



SORTINO
M&A GROUP

J.M. Smucker's Acquisition of Hostess Brands for \$5.6bn

CONSUMER & RETAIL

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TABLE OF CONTENTS

Deal Introduction	1
Acquirer Overview	4
Target Overview	8
Valuation Analysis	11
Deal Analysis	15
Glossary	20



Deal Introduction

DETAILS ABOUT THE DEAL

On September 11, 2023, The J.M. Smucker Company (Smucker) announced a landmark \$5.6 billion acquisition of Hostess Brands, Inc. (Hostess) through a strategic cash and stock transaction. The agreement of the deal specifies J.M. Smucker to acquire all outstanding shares of the target Hostess.

Operating within distinct yet complementary segments of the consumer-packaged goods (CPG) industry, J.M. Smucker and Hostess cater to diverse consumer needs. Smucker, known for its established portfolio of jams, jellies, peanut butter, coffee, and pet food, focuses on delivering core pantry staples and functional everyday options. In contrast, Hostess specialises in iconic sweet treats like Twinkies and Ding Dongs.

The acquisition cost reflects an approximate 54% premium over the closing share value of \$22.18 on August 24, 2023, which was the final day of trading before reports emerged suggesting a possible deal.

It is anticipated that the cash segment of the deal will be financed using a mix of available cash reserves, a term loan from a bank, and the issuance of long-term bonds to the public.

This pivotal move, financially advised by Morgan Stanley and legally advised by Lewis & Bockius LLP for Hostess, significantly bolsters Smucker's portfolio with iconic brand names like Twinkies and Ding Dongs.



DETAILS ABOUT THE DEAL (CONTINUED)

On the other hand, RBC Capital Markets LLC is acting as the principal financial advisor to J.M. Smucker, with additional financial advisory services being provided by Bank of America Securities. Legal counsel for the transaction is being offered to Smucker by Wachtell, Lipton, Rosen & Katz.

This complementary expansion not only strengthens Smucker's position in the CPG industry but also broadens its reach to a new loyal customer base. The combined entity boasts a much more diversified product range and a wider distribution network, fuelling anticipated growth in both revenue and profit.

REASONS FOR M&A

The Smucker-Hostess acquisition is expected to create significant cost and revenue synergies. Cost synergies are expected to be achieved through the consolidation of JM Smucker's expertise in increasing project shelf stability, which is a crucial factor in the food industry.

This opens doors for this deal to streamline operations, reduce wastage, and thereby lower costs. Revenue synergies could arise from cross-promotion opportunities between Smucker's staples and Hostess's sweet treats. This approach is anticipated to exploit the complementary nature of the product lines, driving increased sales through targeted marketing initiatives and expanded product offerings.

The strategic alignment between the two brands aims to capture a larger share of consumer spending by offering a diversified range of high-quality products that cater to varying consumer preferences.



REASONS FOR M&A (CONTINUED)

The strategic acquisition of Hostess marks a deliberate move towards the diversification of business operations, a crucial step for companies seeking to solidify their market presence and enhance resilience against economic fluctuations.

By integrating Hostess's renowned offering of sweet snacks with JM Smucker's broad spectrum of staple food products, the combined entity is also strategically positioning itself to tap into new consumer segments and preferences. This diversification demonstrates the foresight of both companies, recognising that a broader product range can mitigate risks associated with market volatility and ever-changing consumer taste shifts. Moreover, this acquisition is set to significantly boost the market power of the newly formed conglomerate. This increased market power enhances the company's ability to negotiate with suppliers and retailers and positions it as a formidable competitor capable of shaping market trends and consumer preferences.

Hostess Brands was acquired at a valuation that reflected a 54% premium over its last closing share price before rumours of the deal arose, indicating an attractive purchase price for Smucker.

