



Direct Assets Review

Dexus Wholesale Australian Property Fund

ISSUE DATE: 9-05-2024

Fund financial position	December 2023*
TOTAL ASSETS	\$2152.8M
DEBT	\$698M
GEARING (DEBT/TTL ASSETS)	32.4%
GEARING	TARGET 0-15%; MAX 35%
UNIT PRICE	\$1.07

Portfolio summary	
NO. OF PROPERTIES	27
PROPERTY/ASSET TYPE	OFFICE 22%; RETAIL 30%; INDUSTRIAL 39%; MIXED USE 9%
PROPERTY LOCATION	NSW 40%; QLD 35%; VIC 23%; SA 2%
WTD AVG LEASE EXPIRY	4.5 YRS
OCCUPANCY	95.5%

Other Fund details	
APIR CODE	NML0001AU
DISTRIBUTION PAID	QUARTERLY
MINIMUM INVESTMENT	DIRECT \$10,000 (+\$5,000 LOTS)
INVESTMENT TERM	OPEN-END
REDEMPTIONS	MONTHLY
RESPONSIBLE ENTITY / INVESTMENT MANAGER	DEXUS CAPITAL FUNDS MANAGEMENT LIMITED
RELATED PARTY HOLDINGS	25.76%

RE/Manager fees & expenses	
ACQUISITION / SALE FEES	0.4% OF PURCHASE PRICE / 0.5% OF GROSS SALE PROCEEDS
ANNUAL FEES & EXPENSES	1.01% P.A.
BUY / SELL SPREAD	NIL
PERFORMANCE FEE	N/A

*Data as at, unless otherwise stated.

What this Rating Means

The 'Recommended' rating indicates that Lonsec has strong conviction the financial product can generate risk adjusted returns in line with relevant objectives. The financial product is considered an appropriate entry point to this asset class or strategy.

Strengths

- The Dexus Wholesale Australian Property Fund (DWAPF) gives investors exposure to a diversified portfolio of direct property difficult for retail investors to replicate.
- The ability to access institutional-grade direct property assets and leverage the depth of Dexus's direct property personnel and market links.
- The Manager has a conservative approach to gearing on its Australian direct property funds.
- The Fund has demonstrated its ability to provide consistent income over a long period.
- Total fees are significantly below the sector average.

Weaknesses

- Compared to some peers, the DWAPF is characterised by a relatively older asset portfolio with mixed tenant strength. However there has been ongoing investment by way of capital expenditure and maintenance.

Lonsec Opinion of this Fund

- Lonsec has maintained the Fund's 'Recommended' rating after the latest review. Lonsec continues to believe the Fund offers investors a high-quality diversified exposure to direct Australian real estate, which delivers a consistent and competitive income yield. The Fund is undergoing some proactive changes aimed at addressing higher gearing (still lower than peers) which Lonsec is supportive of, and the Manager has transitioned to new ownership under Dexus.
- The property portfolio has maintained a high occupancy (currently 95.5%), though there are pockets of vacancy in a few assets. The current weighted average lease expiry (WALE) has increased from 3.8 to 4.5 years and remains at the low end of the peer group. Nevertheless, the portfolio has around 360 tenants with lease expiries evenly spread over the next ten years and beyond.
- Total returns over the last few years have not kept pace with the peer group of open-end unlisted funds. This performance must be viewed in the light of the Fund's moderate gearing amongst its direct property peers. DWAPF's total returns over the long term have kept pace with wholesale fund benchmarks where gearing is lower.

We strongly recommend that potential investors read the product disclosure statement or investment statement. Lonsec Research Pty Ltd ABN 11 151 658 561 • AFSL No. 421 445 • This information must be read in conjunction with the warning, disclaimer, and disclosure at the end of this document. This report supersedes all prior reports.

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- The DWAPF's annual fee structure is in line with other open-end funds on a gross asset basis. Yet Lonsec's overall fee analysis reveals that the DWAPF is well below the average on a net assets basis. This is due to the Fund's lower gearing, modest property acquisition/disposal fees and no performance fee.

