A-REIT SURVEY 2022

Navigating Choppy Waters

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WELCOME TO BDO IN AUSTRALIA'S 28TH ANNUAL SURVEY OF AUSTRALIAN REAL ESTATE INVESTMENT TRUSTS

NAVIGATING CHOPPY WATERS: FINDINGS FROM BDO AUSTRALIA'S 28TH ANNUAL SURVEY OF AUSTRALIAN REAL ESTATE INVESTMENT TRUSTS

The Australian economy faced tumultuous market conditions in the 2022 financial year (FY22), including the effects of inflation, geopolitical tensions, and the remnants of the COVID-19 pandemic. Many industries and businesses struggled over the course of the year and the Australian Real Estate Investment Trusts (A-REITs) were no exception, with their returns experiencing significant volatility in FY22.

This survey tracks the listed Australian property industry over FY22 by ranking the S&P/ASX 200 A-REIT Index trusts (A-REIT Index) using key financial and investment indicators.

Our analysis finds that in FY22, the A-REIT Index underperformed the S&P/ASX 200 Index by 5.1 per cent and delivered a total negative return of 15.4 per cent. All market sectors, including industrial, retail, office, and diversified, delivered negative returns for FY22 – a stark contrast to the remarkable performance delivered in FY21.

The decline for A-REITs came after a strong start to FY22, having initially outperformed the S&P/ASX 200 Index for the first half of the year. This strong performance was driven by increased foot traffic across office and retail due to the lifting of national lockdown mandates, and increased demand in the industrial sector resulting from increased online retail driving warehousing and logistics.

The second half of FY22 saw the A-REITs performance turn, resulting in a decline that outpaced the overall market decline. As long bond yields increased as a result of rising interest rates and inflation, both consumer confidence and property valuations began to erode. Consequently, investors were driven toward defensive assets with strong market share, high occupancy levels, and improving rental yields.

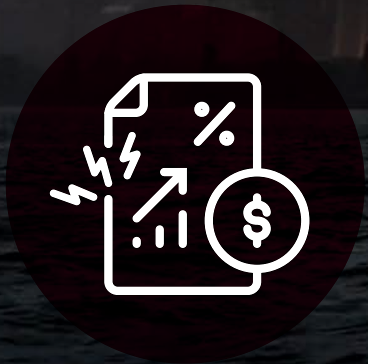
Our findings have uncovered four key themes from FY22, and we anticipate these will continue to play a role in the performance of A-REITs over the current financial year.

1. STRESSED A-REIT VALUATIONS AS INTEREST RATES RISE

Interest rate hikes have been a key driver of A-REIT valuations through the latter half of FY22. Investors are currently favouring A-REITs with strong balance sheets, free cash flow, and interest coverage to combat rising interest expenses.

For highly leveraged A-REITs that are struggling to alleviate increased borrowing costs, improving rental yields will assist in passing inflationary pressures on to tenants. For A-REITs with lower weighted average lease expiries (WALE) such as hotels, self-storage facilities, and apartments, inflationary pressures can be managed by rapidly adjusting rent through frequent resets. A-REITs with higher WALEs, such as retail and office, can build protection into new leases through inflation-adjusted rental increases. As a result, the A-REITs' ability to periodically adjust their revenue streams will assist in stabilising performance and provide investors with greater certainty of distributions.

Despite abrupt rises in inflation, rises in bond yields could moderate as recessionary risks in the global economy loom, thus easing the pressure on A-REITs. This appears supported by a **study by Wu et al**, which suggests REITs exhibit lower volatility than traditional equities and that periods of heightened volatility are often transitory. If bond yields stabilise, A-REITs may outperform traditional equities.



2. FLUCTUATIONS IN TENANT DEMAND DUE TO VOLATILE MARKET CONDITIONS

The COVID-19 pandemic has reshaped society's approach to everyday activities, prompting discussion around the "new normal" for daily life. As consumers navigate their changing usage of office, retail and warehouse spaces, A-REITs ultimately feel the effects of changing customer preferences through fluctuating tenant demand. While shifts in consumer behaviour varied between regional and urban centres, ensuring the continued demand for commercial hubs will be difficult for A-REIT operators moving forward.

As society increasingly shifts to a digital way of life, the creation of holistic, physical experiences will drive tenant demand in the A-REIT sector. Employers and office-based A-REITs struggled to attract employees and tenants back to the workplace as COVID-19 solidified flexible working conditions nationwide. Changing workplace dynamics may see larger occupiers adopt smaller leases in the future to combat rental costs. This could be somewhat mitigated by the need for increased personal space and collaboration experience in the office rather than the previously favoured high density "hot desk" format. Further, retail-based A-REITs competed with e-commerce offerings throughout FY22's COVID lockdowns. However, as the debate between brick-and-mortar stores and e-commerce continues, consumer activity will remain consistent as long as consumers have opportunities to get out of the house and engage in experiences. During FY22, property operators noticed this as some retail assets were repurposed for alternative uses in an attempt to unlock value.

3. TACKLING ESG FOR COMPETITIVE ADVANTAGE

A-REITs will face an **immense competitive disadvantage** if they are slow to adapt to impending regulation and investor expectations surrounding ESG. Environmental impacts are of particular concern for A-REITs, as the Australian Federal Government has committed to a target of net zero carbon emissions by 2040.

The risk of ESG litigation in Australia is rising while ESG disclosure requirements are transforming. Countries within the European Union and the United Kingdom have already started legislating bills which require whole-life carbon emissions of buildings to be reported and have limits set on carbon emissions in constructions.

Apart from regulatory issues, fund managers have increased ESG weightings in their valuations to attract capital from a breadth of retail and institutional investors. International fund managers that have higher regulatory standards will struggle to find A-REITs that fit their investment mandate, as **A-REITs are not fully offsetting** or measuring their embodied carbon footprint at present.

