Diversified Property Fund

Fund Update
30 June 2022

Established in August 2006, the Australian Unity Diversified Property Fund (Fund) currently holds 9 properties* in New South Wales, Victoria, South Australia and Western Australia. The Fund aims to deliver a stable income stream with the potential for capital growth. *Consolidated for reporting purposes.

Busselton Central Shopping Centre Stage 3 (artists impression of development), Busselton, WA

Fund Facts as at 30 June 2022

Gross Asset Value	Unit Price	June Quarter Ordinary Distribution~
$538.75 m	**$1.1972**	**1.4600 cents per unit (CPU)**
($612.31m at 31 March 2022)	exit price (cum distribution)	(1.3800 CPU March 2022 quarter)

Gearing Ratio	Portfolio Occupancy	Weighted Average Lease Expiry (WALE)
35.08%	**98.2%**	**8.8 years**
(43.13% at 31 March 2022)	(leased by income)	(by base rental income)

~ distributions are paid monthly

Ratings / Awards

Recommended
Lonsec Research

Core Property
Fund Research & Ratings
Recommended

Zenith
APPROVED

Performance as at 30 June 2022

	3 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	7 yrs % p.a.	10 yrs % p.a.	Since inception % p.a.
Distribution return	3.17	7.14	8.70	8.18	8.36	8.77	8.23
Growth return	(1.26)	0.43	4.34	4.86	6.22	4.39	0.99
Total return	1.91	7.57	13.04	13.04	14.58	13.16	9.22
Benchmark distribution return	0.70	2.87	3.10	3.43	3.72	4.28	5.15
Benchmark total return	2.60	11.63	5.59	7.16	8.62	8.73	7.91

Inception date for performance calculations is 22 August 2006.
Returns are calculated after fees and expenses and assume the reinvestment of distributions. Past performance is not a reliable indicator of future performance.
The Fund's Benchmark distribution return is 1% p.a. above the average Commonwealth Government 10-year bond yield calculated on a rolling basis over the previous five-year period. The Fund's Benchmark total return is the MSCI/Mercer Australia Core Wholesale Monthly Property Fund Index.

Contribution summary as at 30 June 2022

The relative contribution of major variables on growth returns over the last quarter and year.

Contributor	3 mths %	1 yr %
Property revaluations	1.70	4.67
Interest Rate Swaps (realised and unrealised marked to market movements)	0.00	0.00
Unrealised gains/losses on investments in listed/unlisted trusts	(0.74)	(1.19)
Performance fee	0.00	0.00
Capital distribution	(1.94)	(1.97)
Other	(0.28)	(1.07)
Growth return	(1.26)	0.43

Return calculations are based on actual distributions reinvested, which may vary slightly to the performance table illustrated above. Past performance is not a reliable indicator of future performance. Property revaluations are calculated in accordance with accounting standards and includes capital expenditure, lease incentives and/or commissions (both of which are amortised), this represents the increase/decrease from the property book value immediately prior to valuation. 'Other' may include: retained earnings during the period, swap break costs, estimated gains distributed, realised gains/losses on property, distributions from prior period retained earnings, realised gains/losses from unlisted property trusts and non-material movements.

Key portfolio statistics as at 30 June 2022

Geographical allocation (by value)

State	No. assets	%
NSW	3	39.47
WA	4	30.66
VIC	1	19.99
SA	1	9.87
Total	9**	100.00

** Consolidated for reporting purposes.

Sector allocation (by value)

Sector	No. assets	%
Retail	4	47.80
Convenience	2	28.03
Industrial	2	12.73
Office	1	11.45
Total	9**	100.00

** Consolidated for reporting purposes.

Top 5 tenants (by income)

Tenant	%
Caltex - Ampol	23.99
Woolworths	12.25
Coles	11.70
Australian Naval Infrastructure Pty Ltd	9.01
Boeing	3.87
Total	60.82

Property data

Number of properties	9**
Total number of tenants	114
WALE (by income)#	8.8 yrs
Occupancy rate (by income)	98.2%

** Consolidated for reporting purposes
# Excludes assets under development.

Financials

	$m
Gross assets	538.75
Total debt	188.99
Other liabilities^	5.28
Net assets	344.48

^ Other liabilities include a provision for the distribution.