What is this Fund?

- The Dexus Wholesale Australian Property Fund is an unlisted property trust which primarily invests in direct property and may also invest in Australian listed property securities and cash to assist with managing liquidity and returns. As at 31 December 2023 the allocation was as follows:

Asset Class	Current	Target	Range
DIRECT PROPERTY	99.2%	> 75%	50% - 100%
LISTED PROP. SECS.	0.0%	< 25%	0% - 50%
CASH	0.8%		0% - 50%
TOTAL	100%	100%	

- The Fund aims to provide a reliable income return and long-term capital growth.
- The Manager has also indicated that there is potential to intensify the use of some assets through development, including into niche property sub-sectors (eg: medical/healthcare; data centres; student housing etc) where the Manager already has expertise. The long term objective is still to have a reasonably balanced spread of assets by property sub-sector, with the Fund increasing its allocation to these other sub-sectors over time.

Changes Since Previous Lonsec Review

Changes in the Fund's key metrics are summarised below:

	PREVIOUS REVIEW	THIS REVIEW
GROSS ASSETS	\$2208M	\$2153 (▼)
UNIT PRICE	\$1.38	\$1.07 (▼)
NO. OF PROPERTIES	26	27 (▲)
WALE (INCOME) - YRS	3.8	4.5 (▲)
OCCUPANCY	94%	95.5% (▲)
NO. OF DIRECT TENANTS	377	360 (▼)
CAP'N RATE (WTD AVG)	5.44%	6.18% (▲)
PRE-TAX YIELD	5.00%	5.58% (▲)
GEARING (DEBT/TA)	28.9%	32.4% (▲)

Using this Fund

This is General Advice only and should be read in conjunction with the Disclaimer, Disclosure and Warning on the final page.

- Lonsec notes that the Manager has produced a Target Market Determination (TMD) which forms part of the Responsible Entity's Design and Distribution Obligations for the Fund. Lonsec has sighted the TMD that has been provided by the Manager and notes that this should be referred to for further details on the Target Market Summary, Description of Target Market and Review Triggers.
- Forward looking estimates of returns are either sourced from the PDS forecasts or Lonsec estimates based on data supplied by the Manager, external valuation reports or other third-party data sources deemed to be reliable but are not a guarantee of future performance.
- While the returns of the Trust are expected to be less volatile than equities and listed property securities investments, investors should be aware that the Fund may experience periods of negative returns and that there is a risk of incurring capital loss on the Trust.
- As such, Lonsec considers the Trust suitable for medium to high-risk profile investors with a five+ year investment time horizon. The Trust will generally sit within the growth component of a balanced portfolio.

Risk Assessment

Lonsec rates the **key risk factors** associated with the DWAPF in the following table, which are assessed in the overall context of both competing unlisted property funds and relative to other asset classes.

Level of assessed risk	Low	Med	High
OPERATIONAL EARNINGS			
BUSINESS	●		
LEASING	●		
CAPITAL GAIN VS. INCOME		●	
DIVERSIFICATION	●		
MARKET VOLATILITY		●	
FINANCIAL			
LEVERAGE (GEARING)		●	
REFINANCING	●		
INTEREST COST / HEDGING		●	
CURRENCY	●		
COUNTERPARTY	●		
SUPPORT TO DISTRIBUTIONS	●		
MANAGEMENT & OTHERS			
EXPERIENCE	●		
INDEPENDENCE	●		
RELATED PARTY TRANSACTIONS	●		
LIQUIDITY			●

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Capital Gain vs. Income is deemed medium given that property funds have a higher element of capital risk than some other asset classes (e.g. cash or bonds).

Gearing Risk is considered moderate, given the Fund's target range of 0-15% and maximum 35%.

Refinancing risk is low as Lonsec considers that the DWAPF should have no difficulty in refinancing bank debt (on suitable commercial terms) given the low gearing and subsequent high headroom to covenants. In addition, the Manager has a good track record of being able to refinance its other debt facilities.