4. BOLSTERED WAR CHESTS LEAD TO CONSOLIDATION OPPORTUNITIES

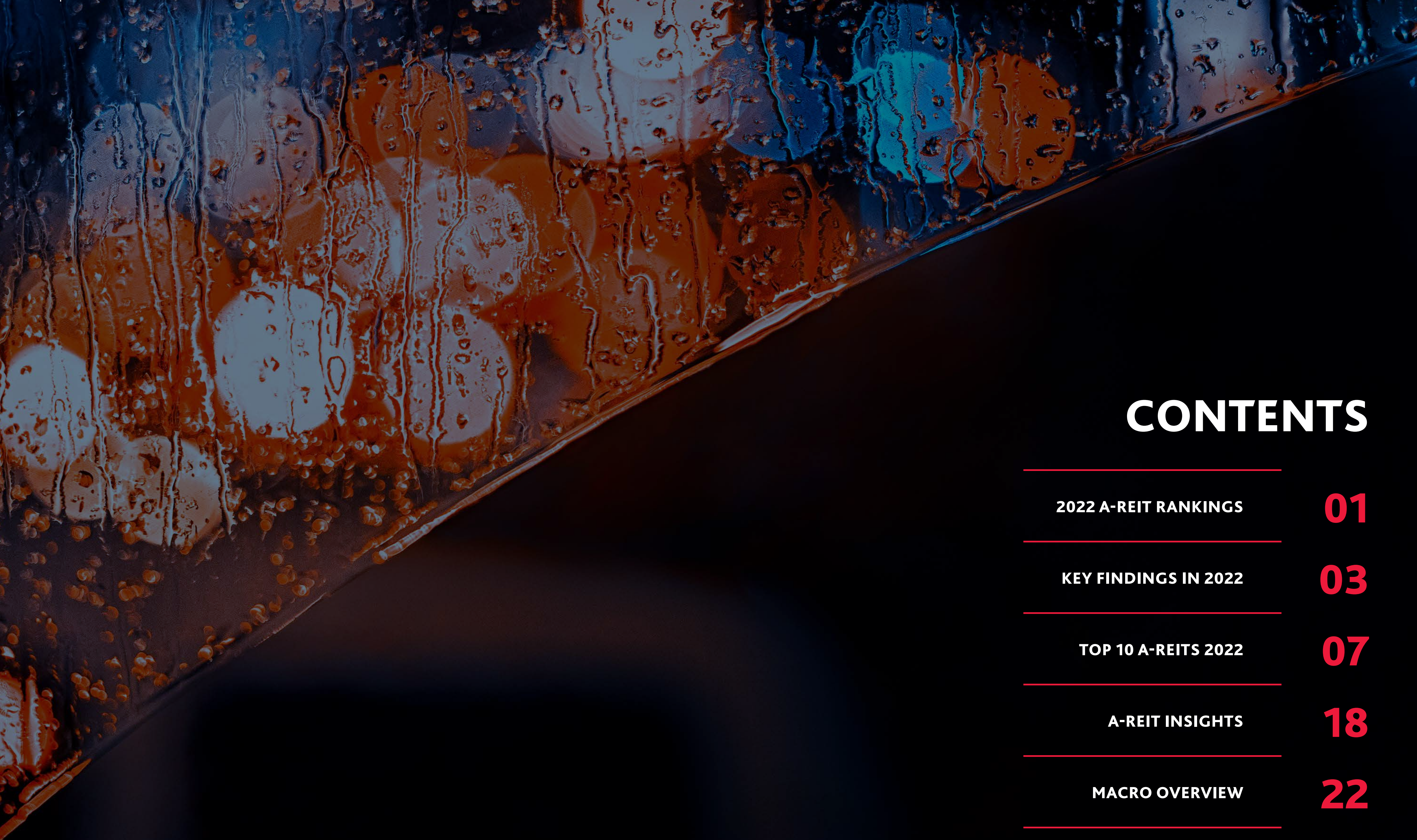
FY22 saw landmark deals across the hospitality, industrial, and office sectors. While increases in borrowing rates made leveraged acquisitions harder to stomach, subdued valuations allowed A-REITs with strong balance sheets and dormant dry powder to flex their muscle.

Consequently, A-REITs that bolstered their war chests during the past few years seized the opportunity to acquire traditionally highly priced targets in prime locations. This was facilitated by falling valuations, due to rising interest rates and shifts in consumer norms, following the COVID-19 pandemic.

Consequently, FY22 saw 29 transactions completed for a total value of $7.8 billion, an 85.7 per cent improvement on FY21 total transaction value. Successful deals included capital raisings for HealthCo Healthcare and Wellness REIT and Ingenia Communities Group, as well as the acquisition of ALE Property Group and Aventus Group.

Alternative real estate assets, such as early education, retirement living, and healthcare, are anticipated to be sought after at any point in the market cycle. This is due to them being a constant necessity in an economy which has an aging population and a high number of households with two working parents.

SEBASTIAN STEVENS
Partner, Head of Advisory
Sydney



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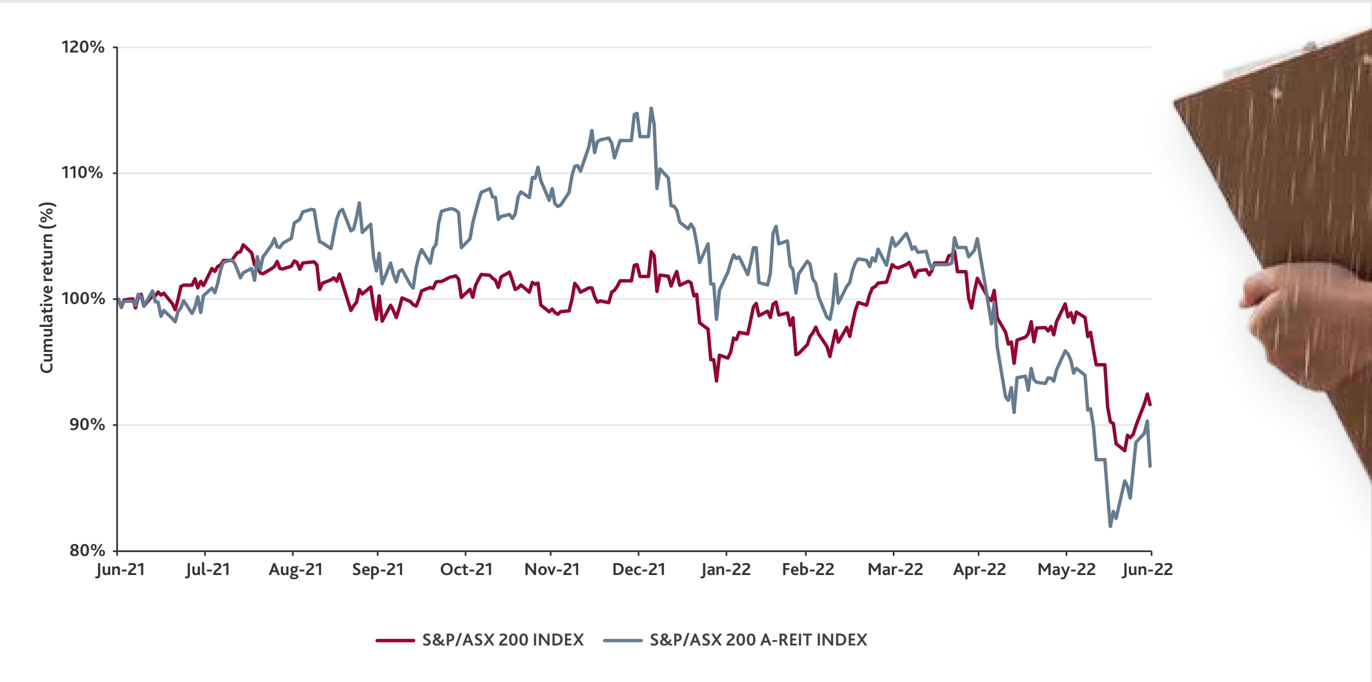
KEY FINDINGS IN 2022

A-REIT SECTOR PRICE RETURN

The S&P/ASX A-REIT 200 Index returned -15.4 per cent in FY22, underperforming the broader market index (ASX 200 Index) by -5.1 per cent by year end.

