Lonsec

Recommended

ISSUE DATE: 23-12-2021

Direct Assets Review
Cromwell Direct Property Fund

Fund Financial Position	As at Dec 2021
TOTAL ASSETS	$691M
DIRECT PROPERTY ASSETS	$587M
INVESTMENTS & CASH	$104M
DEBT - FUND	$282M
FUND LVR[1]	45.7%
FUND GEARING[2] (LOOK THRU)	38.6% (40.1%)
NTA/UNIT	$1.31
UNIT PRICE[3]	$1.35

Portfolio Summary	
NO. OF PROPERTIES	9 (7 DIRECTLY HELD)
PROPERTY TYPE[4]	OFFICE 100%
PROPERTY LOCATION[4]	QLD 71%; NSW 23%; VIC 3%; ACT 3%
WTD AVG LEASE EXPIRY	5.1 YRS
OCCUPANCY (BY INCOME)	95%

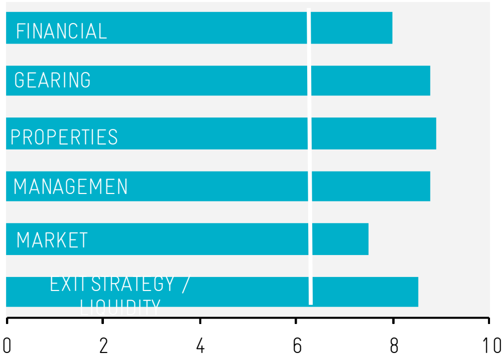
Fund Returns	Lonsec Estimates	
YEAR END JUNE	FY22-24	(RANGE)
DISTRIB. PER UNIT (INCOME)	7.40C	7.60C
PRE-TAX YIELD [3]	5.5%	5.6%
TAX DEFERRED	60%	60%

Other Fund Details	
RESPONSIBLE ENTITY	CROMWELL FUNDS MANAGEMENT LTD
APIR CODE	CRM0018AU
DISTRIBUTION PAID	MONTHLY
MINIMUM INVESTMENT	$10,000 (THEREAFTER $1,000 LOTS)
FUND INVESTMENT TERM	TERM EXPIRES 1 JULY 2025
REDEMPTIONS	MONTHLY (0.5% NET ASSETS) FULL LIQUIDITY EVENT EVERY 5 YRS (NEXT JULY 2025)
MANAGER FUND HOLDING	4.7%

Manager Fees & Expenses	
ACQUISITION FEE	2.0% OF GROSS VALUE OF DIRECT ASSETS[5]
ANNUAL FEES & EXPENSES	0.69% (GROSS); 2.05% (NET)[6]
DISPOSAL FEE	1.0% OF SALE PRICE
PERFORMANCE FEE	20% OF OUTPERFORMANCE ABOVE BENCHMARK (PCA/IPD UNLISTED RETAIL PROPERTY FUND CORE INDEX)
BUY / SELL SPREAD	NIL
R.E. REMOVAL FEE	NIL

1: Loan to direct property value (post CMW 4.7% stake in CDPF).
2: Gearing is Debt less unamortised loan transaction costs/ Total Assets (post CMW 4.7% stake in CDPF).
3: Unit price (ex-distribution) of $1.3483 as at 30 November 2021.
4: By CDPF share of gross assets.
5: Acquisition Fee of 2.0% may also be charged when Fund purchases units in a syndicate which has recovered its initial acquisition costs.
6: Includes indirect costs and performance fees.

Lonsec Rating of Critical Determinants



Conclusion and Ratings Rationale

Lonsec has downgraded the rating for the **Cromwell Direct Property Fund** ('CDPF', or 'the Fund') to **'Recommended'** due to a number of criteria being lower than at the last review and in relation to peers, including the portfolio property sub-sector diversification and building grade, WALE, occupancy, prospective fund returns, gearing and fees.

- Since Lonsec's last review, the CDPF has made two large acquisitions of Brisbane office buildings. While this has boosted the portfolio's exposure to Queensland from 44% to 71%, this is a market that Cromwell knows very well and was able to complete due diligence in its home state while interstate travel was restricted. The focus remains on finding value, but future acquisitions are likely to rebalance the exposure to other states.
- The purchase of the new assets has been partly funded by the sale of other direct assets or funds realised from the interests in Cromwell syndicates. The Manager has taken advantage of strong interest in two hardware properties and other assets within syndicates, realising prices above book values.
- One major tenant (International Education Services) and some smaller tenants were provided with $0.4m of rent relief during FY21 (44% of which is deferred rent). Post the new acquisitions, the portfolio tenant profile is more diversified (from 21 to 95 tenants), with 57% of passing gross rental income derived from Government organisations or listed companies.
- Post the divestment of long leased hardware properties and an industrial/logistics asset within a syndicate, CDPF is comprised of 100% office assets (including a small portion of retail tenants). This has resulted in the WALE reducing from 7.0 to 5.1 years, which is below the peer group average (for all types of property) of 8.4 years. Occupancy has also ticked down from 100% to 95%, with a 19% vacancy in the newly acquired 100 Creek St building. Given this is a B-grade building, the proportion of the portfolio represented by this grade rises to 30%.

Cromwell Direct Property Fund

- The Manager has a mandate to continue to build a portfolio of direct assets that meet the requirements of CDPF, although it now appears that the focus will be on office properties, rather than a diversified approach to property sub-sectors.
- However, there is some uncertainty in the office sector given the impact of COVID-19 lock-downs on tenant demand and the longer-term impact of the work-from-home trend. Sydney and Melbourne are seeing CBD's gradually recover and occupancy is expected to pick-up considerably from late January 2022 (assuming no further lock-downs). Globally, there is strong demand for A-grade and above space that provides modern and safe amenity for a more flexible workforce.
- In order to complete recent acquisitions, the Fund has established and drawn down on further debt facilities. Gearing (LVR) is currently 48.3% which is just under the 50% bank covenant. Post CMW making an investment of about 4.7% into CDPF during December 2021, gearing (LVR) will reduce to 45.7%. This is high compared to Lonsec's peer group.
- Furthermore, the syndicate investments have separate debt funding arrangements, with varying maturities and attractive / flexible funding terms. On a look-through basis, gearing (Debt*/Total Assets) is 40.1% post the CMW investment in CDPF.