This premium may be justified by Hostess's strong brand recognition and the expected growth trajectory post-acquisition. The acquisition aims to blend Smucker's robust supply chain and Hostess's unique brand equity to build a powerhouse in the consumer-packaged goods sector. This will help both companies drive long-term shareholder value and create a more resilient business model in the face of the dynamic market conditions in the consumer and retail industry.



Acquirer Overview



J.M. Smucker Company, founded in 1897, is an American consumer packaged goods firm with a rich history deeply rooted in the food industry.

Headquartered in Ohio and employing over 5800 people, J.M Smucker has been led by CEO Mark Smucker since August 2022.

KEY FINANCIALS

MARKET CAP: \$13.86 BILLION

EPS: 2.59, BEAT ANALYST
PREDICTIONS BY 4.81%

REVENUE: \$8.5 BILLION

NET PROFIT MARGIN: 10.05%

EBIT \$142.8 MILLION

DEBT TO EQUITY RATIO: 1.10

EBITDA \$573.8 MILLION

LEVERAGE RATIO: 2.24

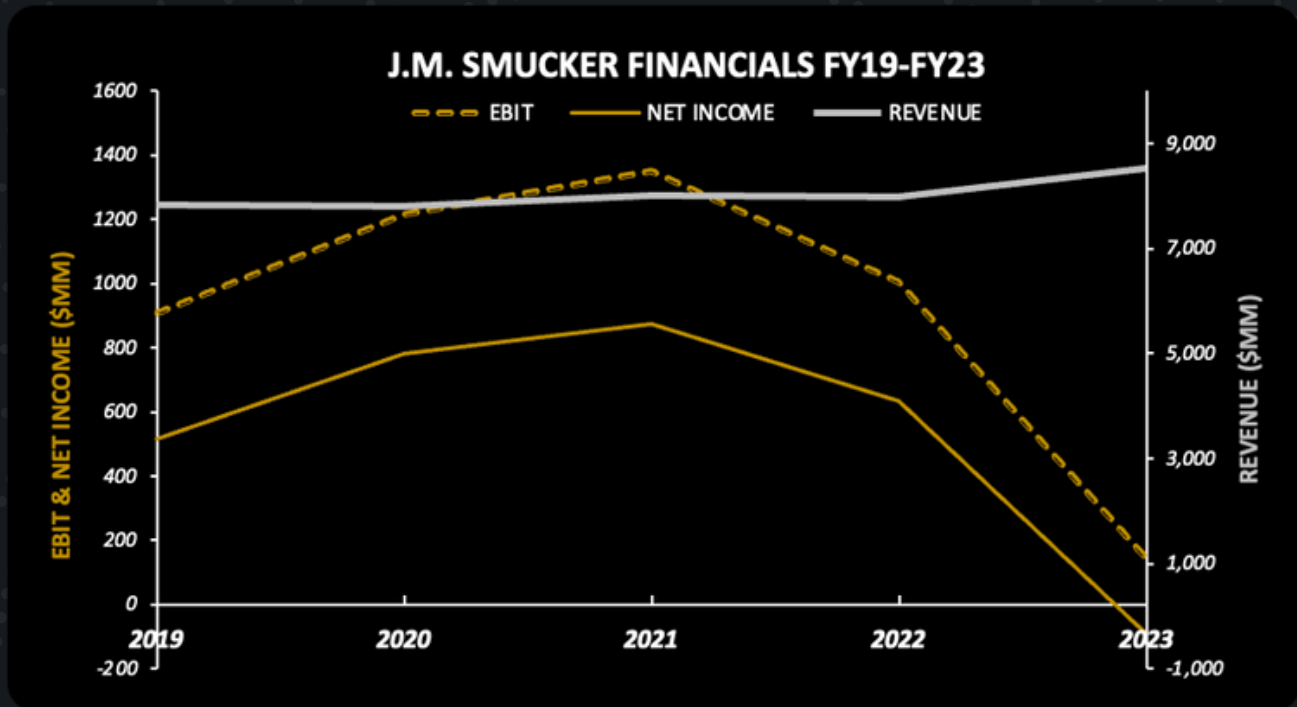
NET INCOME: -\$13.7 MILLION
(23Q1 loss of -\$600m, driven
by divestiture of pet food
brands)

LIQUIDITY RATIO: 3.20

PE RATIO: 13.25



KEY FINANCIALS (CONTINUED)



In October 2023, J.M Smucker issued bonds with 20- and 30-year tenors, in the amount of USD 750m and USD 1000m respectively, presumably to support the funding of the \$5.6b acquisition of Hostess brands.