During FY22 the A-REIT sector experienced more volatility than the broader market, initially outperforming the S&P/ASX 200 (ASX 200 Index) for the first three quarters of FY22, but ultimately underperforming the ASX 200 Index by 5.1 per cent by year end.

FIGURE 1: S&P/ASX A-REIT 200 ACCUMULATION INDEX VS S&P/ASX 200 INDEX

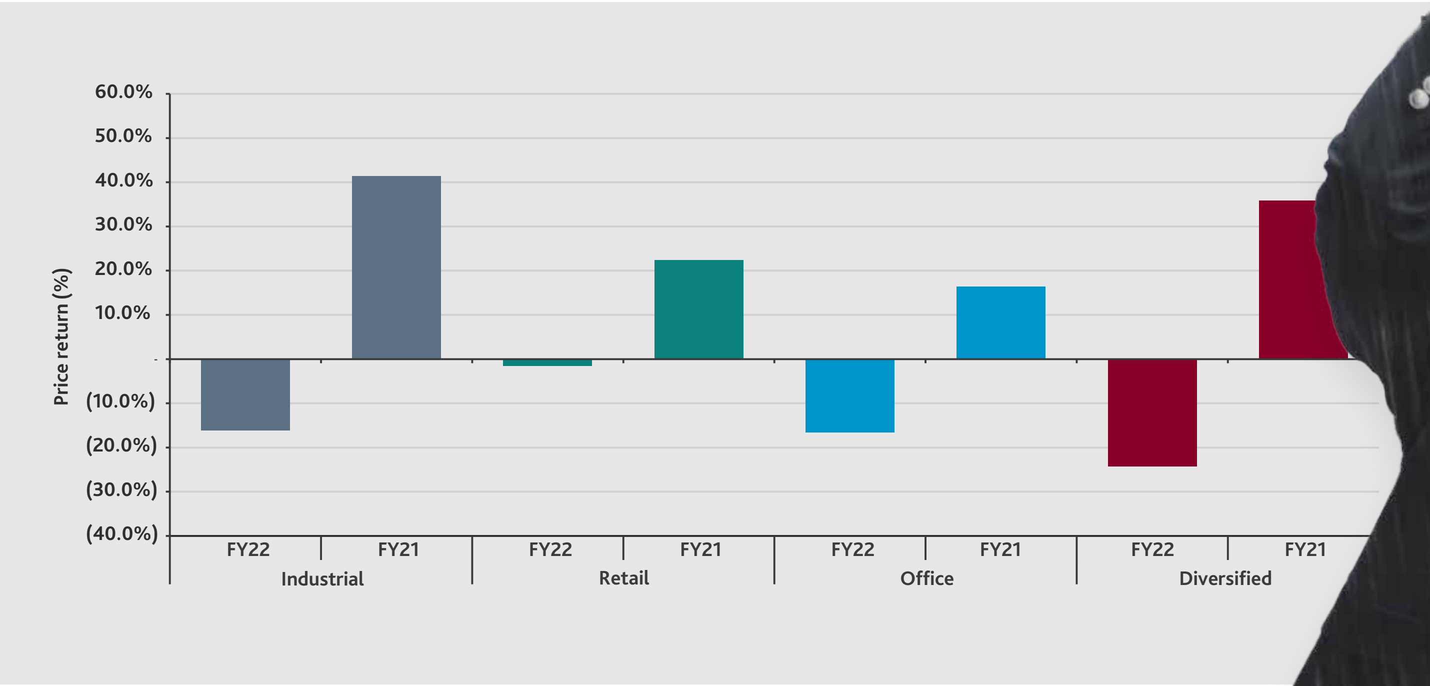


Source: CapitalIQ and BDO analysis

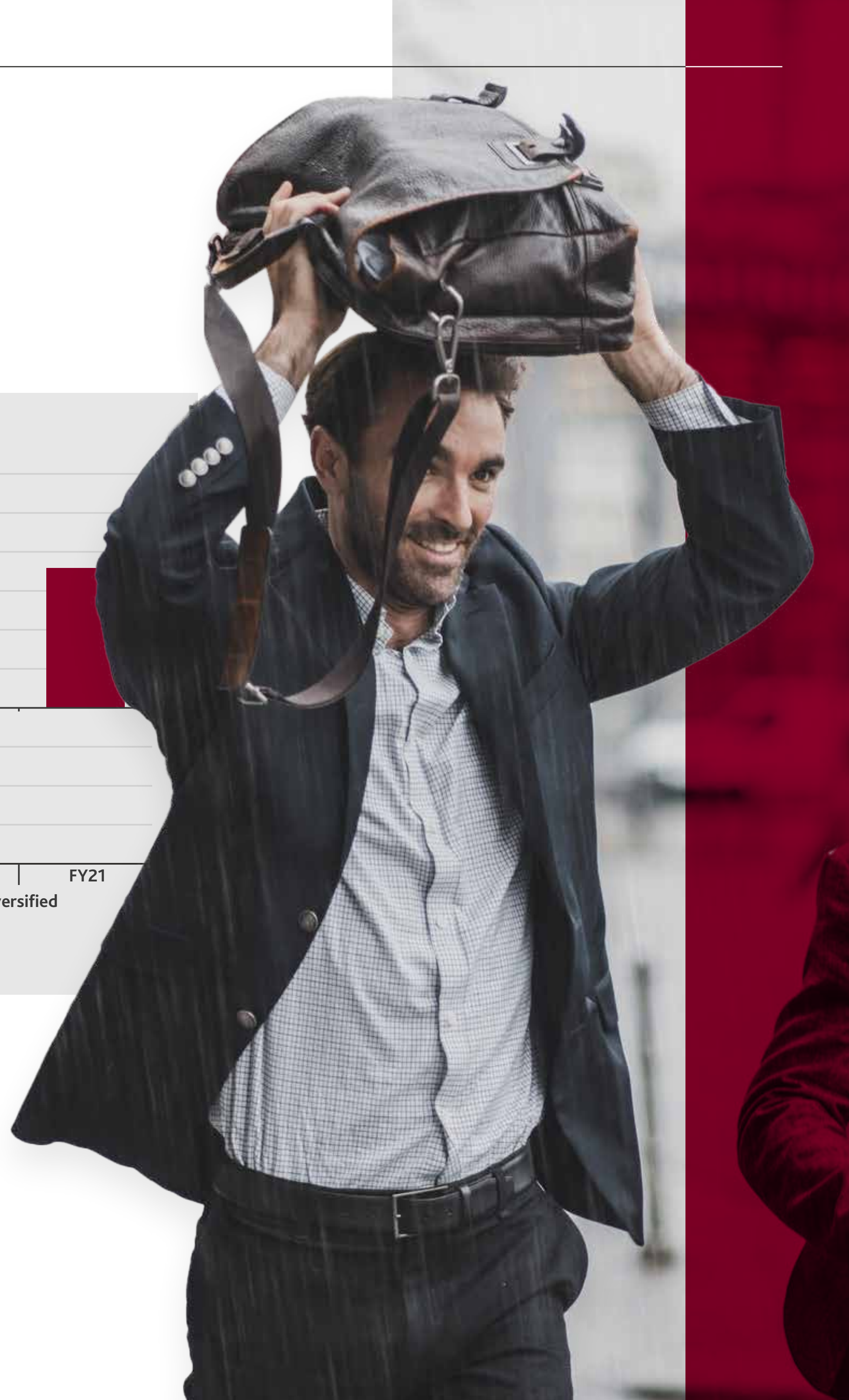
INDIVIDUAL CATEGORY PERFORMANCE

All categories underperformed their FY21 result during FY22, with the diversified category performing the worst with -24.3 per cent (FY21: 35.9 per cent), followed by office with -16.6 per cent (FY21: 16.4 per cent), industrial with -16.2 per cent (FY21: 41.4 per cent), and retail with -1.6 per cent (FY21: 22.4 per cent).

FIGURE 2: 2022 A-REIT SECTOR PRICE RETURNS



Source: CapitalIQ and BDO analysis



INDUSTRIAL

The industrial sub-sector experienced a period of rapid growth during the first half of FY22, which compounded upon the growth experienced during the initial period of COVID-19 lockdowns. This growth stemmed from higher consumer demand for goods which required warehousing, transport, and logistics facilities. Further, supply chain disruptions caused by the COVID-19 pandemic and geopolitical events caused an uptick in demand for distribution and warehousing locations as vendors attempted to meet consumer demand.

However, as the RBA commenced contractionary monetary policy measures involving quantitative tightening to stem inflationary pressures, business confidence was subdued. Subsequently, overall industry revenue is predicted to have risen at a meagre annualised rate of 0.3 per cent per cent for the five-year period through FY23 (IBISWorld, "Industrial and other Property Operators in Australia", 2022).

Despite this, the historically low interest rates observed over the past five years caused rapid expansion through purchases of industrial properties funded by cheap debt. As interest rates rose sharply from May, property valuations stagnated which caused rental yields to rise as property operators sought income to compensate for lower capital appreciation. Increases in rental yields suffered interruptions between June and September 2021 as tenants were able to negotiate with property owners throughout the COVID-19 pandemic.

RETAIL

The retail sub-sector fared the best over FY22, but still notching an annual decline of 1.6 per cent. Sporadic lockdowns, store closures, and dwindling consumer confidence did little to lessen demand for essential retail assets in neighbourhoods with strong growth. As retail stores closed during early- to mid-FY22 due to the Delta and Omicron outbreaks, the A-REIT Index declined due to significantly reduced foot traffic in retail spaces, and the lowest level of consumer confidence since **October 2020**. COVID-19 induced lockdowns caused essential retail services, such as supermarkets, to flourish as consumers spent more time at home instead of going out to restaurants. Services such as click and collect provided consumers with the ability to social distance while still visiting a brick-and-mortar establishment. Investors noticed this as FY22 was a record year for retail investment.

This growth is predicted to continue as retail property revenue is predicted to grow at an annualised rate of 2.1 per cent between 2022 and 2027.

Retail A-REITs will continue to prioritise securing tenants with longer WALEs to capitalise on the emergence of hybrid models which couple retail with medical, office, and residential spaces. Landlords will aim to pass inflationary pressures onto tenants through structured rental increases or inflation-linked rent after suffering three years of low rental yields due to COVID-19 rental negotiations.