Interest Cost/Hedging is considered medium risk given the increase in gearing level and the low level of interest rate hedging.

No Related Party Property acquisitions or sales within the Fund. Therefore, related party transaction risk is deemed to be low.

Liquidity risk is deemed high due to redemptions are at the discretion of the RE and the possibility that assets may not be able to be sold and that other liquidity options (cash, property securities, debt or equity inflows) may be limited. This is opposed to listed entities where investors' units can be readily offered for sale on the share market. It should be noted that DWAPF has to date met all redemption requests in a timely manner.

Product

The Fund is an open-ended unlisted unit trust investing in both direct and indirect property (via investing in units in Property Trusts). Where the Fund acquires a property directly it may acquire the property through a sub-trust, which may be wholly or jointly owned.

Withdrawals and Liquidity

- Fund withdrawals are on a monthly basis and the Responsible Entity aims to pay withdrawal requests within 6 months. However, redemptions are at the discretion of the Responsible Entity as set out below.
- Redemptions are subject to the following:
 - While the Fund is 'liquid', unitholders may withdraw all or part of their investment monthly.
 - The RE aims to process withdrawal requests within 12 months.
 - When the amount of funds available for meeting all withdrawal requests is not sufficient, withdrawal requests may be paid in part or the limit can be waived at the discretion of the RE.
 - If the Fund were to be declared 'not liquid', redemptions would be at the discretion of the RE.
- This obligation may be met via the Fund's cash holdings; liquid A-REIT holdings, utilising the debt facility or by selling properties. Most closed-end funds do not offer liquidity facilities and open-end funds in Lonsec's peer group have an annualised cap (5%-10%).

- Nevertheless, unitholders and potential investors should take a **medium to long-term view of their investment (at least five years)**.

Fee Structure

- Management fee 1.01% p.a. of net assets.
- Acquisition / Disposal Costs: The Investment Manager may be paid for completing direct property transactions (acquisition fee of 0.4% of the purchase price; 0.5% of gross sale proceeds). Costs involved in the process of selling properties (e.g. agent's & legal fees) will be deducted from such proceeds and the net amount distributed to unitholders.
- It should also be highlighted that there is no 'poison pill' fee payable should the RE be replaced by way of unit-holder vote (Extraordinary Resolution) under the Corporations Act.
- There is no Performance Fee applicable to DWAPF.
- The level of gearing has a significant impact when comparing DWAPF against its peers as a proportion of net assets. DWAPF's total fees are considered to be significantly below the sector average.

Valuation Policy

- The Manager has properties externally valued on a quarterly basis, which is superior to industry best practice. During the COVID-19 period, valuations were undertaken on a monthly basis. Most funds revalue on an annual basis (part of the portfolio each quarter).

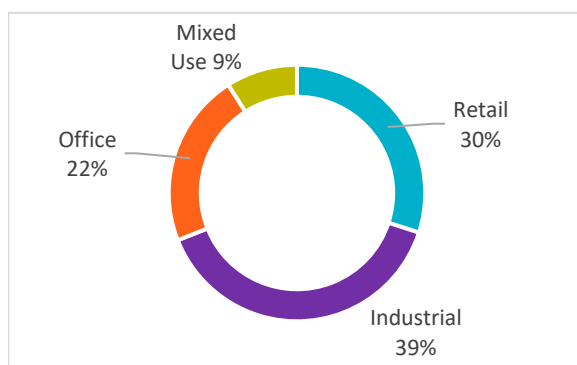
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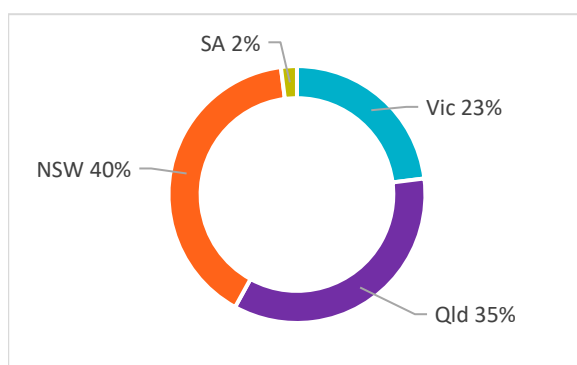
Property Portfolio

The Fund only holds Australian property, and the portfolio is well diversified, with a focus on the three main eastern seaboard state capital cities.

