



24 December 2018

Fund Update, Outlook and Liquidity Event

APN Funds Management Limited ACN 080 674 479 (**APN FM**) as responsible entity of the APN Regional Property Fund ARSN 110 488 821 (NSX:APR) (**Fund**) is pleased to provide an update on the Fund and the proposed liquidity event for unitholders.

Background on Liquidity Event and Fund Update

The liquidity event is a transaction designed to provide unitholders the opportunity to realise their investment in the Fund for cash. This event is in addition to investors' ongoing ability to transact their units on the NSX. APN FM has committed to work towards a liquidity event that is fair to all investors in the fund including all those who wish to exit.

As announced on 24 May 2018, the APN FM Board (**Board**) set a target date for the liquidity event of 31 December 2018. Since that time, significant progress has been made on initiatives which the Board believes will maximise investor value in advance of the liquidity event, including:

- Signing a new lease with Sparke Helmore Lawyers for ~1,700 square metres on levels 6 and 7 of 28 Honeysuckle Drive, Newcastle for an additional eight year term expiring 31 January 2027; and
- Entering into a heads of agreement with a new tenant intending to occupy ~650 square metres of level 5, 28 Honeysuckle Drive, Newcastle for a 10 year term, subject to negotiation and execution of a binding lease.

As part of its active management approach, APN FM has also continued to progress capital improvement initiatives, including:

- Improving tenant amenity and retention rates by upgrading the end of trip facilities (construction commenced);
- Upgrading the buildings' entrance foyers (construction commenced);
- Refurbishing the bathroom facilities, including installing energy efficient lighting and new carpet across levels 6 and 7 of 28 Honeysuckle Drive (to commence early in 2019);
- External repainting of both 26 and 28 Honeysuckle Drive (complete); and
- Undertaking works to improve the buildings' energy efficiency with a target minimum NABERS rating of 4.5 stars (complete).

The above leasing outcomes and capital improvement initiatives are important steps in positioning the properties to deliver maximum value for investors in advance of the proposed liquidity event.

Fund Outlook - well positioned to deliver strong returns

The Fund has provided a total return since the Fund's inception on 28 October 2004 of 9.3% per annum (to 30 September 2018).

As property investors focused on fundamental value drivers, the Fund's two Newcastle office properties are very well positioned to continue delivering strong future investment returns:

- Current property valuation metrics including 7.5% capitalisation rate and ~\$5,395 per square metre of NLA (as at 30 June 2018);
- Track record of strong cash generation with average cash on cash yield of 9.2% pa over the three years to 30 June 2018¹;
- 100% tenant occupancy (30 September 2018) with an average occupancy over the last 10 years of 99%;
- Strong history of tenant retention with 6 tenancies completing lease extensions over the past 6 years and numerous tenants renewing for a second and third time;
- High quality tenancy profile with over 96% of rental income generated from government, multinational or nationally recognised tenants;
- Average net face rents of ~\$400 per square metre that are competitive within the local market and substantially lower than markets such as Sydney for businesses looking to maintain or lower their occupancy costs;
- Upgraded facilities including new entrance foyers, bathrooms and end of trip facilities offering excellent tenant amenity and competitive advantage;
- The buildings' energy efficiency continues to improve with an indicative NABERS rating of 4.5 stars following completion of the works;
- Excellent location in the heart of Newcastle's central business district with the buildings offering excellent transport amenity given proximity to public transport (light rail, heavy rail and bus) along with convenient on-site tenant car parking for 164 cars;
- Newcastle is undergoing significant change with major investment into the region including infrastructure spending on the new light rail that provides a connection between the Newcastle interchange, the city centre and beachfront; and a long-term commitment from the Australian Defence Force with approximately 50 of the new F-35A stealth fighter aircraft to be based at the local Newcastle airport. In addition, the education sector is expanding with University of Newcastle developing a new \$95 million campus located in the heart of Newcastle CBD and Japanese based Nihon University purchasing the former Newcastle Law Court to house the university's first ever Australasian campus;
- Newcastle's attractive cost of living with a median house price of \$598,000 (October 2018) being approximately 25% below that of Sydney; and
- Attractive Newcastle office market with favourable short to medium term supply / demand dynamics (volume of competing space) underpinning the properties' future leasing prospects.

As a result of the above, the buildings will continue to offer contemporary and competitive accommodation to businesses and other organisations including government bodies based in the city.