Debt

Gearing (RG 46 ASIC definition)	35.08%
Loan-to-Value Ratio (LVR) (Financier's definition)	38.26%
Interest Cover Ratio (ICR) (RG ASIC definition)	3.96 times
Hedging (% of debt hedged)	0.00%

Valuations

Valuations during the quarter	2
Change in total direct property book value	2.79%
Change in book value of the properties revalued	2.72%

* Change in book value over the quarter includes revaluation impacts along with capital expenditure and other minor variations but excludes acquisitions and disposals.

Market commentary

The end of the 2022 financial year has coincided with a changing global and local economic and political environment. In particular, May 2022 saw a change in Federal Leadership with the Australian Labour Party elected, while the Reserve Bank of Australia (RBA) also began increasing the cash (interest) rates. Concerns over escalating inflation levels and the consequent rising cost of living are being experienced in many global markets, while geo-political pressures remain with the Russian-Ukraine conflict ongoing and COVID-19 constrained goods production in China continuing to hamper global supply chains. As a result, the June 2022 quarter saw increased volatility across financial markets, sensitive to economic changes as stakeholders adjust to a post COVID-19 financial environment.

As the direct implications of the COVID-19 pandemic subside, the Australian economy continues to perform relatively well with GDP growth of 0.8% over the March 2022 quarter, meaning the economy is now 4.5 percent larger than it was in Q4 2019 (KPMG, June 2022). A historically low unemployment rate, 3.9% in May 2022, together with reduced underemployment has resulted in significant tightness in the labour market, driving an acceleration in wages growth in some sectors. However, despite such labour supply restrictions, the Australian Bureau of Statistics (ABS) reported that year on year wage growth to March 2022 was 3.4% below the current inflation levels being experienced; albeit the national minimum wage level was increased by 5.2% in July 2022. Continued supply restrictions and a post COVID surge in demand for goods saw rising costs passed on to consumers who are also now also facing increasing mortgage repayment levels, surging energy costs and rising fuel costs as Government stimulus simultaneously rolls off. While household savings levels remain healthy, consumer demand is forecast to subside as increasing costs of living are absorbed which may serve to dampen economic growth expectations going forward. Inflation is currently forecast to peak at 7% (KPMG, June 2022) with NAB anticipating GDP to grow by 2.7% over 2022 (previously 3.4%) and a below-trend 1.8% in 2023 (previously 2.1%).

Following the cash (interest) rate increases in both May and June, July 2022 saw the RBA increase the cash rate by a further 50bps to 1.35%, its highest level since 2019. The decision was taken to combat rising inflation levels as the country winds back COVID-19 related stimulus following resilient economic performance. While current (official) headline inflation levels in Australia are c.5.1% (ABS March 2022), substantially above the RBA's target range of 2%-3%, it remains below levels currently being experienced by other western economies. As such, the RBA's somewhat hawkish approach to these initial rate rises would appear to reflect a desire to address the position sooner rather than later, arguably somewhat ironic given its sluggishness to commence rising rates in comparison to the stance taken by some other central banks globally. The attention is now at what level the cash rate is forecast to peak. In its July 2022 statement the RBA Board noted that they expect to take further steps to raise rates over the coming months, with decisions and timing to be guided by their assessment on the outlook for inflation and the labour market.

Preliminary data from Jones Lang LaSalle (JLL) noted positive net absorption (i.e., where take up of accommodation is higher than office space becoming vacant) in three of the six capital city markets for the June 2022 quarter. Negative absorption was noted in both Melbourne CBD and Sydney CBD markets despite Property Council of Australia (PCA) data continuing to demonstrate increasing office attendance in their May 2022 data. Consolidation of space from larger corporates together with an increase in backfill space from occupiers moving to recently completed developments was noted as increasing the vacancy in these markets. Effective rental growth was largely unchanged for the quarter with some minor positive movement recorded in prime rental levels in Sydney and Brisbane. Prime incentive levels were broadly stable across all markets; albeit they remain elevated with totals ranging across the six major CBD markets from c.24% to c.49% in Canberra and Perth respectively. Despite the relative uncertainty regarding the future of office use, recent CBRE research notes that since 2021, nearly three quarters of office CBD relocations have resulted in the same or higher market rents. This reinforces the 'flight to quality' narrative as occupiers choose to prioritise their workplace location, design and environmental credentials in order to attract and retain talent in the current, highly competitive staff retention setting. Despite rising bond rates, office property yield levels across the major CBD markets were effectively unchanged within JLL's latest data.