Assets by sector



Assets by location



Portfolio Strengths:

- Diversified portfolio across sectors, with presence in the major east coast metropolitan markets.
- 360 tenants, with strong ASX listed and national companies as well as Government departments that provide a sound underlying income.
- The backbone of the portfolio comprises four retail assets, anchored by food-based retailers (Coles, Woolworths, Ferry Rd Markets).
- Built-in rental growth clauses (CPI or above).
- Some capacity to add value through lease/rental negotiations tied to either area expansion or capital expenditure.
- 100% interest in 27 properties (more saleable than co-ownership).

Portfolio Weaknesses:

- Some older properties in the portfolio, although most of the buildings have been refurbished more recently and are generally in very good condition. That said, the Fund has added five brand new facilities to the portfolio in the last 12 months via developments in western Sydney and Brisbane.

- Relatively short lease expiry period of 4.5 years, although there is an even spread of major lease expiries over the next several years.
- A mixture of tenant covenant strength.

Main Tenants and Upcoming Leasing Expiries

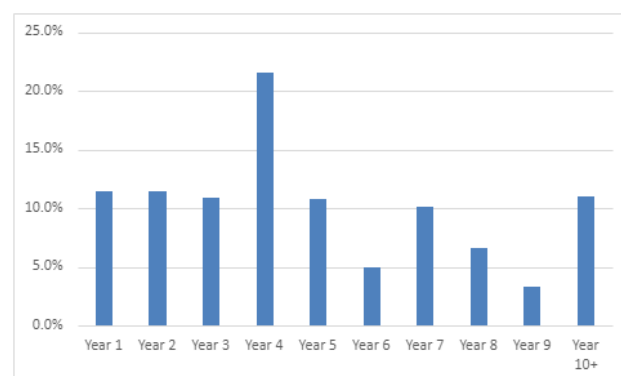
- The portfolio has a large number of tenants, with only a few representing more than 2-3% of total income from the direct property portfolio.

Top Tenants

Tenant (Property)	% Income (Dec '23)	Lease Expiry
DENTSU (WALSH BAY)	4.6%	MAY-2027
KMART (CASULA)	2.6%	SEP-2027
CODAN (MAWSON LAKES)	2.2%	DEC-2030
C'TH GOV'T DEPT OF AGRI (MASCOT)	2.0%	SEP-2027
COLES (CASULA)	1.8%	SEPT-2027
KONE ELEVATORS (MASCOT)	1.5%	SEP-2032
VISY (LAVERTON)	1.7%	OCT-2026
JAGUAR LAND ROVER (MASCOT)	1.4%	AUG-2030
WOOLWORTHS (STUD PARK)	1.2%	AUG-2033

- The leases generally have built-in rental growth in line with annual CPI increases, or alternatively fixed rental increases averaging around 3.0% to 3.5% pa. This will underpin a steadily growing income stream. There is a provision for market reviews generally every three to five years (and upon lease expiry).
- Lonsec anticipates most anchor tenants are likely to renew their leases or exercise optional extensions. However, the estimates of income make provision for a conservative probability of leases not being renewed.
- The portfolio has a lower WALE than many peers in the sector. However, the diversification provided by the number of properties and tenants is superior to most peers.
- The portfolio has a high occupancy of 95.5%, slightly higher than 12 months ago.

Lease Expiries



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Debt Position / Interest Costs

- The Manager has a debt facility which is syndicated across three major Australian banks and one major offshore bank, with the terms detailed in the following table.