In this year prior to the announcement, J.M Smucker's share price peaked at \$162.3 per share in December 2022 and reached lows of \$108 post acquisition announcement. After the announcement in September, share prices fell by 700bps. A month after announcement, shares had fallen by 25%. J.P Morgan analysts have said they feel J.M. Smucker have overpaid for Hostess Brands, with the acquirer paying a 21.8% premium for the TWNK shares. Today SJM is trading at \$130.84 following strong 23Q4 earnings.



BUSINESS MODEL

With total revenue of \$7.6 billion in FY2022, J.M. Smucker Company operates across multiple primary business segments catering to diverse consumer preferences.

- **Coffee:** J.M. Smucker is renowned for its iconic coffee brands, including Folgers, Dunkin' Donuts, and Café Bustelo.
- **Consumer Foods:** J.M. Smucker's consumer foods segment encompasses a wide array of household favourites, including Jif peanut butter, Smucker's jams and jellies, Pillsbury baking products, and more, catering to the diverse culinary needs of consumers.

Leveraging its reputation for quality and innovation, J.M. Smucker continues to expand its market share and drive growth through strategic acquisitions and brand management.

The company's acquisition strategy focuses on acquiring well-established brands with strong market positions, complementing its existing portfolio. Successful past acquisitions such as Folgers prove J.M. Smucker's track record with growing household brands. However, in early 2023, J.M. Smucker completed the divestiture of several large Pet Food brands to Post Holdings, with a total transaction value of \$1.2 billion.



ESG PRACTICES

The company has an established ESG framework that includes commitments to sustainability, responsible sourcing, and reducing its environmental impact. The company's sustainable sourcing efforts include investing in programs that promote sustainable farming practices and working with suppliers to ensure responsible sourcing of ingredients

Positioned for continued success, J.M. Smucker Company aims to drive growth through product innovation, strategic partnerships, and expansion into emerging markets, ensuring its place as a leader in the ever-evolving consumer packaged goods industry.

J.M. Smucker has made notable progress in reducing its greenhouse gas emissions, achieving a 93% reduction in GHG emissions, surpassing its Scope 1 and 2 greenhouse gas emissions goals.



Target Overview



Hostess Brands is a leading sweet snacks company based in the United States. The company was formed in 2013 and has since grown to become a significant player in the North American market.

Hostess Brands is known for making, marketing, and distributing a variety of popular treats, employing approximately 3,000 people.

The stock price has increased by +16.47% in the last 52 weeks, following a positive linear trend driven by strong and consistent brand performance. The beta is 0.53, so Hostess Brands's price volatility has been lower than the market average.

