Dexus Wholesale Australian Property Fund

APIR code: NML0001AU

31 March 2024

Summary

- Over the quarter, the Fund returned 1.48% as a quarterly distribution (or approximately 5.92% on an annualised basis). On average, over 80% of the quarterly distributions in 2023 were comprised of tax-deferred income. The total return was -1.50% due to a -2.98% growth component as cap rates increased by 24 basis points.
- At an operational level, the Fund continued to perform well: maintaining an occupancy above 95%; extending the weighted average lease term to 4.6 years; and maintaining a low level of income arrears. And within the retail portfolio, sales growth was generally very strong.
- There was substantial progress with the Fund's divestment program: CentralWest Distribution Centre – a property purchased for $49 million and valued at $57.5 million, immediately prior to covid, was sold for $92 million; 704-744 Lorimer St, Port Melbourne was exchanged and settled for a contract price of $61 million – an 11% premium to the 31 December 2023 valuation; and non-binding terms have also been agreed to sell 121 Evans Rd, Sailsbury at a price ahead of book value after an off-market negotiation.
- Construction at Crossbank 141 in Brisbane continued and once complete, it will be the fifth modern facility to be added to the portfolio in the last 12 months.

Key Objective

To provide income and long-term capital growth by investing in a diversified portfolio of Australian commercial properties and Real Estate Investment Trusts (AREITs).

Fund Facts	
Fund size (gross assets)	$2,035.6 million
Debt (% of gross assets)	25.8%
No. of Properties	26
Portfolio Occupancy	95.3%
Inception date	31 March 1985
Minimum investment	$10,000
Minimum suggested time frame	5 years
Management costs	1.01%
Buy/sell spread	Nil
Distribution frequency	Quarterly
Date of last distribution	31 March 2024
Distribution cents per unit	1.54

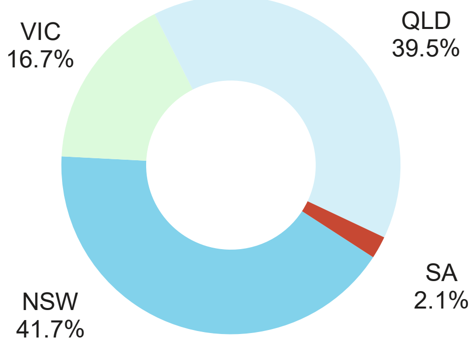
Fund Performance

	3 months %	1 year %	3 years %	5 years %	Since inception %
Distribution return	1.48	5.74	5.53	5.64	7.80
Growth return	-2.98	-25.46	-6.75	-4.98	0.16
Total return (after fees)	**-1.50**	**-19.71**	**-1.22**	**0.66**	**7.96**

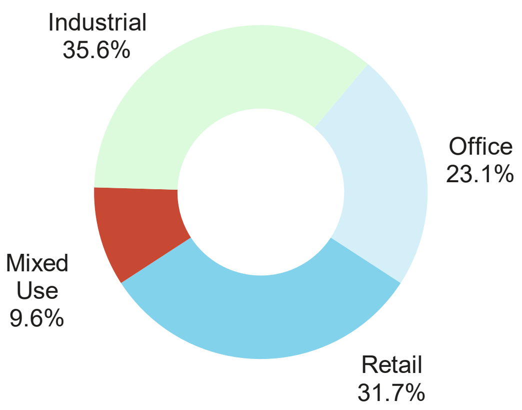
Past performance is not a reliable indicator of future performance.

Performance is annualised for periods greater than one year. Performance figures are calculated using exit prices, are net of management fees, ongoing fees and expenses, assume tax is not deducted. The Distribution return reflects total distributions paid from the Fund, while the Growth return reflects changes in the capital value of units.

Asset Allocation – by state



Asset Allocation – by sector



Fund Commentary

Over the quarter, the Fund returned 1.48% as a quarterly distribution (or approximately 5.92% on an annualised basis). On average, over 80% of the quarterly distributions in 2023 were comprised of tax-deferred income.

At an operational level, the Fund continued to perform well: maintaining an occupancy above 95%; extending the weighted average lease term to 4.6 years; and maintaining a low level of income arrears. Rental escalation provisions contained within the leases resulted in income rising and within the retail portfolio, the sales generated by the tenants was generally very strong.

However, commercial property values have softened substantially across the market in the last 12 months. This has primarily been a response to rising interest rates and declining confidence in the office markets from global capital. This quarter, there was a modest softening for industrial cap rates as evidence emerges that rental growth has peaked.