OFFICE

Office A-REITs were battered during FY22 as property operators in urban centres attempted to recover from COVID-19 lockdowns, the "new normal" of working from home, and shaky business confidence. Although lockdowns have since lifted, tenancy has been slow to recover, with occupancy at **55 per cent and 48 per cent** of pre-COVID-19 levels for Sydney and Melbourne, respectively. However, Australia's continual shift towards a non-manual labour-based economy combined with increased capital expenditures from the private sector has stabilised demand for office spaces. Further, many tenants have downsized their office presence and adopted flexible working practices in an attempt to save on rental expenses.

These trends have increased vacancy rates, weakened rental yields, and constrained industry profit in the short-term. Despite these pressures, the growth in the service-based economy is projected to continue and tenants are expected to prioritise flexibility over cost through short-term lease agreements. This will drive up rental yields and benefit profit margins. Historically, superannuation funds have been major investors in office property due to the stable rental yields and attractive returns. Demand from superannuation funds rose during the latter half of FY22 due to compressed valuations. Due to these factors, industry-wide revenue is expected to grow at an annualised rate of 3.2 per cent between 2022 and 2027 (IBISWorld, "Office and Other Property Operators in Australia", 2022).

PREMIUM/DISCOUNT TO NET TANGIBLE ASSETS (NTA)

The median discount to NTA for A-REIT's in FY22 was 17.4 per cent, implying that current unit price valuations are not reflective of the underlying assets held by the A-REITs. There were 11 A-REITs which traded at a premium to NTA and the largest premia was Goodman Group at 139.6 per cent.

GEARING LEVELS

A-REITs continue to maintain lower gearing levels, with an average 27.9 per cent gearing in FY22. This compares with the sector's long-term gearing levels of c.30 per cent.

The weighted average cost of debt for the A-REIT sector grew as the fiscal year came to a close and averaged 3.0 per cent.

CAPITAL RAISING

FY22 saw a continuation of strong market activity, with total transaction value increasing from $4.2 billion in FY21 to $7.8 billion in FY22. Although average transaction value increased from c.$163 million in FY21 to c.$270 million in FY22, this was primarily driven by the largest transaction of the year, being the $3.0 billion acquisition of Australian pubs owner ALE Property Group (ASX:LEP) by Host-Plus Pty Limited and Charter Hall Long WALE REIT (ASX:CLW).

Other notable activity included the announced acquisition of Irongate Group (ASX:IAP) by a managed partnership between Charter Hall Group (ASX:CHC) and Dutch pension fund PGGM. The scheme of implementation agreement to acquire all IAP stapled securities was successfully approved by shareholders, resulting in the delisting of IAP in July 2022.

2022 **TOP 10** A-REITs

01 ARENA REIT

Arena REIT (ASX:ARF) is a constituent in the S&P/ASX 200 Index that develops, owns, and actively manages social infrastructure properties across Australia. They invest in social infrastructure properties in growing sectors that are supported by demographic and economic trends. Currently, their portfolio contains 256 properties that are 100 per cent per cent occupied by a diverse tenant base in the childcare and healthcare sectors. As at the date of this report, the total value of the portfolio is $1.31 billion.