  (Note* - Less unamortised transaction costs)
- On current monthly net equity inflows the CDPF gearing should reduce to around 30%-35% (LVR) in twelve months.
- The Fund's estimated **distribution yield** (both on a pre-tax and after-tax basis) is slightly below the peer group average. Total returns of the CDPF have been strong in absolute terms achieving 9.9% p.a. (6.0% income and 3.9% growth) since inception just over eight years ago. In relation to Lonsec's peer group, the CDPF has slightly underperformed the average by -1.7% to -1.9% during the last five years.
- On Lonsec's fees analysis including data provided by the Manager on indirect costs and performance fees, the **Fund's overall fees and expenses are higher than the Lonsec peer group** on both a gross and net assets basis. The Performance Fee share of 20% excess above the Benchmark is at the high end of Lonsec' sample of unlisted property funds and Lonsec would prefer to see a performance fee payable only if the Fund achieved a positive return. There could also be some double charging if performance fees at the underlying syndicate level (20% share above 10% p.a. return) are triggered.
- The CDPF **net asset backing** is equivalent to $0.97 on a per dollar invested basis, is slightly above the average for open-end funds and well above that for closed-end funds as a lot of the establishment costs have already been absorbed by the Fund.
- Lonsec has observed the change in the Cromwell Property Group Board and note that there has been a refresh of a number of directors, although the majority of independents has remained. Oversight of the Fund by the Cromwell Funds Management Board remains largely unchanged, with all the independent/ external directors continuing in their roles.
- The change in CEO and recent changes to the personnel at Cromwell Funds Management / Cromwell Direct Property Fund will be monitored by Lonsec. A positive change is that CMW has committed to a permanent holding in the Fund (initially 4.7% of units). Along with some senior management having holdings in the Fund, this shows an improved alignment of interest with investors.
- Cromwell retains an experienced team of property professionals, who have demonstrated an ability to make sound strategic decisions and form strong relationships with industry participants for the benefit of investors.
- The Manager offers investors a **limited monthly redemption facility** up to 0.5% of the Fund's net asset value per month (6% p.a.) but can be higher if the Fund's cash exceeds 6% of assets. On the lesser amount, the Fund's liquidity feature is lower than the peers average of around 8% p.a. of net assets.
- The Manager also intends to offer a **full Periodic Withdrawal Opportunity**, with the next scheduled on or around 1 July 2025 and thereafter every five years.
- While the individual properties could readily be sold in normal market conditions, it has been shown with similar fund-of-funds during financial market crises, disposing of investments in unlisted funds may not be readily completed.

Changes Since Previous Lonsec Review

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

	PREVOUS REVIEW	THIS REVIEW
GROSS ASSETS	$405M	$691M (▲)
UNIT PRICE	$1.24	$1.38 (▲)
NO. OF ASSETS - DIRECT (INDIRECT)	6 (3)	7 (2) (-)
WALE (INCOME) - YRS	7.0	5.1 (▼)
OCCUPANCY	100%	95% (▼)
NO. OF DIRECT TENANTS	21	94 (▲)
PRE-TAX YIELD	5.9%	5.5% (▼)
CAP'N RATE (WTD AVG)	6.13%	5.85% (▼)
GEARING (LOOK-THRU)	27%	40% (▲)

- In May 2021, the Fund acquired a 100% interest in 545 Queen St, Brisbane for $117.5m (excluding costs).
- In December 2021, the Fund acquired a 100% interest in 100 Creek St, Brisbane for $184.7m ($199.0m including costs).
- The Funds 100% interest in Bunnings Munno (SA) was sold in August 2021 realising $48.8m (before costs).
- The property owned by the CICHT (117 Brisbane Rd, Ipswich) is being sold and CDPF's interest in this Fund is expected to realise $13.5m.

Cromwell Direct Property Fund

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.

Fund Strategy/Objective

- Cromwell Direct Property Fund is an unlisted property trust which invests in a portfolio of direct properties and unlisted trusts with a cash reserve.
- The Fund invests in non-residential Australian property, with a primary focus on commercial, industrial and retail property. The property trusts invested in may be operated by Cromwell or other managers.
- The Fund aims to provide investors with a monthly tax advantaged income, along with the potential for capital growth.
- The Fund aims to deliver a total return (after fees) in excess of the PCA/MSCI Unlisted Retail Property Fund Core Index over rolling three year periods.

Risk Assessment

- Lonsec rates the **key risk factors** associated with the Cromwell DPF in the following table, which are assessed in the overall context of both competing unlisted property funds and <u>relative to other asset classes</u>. Taking all these factors into consideration, Lonsec considers an investment in the Fund to be of **low to medium risk.**
- **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 high at 46% (LVR as at December 2021) compared to Lonsec's unlisted peer group average of 38%. The gearing of the Fund (Debt/Total Assets and on a look-through basis) of 40% is lower and has historically been managed well below the 50% maximum. CDPF's gearing is expected to reduce on current net equity inflows.
- The risk of **Related Party Transactions** is deemed medium as some of the Fund's property and leasing services are provided by other CMW entities. The Manager will also utilise Cromwell's internal resources, with clearly defined protocols for managing conflicts of interest.
- While the **liquidity** of separate interests in direct properties and other unlisted property trusts in theory may be more liquid than ownership of units in a single unlisted property trust, liquidity risk in the unlisted property sector is regarded as high compared 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			●

Cromwell Direct Property Fund

1. Properties

1.1 Portfolio Overview

- The portfolio consists of investments in nine properties via 100% ownership of seven direct properties and two properties via Cromwell syndicates.
- Since the last Lonsec review, the Fund has sold one and purchased two direct properties (all 100% interest) and one syndicate investment property has been sold – with the proceeds distributed to unitholders (including CDPF) in November 2021.

Assets by sector

- The Fund is currently invested only in the **office property** sector, although some buildings have a small retail tenancy component. While the Fund has the capability to invest in industrial and retail properties (it has owned hardware properties in the past), the Manager has indicated that the Fund will predominantly invest in office properties.