The Fund has been and continues to be conservatively financed with a target gearing range of 30% - 40%.

Mr Tom Forrest, Head of Direct Property, commented: 'We believe the Fund is in excellent shape to continue to deliver attractive cash income returns for investors with two high quality and consistently strong performing assets. The Newcastle office market is competitively positioned for existing and new tenants, and with significant investment in the region underway, as well as its proximity to Sydney underpinning its future prospects, we consider Newcastle is an excellent commercial property investment destination'.

¹ Calculated as net property income / (June 2016 valuation plus capital expenditure)

Debt Facility update

The Fund has received a credit endorsed three year extension of the debt facility from the incumbent financier, Bank of Melbourne, including an increase in the facility limit and revised pricing; however, this is subject to agreeing final form documentation. Bank of Melbourne has provided a short term extension of 60 days through until 28 February 2019 on the same terms of the existing facility so there is sufficient time to finalise documentation.

Management Fee review

APN FM as the Manager of the Fund has undertaken a review of its own fees in the context of the proposed liquidity event and as part of its ongoing efforts to ensure that its fees are competitive and market based. As a result of this review, a proposal has been accepted by the Board to adjust the ongoing management fees from 0.75% of Gross Asset Value per annum to 0.65% of Gross Asset Value per annum, effective from 31 March 2019.

Consideration of liquidity event options

The Board has considered the options available to deliver an outcome which is in the best interests of all unitholders.

Factors considered by the Board include:

- maximising value for all unitholders;
- providing liquidity for unitholders wishing to realise their investment; and
- providing unitholders who wish to remain invested in the Fund for a range of reasons, including the tax implications of exiting their investment, the opportunity to do so.

In addition, the Board has taken feedback provided by investors into account in forming its view.

The liquidity event options considered by the Board include:

- disposing of either one of the Fund's two assets individually (and returning capital to unitholders);
- disposing of both properties and winding up the Fund (and returning capital to unitholders);
- merging the Fund with another fund, providing investors with a larger fund in which to invest with potentially greater ongoing liquidity or cash consideration for their units; or
- raising new equity and debt to fund the withdrawal of unitholders wishing to realise their investment at an agreed unit value.

Different liquidity options may be more or less attractive to certain types of investors for a range of reasons including investors' individual liquidity preference, tax situations and ongoing investment preferences including the ability to continue to benefit from the attractive features of the Fund.

The Board has sought to implement an option which generates the best outcome for all unitholders – including an option which will deliver full liquidity to any unitholder wishing to realise their investment for cash.

Consideration of asset sale

The Board has reviewed the potential sale of the properties which has included a consideration of market evidence of comparable office sale transactions, available leasing evidence and information regarding the future prospects of the Newcastle market generally, and more specifically, the office property market and the future conditions likely to impact the value of the Funds' properties.

The Board acknowledges that the outcome of any asset sale process would involve a degree of uncertainty as to the final sale terms. The Board has sought to form the best possible view on the market and the value of the properties through its management team's analysis as well as through commissioning two independent valuation reports that will be made available as part of the liquidity event.

As part of the Board's consideration of current market evidence, multiple transactions have been reviewed with the analysis providing a range of capitalisation rates, including a number of capitalisation rates lower than the capitalisation rates used as part of the Fund's existing carrying value of the assets (implying a higher value). As part of the review, the Board notes the recent (December 2018) announcement regarding the exchange of contracts for the sale of 90 Crown Street in Wollongong at a cap rate of 7.75%. The Board's view is that while this transaction is not perfectly comparable, it has a number of similarities to a potential sale of the Fund's properties, including its tenancy composition, weighted average lease profile and approximate value.

Commitment to delivering liquidity

The Board has determined that the preferred transaction structure is to raise new equity and debt to fund the withdrawal of unitholders wishing to realise their investment. This process for the liquidity event will commence in early February 2019. The Board believes that this timing will provide an orderly liquidity process for existing unitholders who wish to realise some or all of their current holdings and to attract new investors to the Fund.

The ability to implement this transaction (or any liquidity event) will depend on market conditions at the time. As part of its commitment to delivering liquidity to all investors, if there is insufficient capital available to meaningfully satisfy those investors seeking to withdraw, the Board will move to implement a sale process of the properties and seek to wind up the Fund.