Bank Loan Terms

FACILITY LIMIT	\$800M TOTAL
EXPIRY	\$65M (OCT 2025); \$275M (NOV 2025), \$85M (JAN 2026); \$375M (AUG 2026)
DEBT DRAWN DOWN	\$698.3M
LOAN TO VALUE RATIO (LVR)	32.4%
LVR COVENANT	50%
TARGET GEARING (MAX)	0%-15% (35%)
WEIGHTED AVE COST OF DEBT	6.0%
% HEDGED	42.9%
INTEREST COVER RATIO	2.5X
ICR COVENANT	1.8X

- The Fund's actual level of debt will fluctuate depending upon acquisitions, capital expenditure and the level of equity inflows.
- Hedging is currently at 42% and expected to increase over the next 12 months as asset sales are completed.
- Dexus's in-house treasury team will be involved in any hedging decisions regarding DWAPF.

Management

The Responsible Entity (RE)

- The RE of the DWAPF is Dexus Capital Funds Management Limited (DCFM). The Fund is also managed by the Responsible Entity.
- DCFM is a subsidiary of the ASX-listed Dexus ASX: DXS).
- Dexus is a fully integrated real asset group and manages real estate and infrastructure portfolio valued at over \$57.1 billion.

Management Team

Real Estate Investment Committee

Name	Position
ROSS DU VERNET	GROUP CEO & MANAGING DIRECTOR
DEBORAH COAKLEY	CHIEF EXECUTIVE, FUNDS MANAGEMENT
STEWART HUTCHEON	EXECUTIVE GM, INDUSTRIAL, HEALTHCARE AND ALTERNATES
KEIR BARNES	CFO
JONATHON HEDGER	EXECUTIVE GM, STRATEGY

Key investment decisions and the Fund's annual strategy must be approved by the Real Estate Investment Committee.

Key Fund Personnel

DWAPF & Other Senior Property Personnel

Name	Position
CHRISTOPHER DAVITT	FUND MANAGER - DWAPF
ANDY COLLINS	EXECUTIVE GENERAL MANAGER, OFFICE
MARCO ETTORE	EXECUTIVE GM, RETAIL

- Christopher Davitt** is the dedicated DWAPF Fund Manager with day-to-day responsibility for the management and performance of the Fund, assisted by the above and other professional staff. While the assets are managed by the Dexus Capital team, Chris is instrumental in instigating potential acquisitions or divestments. Chris joined the business in 2010 and prior to this was Assistant Fund Manager with MGPA in Europe.
- The listed property securities portfolio is managed within a separate DWAPF trust and according to the needs of the Fund. The Fund has the option to hold AREITs (none currently held), however it is unlikely an allocation will be made in the near term as the priority is to decrease the Fund's gearing level. The REIT allocation is usually used to manage excess liquidity when there are no imminent direct property acquisitions.
- Staff are incentivised by a bonus component, with a portion directly related to the performance (and risk profile) of the fund they are associated with.

Investment Process

Portfolio Construction

- The DWAPF has been positioned as a direct property fund with the long-term aim of investing 50-100% of its assets in direct property. It may also hold either property securities listed on the Australian Securities Exchange (A-REIT's), or cash (0-50%). These are mainly for liquidity purposes. That said, the PDS target is to hold 75%+ in direct property and REITs haven't exceeded 15% in the last 10 years.
- The Fund Manager is responsible for monitoring performance against benchmarks, including the analysis of capital management, tax and other issues.

Process

- The central aspect of the Manager's direct property process is the formulation of the following detailed plans:
 - A formal strategy and asset plan for each asset tailored to the Fund strategy over ten years.
 - A business plan sets more immediate objectives for the next 1-3 years.
- The plans are formulated at the acquisition due diligence stage or annually and reviewed quarterly.