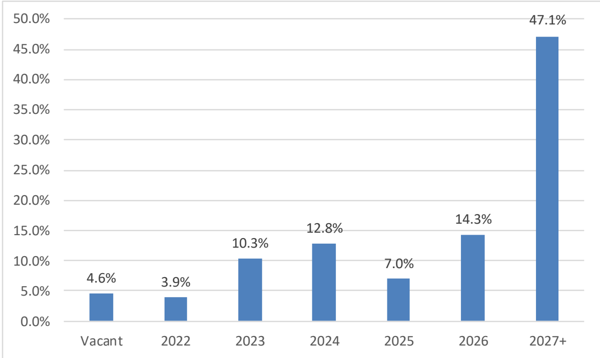
Assets by location

- The latest two acquisitions of direct properties have been in Brisbane, bringing the Fund's exposure to Queensland up from 44% to 71%. As a result of this, the Fund's exposure to NSW has reduced from 36% to 23%. The representation in South Australia has dropped from 9% to zero following the sale of the property located there.
- The changes in geographical exposure is more a result of opportunities to realise and purchase assets at attractive prices, rather than a deliberate strategy to gain exposure to a particular location. As further portfolio changes are made, the high exposure to Queensland is likely to reduce.

1.2 Tenants and Leases

- The Fund's Weighted Average Lease Expiry (WALE) has reduced from 7.0 to 5.1 years which is lower than Lonsec's peer group average.

Lease Expiry by Year



Source: Cromwell as at 2 December 2021.

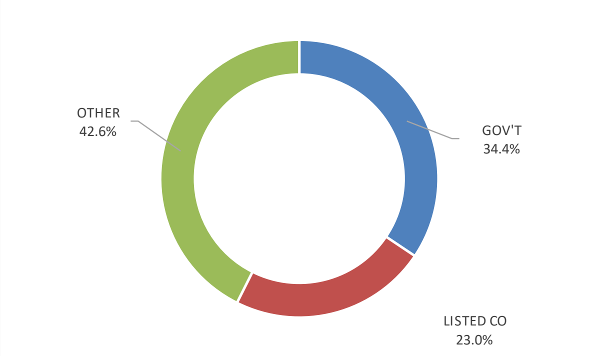
- From the following table of top ten tenants, there is a cluster of expiries in 2028/2029/2030, but generally the lease expiries are now more evenly spread than at the last review.

Top Ten Tenants

TENANT (PROPERTY)	% GROSS INCOME	EXPIRY
ERGON ENERGY (T'VILLE)	10.6%	2029
ENERGEX (NEWSTEAD)	9.4%	2026
INT'NAL EDUCATION SERVICES (SPRING HILL)	6.6%	2030
WINC AUSTRALIA (MASCOT)	6.3%	2028
GOV'T PROPERTY NSW (QUEANBEYAN)	5.5%	2028
CONTAINER EXCHANGE (CREEK ST)	3.6%	2023
SONIC HEALTHCARE (QUEEN ST)	3.4%	2029
ELECTROLUX (MASCOT)	3.3%	2030
CALIBRE PROFESSIONAL (QUEEN ST)	3.0%	2024
OTW CORP (CREEK ST)	2.6%	2027

As at December 2021.

Tenant Type



1. Based on CDPF's gross income as at December 2021

- Tenants are of high quality with **57% of major tenants being the Federal or State government, an entity owned by the government, or a listed company**. This compares favourably to peers and has been noted by Lonsec over a number of years.
- Rent relief paid out for the Fund during the COVID-19 lock-down periods was to **International Education Services** (IES), a not-for-profit English language service materially affected due to border restrictions impacting on the entry of international students.
- With $30m annual turnover, IES sought rent relief under the government mandated Code of Conduct. Rent relief totalling 3.2% of the Fund's gross rental income ($705,490) was provided. This was split 50% waived and 50% deferred. IES is a significant tenant for the Fund, contributing 6.6% of gross income (just under 10% prior to the pandemic in 2020).
- IES is now back to paying full rent and IES has taken steps to diversify their income by becoming a certified 'IAB' school, with a student intake expected early 2022.

Capital Expenditure

- The majority of the properties were recently constructed, are of a high standard and require little immediate capital expenditure. The portfolio is further improved by high quality environmental ratings on many of the office properties.

Cromwell Direct Property Fund

1.2 Overview of Fund investments

PROPERTY	STATE/ TERR.	TYPE	OWNERSHIP BY FUND (%)	INDEP. VAL'N DATE	U/LYING PROP VALUE $M	CDPF SHARE (GROSS) $M	% PORT	CDPF SHARE (NET) $M	PROP. NET INCOME $M	INCOME YIELD YR1	NET LETT. AREA (100%) SQM	OCCUP.	CAP'N RATE	DISC. RATE	WALE (INC.) YRS	MAJOR TENANTS
DIRECT INVESTMENTS									(NET)	(NET)						
100 CREEK ST, BRISBANE	QLD	OFFICE	100%	Sep-21	184.7	184.7	27.3%		9.70	5.3%	20,223	81%	5.75%	5.75%	2.6	Vale Australia, Over The Wire, DSS
545 QUEEN ST, BRISBANE	QLD	OFFICE	100%	May-21	117.5	117.5	17.3%		6.98	5.9%	13,363	100%	6.00%	6.25%	4.0	Sonic Healthcare
163 O'RIORDAN ST, MASCOT	NSW	OFFICE	100%	Jun-21	117.0	117.0	17.3%		6.53	5.6%	13,493	100%	5.50%	6.25%	5.3	Winc Aust; Electrolux
420 FLINDERS ST, TOWNSVILLE	QLD	OFFICE	100%	Sep-21	70.0	70.0	10.3%		5.17	7.4%	7,929	100%	6.00%	6.50%	6.8	Ergon Energy (Energy Queensland)
433 BOUNDARY ST, SPRING HILL	QLD	OFFICE	100%	Dec-20	39.0	39.0	5.8%		2.96	7.6%	5,997	100%	6.75%	7.00%	7.7	International Education Services
11 FARRER PLACE, QUEANBEYAN	NSW	OFFICE	100%	Dec-20	38.0	38.0	5.6%		2.21	5.9%	6,300	100%	6.00%	6.25%	6.8	NSW Gov't
64 ALLARA ST, CANBERRA	ACT	OFFICE	100%	Mar-21	18.5	18.5	2.7%		1.31	7.1%	3,155	100%	6.25%	6.50%	3.9	Jacobs Intern'l; Peet; Knight Frank
TOTAL DIRECT					584.7	584.7	86.3%		34.85	6.0%						
SYNDICATE INVESTMENTS																
CRT (33 BREAKFAST CREEK RD, NEWSTEAD)	QLD	OFFICE	22.4%	Sep-21	358.8	71.1	10.5%	50.2	20.38	5.7%	30,604	99.8%	5.75%	6.00%	8.4	Energex Ltd (Energy Queensland)
CICHT (117 BRISBANE ST, IPSWICH)	QLD	OFFICE	14.3%		0.0	0.0	0.0%	13.4								
CPT12 (19 GEORGE ST, DANDENONG)	VIC	OFFICE	15.8%	Oct-21	124.0	21.4	3.2%	15.3	6.46	5.2%	13,865	100%	5.25%	5.88%	8.8	ATO (Commonwealth Govt)
TOTAL INDIRECT					482.8	92.5	13.7%	78.9	26.84	5.6%						
TOTAL/WTD AVG					1067.5	677.2	100.0%		61.69	5.8%		94.8%	5.85%	6.15%	5.1	