HIGHLIGHTS

23%
ONE-YEAR RETURN

72%
THREE-YEAR RETURN

32%
INCREASE IN NTA

46%
PREMIUM TO NTA

ANNUAL REPORT INSIGHTS

Arena REIT was able to mostly evade the effects of COVID-19 through their macroeconomic investment approach and focus on early learning, healthcare, and education. Statutory net profit grew by 102 per cent between FY21 and FY22. This was primarily due to the increase in net operating profit, higher property revaluation gain compared to FY21, and a higher revaluation of derivatives. Further, net operating profit increased by 8.4 per cent due to the increase in rental income arising from periodic rent reviews, lease commencements upon completion of early learning centre developments, and new acquisitions. Over FY22, Arena REIT added nine early learning centre development sites and seven operational early learning centres to their portfolio.

02 HOTEL PROPERTY INVESTMENTS

Hotel Property Investments (ASX:HPI) is an A-REIT with a mandate to primarily invest in pubs and associated specialty stores located on pub sites. The majority of the portfolio is located in Queensland and are freehold sites. Currently, Hotel Property Investment's portfolio is valued at $1.3 billion and is comprised of 62 properties.

HIGHLIGHTS

100% TAX ADVANTAGED DISTRIBUTION

27% INCREASE IN NTA

7% OPERATING CASH YIELD

4% ONE-YEAR RETURN

ANNUAL REPORT INSIGHTS

Hotel Property Investments recorded a total profit after tax in FY22 of $211.4 million including a fair value gain on investment properties of $171.3 million. Moreover, during FY22, Hotel Property Investments increased their portfolio by nine properties across Victoria and South Australia.

03 SHOPPING CENTRES AUSTRALASIA PROPERTY GROUP

SCA Property Group (ASX:SCP) is an A-REIT which owns a diversified shopping centre portfolio throughout Australia. As at the date of this report, there are 91 assets under management which are valued at $4.5 billion. SCA Property Group primarily focuses on convenience retailing through ownership and management of neighbourhood and sub-regional shopping centres and freestanding retail assets.

HIGHLIGHTS

15%	32%	4%
ONE-YEAR RETURN	THREE-YEAR RETURN	PREMIUM TO NTA

ANNUAL REPORT INSIGHTS

During FY22 SCA Property Group was impacted by the COVID-19 pandemic in terms of both operational and financial performance. Further impacts include volatility in retail sales performance of tenants, government-imposed trading restrictions on tenants, and mandated rental relief moratoriums. Despite this, SCA Property Group increased net profit after tax to $487.1 million and consequently increased the distribution per security to 15.2 cents. SCA Property Group completed nine acquisitions across Queensland, New South Wales, and Victoria with a total value of $347.5 million. Moreover, SCA Property Group disposed of eight properties for a total value of $307.6 million at an average premium to book value of 9.5 per cent.

04 CHARTER HALL RETAIL REIT

Charter Hall Retail REIT (ASX:CQR) is the leading owner of convenience retail shopping centres and long WALE assets in Australia and New Zealand with a total portfolio value of $4.3 billion. The portfolio is comprised of 572 properties with an occupancy of 99 per cent. Further, Charter Hall Retail REIT employs an active asset management strategy and enhances portfolio quality through engaging with major tenants.

HIGHLIGHTS

6% DISTRIBUTION RETURN

53% TAX ADVANTAGED DISTRIBUTION

22% INCREASE IN NTA

6% ONE-YEAR RETURN

ANNUAL REPORT INSIGHTS

During FY22, Charter Hall Retail REIT's property portfolio increased 18 per cent in value from FY21 which was a primary driver in the 22 per cent increase in NTA per unit. Charter Hall Retail REIT attributes their continued growth to the development of strong relationships with tenants such as Wesfarmers, Coles, Woolworths, ALDI, and Ampol. It is part of the group strategy to enhance the quality of the portfolio through the acquisition of resilient and defensive assets.

05 NATIONAL STORAGE REIT

Founded in 1995, National Storage REIT (ASX:NSR) is the largest self-storage owner and operator across Australia and New Zealand. The group serves more than 90,000 residential and commercial customers over 226 storage centres. As at 30 June 2022, investment properties held by the Group were valued at $3.73 billion.

HIGHLIGHTS

24% INCREASE IN NTA

13% ONE-YEAR RETURN

37% THREE-YEAR RETURN

ANNUAL REPORT INSIGHTS

During FY22, National Storage REIT increased their total revenue by 28 per cent while improving their underlying earnings by 46 per cent. This allowed the group to increase their distribution per security by 22 per cent. One factor assisting with bottom line growth is the increase in the value of investment properties by 26 per cent. However, this was not due solely to fair value adjustments, National Storage REIT added 15 centres and improved occupancy by 2.8 per cent during FY22.

06 GARDA PROPERTY GROUP

GARDA Property Group (ASX:GDF) is a real estate investor, developer, and manager in the industrial and commercial office sectors. Their current portfolio of 18 properties is valued at $650.7 million, spread across Melbourne, Brisbane, Cairns, and Mackay.

HIGHLIGHTS

41%
INCREASE IN NTA

25%
ONE-YEAR RETURN

25%
THREE-YEAR RETURN

ANNUAL REPORT INSIGHTS

GARDA Property Group was able to deliver return on equity of 46 per cent to their investors, and finish FY22 with a 39 per cent relative over performance when compared with the A-REIT Index. Moreover, GARDA Property Group's portfolio increased in value by 31 per cent, primarily due to property revaluations which drove the 41 per cent increase in NTA. GARDA Property Group's overall strategy is to act as a long-term owner of real estate and to remain market cycle aware. The group's strategy is focused on the commercial office and industrial sectors, as well as debt investments into residential developments.

07 CHARTER HALL GROUP

Founded in 1991, Charter Hall Group (ASX:CHC) is an integrated property group that manages listed and unlisted property funds, worth over $69.1 billion, on behalf of wholesale, institutional and retail investors. Charter Hall Group invests in all core classes of property, including retail, industrial, social infrastructure, and commercial.

HIGHLIGHTS

96%
PREMIUM TO NTA

21%
OPERATING CASH YIELD

12%
THREE-YEAR RETURN

ANNUAL REPORT INSIGHTS

Charter Hall Group's strategy is broken down into four steps, accessing equity from listed wholesale and retail investors, deploying capital into attractive investment opportunities, managing funds and assets, and investing alongside capital partners. It is this structured and well-executed plan which has made Charter Hall Group, as well as their other listed REITs, mainstays within our top 10 performers. During FY22, Charter Hall Group completed $8.5 billion in gross property transactions and increased property funds under management by 26 per cent.

08 VICINITY CENTRES

Vicinity Centres (ASX:VCX), previously known as Federation Centres and Centro Properties Group, is an A-REIT specialising in the ownership and management of Australia shopping centres. As of June 2022, it had stakes in 60 shopping centres, with over 6,800 retailers under their management. The investment properties held by the group are valued at $14.37 billion.