The industrial property sector has continued to perform relatively well over the quarter with over $1.8 billion in sales transactions recorded. While below the record levels achieved in 2021, this still sits substantially above the 10-year average of $1.16 billion industrial assets per quarter. JLL data highlight modest yield compression with the national industrial prime midpoint yield at 3.80% for the quarter. Industrial occupier demand remains strong nevertheless activity levels are being hampered by a lack of available stock. In a July 2022 report, CBRE reported that the national vacancy rate in the industrial property market is currently 0.8%, one of the tightest vacancy rates globally. As a result, competitive tension for accommodation is driving significant rental growth in the sector with Melbourne's West, North and South East precincts reporting average rental growth for the quarter of 7.3% (JLL). Despite some major completions, supply response continues to be constrained by rising construction costs and supply chain delays impacting feasibilities. As such, rental growth in the sector is forecast to continue in the short term with short lease duration industrial properties favoured by investors seeking to capitalise on the strength of the industrial rental market.

Australian retail sales climbed to record high levels in May 2022, the fifth month in a row of positive month on month sales growth. JLL reports that retail leasing demand over the quarter has been muted with most of the activity from those tenants looking to take advantage of current market uncertainty to expand store footprints as well as retail service tenants (hairdressers, opticians etc.) who have seen further uptick in patronage as concerns over COVID-19 become less prevalent in consumers' minds. Rental growth for the quarter has been largely flat across most categories, however CBD rents remain under pressure with Sydney in particular recording further falls. Essential spend shopping centres continue to be highly preferred by investors. This quarter SCA Property Group purchased a portfolio of 5 neighbourhood centres from Centuria for $180 million reflecting a fully let yield of 6.0%. Retail property yield levels have remained largely stable this quarter with JLL recording some softening (25 bps) across some of the slightly larger shopping centres in Sydney and Melbourne.

The pressures of rising inflation and further interest rate increases are anticipated to continue in the short term, as both businesses and consumers deal with escalating costs. From a property perspective the higher inflationary and interest rate environment is likely to impact individual assets and sectors to varying degrees going forward. It is worth noting most commercial real estate leases provide for annual contractual rent escalations, either indexed to inflation or a fixed amount, acting as a partial hedge against inflation. Some sectors such as industrial property are currently benefiting from strong underlying rental conditions while essential spend shopping centres, hospitals and childcare assets as an example continue to be highly prized by investors. In addition, Australia is regarded as a highly desirable destination by global real estate investors (JLL 2022). Overall, properties with strong underlying cash flow profiles and owned in investment structures with conservative debt and interest rate profiles are better positioned to weather any future market uncertainty.

Portfolio activity for this quarter

Developments

Blackburn Square Shopping Centre

Stage 1 of the Blackburn Square Development reached completion in mid-April 2022, with Coles commencing trade. Stage 2 construction commenced in late April 2022 with a projected programme of thirteen months. The head contractor for Stage 2 is Maben Group, with a contract value of $35m. Stage 2 comprises of a new Aldi, Woolworths Direct to Boot facility, medical centre, gyms, 102-place childcare centre, external dining precinct and approximately 35 specialty shops.

Stage 2 leasing is progressing well with 75% of net income pre-committed.

Busselton Central Shopping Centre

Busselton Central Shopping Centre Construction for Stage 3 of the redevelopment commenced in November 2021. The Stage 3 works underway comprise an additional 6,180 sqm of GLA with ~4,000 sqm of quality food and beverage on the ground floor to include a boutique tavern, as well as more than ten dining and retail stores including Benesse, Dome, Funkee Monkee Bar & Eatery, Asian Kitchen and Cotton On Mega. A new five-screen Reading Cinema will be located on level one. The state-of-the-art complex will feature Titan Luxe auditoriums with Dolby Atmos, bespoke dine-in menu options and powered full recliner seating. The centre will create a unique dining and entertainment experience for the Southwest region of WA.

Stage 3 leasing is at an advanced stage with 80% of leasing income pre-committed. The project is scheduled to be complete and trading in early 2023.