1: CRT (Cromwell Riverpark Trust.)
2: CICHT (Cromwell Ipswich City Heart Trust) – building sold Oct 2021 and fund currently being wound up.
3: CPT12 (Cromwell Property Trust 12.)
4.CDPF share of gross property assets are valued at $677m. This differs from the value in the balance sheet (p.g.13), due to the underlying property syndicates being recorded in the balance sheet at their net tangible asset (NTA) value, as opposed to their gross asset value.

Cromwell Direct Property Fund

Assessment of Fund investments

	% PORTFOLIO (GROSS)	LOCATION / INFRA.	BUILDING CONDITION	TENANTS / LEASES	MARKET / POTENTIAL	NABERS ENERGY[1]	NABERS WATER[1]	GREEN STAR
DIRECTLY HELD								
100 CREEK ST, BRISBANE	27.3%	EXCELLENT	GOOD	GOOD	EXCELLENT	5.0	4.0	
545 QUEEN ST, BRISBANE	17.3%	EXCELLENT	GOOD	EXCELLENT	GOOD	5.0	-	
163 O'RIORDAN ST, MASCOT	17.3%	EXCELLENT	EXCELLENT	GOOD	EXCELLENT	5.0	3.0	
420 FLINDERS ST, TOWNSVILLE	10.3%	GOOD	EXCELLENT	EXCELLENT	AVERAGE	5.5	5.5	
433 BOUNDARY ST, SPRING HILL	5.8%	GOOD	GOOD	GOOD	GOOD	NR	NR	
11 FARRER PLACE, QUEANBEYAN	5.6%	GOOD	EXCELLENT	EXCELLENT	AVERAGE	5.0	5.0	
64 ALLARA ST, CANBERRA	2.7%	GOOD	GOOD	AVERAGE	GOOD	4.5	5.0	
INDIRECTLY HELD (VIA SYNDICATES)								
ENERGEX HOUSE	10.5%	EXCELLENT	EXCELLENT	EXCELLENT	EXCELLENT	5.5	4.0	
ATO DANDENONG	3.2%	GOOD	EXCELLENT	EXCELLENT	GOOD	5.5	6.0	6.0

1.Only office buildings can get a NABERs rating. Therefore, retail and industrial properties are not rated by NABERs. 433 Boundary Street does not require NABERs criteria because it is exempt being an educational facility, rather than office space.

Cromwell Direct Property Fund

	Strengths	Weaknesses
100 Creek St, Brisbane	• Excellent location in 'golden triangle' of Brisbane CBD. • Although B-grade building constructed in 1977, periodic refurbishment (last 2018). Floor to ceiling windows gives good light and views. • Flexible floor plates which suit sub-division. • Diversified tenancy profile (47 total)	• Current vacancy of 19% of space (9 tenancies) which is not covered by a vendor rental guarantee. • Relatively short WALE of 2.6 years. • Outstanding incentives of $9.8m (although acquisition price adjusted for this).
545 Queen St, Brisbane	• A-grade building significantly refurbished in 2008 (five star NABERS Energy). • Fully let with top four tenants making up 63% of total (including ASX-listed Sonic Healthcare 20% and Dept of Defence 12%). • Fixed rental increases (CPI to 4% p.a.) and lease expiries reasonably well spread.	• Peripheral location on edge of CBD. • Podium floor plates are large and irregular shape, which may result in NLA loss if split.
163 O'Riordan St, Mascot	• The property is well located, being within walking distance of Mascot Station and close to Sydney Airport. • A-Grade office building, constructed in 2007, with a five-star NABERs energy rating. • Long-term, the general area has excellent development potential. • The property is slightly under market rent, but good value compared to CBD.	• Secondary non-CBD location. • While noting that 163 O'Riordan St is fully let, competitor building nearby at 185-191 Riordan St 'Connect Corporate Centre' comprises 38,303sqm of office.
11 Farrer Place, Queanbeyan	• Built in 2008, the property is fully let to the NSW Government until 2028. The tenant is of a high quality and is committed for the long term. • While in a fringe market, Queanbeyan is only 15km from the Canberra CBD.	• The property is the premiere building in the city and is of a standard well above the market average. Given the niche market and limited/no comparable transactions, the sale price of the property may vary significantly from the valuation.
420 Flinders St, Townsville	• Major tenant is **Energy Queensland** (93% NLA), a Queensland State-Owned Corporation. • Good WALE of 6.8 years remaining, with fixed rental increases of 4% p.a. • A-Grade office building last refurbished in 2013. 5 Star NABERS Energy and Green Star Ratings.	• The property is over market rent. • Given the comparatively thin market in Townsville for this type of property, there may be some unpredictability in the sale price should the building be sold.
433 Boundary St, Spring Hill	• Good WALE of 7.7 years by income. • Primary tenant, **Independent Education Services Limited (IES)**, has exclusive agreements with leading organisations such as the University of Queensland to be a feeder university for international students. • IES is diversifying its student base to IAB domestic students. • Large site area of 3,776sqm provides some potential for the property to be incorporated in either tenant development plans (eg: residential) or alternative use (healthcare).	• IES is a Brisbane-based not-for-profit organisation and is deemed a lower quality tenant than a government entity or long-running, profitable, ASX-listed company. • High tenant concentration risk with IES the sole tenant of the property (aside from Wilson Carparking). • Pandemic risks remain that international students may not be able to travel to Australia.
64 Allara St, Canberra	• Modern A-grade building with good car park allocation (4.1 per 100 sqm). • Major tenants include **Jacobs International** (US based engineering firm); **Peet Group**; **Knight Frank** property group. • Minimum short and medium-term capital expenditure anticipated. • Good location with broad purpose clause permitting alternate use (hotel/residential).	• Fringe Canberra CBD location. • Although improved, relatively short WALE of 3.9 years.