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- Several personnel will be involved in various aspects to implement and monitor the actions of these plans. The Fund Manager has access to Dexus’s research team, which together with input from sector specialists, formulates Dexus’s House View for various property sub-sectors. The final House View has input from senior property executives to identify market trends, opportunities and risks. The unit utilises proprietary econometric models as well as external sources of information (e.g.: PCA; IPD and real estate agent publications).
- Key investment decisions and the Fund’s annual strategy must be approved by the Investment Committee (IC).
- Acquisitions and disposals are co-ordinated by Dexus’s Transactions Team that ties in asset managers, property managers and the DWAPF Fund Manager. A formal Transaction Committee is established to oversee the transaction on behalf of the Fund. After reviewing all due diligence material, a recommendation is put to the IC for consideration.

Apportionment of Deals

- Individual funds set their strategies and send a buyer’s brief to the Property Transactions Team. As opportunities arise, the first filter is to ascertain whether they meet the criteria of one or more funds. If more than one fund is interested, an asset allocation process is instigated. Each interested Fund Manager submits the maximum price, terms and conditions, as well as their ability to finance the transaction. The fund which is considered to have the greatest chance of succeeding is then selected and the Transactions Team will submit a bid on its behalf.

Lonsec Comment:

- Dexus has the largest direct property team in Australia, providing investors with access to strong industry relationships and scale efficiencies.
- The dedicated Transactions Team enables Dexus to be offered and involved in many transactions and can undertake due diligence and settlement quickly.

Potential Conflict of Interest / Related Party Issues

- Should a related party transaction occur there is a policy and process to follow, stipulating that any dealings are at an arms-length basis and on commercial terms.
- Related party entities own 25.76% of DWAPF units, with 6.6% held passively by the feeder fund (the Australian Property Fund). Investment decisions are directed by non-wholesale investors. The balance of 19.1% is held by Dexus.

Previous performance

- Since the DWAPF was established in 1985 it has delivered a consistent income return over 35 years, with a modest amount of gearing.
- In 2023, commercial property values softened substantially in response to sharply rising bond rates. This was compounded by a lack of confidence in the office and retail markets from global capital. This resulted in low liquidity and falling values across the market which were reflected in the Fund’s third-party valuations.
- In recent years, DWAPF income returns (5%-6%p.a.) have been lower than historical averages given the portfolio values (unit price) has risen on the back of tighter market capitalisation rates and higher incomes.
- It should be noted that income returns also include capital returns and therefore the growth returns shown in the table below are understated.
- Over the long term, DWAPF’s total return performance is in-line with sector benchmarks.

Returns (Net of Fees)

(to Dec 2023)	1 Yr	3 Yrs p.a.	5Yrs p.a.	10 Yrs p.a.	Incep. ¹ p.a.
DISTRIBUTION	5.58%	5.51%	5.62%	6.00%	7.81%
GROWTH	-23.24%	-5.05%	-4.14%	-0.92%	0.24%
TOTAL RETRUN	-17.67%	0.47%	1.49%	5.08%	8.06%

1: Inception date 31 March 1985.

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About Lonsec

Lonsec Research Pty Ltd (Lonsec) is an investment research house with specialist areas of expertise, that was originally established in 1994 and the current entity was registered on 23 June 2011. From 1 July 2011, Lonsec became a fully owned subsidiary of Lonsec Fiscal Holdings Pty Ltd, a privately owned and independent entity with a multi-brand strategy of providing leading financial services research and investment execution.

Lonsec believes that professional financial advisers need informed opinions on the best investment strategies and financial products to provide real value for their clients. To meet this need, Lonsec has in place an experienced research team, which draws on a robust research process to undertake in-depth assessment of managed fund products.

Analyst disclosure & certification

Analyst remuneration is not linked to the research or rating outcome. Where financial products are mentioned, the analyst(s) may hold the financial product(s) referred to in this document, but Lonsec considers such holdings not to be sufficiently material to compromise the rating or advice. Analyst holdings may change during the life of this document. The analyst(s) certify that the views expressed in this document accurately reflect their personal, professional opinion about the matters and financial product(s) to which this document refers.

Date released

May 2024

Analyst

Michael Elsworth

Approved by

Peter Green

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