Centuria

Fund Update
September 2023

# Centuria 8 Central Avenue Fund No. 2

(ARSN 605 264 211)

## Key points

- FY24 monthly distributions confirmed at 5.50 cpu (annualised) reflecting a yield of 7.5% on remaining original equity.
- 30 June 2023 Net Asset Backing confirmed at $1.74 per unit, in addition to early capital return of $0.27 per unit in March 2021.
- Level 8 leased to Kelloggs Australia on a 10-year deal following completion of the tenancy refurbishment in early 2023.
- The property is now 100% occupied with a weighted average lease expiry (WALE) of approximately 6.85 years.
- Fund term due for consideration prior to 1 January 2024. Investor correspondence to be issued shortly.

## Fund summary

Distributions for the **Centuria 8 Central Avenue Fund No.2** (Fund) have been paid in line with the FY24 forecast of 5.50 cents per unit (annualised). This distribution rate reflects a yield of 7.5% on remaining initial equity (following the early return of capital in March 2021). The corresponding distribution statement for the Fund is enclosed with this report and can also be accessed from our online investor portal at **CenturiaInvestor.com.**

We are pleased to report that the Fund's last remaining vacancy on Level 8 (1,257 sqm) has been leased to Kelloggs Australia for 10-years (with a break right at 6 years), expiring 30 September 2033. As a result, on a stand alone basis, this bolsters the property's WALE by approximately 0.23 years. The Fund is now 100% leased, with no major expiries until 2025. The new lease with Kelloggs provides excellent tenure and tenant covenant.

The 30 June 2023 audited financial report is now available to download from our online investor portal at **CenturiaInvestor.com.** The report confirms the Fund's Net Asset Backing (NAB) per unit reduced from $1.81 (as at 31 December 2022) to $1.74 (as at 30 June 2023). The 3.8% change in the NAB is a result of a minor reduction in the value of the Fund's share in the investment property (2.2% or $4.5 million for a 50% share). Unfortunately, elevated debt costs, attractive bond yields, term deposit rates and a challenging office sector are all currently having an impact on capital values. Despite these tough market conditions, we still maintain confidence in the resilience of high quality and well located commercial real estate, such as 8 Central Avenue, South Eveleigh NSW.

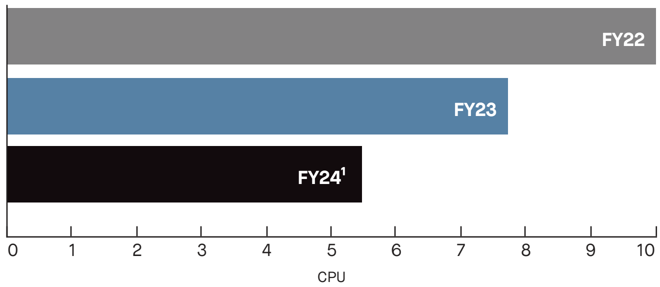
The Fund's current term is due due for consideration prior to 1 January 2024. Management will issue correspondence to Investors in the coming months outlining the current position of the Fund along with a recommendation relating to the future strategy for the Fund.

## Financial snapshot

| | |
|---|---|
| **Fund Commencement Date** | 1 July 2015 |
| **Net Asset Backing** | $1.74[1] |
| **Distribution Rate (cents per unit)** | 5.50[2] |
| **Weighted Average Lease Expiry (WALE) (years)** | 6.85[3] |
| **Next Investor Vote on Term of Fund** | 1 January 2024 |

## Distribution details

**ANNUALISED DISTRIBUTION**




1. FY2024 Forecast.

The reduction of distributions are directly a result of significantly higher interest costs following the Fund's interest rate hedges expiring in June 2023. Unfortunately, the loan and any fixed rate swaps are unable to be extended prior to the outcome of the approaching Fund term expiry which is due for consideration prior to January 2024. Specifically, the forecast cost of interest in FY24 has increased by ~$1.9m (or >3.0 cents per unit) in comparison to the prior year. The underlying property investment continues to perform well, with a 100% occupancy rate and a weighted average lease expiry of 6.85 years as at 30 June 2023.

The distribution rate for the remainder of the 2024 financial year is forecast to remain at 5.50 cents per unit (annualised) and reflects a yield of 7.5% on original equity (following the early capital return in March 2021).

1. Based on most recent audited accounts (30 June 2023) and after deducting the $0.27 early return of capital made in March 2021. Without the Mark to Market of the Fund's interest rate swap, the NAB of units in the Fund would remain at $1.74.
2. September 2023 quarter annualised.
3. As at 30 June 2023.

Noting the Fund does not have hedging arrangements in place, the Fund's 'all-in' cost of debt may fluctuate which may negatively (or positively) impact distributable income for the Fund. Please note, that the Fund is unable to enter into longer term hedging arrangements due to the approaching Fund term expiry. Should there be any material departures from the Fund FY24 forecast, an out of cycle Investor update will be provided. Looking ahead, and pending the result of the approaching Investor meeting, Management may enter into hedging arrangements to assist in mitigating interest rate volatility. More detail on hedging and distributions for the the 2025 financial year (if applicable) will be provided in the March 2024 Fund Update once there is greater clarity regarding the fund term and interest rates.

This forecast distribution rate reflects the current performance of the Fund and assumes all tenants will satisfy their contractual obligations under their respective leases within a timely manner. It also assumes there are no significant unforeseen capital costs and no material changes to the Fund's financial or interest expense obligations.