Energex House	• A-grade office building with 6-star Green Rating and 5.5-star NABERS Energy Rating. • Excellent location within 2kms Brisbane CBD. Was the first major office development in the Riverpark/Gasworks precinct in 2010. Considerable office development has occurred in the area since. • 92% leased to **Energex** (Queensland Government entity) with long WALE of 8.4 yrs and 3.75% or CPI (whichever greater) annual rental increases. • Large floor plates & expensive tenant fit-out.	• Leasing risk due to limited re-leasing opportunities on a single tenant basis. • The Brisbane 'near city' office market has considerable competition for tenants.
ATO Dandenong	• Modern building purpose built for the **Australian Tax Office (ATO)** completed in September 2015. • 92% leased to a Commonwealth Government tenant with a long WALE of 8.8 years and 3.75% p.a. rental increases.	• Secondary suburban location. • Lower level retail has no main street frontage. • The property's current Net Passing Income is above the Valuer's assessed Net Market Income resulting in the potential for a decrease in rent if the ATO was to vacate the building.

Cromwell Direct Property Fund

2. Financial Analysis

2.1 Income / Expense analysis

Year end	FY22 $m	FY23 $m	FY24 $m
NET PROPERTY INCOME (DIRECT)	31.000	36.500	35.600
INCOME SYNDICATES*	3.200	0.800	0.900
CAPITAL RETURN SYNDICATES	16.800		
TOTAL INCOME	51.000	37.300	36.500
RE MANAGEMENT FEE	-3.000	-3.600	-3.600
OTHER EXPENSES	-0.500	-1.400	-1.500
INTEREST EXPENSE	-5.600	-9.000	-8.200
TOTAL OPERATING EXPENSES	-9.100	-14.000	-13.300
NET OPERATING INCOME	41.900	23.300	23.200
INCOME SUPPORT (RETAINED)	-2.780	-0.680	-0.300
NET DISTRIBUTION PAID	39.120	22.620	22.900
WTD AVG UNITS (MILL)	301.500	301.500	301.500
TOTAL DISTRIB./UNIT	12.98c	7.50c	7.60c
CAPITAL DISTRIB./UNIT	5.57c		
INCOME DISTRIB./UNIT	7.40c	7.50c	7.60c
INCOME YIELD (ANNUALISED)	5.49%	5.56%	5.63%
% TAX DEFERRED	60%	60%	60%

1. Lonsec estimates.

The above income and expense estimates are based on:

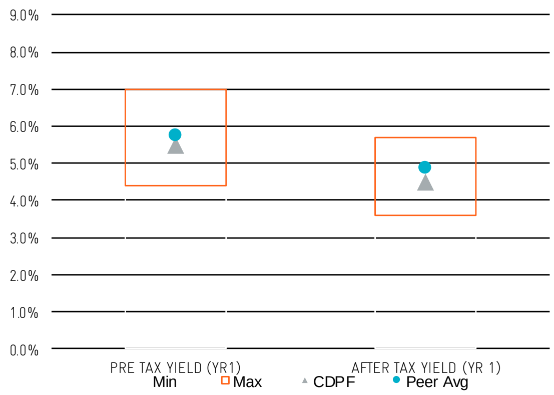
- The Manager's and Valuer's estimate of net income from the portfolio of direct properties (including the latest acquisition of 100 Creek St). The income estimates also include reasonable allowances for potential vacancies, incentives and leasing costs.
- The Manager's estimates for distributions from the Cromwell property syndicates that CDPF has an interest in. This includes a one-off distribution from the sale of properties and/or wind up of syndicates (eg: Ipswich City Heart Trust).
- Capital expenditure requirements on average over the next five years on the direct properties is $3.5m p.a., funded from cash flow.

2.2 Distribution yield comparison

Cromwell DPF Estimated Distributions

Year end June	FY22 to	FY24e
DISTRIBUTION/UNIT	7.40C	7.60C
PRE-TAX YIELD (@ $1.3483)	5.5%	5.6%
TAX ADVANTAGED	60%	60%
YIELD AFTER 47% TAX	4.5%	4.6%
GROSSED-UP YIELD	8.4%	8.6%
YIELD AFTER 15% TAX	5.2%	5.3%
GROSSED-UP YIELD	6.1%	6.2%

Lonsec Industry Distribution Comparison



- Lonsec has compared CDPF's estimated distribution yield with a sample of open-ended direct property trusts. The Fund offers a distribution yield (both on a pre-tax and after-tax basis) slightly below Lonsec' average for unlisted property trusts.

Cromwell Direct Property Fund

2.3 Debt Position / Interest Costs

- The Manager has three loan facilities (each for three years):
  - Bank Loan Facility 1 ($146.5m) with an Australian bank was extended in February 2021 and is drawn to $86.9m as at 2 December 2021.
  - Bank Loan Facility 2 ($75m) with a new lender is fully drawn.
  - Bank Loan Facility 3 ($120m) with a new lender is fully drawn.
- The loans are secured against all directly held properties with a total pool value of $583.7m.