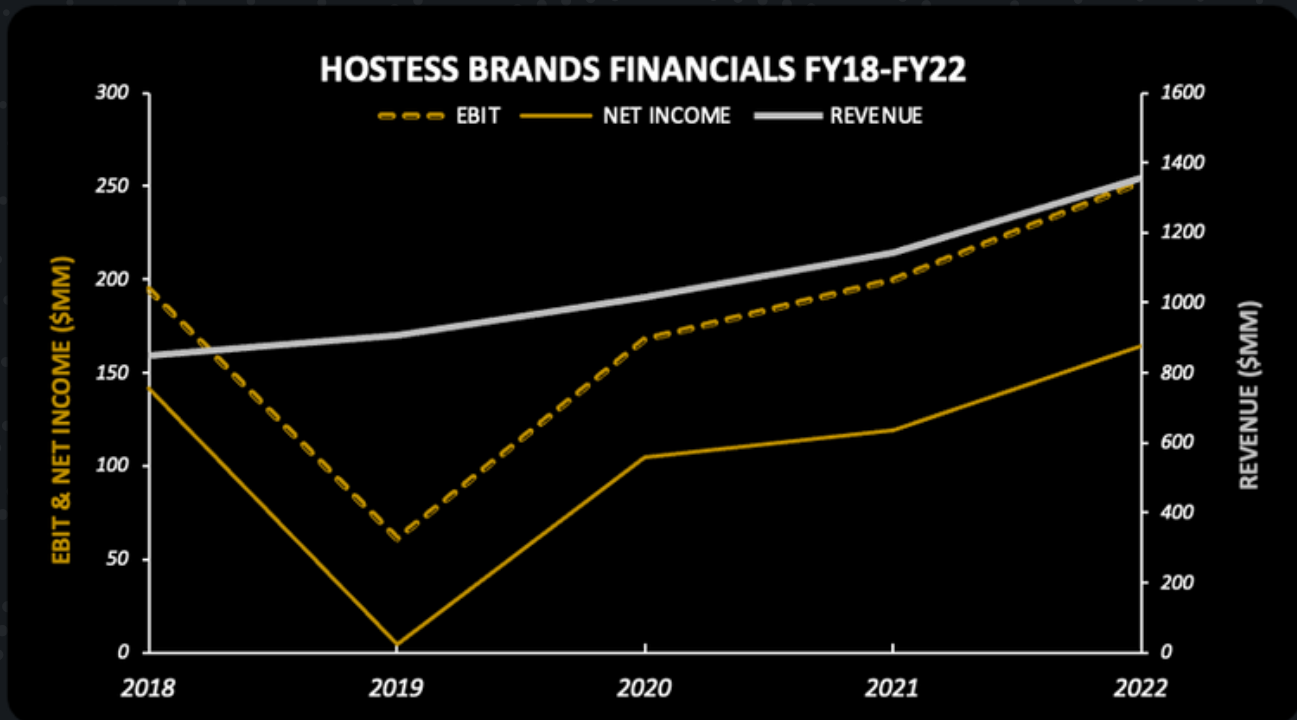
KEY FINANCIALS

MARKET CAP (when traded):
\$4.42 BILLION
REVENUE \$1.39 BILLION
EBIT \$215.9 MILLION
EBITDA \$287 MILLION
NET INCOME:\$126.48 MILLION

EPS: N/A
NET PROFIT MARGIN: 34.3%
DEBT TO EQUITY RATIO: 0.53
LEVERAGE RATIO: N/A
LIQUIDITY RATIO: N/A
PE RATIO: 35.81



KEY FINANCIALS (CONTINUED)



BUSINESS MODEL

Hostess Brands operates primarily in two segments of the consumer industry, generating over \$1.3 billion:

- Sweet baked goods: This segment includes a range of sweet baked goods sold under Hostess brands; this includes products ranging from donuts to breads and buns. Some of the most popular products in this segment include Donettes, Twinkies, CupCakes, Ding Dongs, and Zingers.
- Voortman Cookies and Wafers: Acquired in 2020, Voortman Cookies Limited has added a variety of cookies and wafers to the Hostess Brands portfolio.



BUSINESS MODEL (CONTINUED)

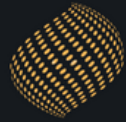
Hostess Brands introduced festive takes on its customer-favourite brands, including Hostess Holiday CupCakes, Hostess Mint Chocolate Flavored Twinkies, and Hostess Hot Cocoa & Marshmallow Flavoured Donettes to drive revenues in seasonal periods.

Like the example above, the company's innovation strategy plays a crucial role in driving revenue. For example, new product introductions like Hostess Kazbars and chocolate Baby Bundts are part of the company's efforts to maintain its position as a top innovator in the sweet baked foods category.