HIGHLIGHTS

26%
ONE-YEAR RETURN

6%
OPERATING CASH YIELD

48%
LIQUIDITY

ANNUAL REPORT INSIGHTS

In FY22, Vicinity Centres showcased a 16 per cent improvement in sales on the second half performance of FY19, which shows growth on pre-COVID levels. The group boasted a $1.215 billion statutory net profit after tax and 22 per cent total securityholder return. There was also a $554 million increase in asset valuation. The group also experienced stability in the occupancy rate as it remained relatively unchanged through FY22.

09

CHARTER HALL SOCIAL INFRASTRUCTURE REIT

Charter Hall Social Infrastructure REIT (ASX:CQE) is the largest Australian Property trust investing in social infrastructure properties within Australia and New Zealand. The group currently holds 368 properties with a gross asset value of $2.1 billion. Out of these 368 properties, they boast a 100per cent occupancy rate.

HIGHLIGHTS

26%
INCREASE IN NTA

2%
ONE-YEAR RETURN

6%
THREE-YEAR RETURN

ANNUAL REPORT INSIGHTS

Charter Hall Social Infrastructure's gross assets grew by 35 per cent in 2022 to $2.1 billion. $1.97 billion of this is attributable to their property portfolio, which grew by 39 per cent. This is driven by a valuation uplift of 19 per cent equating to $269.4 million and new acquisitions of $232.7 million. The group were able to increase their NTA per unit by 26 per cent to $4.08. Further, the group delivered operating earnings of $62.9 million, representing a yearly increase of eight per cent.

10 ASPEN GROUP LIMITED

Aspen Group Limited (ASX:APZ) is a leading provider of quality accommodation in the residential, retirement and short stay sectors. The group holds 18 properties and over 2,950 sites and dwellings valued at $366.06 million. Despite all of this, the group still managed to materially increase earnings and net asset value per security due to a massive growing demand for their more affordable accommodation.

HIGHLIGHTS

17%	58%	32%	7%
ONE-YEAR RETURN	THREE-YEAR RETURN	INCREASE IN NTA	OPERATING CASH YIELD

ANNUAL REPORT INSIGHTS

Aspen Group Limited generated a statutory net profit of $75.38 million and Operating Earnings of $11.84 million. Their total rental and ancillary services revenue increased by 22 per cent to $17.25 million. Property net operating income also increased by 17 per cent to $14.84 million. Most impressively, the groups' property portfolio expanded by 80 per cent in the last year to over $412.59 million, through valuation gains and acquisitions. During the year, they acquired the Perth Apartment Portfolio in WA consisting of 514 apartments for $52 million.

A-REIT INSIGHTS

ARENA REIT

ROB DE VOS
Managing Director

What does Arena REIT attribute its outstanding performance in FY22 to?

Despite the lingering direct and indirect impacts of the pandemic, changing work patterns, increased inflation, and increased interest rates, the community demand for the services that Arena's properties accommodate has remained strong. In this context, financial year 22 was another successful year for the business, we made solid progress against our investment objective and ultimately achieved strong outcomes for our stakeholders and ongoing positive outcomes for the many communities across Australia that rely on the essential services delivered by tenant partners that occupy Arena's properties.

Arena's highlights for financial year 22 include:

- A record statutory profit of $334m
- Underlying cash based net operating profit of $56m, reflecting an increase of 8.4 per cent on FY21
- Valuation growth across the portfolio contributing to an increase in NAV of 32 per cent over the 12-month period
- Progress on our organisational sustainability programs, including Arena REIT being certified carbon neutral by Climate Active for business operations in FY21-22
- Advancing our sustainability programs across our investment portfolio, with solar renewable energy systems now installed at over 200 or 80 per cent of our properties and over 100 solar installations were completed in the last 12 months
- Successful delivery of early learning centre development projects and replenishment of the development pipeline which will support future earnings growth
- We upgraded our FY22 distribution during the period to 16 cents per security, reflecting an increase of 8 per cent on FY21 and provided distribution guidance for financial year 23 of 16.8 cents per security, reflecting an increase of 5 per cent on FY22.

FY22 contained reverberations of the COVID-19 pandemic in the form of the Delta and Omicron outbreaks. How did Arena REIT adapt during the initial COVID-19 lockdown to ensure resilience during subsequent outbreaks?

The COVID-19 pandemic, including its recent variants, presented challenges for all of our stakeholders and particularly our tenant partners during financial year 2022.

Understanding our tenant partners' needs and those of the community during this time has positioned the business well to better deal with any future out breaks. More recently, the challenges for our tenant partners relates to a changing economic environment arising from inflationary pressures, interest rate increases, wages pressures and staff shortages which have combined to create new uncertainties. We acknowledge these challenges and express our gratitude for our tenant partners continued resilience and ability to deliver essential services to Australian communities.

A-REITs are typically a defensive asset in times of high inflation. How is Arena REIT positioned to respond to the coming period of rising interest rates and inflation?

In an environment of heightened external risks Arena has maintained high conviction in our investment discipline and executing on our strategy. Being an internalised manager with strong governance protocols means that we are aligned with our stakeholders over the long term, actively pursuing sustainable growth and quality in our financial metrics, not short-term balance sheet scale.

Arena has maintained a disciplined approach to capital management, prioritising resilience and risk reduction through relatively low gearing, ongoing high levels of interest rate hedging and maintaining immediately available liquidity in excess of our development commitments. Our property portfolio

"We made solid progress against our investment objective and ultimately achieved strong outcomes for our stakeholders"

is 100 per cent occupied with a 20-year WALE and a transparent and highly predictable rental profile that has strong inflation protection. Approximately 80 per cent of FY23, FY24 and FY25 annual rent escalations are contracted at the higher of CPI or a fixed amount.

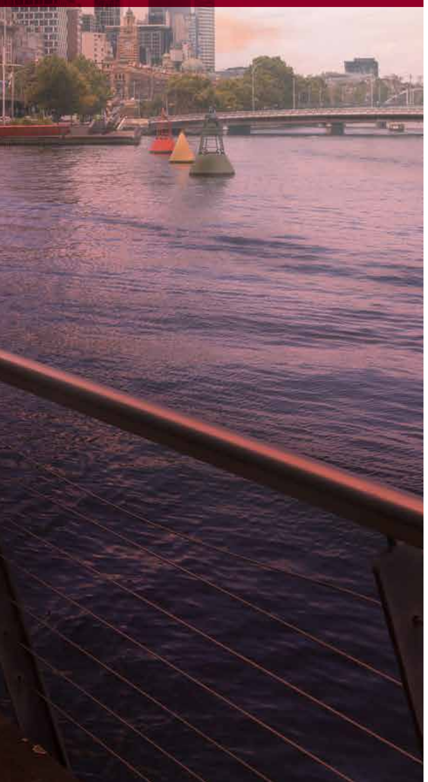
Are there any other observations on the general A-REIT market looking forward that you are able to share?