Bank Loan Terms

FACILITY LIMIT	$341.5M
DRAWN-DOWN	$281.9M ($263M*)
EXPIRY	FEB; APR; OCT 2024
COST OF DEBT [1]	3.07% p.a.
HEDGED (FIXED FOR 3 YRS)	($73.25M) 21.0%
HEDGE EXPIRY	30 JUNE 2022
BANK LVR COVENANT	50.0%
FUND LVR[2]	48.3% (45.7%*)
FUND GEARING[3]	40.8% (38.6%*)
LOOK-THRU GEARING[4]	42.5% (40.1%*)
ICR	6.7X
ICR COVENANT	2.0X

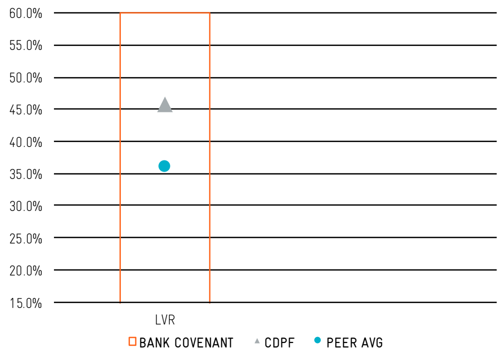
1: Including amortisation of debt establishment costs (2.83% excl).
2: Loan to direct property value.
3: Gearing is Total Debt less unamortised loan transaction costs / Total Assets.
4: Look-through gearing includes interest in syndicate as % CDPF.
(Note *: Assumes CMW 4.7% investment in Fund)

- Following the acquisition of the 100 Creek St property, the Fund's LVR is 48.3%, just below the Bank covenant of 50%. Assuming Cromwell Group's investment of 4.7% into CDPF during December 2021, the LVR will be 45.7%.
- The 'look-through' positions includes the syndicate investments LVR and gearing in proportion to the level of CDPF's investment.
- The Fund's actual level of debt will fluctuate depending upon acquisitions, capital expenditure and the level of equity inflows. The Manager intends to limit gearing on the direct properties to a maximum 50% and won't acquire units in any unlisted property trust that would result in a look-though gearing level above 50%.

Cromwell Trusts	Gearing* (LVR)
RIVERPARK TRUST (NOV 2021)	27.7%
CPT 12 TRUST (SEPT 2021)	30.6%

*Debt/Value of Investment Property

Lonsec Industry Gearing Comparison



Sensitivity analysis – gearing covenants

- The Fund's LVR is sensitive to changes in capitalisation rates for properties - as determined by market transactions and valuations.

Cap'n rate	Portfolio value (Direct)	Value chg	LVR	H'room to covenant
BASECASE 5.9%	$587M	0%	45.7%	4.3%
6.54%%	$526M	-10%	50.0%	0%

- As at December 2021, the CDPF has a slim coverage above the bank LVR covenant, with the directly owned portfolio able to **withstand a 10% reduction in the value of the property** before breaching its 50% covenant. A rise in income or property value will improve the headroom.
- **Interest Cover Ratio** (as calculated in accordance with the bank covenant) of **6.7x is strong**, with the property net income having to reduce by 70% before the bank covenant of 2.0x is breached.

2.4 Fee Structure

- The Manager is entitled to receive a number of fees and incurs other expenses related to the management of the Fund.
  - Acquisition & Disposal of properties;
  - Annual management fee & expenses;
  - Performance Fee
- Note that property-related expenses (such as stamp duty) are not included in this analysis.
- Should the CDPF acquire any properties directly (or via an interest in another trust/fund), an **acquisition fee of 2% of gross assets** will be payable to Cromwell Funds Management.
- **Property Sale Fee of 1% of the gross value of assets sold** may be payable to CFM if it acts as the selling agent on the fund's direct properties. If an external agent is appointed, the total fees (including those paid to the agent) will not exceed 1% of gross assets sold.
- The acquisition/disposal fee on units in an unlisted property trust/fund will be reduced so that CFM does not double up on fees already earned in an underlying property syndicate (unless that fee has been recovered since the issue of the units by an improvement in the net asset value of the property trust/fund).
- The Manager will ensure that investors in the CDPF will only pay an **annual management fee** of 0.60% p.a. of the Fund's gross assets (including any fees already paid in underlying property syndicates). On a net assets basis this equates to 0.75% p.a.
- **Expenses** of the CDPF (at the fund level) are quoted by the Manager to be 0.18% p.a. of net assets. However, there are indirect fees (including any performance fees) and expenses from the syndicates amounting to a further 0.38% p.a. of net assets.
- **Performance Fee**: The RE/Manager is entitled to be allocated a 20% share of the excess total return above the benchmark index (PCA/MSCI Unlisted Retail Property Fund Core Index). The Performance Fee is payable provided the Fund beats the benchmark, therefore a performance fee may still be payable if the Fund incurs a negative return. However, the Performance Fee will only be charged for a quarter if any previous underperformance of the benchmark has been recovered.
- There is no 'poison pill' fees payable should the RE be replaced by way of unit-holder vote (Extraordinary Resolution) under the Corporations Act.

Comparison of management costs (RG97)

% Net Assets	CDPF	Open-end Avg
M'MENT FEE	0.75%	
EXPENSES (CDPF)	0.18%	
	0.93%	1.32%
INDIRECT COSTS/PERF FEE	1.12%	
TOTAL ANNUAL	2.05%	1.64%

Overall fee and expense comparison

- For the total fees comparison, Lonsec has estimated the present value of total fees and expenses paid to the RE/Manager by the Fund over a ten-year period. This takes into consideration the differences in timing of initial establishment costs, on-going expenses and back-end performance/ disposal fees and varying investment terms.

Comparison of PV of total fees and expenses

	% Total Assets	% Net Assets
CDPF	**8.2%**	**12.4%**
LONSEC AVG (OPEN-END)	7.4%	11.1%

- Lonsec' overall analysis shows CDPF's management costs to be above the average for open-end funds, mainly due to the inclusion of the indirect costs and performance fee data from the Manager. Previously, Lonsec did not include a Performance Fee payable at the CDPF level as this was difficult to assess given it is relative to a high performing 'retail fund' index. In the future, these costs could be impacted by higher than current Performance Fees, both at the CDPF level and underlying Cromwell trust level. However, total net returns (after fees) to the investor may still be higher in these circumstances.