ESG PRACTICES

Hostess Brands engages in ESG initiatives to ensure sustainable growth:

- **Water, Energy, and Packaging Lifecycle Management:** Hostess Brands has committed to conserving water, reducing energy use, and managing its packaging lifecycle more sustainably. The company has achieved a 25% reduction in water usage, a 14% decrease in energy use, and a 19% reduction in greenhouse gas emissions over the past two years.
- **Sustainability-First Bakery:** In February 2022, Hostess Brands began converting an idled factory in Arkadelphia, Arkansas, into a major sustainable facility. This initiative is part of the company's broader effort to incorporate sustainability best practices across its bakery network.



Valuation Analysis

COMPARABLES ANALYSIS

Hostess Brands Trading Comparables Valuation				
	EV/Revenues	EV/EBIT	EV/EBITDA	P/E
High	4.67x	26.42x	24.08x	35.70x
Low	1.20x	11.50x	11.10x	14.20x
Median	2.07x	21.16x	17.13x	26.18x
Average	2.66x	20.32x	16.68x	25.85x
Implied Enterprise Value	2,811.49	4,661.08	4,802.64	4,298.63
Net Debt	863.64	863.64	863.64	863.64
Implied Equity Value	1,947.85	3,797.44	3,939.00	3,434.99
Implied Share Price	14.65	28.57	29.63	25.84

J.M. Smucker CCA Model

In millions, except per share data

	EV/Revenues	EV/EBIT	EV/EBITDA	P/E
Nestle	3.18x	19.75x	15.97x	27.34x
Kraft Heinz	2.37x	11.91x	11.50x	15.32x
General Mills	2.41x	16.22x	12.26x	15.70x
McCormick & Company	3.40x	26.42x	18.90x	27.40x

J.M. Smucker Trading Comparables

	EV/Revenues	EV/EBIT	EV/EBITDA	P/E
High	3.40	26.42	18.90	27.40
Low	2.37x	11.91x	11.50x	15.32x
Median	2.80x	17.99x	14.12x	21.52x
Average	2.84x	18.58x	14.66x	21.44x
Implied Enterprise Value	22,356.93	18,413.04	20,931.13	N/A
Net Debt	3,889.40	3,889.40	3,889.40	N/A
Implied Equity Value	18,467.53	14,523.64	17,041.73	N/A
Implied Share Price	173.99	136.83	160.56	N/A

Hostess Brands Transaction Comparables Valuation

Last Twelve Months (LTM)

Year 1 Forecast - Calendar Year

	EV/Revenues	EV/EBITDA	EV/EBIT	EV/Revenues	EV/EBITDA	EV/EBIT
High	3.60	24.31	47.70	2.96	19.54	28.73
Low	1.28	16.73	20.89	1.19	18.87	21.42
Average	2.62	20.52	34.86	2.08	19.20	25.08
Median	2.99	20.52	36.00	2.08	19.20	25.08
Implied Enterprise Value	4,252.99	5,952.13	7,991.25	3,085.73	5,835.76	5,837.67
Net Debt	863.64	863.64	863.64	863.64	863.64	863.64
Implied Equity Value	3,389.35	5,088.49	7,127.61	2,222.09	4,972.12	4,974.03
Implied Share Price	25.50	38.28	53.62	16.72	37.40	37.42
Implied Premium % (no discount)	15%	73%	142%	-25%	69%	69%

Please click on the table to access the full model



JM SMUCKER DISCOUNTED CASH FLOW MODEL

Valuation						
Exit EV/EBITDA Multiple	8.56x					
WACC	5.20%					
Mid-Year Convention	No					
Discount Year		1.00	2.00	3.00	4.00	5.00
Terminal Value						6.00
Present Value Unlevered Free Cash Flow		746	840	823	801	779
Present Value Terminal Value						11,545
Enterprise Value	16,291					
Net Debt	3,889					
Equity Value	12,402					
Diluted Shares Outstanding	106					
Implied Share Price	\$116.84					

Valuation is calculated using a Weighted Average Cost of Capital (WACC) of 5.20%, which informs the Enterprise Value of \$16,291 million, Net Debt of \$3,889 million, Equity Value of \$12,402 million, and an Implied Share Price of \$116.84.