In an environment of increasing interest rates, we see the likelihood of yield expansion in real estate markets, including in the social infrastructure property sector. A mitigating factor for yield expansion is of course rental growth, for which Arena's portfolio is well positioned to provide, as a result of the majority of its leases escalating in line with inflation and our long-held focus of ensuring rents had room for growth over time, so effectively coming from a lower base.

We encourage A-REIT investors to carefully assess increasing interest rates, security of income and tenant prosperity in this changing economic environment.

GARDA PROPERTY GROUP

MATTHEW MADSEN
Executive Chairman



What does GARDA Property Group attribute its outstanding performance in FY22 to?

GARDA's commercial and industrial portfolio delivered a 46.3 per cent return on equity during FY22 as a result of our 'build to own' strategy. GARDA has a sizeable development pipeline totalling approximately 160,000m² of industrial built form in Brisbane. Supporting this strategy, was the acquisition of development sites prior to, and continuing through the COVID-19 pandemic years, prior to a substantial rotation into the industrial sector by a weight of institutional capital.

GARDA positioned itself by acquiring well-located sites and developing quality industrial assets that provided exposure to this sector re-rate. We maintain a strong focus on 'yield on cost' within the 'build to own' strategy. Substantial investor value has been delivered by advancing development applications and pre-committed leasing on sites acquired as englobo parcels during the pandemic.

FY22 contained reverberations of the COVID-19 pandemic in the form of the Delta and Omicron outbreaks. How did GARDA Property Group adapt during the initial COVID-19 lockdown to ensure resilience during subsequent outbreaks?

GARDA is Brisbane-based so unlike our southern counterparts; day-to-day operations were only occasionally impacted by the short lockdowns implemented by the Queensland Government. Notwithstanding, investment into more sophisticated technology systems has allowed our team to operate remotely, effectively servicing our customers and engaging with our investors during those periods. Importantly, we are believers that a strong office culture is the best work environment and we have continued to work full time from our Brisbane office. The benefits of all being in the one place at the same time cannot be replaced through technology.

A-REITs are typically a defensive asset in times of high inflation. How is GARDA Property Group positioned to respond to the coming period of rising interest rates and inflation?

A-REITs are now experiencing higher expenses to service their variable debt but those with inflation linked annual rent reviews and the ability to access higher rents through leasing outcomes at expiry or new development will be better placed to offset these costs and potentially provide a pathway to earnings growth.

GARDA's existing portfolio of approximately 140,000m², which is 90 per cent occupied and provides 5-year WALE, has approximately 25 per cent of leases exposed to inflation (CPI) based lease reviews. More importantly, we have 160,000m² of industrial pipeline we are building out over the next few years that will continue to access the higher rents being experienced and forecast in the industrial sector.

Are there any other observations on the general A-REIT market looking forward that you are able to share?

We ask ourselves how resilient the Australian economy is, how quickly the RBA will address the inflation challenge, and what does that mean for both the terminal interest rate and the duration to get there.

> **"GARDA positioned itself by acquiring well-located sites and developing quality industrial assets"**

A-REIT market sentiment is currently poor and reflected in the deep discounts to underlying value. It will continue to be difficult for investors to assess value until there is greater clarity on defeating inflation.

A-REITS with a strong pathway to earnings growth will perform the best. To that end, industrial is the standout for rental growth and those with the ability to develop high quality 'build to own' assets over the coming years will be best placed to deliver both the quality of built form and the type of financial returns required in this very challenging environment.

VICINITY CENTRES

PETER HUDDLE
Chief Operating Officer

What does Vicinity Centres attribute its outstanding performance in FY22 to?

The pandemic presented challenges to the retail industry, to which Vicinity was not immune, but we utilised this to strengthen our business proactively in three ways. First, we fostered strong relationships with retailers, driving improved leasing spreads, higher tenant retention and reducing centre vacancies.

Secondly, our balance sheet is a competitive advantage, with gearing at the lower end of our target range and high level of drawn debt hedged to insulate against interest rate volatility. And finally, we prepared for future growth by progressing the planning and approvals for a range of highly attractive retail and mixed-use developments, a number of which are now in construction.

We've also introduced targeted marketing campaigns to take advantage of customers keen to get back into their local centres, which has supported strong retail sales growth particularly across the Luxury category, where we are industry leaders.

FY22 contained reverberations of the COVID-19 pandemic in the form of the Delta and Omicron outbreaks. How did Vicinity Centres adapt during the initial COVID-19 lockdown to ensure resilience during subsequent outbreaks?

Additional Safety protocols and Standard Operating procedures were created when the initial Covid outbreak occurred, and those were consistently reviewed and modified as the situation evolved.

Increased sanitisation and hygiene practices were supported by overt consumer messaging and visual social distancing practices. Covid safety measures were regularly updated to reflect the most up to date advice from government and benchmarked against competitors within the Shopping Centre Industry to ensure best practice.

We also introduced an interactive feature to each centre's website that uses real-time data to shows visitation numbers and forecasts. This helps customers plan when and where they shop before they leave home, and enables them to avoid peak times if necessary.

A-REITs are typically a defensive asset in times of high inflation. How is Vicinity Centres positioned to respond to the coming period of rising interest rates and inflation?

Vicinity is well positioned for higher interest rates with a strong balance sheet with gearing at the bottom end of the target range, and strong investment grade credit ratings providing access to range of debt capital sources.

Vicinity's debt book is also relatively highly hedged, providing protection against higher interest rates over the short to medium term.

From a CPI perspective, our net lease structures provide a level of inflation protection and deliver favourable fixed increases over end-to-end lease terms. Vicinity will also maintain its focus on containing costs and driving efficiencies (e.g. multi-year energy contracts in place, focused solar program roll-out continues and process improvement initiatives commenced).

> **"We prepared for future growth by progressing the planning and approvals for a range of highly attractive retail and mixed-use developments"**

Are there any other observations on the general A-REIT market looking forward that you are able to share?

We believe that the recovery of CBDs will continue and they will return, in some way, to their former vibrancy as the main focal point for commerce, tourism and leisure.

ASPEN GROUP LIMITED

JOHN CARTER
Joint Chief
Executive Officer

What does Aspen Group attribute its outstanding performance in FY22 to?

We have improved the management of our assets leading to strong increases in income at some assets, such as Darwin Freespirit. Overall operating income and development income were up in a challenging environment. We have reduced our management expense ratio ("MER") so that it is now approximately 1 per cent of assets at the end of FY22. Further, we improved the quality of the management team and placed head office team members in Adelaide and Perth to be closer to the assets. Finally, we increased development income but still at a manageable level of around 25 per cent of total income. Aspen's positioning to target the lowest 40 per cent of income earners is not a crowded space and so there is strong demand and challenges to bring on supply.