## Property details

| ASSET VALUES | |
|---|---|
| **Property Address** | 8 Central Avenue, South Eveleigh, NSW |
| **Purchase Price (Jul 15)** | $109.4m[1] |
| **Previous Valuation (Dec 22)** | $205.5m[1] |
| **Current Valuation (Jun 23)** | $201.0m[1] |
| **Cap Rate (Dec 22)** | 5.375% |
| **Valuer** | Director |

The key metrics of the 30 June 2023 valuation are outlined in the table above.

Referencing the market conditions outlined in the 'Fund Summary' section, the Australian property market continues to adjust following what has been a highly aggressive interest rate tightening cycle.

Following the board meeting on 3 October, the Reserve Bank of Australia (RBA) has opted to keep the cash rate on hold for a fourth consecutive month, suggesting recent counter-inflationary measures are beginning to take effect. Prior to this announcement, the four major Australian banks had revised their terminal cash rate expectations down, now sitting between 2.85% and 3.35%, and have forecasted the potential for interest rate cuts in late 2024.

However, it is important to note that major economists have highlighted the lingering risk of up to two rate hikes (+0.50%), should inflationary data surprise to the upside. Despite these challenging market conditions, we again maintain our confidence in the resilience of high quality and well located commercial real estate.

During this period of stabilisation, and dependant on prevailing interest costs, bond yields, term deposit rates and transactional evidence in the market, there may be continued pressure on distributions and valuations moving forward. Asa result, we will continue to monitor the market and take additional protectionary measures where required.

## Top five tenants by net lettable area (NLA)

| | |
|---|---|
| **Pacific Magazines**<br>Lease expires 31 Dec 2029 | 25.5% |
| **Government Property NSW**<br>Lease expires 30 Nov 2025 | 21.1% |
| **NEP Australia**<br>Lease expires 31 Dec 2044 | 18.8% |
| **Seven Network**<br>Lease expires 31 Dec 2029 | 15.8% |
| **SpeeDx**<br>Lease expires 31 Aug 2025 | 8.2% |

The property is now 100% occupied with a weighted average lease expiry (WALE) by income of approximately 6.85 years as at 30 June 2023.

## Property statistics

| | INITIAL[2] | DEC-22 | JUN-23 |
|---|---|---|---|
| **Net Asset Backing** | $0.90 | $1.81[3] | $1.74[3] |
| **Property Occupancy Rate** | 100% | 97% | 100% |
| **Weighted Average Lease Expiry (WALE) (years)** | 10.97 | 7.03 | 6.85 |

## Market overview

- The Sydney Fringe recorded negative net absorption of 12,413 sqm over the quarter to 30 June 2023. As a result, headline vacancy increased marginally by 0.1% to 7.7%.
- Prime gross effective rents decreased by 0.5% over the quarter, illustrating a Year-on-Year increase of 4.9%.
- Prime and secondary incentives remained relatively flat, with prime incentives stable at 29.5% and secondary incentives 0.1% lower at 25.5%
- There was no completions recorded over the quarter. There are currently four projects under construction that will add a total of 34,825 sqm to the market over the next 12 months.
- There were no sales recorded over $5 million in the Sydney Fringe over Q2 2023.
- Prime yields softened by 25 bps on the lower end and by 38 bps on the upper over the quarter to range between 5.38% - 6.13%.

Source: JLL Research Q2 2023

1. Based on 50% of the property.
2. Based on the Product Disclosure Statement dated 8 April 2015.
3. After deducting the $0.27 early return of capital made in March 2021.

## Debt summary

| | CURRENT PERIOD | LOAN COVENANTS |
|---|---|---|
| **Total Facility Limit** | $85.1m[1] | |
| **Undrawn Amount** | $4.4m[1] | |
| **Loan Expiry** | 8 Jan 2024 | |
| **% of Debt Hedged** | -[2] | |
| **Loan to Value Ratio (LVR)** | 39.3%[3] | 60.0% |
| **Interest Cover Ratio (ICR)** | 2.19[4] | 1.95 |

Under the terms of the debt facility, the Fund is required to comply with certain loan covenants over the course of the year. Based on the most recent audited accounts as at 30 June 2023, the Fund remains compliant with all covenants including the Interest Cover Ratio (ICR) and Loan to Value Ratio (LVR). Noting the recent increase in the interest rate expense for the Fund, management is closely monitoring the forward looking ICR for the Fund. Based on the Fund's current ICR forecast, management will require amendments to the existing facility covenants which we believe will be achieved prior to the debt facility expiry in January 2024. Management will keep investors abreast of any material developments in future investor updates.

## Centuria investor website

You can access all information relating to your Centuria investments at **CenturiaInvestor.com.au**.

## Contact details

If you require assistance with your Centuria Investor account or have any questions regarding your investment in the Fund, please contact Centuria Investor Services on 1800 182 257 (within Australia); +61 2 9290 9689 (outside Australia) or by email on **Property.Enquiry@CenturiaInvestor.com.au**.

**Note:** The latest RG46 Statement for the Fund is available at **CenturiaInvestor.com.au**. It includes gearing ratio (calculated using ASIC methodology), gearing covenant sensitivities, details of the related party transactions in the period and further information on the source of distributions.

1. As at 30 June 2023.
2. As at 30 June 2023. The Fund's existing heding rolled off in June 23, ahead of fund term expiry in December 2023.
3. The LVR is as at 30 June 2023 and based on the most recent independent valuation as defined under the debt facility agreement.
4. The stated ICR figures are based on the most recent audited accounts (30 June 2023).