		Exit EV/EBITDA Multiple						
		7.06x	7.56x	8.06x	8.56x	9.06x	9.56x	10.06x
WACC	3.70%	\$108.15	\$115.08	\$122.00	\$128.93	\$135.85	\$142.78	\$149.70
	4.20%	\$104.58	\$111.31	\$118.04	\$124.77	\$131.49	\$138.22	\$144.95
	4.70%	\$101.12	\$107.66	\$114.20	\$120.74	\$127.27	\$133.81	\$140.35
	5.20%	\$97.77	\$104.13	\$110.48	\$116.83	\$123.19	\$129.54	\$135.89
	5.70%	\$94.53	\$100.70	\$106.88	\$113.05	\$119.23	\$125.40	\$131.58
	6.20%	\$91.38	\$97.38	\$103.38	\$109.39	\$115.39	\$121.39	\$127.39
	6.70%	\$88.33	\$94.16	\$100.00	\$105.84	\$111.67	\$117.51	\$123.34

[Please click on the table to access the full model](#)



HOSTESS BRANDS DISCOUNTED CASH FLOW MODEL

Valuation					
Exit EV/EBITDA Multiple	16.02x				
WACC	6.60%				
Mid-Year Convention	Yes				
Discount Year		1.0	2.0	3.0	4.0
Terminal Value					5,593
Present Value Unlevered Free Cash Flow		137	138	136	134
Present Value Terminal Value					4,064
Enterprise Value	4,741				
Net Debt	864				
Equity Value	3,877				
Diluted Shares Outstanding	133				
Implied Share Price	29.17				

Valuation is calculated using a Weighted Average Cost of Capital (WACC) of 6.60%, which informs the Enterprise Value of \$4,741 million, Net Debt of \$864 million, Equity Value of \$3,877 million, and an Implied Share Price of \$29.17.

		Exit EV/EBITDA Multiple						
		14.52x	15.02x	15.52x	16.02x	16.52x	17.02x	17.52x
WACC	5.10%	\$28.56	\$29.58	\$30.60	\$31.63	\$32.65	\$33.68	\$34.70
	5.60%	\$27.78	\$28.78	\$29.78	\$30.78	\$31.78	\$32.78	\$33.78
	6.10%	\$27.03	\$28.01	\$28.98	\$29.96	\$30.94	\$31.91	\$32.89
	6.60%	\$26.30	\$27.25	\$28.21	\$29.16	\$30.12	\$31.07	\$32.02
	7.10%	\$25.59	\$26.52	\$27.45	\$28.39	\$29.32	\$30.25	\$31.18
	7.60%	\$24.90	\$25.81	\$26.72	\$27.63	\$28.54	\$29.45	\$30.36
	8.10%	\$24.22	\$25.11	\$26.00	\$26.89	\$27.78	\$28.67	\$29.56

[Please click on the table to access the full model](#)