FY22 contained reverberations of the COVID-19 pandemic in the form of the Delta and Omicron outbreaks. How did Aspen Group adapt during the initial COVID-19 lockdown to ensure resilience during subsequent outbreaks?

The group actively moved from short-term letting in the parks to 89 day letting if travel movements occurred. Moreover, we employed head office members in South Australia and Western Australia, as mentioned above, in case there are further border closures. Finally, we improved technology systems across the group.

A-REITs are typically a defensive asset in times of high inflation. How is Aspen Group positioned to respond to the coming period of rising interest rates and inflation?

We have low gearing of approximately 20 per cent debt/total assets after our recent capital raising (of which, the large majority is hedged at attractive rates). Further, we are tactically recycling capital from low yielding assets like single houses which only yield around 3 per cent. Our acquisitions have been well priced and so we have less pressure on land values compared to some REITs. We have a large portfolio of multifamily residential which is experiencing strong rental growth. Our retirement assets have annual reviews which will generally keep up with inflation. Moreover, we have been increasing the sale prices of retirement assets where possible to maintain margins and recover some or all of the construction price increases. Finally, we are using technology and solar to reduce the increases in water and electricity prices.

Are there any other observations on the general A-REIT market looking forward that you are able to share?

Capitalisation rates are expected to increase over the next FY at a minimum as valuations reflect sales and increases in funding costs. Therefore, achieving earnings and subsequently distribution growth over the FY22 levels will be challenging for many.

> **"Overall operating income and development income were up in a challenging environment"**

MACRO OVERVIEW

During FY22, the A-REIT sector, was greatly impacted by a myriad of macroeconomic factors. The year commenced with lockdowns impeding GDP growth forecasts and consumer confidence, but as the economy opened, inflationary pressures, pent up from COVID-19 lockdowns and supply chain constraints, rapidly grew.

Further drivers of inflation in FY22 included geopolitical events such as the Russia's invasion of Ukraine and China's pursuit of COVID-zero by shutting down freight channels.

Surging inflationary pressures have warranted tight monetary policy from central bankers, with the Australian 10-year treasury rising from 1.3 per cent to 3.5 per cent in FY22. Increases in bond yield typically stress A-REIT valuations due to their higher leverage when compared with other asset classes, especially as many A-REITs have taken advantage of an extended period of cheaper borrowing.

Year-on-year headline CPI, a measure of price increases in the economy, grew from **3.8 per cent in September 2021, to 6.1 per cent in June 2022**. A-REITs have historically posted positive returns in periods of rising inflation as these periods are typically concurrent with stronger economic growth as when prices rise, property values tend to appreciate. Further, cash flows improve due to landlords passing on price increases through both fixed-rate and inflation-linked rental increases.

However, property prices are also inversely related to increases in long-dated government bond yields as this indirectly increases the cost of borrowing. Therefore, the RBA's contractionary monetary policies stagnated economic growth forecasts and increased investor's exposure to default risk. Future increases in policy rates were rapidly priced into long-duration government bond yields after the first rate rise in May 2022, which impacted the A-REIT sector.

METHOD OF RANKING

1 EXPLANATION OF CRITERIA AND RANKING

A brief explanation of each criterion used to rank REITs in the 2022 Survey is provided below.

1.1 FINANCIAL CRITERIA

- **Operating Cash Yield on Average Net Assets**

  Calculated by dividing operating cash flow (including interest expense); by the average of opening and closing net assets for the period.

  The financial year end of the entity has been used in all cases, except for 31 December entities where 30 June 2022 figures have been sourced from half year reports.

  Where accounts have been prepared for a period of less than one year, the operating cash measure has been annualised.

- **Distribution Return on Investment**

  Calculated by dividing the distribution per Security paid for the entity's financial year by the average ASX price of the Security through the year. The average ASX price is calculated on a daily closing price basis, with prices sourced from S&P Capital IQ.

  Where accounts have been prepared for a period of less than one year, the distribution has been annualised.

- **Tax Deferred Distribution Component**

  The percentage of the total annual distribution from each entity which is tax deferred.

  Where this information was not disclosed in the annual report, BDO attempted to obtain the detail required from other sources.

- **Movement in NTA Per Security**

  Calculated by assessing the percentage increase (or decrease) in NTA per Security over the entities' financial year by using the opening and closing figures for NTA per Security.

  Where an entity was listed during the year, BDO has assessed the opening NTA as being equal to the issue price.

  In all cases the financial year end of the entity has been used, except for 31 December year ends where we have used NTA from the 30 June 2021 and 2022 half year reports.

- **Premium/Discount to NTA**

  Calculated by subtracting the average of NTA per Security (being opening NTA plus closing NTA divided by two) from the average ASX price per Security and dividing this by the average NTA per Security.

  We have ranked entities trading at a premium to NTA as having the highest ranking in this metric.

1.2 INVESTMENT CRITERIA

- **Total Return**

  This measure, over both the one year and three years to 30 June 2022, records both the income return (i.e. distributions) and capital appreciation (i.e. movement in ASX price).

  Information sourced from the ASX has been used to compile this criterion.

- **Volume of Trading on ASX (Liquidity)**

  This liquidity measure is expressed as a percentage and is calculated by dividing the total volume of Securities traded in each entity for the year ended 30 June 2022 by the weighted average total number of Securities on issue.

  This provides an indication of relative liquidity, irrespective of entity size.

1.3 METHOD OF RANKING

A total score of 100 (maximum) has been used, comprising 65 points for financial criteria and 35 points for Investment criteria. In determining the final rankings, the scores on each component were aggregated (not the rankings) such that the relative performances within each criterion are maintained in determining the overall rankings.

- **Financial Criteria**

  The tests used in the financial criteria and assigned weightings are as follows.

FINANCIAL CRITERIA	SCORE
	2022
Operating Cash Yield (on net assets)	15
Movement in NTA	15
Premium/Discount to NTA	15
Distribution Yield	10
Tax Deferred Distribution Percentage	10
PERFECT SCORE	**65**

  In each of the above tests the scores were scaled so that the top performer in each test received the maximum available score for that criterion. Rankings were then assigned based on the scaled scores.

- **Investment Criteria**

  The tests used in the investment criteria and assigned weightings are as follows.

INVESTMENT CRITERIA	SCORE
	2022
Total Return (One Year)	20
Total Return (Three Year)	10
Volume of Trading on ASX	5
PERFECT SCORE	**35**

  The above tests have been ranked using a variable points system for each test, based on the number and importance of aspects considered. In each of the tests, the scores were scaled so that the top performer in each test received the maximum available score for that criterion. Rankings were then assigned based on the scaled scores.

- **Median Results**

  For an entity which could not be scored equitably in a particular metric, due to its recent listing, the unique nature of an entity's activities, or lack of available information for the relevant criteria, that entity was allocated a median result for the purpose of ranking. This ranking was then weighted and scored as usual. For all such instances 'N/A' appears in the result column for the individual criteria tables.

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