Property revaluations and sales resulted in a 1.7% decrease in the portfolio's value during the quarter. The main reason for this was an increase in the capitalisation rates used to value the properties in the industrial and business park portfolios. Excluding sold properties, the average cap rate across the portfolio sits at 6.42% (up 124 basis points from the peak of 5.18% in June 2022). The growth return at the Fund level was impacted by gearing, transaction costs, hedging and capex.

In Q4/2023, non-binding terms were agreed to sell CentralWest Distribution Centre. This property was purchased for $49 million and immediately prior to covid was valued at $57.5 million. A binding contract to sell the property for $92 million was exchanged and settlement is expected to take place in Q2/2024 (though this is subject to FIRB approval being received).

Following an open-market campaign launched in February, 704-744 Lorimer St, Port Melbourne was exchanged and settled for a contract price of $61 million. This represented an 11% premium to the 31 December 2023 valuation. Settlement is scheduled to take place in May 2024. Terms have also been agreed to sell 121 Evans Rd, Sailsbury at a price ahead of book value. This transaction was negotiated off-market it is expected that a binding contract will be signed, and the proceeds received in Q2/2024.

We will continue to assess the portfolio over the next quarter taking account: the objective of keeping the Fund's debt level low; the individual prospects of each asset and the markets they sit in; the support from stakeholders – in particular the platforms; and the monthly level of net applications/redemptions.

Private investors are active in the market. Five of the six properties which have been sold (or are in due diligence) are to experienced individuals or families who see an opportunity to take advantage of the re-rating that has happened and recognise the quality of the properties held by the Fund.

Construction of the Fund's facility at Crossbank 141, Brisbane continued and is on track for a Q4/2024 completion. Logistics tenant, Freight Specialists will then join Visy whose 15-year lease commenced in February 2024. Following the completion of this property, the Fund will have added five brand new buildings to the portfolio within a 12-month period and diversified into the mixed-use sector with the acquisition of the iconic property, The Mill – Alexandria. Paired with the sale of some of the fund's older assets, the overall quality of the portfolio, depreciation benefits and income security has been markedly improved.

Market Commentary

Australia's headline monthly inflation rate slowed to 3.6% in March 2024 and the 10-year bond yield has remained relatively steady at 4.1% over the past quarter. However stronger than expected labour force data in February has raised concerns that wages inflation may be persistent, keeping interest rates where they are for longer than previously expected.

Stronger economic growth means occupier markets for real estate may be more resilient than first thought. The longer-term demand outlook for the real asset sectors will be buoyed by population growth. Australia's population increased by 659,800 in the year to Q1 2024 (+2.5%) driven by a surge in net migration to around double the pre-COVID average.

The business sector has remained surprisingly resilient despite a weakening in confidence. Business investment grew by 8.5% in 2023. The unemployment rate remains low at 3.7%. Growth in the Australian economy slowed to 1.5% per annum in Q4 2023 as high interest rates continued to impact consumption spending. GDP growth is forecast to slow to 1.1% in Q2 2024.

Over the last quarter, both real asset performance and transaction markets have continued to be challenging. Transaction volumes have been at decade-low levels over the past year as investors adjust to the impact of higher costs of capital. Office sentiment has been affected by high levels of vacancy and caution about structural impacts of flexible working.

Investment demand is anticipated to pick up through FY25, assuming that interest rates are seen to peak and that investors gain a clearer understanding of the cost of capital and market pricing. Impressive performance by the listed real estate market in Q1 2024 is an encouraging sign for real assets more broadly as it reflects investor confidence and tends to be leading indicator for unlisted real estate values.

In the office sector, several key indicators are now pointing towards an improvement in market fundamentals over the next year or two. Net absorption in the Sydney and Melbourne CBDs turned positive in Q1 2024 after two negative quarters. Net face rents have grown in all markets through the quarter, with Brisbane CBD leading at 2.9%. The Brisbane and Perth CBDs continue to show the strongest improvement in vacancy, falling 2.5 ppts and 4.1 ppts in the past year respectively. Vacancy in Melbourne continues to diverge across precincts.

A contraction in the forward supply pipeline will serve to protect existing stock from supply risk and support rent growth through the cycle. Rising construction costs, interest rates and vacancy have put pressure on the feasibility for uncommitted developments. Capital is also diverting towards sectors with higher returns, shown by an increase in planned non-office developments in CBDs.