MERGER MODEL & SYNERGIES DCF

Target WACC		6.60%				
£'s	2023F	2024F	2025F	2026F	2027F	
Gain in Operating Income from Cost Reduction	-	50	100	100	100	
Total Gain in Operating Income	-	50	100	100	100	
Tax Rate	21%	21%	21%	21%	21%	
Provisions for Income Taxes	-	11	21	21	21	
After-tax Gain in Operating Income	-	40	79	79	79	
FCF	-	40	79	79	79	
Terminal Growth Rate					2%	
Terminal Value					1,753	
Discount Year	1	2	3	4	5	
PV(FCF)	-	35	65	61	57	
Sum of PV(FCF)	219					
PV (Terminal Value)	1,753					
Total PV of Synergies	1,971					
Diluted Shares Outstanding	133					
Value of Synergies per Share of Hostess	14.83					
Hostess Share Price Pre-Merger Announcement	\$22.18					
Implied Share Price (with synergies)	\$37.01					
Accretion / Dilution Analysis						
<i>EPS Accounting:</i>		FY 2023	FY 2024	FY 2025		
		11/09/2023	11/09/2024	11/09/2025		
<u>Acquirer</u>						
Net income		188.55	700.08	757.87		
EPS		1.8	6.6	7.1		
Diluted shares outstanding (weighted avg.)		106.14	106.14	106.14		
<u>Target</u>						
Net income		150.60	148.12	156.89		
EPS		1.1	1.1	1.2		
Diluted shares outstanding (weighted avg.)		132.93	132.93	132.93		
<u>Transaction related expenses/income⁽¹⁾</u>						
Less: Interest expense from new deal debt		(247.6)	(247.6)	(247.6)		
Less: Interest income on cash forgone		0	0	0		
Plus: Synergies		18.4	68.4	100		
Less: Incremental D&A expense		(125.2)	(125.2)	(125.2)		
Less: Financing fee amortization		(2.2)	(2.2)	(2.2)		
Taxes (assumed at acquirer's rate)		89.2	89.2	89.2		
Total after tax transaction related income/ (expenses)		(267.5)	(217.5)	(185.8)		
Pro Forma		71.69	630.73	728.94		
Pro Forma Shares Outstanding		117.8	117.8	117.8		
Pro forma		0.61	5.36	6.19		
Acquirer standalone EPS		1.78	6.60	7.14		
Accretion / Dilution per share		(1.17)	(1.24)	(0.95)		
Accretion / Dilution %		-65.7%	-18.8%	-13.3%		
Additional pretax synergies required to breakeven		183.38	194.80	149.36		
Pro Forma Market Equity	15,522.89					
Pro Forma Shares Outstanding	117.78					
Pro Forma Share Price	131.80					



Deal Analysis

STRENGTHS

ENHANCING MARKET PRESENCE & EXPANDING PRODUCT PORTFOLIO

- Hostess Brands' strong position in the sweet baked goods category, which is one of the largest and fastest-growing in the industry, complements J.M. Smucker's existing portfolio, and adds iconic sweet brands Hostess Donettes, Twinkies, CupCakes, DingDongs to J.M Smucker.
- Helps diversify J.M Smucker's portfolio of brands into 'sweet snacks', working alongside their 'healthy snack' range. This follows with data that suggests Americans are snacking more frequently.
- Projections estimate Hostess Brands would present approximately 20% of Smucker's overall revenue and provide another growth vehicle beyond Uncrustables in its US business. As for growth, Hostess adds \$1.5 billion in annual revenue with mid-single-digit growth

DISTRIBUTION CHANNEL SYNERGY

- Hostess Brands brings an expanded distribution model, including strength in the convenience store channel, which can be leveraged by J.M. Smucker to improve its distribution and reach.
- Hostess will now get access to J.M. Smucker's "very strong" presence in grocery retailers. J.M. Smucker said the company will "continue to expand this presence and partnerships", hinting at increasing their shelf presence in supermarkets.



Deal Analysis

WEAKNESSES

COST

- General consensus is that J.M. Smucker have overpaid, with the acquirer paying a 21.8% premium for the TWNK shares. JPMorgan analyst Ken Goldman wrote, "All in, we can't say we love this transaction from Smucker's perspective. We are very surprised that SJM (or anyone) is paying this amount."
- Markets seemed to agree with this statement, with SJM shares falling 25% a month after the announcement of the deal, indicating investor concerns over the purchase price and future growth outlook.
- The deal will add considerable debt to Smucker's balance sheet, although 12% of the deal is in stock. J.M. Smucker are assuming \$900 million in net debt from Hostess, in addition to financing 88% of the remaining \$4.7 billion in equity. As of July 2023, Smucker had \$4.32 billion in debt, so this deal will essentially double its leverage. Annualised, more than doubling its debt increases its annual interest payments to more than a quarter of a billion dollars, which becomes incredibly risky especially when refinancing.