June 2022 property revaluations

Two of the Fund's properties were independently valued during June 2022, with a net increase of $5.27 million or 2.71% from the properties' book value immediately prior to valuation. Valuation changes include:

- Caltex Service Centres, Wyong NSW – The property's value increased by $5.30 million or 3.88% from the book value prior to valuation. This increase in value is primarily attributable to income growth.
- 1 and 2 Technology Place, Williamtown, NSW – The property's value decreased by 0.05% from the book value prior to valuation, with income growth largely offsetting a softening of the capitalisation rate due to the current macro-economic climate. The independent valuation remains unchanged at $58 million.

Sale of 20 Smith Street, Parramatta, NSW

During the quarter, the Fund disposed of 20 Smith Street, Parramatta, NSW for $87.251m, which was 4.5% above the previous book value. Settlement occurred on 30 June 2022.

Distributions

Following the sales of 19 Corporate Avenue, Rowville VIC on 22 December 2021 and 20 Smith Street, Parramatta NSW on 30 June 2022, a special distribution cash payment of 2.30 cents per unit was paid (capital gains) and a non cash attribution of 16.938 cents per unit for capital gains.

An ordinary cash payment of the Fund's regular income of 1.46 cents per unit was paid for the June 2022 Quarter which brings total ordinary distributions paid for the 2022 financial year to 5.90 cents per unit.

North Blackburn Shopping Centre Stage 2, North Blackburn, VIC

Busselton Central Shopping Centre Stage 3, Busselton, WA

Fund portfolio as at 30 June 2022

Property Details			Tenancy Details				Valuation Details			
Address	Note	Lettable Area (sqm)	Major Tenant	Number of Tenants	Occupancy Rate (% by income)	WALE (years by income)	Current Valuation ($m)	Valuation Date	Capitalisation Rate (%)	Book Value ($m)
Convenience										
Wyong Service Centres, Wyong, NSW	-	4,286	Caltex - Ampol	1	100.0	16.0	142.00	Jun-22	5.00	142.00
Sub total										**142.00**
Office										
1 and 2 Technology Place, Williamtown, NSW	-	7,557	Boeing	16	100.0	3.4	58.00	Jun-22	5.88	58.00
Sub total										**58.00**
Industrial										
Mersey Road North, Osborne, SA	-	8,006	Australian Naval Infrastructure Pty Ltd	1	100.0	8.0	50.00	Dec-21	5.00	50.03
6-8 Geddes Street, Balcatta, WA	-	9,992	IGA Distribution	2	100.0	1.5	14.45	Dec-21	6.00	14.45
Sub total										**64.48**
Retail										
Blackburn Square Shopping Centre, VIC	-	10,535	Coles	19	100.0	10.2	93.00	Dec-21	5.50	101.28
Dog Swamp Shopping Centre, WA	-	8,035	Woolworths	31	94.2	7.6	53.50	Dec-21	5.75	53.67
Busselton Central Shopping Centre, WA	-	7,171	Coles	19	94.9	6.1	48.56	Dec-21	6.00	52.46
Woodvale Boulevard Shopping Centre, WA	-	6,378	Woolworths	25	96.3	3.9	34.50	Dec-21	6.50	34.79
Sub total										**242.20**
Listed property										
Australian Unity Office Fund (AOF)										21.25
Cash and other assets										10.83
Total Cash and other assets										**32.08**
Total (T) / Weighted Average (A)				114 (T)	98.2 (A)	8.8 (A)	494.0 (T)		5.50 (A)	538.75 (T)

Notes

1 Valuation Policy - Regular valuation of underlying property assets is an important aspect of managing the Fund. Valuations are conducted by qualified independent valuers in accordance with industry standards. We also have a policy of generally obtaining independent valuations on Fund direct properties each year and, for assets under development, within an 18-month period. Additionally, as part of our active management approach, we may test asset values on market. At times we may enter arrangements at arm's length with third parties which may impact the value of assets within the portfolio including, but not limited to, put and call options in respect of all or part of an asset within the portfolio. If the value of an asset is impacted in this way, the value may replace the last independent valuation obtained.

2 Weighted Average Lease Expiry (WALE) by base rental income. Vacancies are valued at market income. Assets under development excluded.

3 A market capitalisation rate is the rate, expressed as a percentage, that reflects the likely yield a property will generate over the medium term. It has regard to a property's unique characteristics and is a measure of the property's risk/return profile with higher rates reflecting higher risk and its function is to convert a property's income into value. The market capitalisation rate is assessed by the independent valuer by dividing the stabilised net property income of the property or a portfolio of properties by the assessed valuation of the property or portfolio, excluding costs of acquisitions and fees.

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