery)
- Portfolio, Asset and Facilities Management
- Corporate Valuation Advisory
- Real Estate Solutions and Surveying Practice



Asset Valuation

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