PRODUCT OVERLAP & CONSUMER PREFERENCES

- There may be concerns about product overlap and how to effectively manage and market the combined product portfolio, especially given the differences in how products like Uncrustables and Twinkies are produced, delivered, and merchandised
- As consumer preferences shift towards healthier options, there may be challenges in aligning Hostess Brands' sweet snack offerings with these trends.



Deal Analysis

OPPORTUNITIES

- **Expansion of Product Portfolio and Market Presence:** The acquisition includes iconic Hostess sweet baked snacks brands such as Twinkies®, CupCakes, and DingDongs, along with the Voortman cookie brand. This significantly enhances Smucker's presence in the sweet baked goods category, which is one of the largest and fastest-growing in the industry. The combined capabilities of both businesses offer a tremendous opportunity to capitalize on consumers' increasing reliance on snacking, fitting lifestyle needs and convenience choices.
- **Enhanced Distribution and Manufacturing Capabilities:** Hostess brings an expanded distribution model, including strength in the convenience store channel, a robust innovation engine, and extensive manufacturing capabilities. This is complemented by Smucker's strong retailer relationships in grocery and mass channels, along with advanced commercial organization, marketing, and productivity approaches. The synergy between the two businesses creates a compelling platform for sustainable growth.
- **Market Expansion:** The deal positions Smucker strongly in the attractive segment of sweet baked goods, with popular brands that have a loyal consumer base. This strategic expansion can help Smucker tap into new consumer segments and geographies, leveraging Hostess Brands' established market presence.



Deal Analysis

THREATS

- **High Acquisition Cost and Debt Load:** The deal, valued at \$5.6 billion including debt, has been seen as expensive by investors and analysts. The transaction is expected to be funded through cash on hand, bank term loans, and long-term public bonds, with pro forma total net debt estimated at the closing date to be approximately \$8.6 billion. This high level of debt could impose financial constraints on Smucker, affecting its flexibility for future investments or acquisitions.
- **Integration Challenges:** Merging two companies always comes with the risk of integration challenges, including the harmonization of corporate cultures, systems, and processes. Smucker will need to effectively integrate Hostess Brands' 3,000 employees and its manufacturing and distribution facilities into its operations without disrupting the ongoing business activities. Failure to do so could lead to inefficiencies and a potential loss of value from the acquisition.



Conclusion

The acquisition of Hostess Brands by The J.M. Smucker Company, a landmark \$5.6 billion deal, combines two companies with complementary segments in the consumer-packaged goods industry. Smucker, known for pantry staples and everyday options, and Hostess, famous for sweet treats like Twinkies, aim to create significant cost and revenue synergies. The deal was financed through cash, bank term loans, and long-term bonds. It is expected to diversify Smucker's product range, expand its distribution network, and enhance its market power. However, concerns include the high acquisition cost and potential integration challenges. Smucker's strategic move towards diversification seeks to solidify its market presence and adapt to changing consumer preferences within the industry, despite the risks associated with increased debt and cultural integration. It will be interesting to observe how the two companies tackle the challenges presented by this deal and work towards unlocking the full synergistic potential of being a combined entity.



GLOSSARY

Balance Sheet: Balance sheet shows the assets, liabilities and equity of a company at a specific point of time. It is an important financial statement to understand company's resources as well as sources of funds.

Equity: Equity refers to the ownership portion in firm's capital structure, which includes the share capital (stocks) a company issues as well as the retained earnings.


Goodwill: Premium paid for the intangible resources of a business, such as customer lists or patents.


Leverage: Indebtedness of a firm, which increases as companies issue more debt to fund their investment projects.

Synergies: The realised efficiency after combining two companies, which results in a benefit greater than simply adding the individual impact generated from each company separately.



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