Industrial demand has tapered, with Sydney and Melbourne seeing a slowing in gross leasing take-up over the quarter. Occupier activity is often slower in the first quarter of the year so much will depend on how retail trends affect warehousing requirements over the next few quarters.

On various metrics the investment case for shopping centres is improving. Vacancies have fallen significantly since the pandemic across the main enclosed shopping centre types. City retail vacancies remain high but have plateaued. The return of international tourism has helped drive foot traffic in CBDs which is now approaching pre-pandemic levels.

Fund Manager

Christopher Davitt

Christopher is the Fund Manager for the Dexus Wholesale Australian Property Fund and has overarching responsibility for setting and executing the Fund's investment strategy and capital management plan.

Christopher works with Dexus's specialist teams to formulate asset plans for the properties, source and evaluate acquisitions and manage the portfolio's debt and equity. He joined the business in March 2010 having previously held research, transaction and funds management roles in Australia and Europe.

Balance Sheet – Dexus Wholesale Australian Property Fund

Assets/Liabilities	Valuation / Contract Price	Valuation Date	Cap rate	Occupancy	No. of Tenants	WALE*
Casula Mall	$195.0m	Mar-2024	6.00%	99.7%	64	3.0
Stud Park Shopping Centre	$136.0m	Mar-2024	6.50%	99.4%	63	5.6
Gasworks Plaza	$125.0m	Mar-2024	5.75%	95.1%	37	4.7
Brickworks	$136.5m	Mar-2024	6.00%	96.9%	57	2.9
The Mill, Alexandria	$180.0m	Mar-2024	5.50%	98.4%	15	4.2
Bond One, Walsh Bay	$112.0m	Mar-2024	7.25%	100.0%	4	3.6
636 St Kilda Rd, Melbourne	$60.0m	Mar-2024	8.00%	40.0%	24	1.4
425 Collins St, Melbourne	$39.0m	Mar-2024	5.75%	78.2%	5	3.1
199 Grey St, Brisbane	$82.5m	Mar-2024	7.50%	100.0%	13	2.8
Gasworks Workspace, Brisbane	$65.0m	Mar-2024	7.00%	84.6%	5	2.5
33 Park Rd, Brisbane	$44.2m	Mar-2024	7.50%	97.8%	9	2.1
Stanley House, South Brisbane	$29.0m	Mar-2024	6.00%	100.0%	2	7.5
Connect Corporate Centre B2, Mascot	$88.5m	Mar-2024	7.63%	98.8%	10	5.4
Connect Corporate Centre B3, Mascot	$139.0m	Mar-2024	7.63%	91.3%	15	4.7
Holbeche Industrial Estate, Arndell Park**	$65.0m	Mar-2024	5.25%	100.0%	5	4.3
384-394 South Gippsland Hwy, Dandenong	$24.3m	Mar-2024	5.75%	100.0%	1	3.6
2 Pound Rd West, Dandenong	$10.5m	Mar-2024	5.75%	100.0%	1	7.5
202-228 Greens Rd, Dandenong	$43.7m	Mar-2024	6.00%	100.0%	2	2.1
Crossbank 161, Trade Coast, Brisbane	$87.5m	Mar-2024	5.50%	100.0%	1	14.9
Crossbank 141, Trade Coast, Brisbane	$50.0m	Mar-2024	5.25%	100.0%	1	10.0
121 Evans Rd, Salisbury	$52.7m	Mar-2024	6.75%	100.0%	5	3.7
Acacia Gate Industrial Estate, Acacia Ridge	$35.8m	Mar-2024	6.50%	87.2%	9	2.3
7-9 French Ave, Brendale	$30.2m	Mar-2024	6.00%	100.0%	1	5.8
2 Second Ave, Mawson Lakes	$40.0m	Mar-2024	7.00%	100.0%	1	6.7
704-744 Lorimer St, Port Melbourne***	$61.0m					
CentralWest DC, Laverton North***	$92.0m					
Cash	$11.2m					
Total / Portfolio Average	**$2,035.6m**		**6.42%**	**95.3%**	**350**	**4.6 yrs**
Debt	$525.6m	25.8%				
Other liabilities	$90.5m					
Total	**$616.1m**					
Net Assets	**$1,419.5m**					

* Weighted Average Lease Expiry ** 50% interest *** Contracted price: settlement expected Q2/2024

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