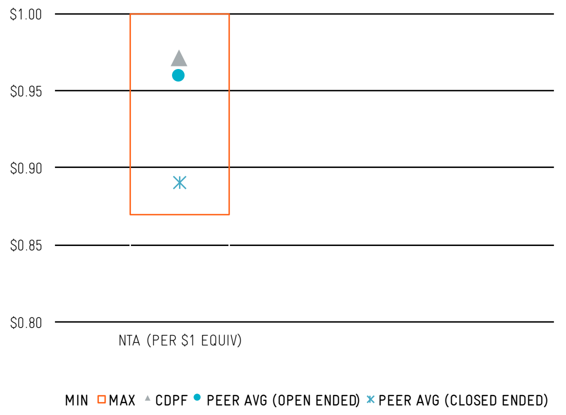
Cromwell Direct Property Fund

2.5 Balance Sheet / Net Asset Backing

Balance Sheet	Latest	Proforma Post Acq'n	Post CMW Equity
As at end	Nov-21	Dec-21	Dec-21
	$M	$M	$M
CASH	$38.3	$37.4	$37.4
PROPERTY ASSETS	$402.1	$586.8	$586.8
OTHER ASSETS	$76.0	$66.8	$66.8
CAPITALISED EXPENSES	$0.0	$0.0	$0.0
TOTAL ASSETS	$516.4	$691.0	$691.0
CURRENT LIABS	-$20.0	-$20.0	-$20.0
INTEREST BEARING LOAN	-$105.0	-$281.9	-$262.1
OTHER NON CURRENT LIABS.	-$0.4	-$0.4	-$0.4
TOTAL LIABILITIES	-$125.4	-$302.3	-$282.5
NET ASSETS	$391.0	$388.7	$408.5
NO. OF UNITS ISSUED	298.200	298.200	312.900
NTA PER UNIT	$1.31	$1.30	$1.31

- The above table shows the CDPF balance sheet as at 31 December 2021 including the 100 Creek St acquisition as well as post CMW taking up approximately a 4.7% equity stake in the Fund at net asset backing by the end of December 2021.

Net Asset Backing Comparison



- Fees, expenses and stamp duty for new acquisitions are amortised in the unit price over a five year period. Fees and expenses related to divestment of properties are amortised over a five-year period in the same manner. The Fund does not charge a buy or sell spread on units when investors enter or exit the Fund.
- New investors to CDPF would start with Net Tangible Asset backing of $1.31 per unit according to the proforma balance sheet on the left. This is at a marginal discount to the current Unit Price of $1.348 (or $0.97 on a per dollar equivalent basis to compare the asset backing to price of different funds). This is in line with most open-end funds. It is also well above the 5%-15% discount for other start-up (mostly closed-end) funds with higher (upfront) establishment costs.

Cromwell Direct Property Fund

3. Management

An assessment of Management is another key performance measure and is largely qualitative, focusing on the ownership, operating and reporting structure, property investment policy and selection criteria. Capable and experienced management is vital to the success of the Fund. Previous performance is evaluated, but is not necessarily a guide to future returns.

3.1 The Responsible Entity (RE)

- **Cromwell Funds Management Limited** (CFML) will act as Responsible Entity (RE) for the Cromwell DPF. CFML is a specialist funds management company licensed by the Australian Securities and Investment Commission (ASIC) to act as the RE for a range of managed investment schemes.
- CFML is a 100%-owned subsidiary of **Cromwell Property Group** (ASX Code: CMW), an integrated property group with its own property portfolio, funds management business and internal property services team. CMW is listed on the Australian Securities Exchange (market capitalisation $2.25b as at December 2021). As at June 2021, CMW had a direct property portfolio of $3.9b and total assets under management of $11.9b across Australia, New Zealand and Europe.
- In September 2020, two representatives of the largest shareholders of CMW (ARA 26.7% and the Tang Family 16.7%) were elected to the Board. **Paul Weightman** (previously CEO) retired in December 2020. The Board of eight was also refreshed during 2021 and now comprises five independent/external directors, two executive directors and the non-executive Chair. **Jonathan Callaghan** (ex Investa) was appointed CEO and joined in October 2021 (replacing Acting CEO Michael Wilde – resumes CFO role).

3.2 Management Team

- In line with industry best practice, Cromwell has established a separate board for Cromwell Funds Management Ltd which has a **majority of independent/external representatives.** Cromwell Funds Management Ltd oversees the CDPF.

Board of Directors – Cromwell Funds M'ment Ltd

Name	Position	Joined C'well (Yrs)	Industry Exp (Yrs)
TANYA COX	NON-EXEC CHAIR	2019	15+
MICHELLE MCKELLAR	NON-EXEC DIRECTOR	2007	35+
JANE TONGS	NON-EXEC DIRECTOR	2015	30+
RICHARD FOSTER	NON-EXEC DIRECTOR	1998	50+

Source: Cromwell

Other Senior Executives & Staff

- In November 2021, CFML appointed **Brett Hinton** as Head of Funds Management Australia. **Lachlan Stewart** continues in his role as Cromwell's Portfolio Manager (with a focus on CDPF and other retail funds). **Peta Tilse** has been appointed Head of Retail Funds Management (replacing Hamish Wehl) and will join Cromwell in January 2022.
- Cromwell has 460 staff in 28 offices across 14 countries. Lonsec also notes Cromwell's strong internal capability in finance, treasury and compliance.

3.3 Investment process

Overview investment style

The Group relies on the following core business strengths:

- Defensive property portfolios with strong recurring cash flows and minimal short-term lease expiries.
- A strong retail direct property brand.
- Traditionally a domestic focus with limited exposure to offshore property markets; however this has recently changed with a focus on overseas acquisitions of fund management businesses.
- A loyal diversified retail and institutional investor base for its unlisted property funds.
- An experienced and stable executive team.

Cromwell acquisition process

The Manager has a five-step acquisition process that is employed to evaluate, approve and implement potential property acquisitions. The Cromwell property acquisitions/property services team has specific experience in project managing more complicated delivery and construction programmes to project completion. They have also shown a discerning due diligence process by passing up opportunities that do not measure up.

The process is mapped out below:

- Step 1: All potential property acquisitions are reviewed in accordance with the Investment Policy of Cromwell, objective market criteria and prevailing market conditions. The acquisition is modelled to ensure that threshold IRR and yield targets can be met.
- Step 2: Potential acquisitions that meet minimum investment criteria are subject to initial technical, financial and legal due diligence. Due diligence models are revised in accordance with due diligence findings. If applicable, an initial conditional Heads of Agreement is negotiated with the potential vendor.
- Step 3: The Board appoints a formal Due Diligence Committee (includes a number of Cromwell Directors) and an Investment Committee (must include at least one non-executive Director) to steer the acquisition process. The Due Diligence Committee undertakes a range of technical, financial and legal due diligence investigations, utilising a range of internal and external experts in this process. Key findings are used to update the acquisition model.
- Step 4: The Due Diligence Committee commissions and reviews an external property valuation and secures a commitment from its financiers to provide debt financing for the

acquisition. The Due Diligence Committee makes a recommendation to the Investment Committee.