Liquidity Event and Timetable

The intended structure of the liquidity event will comprise:

- A withdrawal offer for those existing investors who wish to redeem their investment in the Fund; and
- A capital raise under a product disclosure statement open to existing and new investors.

Both the withdrawal offer and the capital raising will be based on a unit price that is the Net Asset Value (**NAV**) of the Fund, adjusted for costs associated with the liquidity event, and will be based on the midpoint of two independent valuations that are to be issued as at the end of January 2019.

Final details of the NAV and related financial information will be announced on 4 February 2019.

The capital raised will be used to fund (in whole or in part) the withdrawal offer requests that APN FM receives. At this stage, APN FM does not intend to raise additional capital for other purposes (such as asset acquisitions to grow the Fund).

The liquidity event is not currently underwritten nor is the number of unitholders who will seek a withdrawal known. APN FM will consider a potential underwriting of the transaction in due course once final financial and valuation information is available and depending on the terms and availability of any potential underwriter.

It is expected that the recapitalisation process will take approximately eleven weeks from its commencement as outlined in the table below. At the end of this period new units will be issued to those who participate in the capital raise to fund the withdrawal requests. The transaction will be structured to, as far as possible, satisfy all withdrawal requests by the proceeds of the capital raising. However, in the event there is insufficient capital available, the Board will implement a sale process of the properties as outlined under its commitment to delivering liquidity section above. The Board will inform the market if there are any amendments to the indicative timetable.

Indicative timetable (subject to amendment)**Date (2019)**

Voluntary suspension of trading and announcement of Withdrawal Offer, Rights Issue and Public Offer	Monday, 4 February
Withdrawal Offer, Rights Issue and Public Offer opens	Thursday, 7 February
Withdrawal Offer and Rights Issue closes	Monday, 25 March
Public Offer closes	Monday, 8 April
Allotment of new units and confirmation of Withdrawal Offer	By Monday, 15 April

Mr Tom Forrest commented: 'We're very conscious of our commitments to deliver improved liquidity to unitholders and also that there are a range of differing investment preferences across the Fund's unitholder base. The liquidity event we are implementing reflects this and follows careful evaluation of the options available – including a potential sale of the properties. Overall, we are clear that the path chosen is best positioned to maximise value and flexibility for all investors including those wishing to continue their investment in the Fund, as well as those looking to realise their investment.'

Track record and capabilities

APN Property Group (APN), as Manager of the Fund, has a strong track record in managing assets and transactional experience with \$2.8 billion in Funds under Management. A selection of relevant examples includes:

- Established the APN 541 St Kilda Road Fund acquiring the property in May 2013. After undertaking significant leasing activity (increasing occupancy from 80% to 97%) and a number of property management initiatives, APN negotiated and secured an offer to sell the property in July 2014 – delivering an 27.7% IRR for investors.
- Established the APN Retail Property Fund in December 2016 raising over \$70 million in equity from existing APN distribution networks. The fund was subsequently combined with two other portfolios in July 2017 delivering exposure to a larger vehicle and liquidity to investors.
- Acquired a bulky goods site in June 2014 and redeveloped the centre into full-line sub-regional shopping centre. During development, APN negotiated an off-market sale of the property in December 2014 delivering a 54% IRR to investors on completion in April 2015.

As outlined earlier, as part of its active management approach a significant number of initiatives are underway or complete at the Fund's properties in Newcastle in order to maximise value for investors. Combined with our track record, the Board and the Manager remain committed to delivering a liquidity event that is fair to all investors, including those seeking to exit.

Further information

Further information on the liquidity event will provided as outlined above. If you have any queries in the meantime, please contact your financial adviser or APN Investor Services on 1800 996 456, email us at apnpg@apngroup.com.au or at the details below.

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About APN Regional Property Fund

The APN Regional Property Fund (Fund) is a direct real estate fund listed on the National Stock Exchange (NSX code: APR). The Fund is invested in two A-grade office buildings located in the Newcastle CBD, New South Wales.

APN Funds Management Limited (APN FM) is a wholly owned subsidiary of APN Property Group Limited, an ASX listed company (ASX code: APD) that manages approximately \$2.8 billion (as at 30 June 2018) of real estate and real estate securities on behalf of institutional and retail investors. APN is an active investment manager with a concentrated focus on income, and has been investing on behalf of its clients in commercial real estate since 1996.

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