- Step 5: If the Investment Committee is satisfied with the due diligence recommendation and the terms of the financiers, it may elect to proceed with the investment. Major transactions may also require full Board approval.

Portfolio construction / acquisition criteria

- Larger properties with value-add opportunities are usually suited for the Cromwell balance sheet and more passive assets under $100m are ideal for syndication. Generally, acquisitions for the listed entity need to be neutral to Group earnings, although there may be a compelling future upside to consider.
- Recent preference has been for office properties, with government/blue-chip tenants in key CBD markets. Sourcing opportunities have benefited from strong relationships with developers.
- After the internal due diligence process, the target total returns at the property level are determined. The Group noted that they have completed multiple due diligences in recent years and ultimately screened out properties as they have not been able to meet the total return hurdle rate.

On-going Property Management

- Cromwell has an internal Property and Facilities Management team (including Cromwell Project & Technical Solutions) that operates like an external services provider. This team is responsible for the control of the portfolio capital works.
- Each property has a rolling ten-year capital expenditure plan, which is developed as part of the acquisition due diligence process.

They work closely with Property Managers, Leasing Managers and Facility Managers to ensure capital expenditures/tenant fit-outs are well managed.

ESG and Sustainability

- Cromwell Direct Property Fund had a Global Real Estate Sustainability Benchmark ('GRESB') score in FY21 of 78 out of 100 for its Australian properties. This is in line with the peer group average of 86. GRESB is an environmental, social and governance (ESG) benchmark for real estate and infrastructure assets. A focus in this area can assist in improving property management outcomes (e.g. achieving greater energy efficiency) and attracting better quality tenants.

Potential Conflict of Interest / Related Party Issues

- Lonsec has sighted Cromwell's '**Conflicts of Interest Policy and Procedure**' as well as 'Related Party Protocol' documents. It is noted that the Company Secretary has overall responsibility for managing conflicts of interest and the Compliance Manager monitors compliance with the policy and procedure. The Manager has adequate policies and procedures in place to manage the risk of any actual and perceived conflict of interest as a result of related party transactions. The Manager or related parties benefit from charging project management; property management; and leasing fees. "All service arrangements are documented and conducted on arm's-length terms".

3.4 Previous Performance

Cromwell Funds Management Ltd performance

Cromwell Direct Property Funds (Total Return to 30 November 2021)

FUND	1 YR % P.A.	3 YRS % P.A.	5 YRS % P.A.	SINCE INCEPTION.	FUND INCEPTION DATE
CDPF INCOME RETURN	5.9	5.9	5.9	6.0	
CDPF GROWTH RETURN	9.8	2.8	3.1	3.9	
CDPF TOTAL RETURN	15.7	8.7	9.0	9.9	AUG-13
VS LONSEC PEER GROUP#	-1.9	-1.7	-1.8	N.A.	
SYNDICATES					
CROMWELL P/T 12	32.2	21.4	16.8	16.8	OCT-13
CROMWELL RIVERPARK TRUST	24.8	13.9	16.1	15.5	JUN-09
CROMWELL IPSWICH CITY HEART TRUST*				14.6	DEC-11

Note: Return as at 31 July 2021. Property sold and funds to be distributed in due course. # Lonsec selection of unlisted non-wholesale open-end funds.

4. Market Analysis

4.1 Australian Office Property Market

Green – positive *Red – negative* *Yellow - neutral*	OFFICE
Demand/Supply for space	• Demand recovering A-grade, but new supply in Melb & Sydney.
Vacancy	• Sydney & Melb higher than 2019, but flattening.
Rentals	• Incentives higher making effective rents lower.
Yields/Cap Rates	• Tighter, but cautious given interest rates
Transactions	• Recovering, with strong investor demand for quality.

5. Exit Strategy / Liquidity

5.1 Withdrawals and Liquidity

- At the end of the initial investment term of seven years at the end of June 2020 the Manager offered a full withdrawal opportunity. 9.9% of issued capital was paid out and **the fund term has been extended.**
- The term of the Fund is now five years and the Manager intends to offer a **full liquidity event** at the term expiry about July 2025.
- The Manager provides a **Limited Monthly Withdrawal Facility** (up to 0.5% of the Fund's net asset value per month or higher if the Fund's cash exceeds 6% of assets).
- The **two remaining Cromwell syndicate** investments of CDPF have varying exit points, which gives the Manager the opportunity to exit these investments at different times. However, subject to unit-holder votes, the underlying trusts may continue on for further terms.
- Direct properties can be sold at any time by the Manager. The proceeds of selling either an interest in an underlying trust or direct property could be used for withdrawals.

6. Lonsec Methodology

The research methodology includes a rating process designed to assess the qualitative and quantitative factors of the investment. The process is consistent for comparable investment products, enabling projects to be individually rated, comparatively ranked, and to establish a Lonsec Research recommendation status for use by financial planners.

The rating determinants are:

- Financial Analysis / Gearing
- Properties
- Management
- Market Analysis
- Exit Strategy

Lonsec Direct Assets Research Rating Definitions

Highly Recommended	The Highly Recommended rating indicates that Lonsec has very strong conviction the financial product can generate risk adjusted returns in line with relevant objectives. The financial product is considered a preferred entry point to this asset class or strategy.
Recommended	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.
Investment Grade	The Investment Grade rating indicates that Lonsec has conviction the financial product can generate risk adjusted returns in line with relevant objectives. However, if applicable, Lonsec believes the financial product has fewer competitive advantages than its peers.
Fund Watch	The Fund Watch rating indicates that no new investment into this financial product is recommended. A significant change has occurred with the financial product and a detailed assessment of the change is needed and / or series of rectifying actions required prior to this rating being changed.
Screened Out	The Screened Out rating indicates that Lonsec currently does not have conviction that the financial product can generate risk adjusted returns in line with relevant objectives. The financial product currently has insufficient competitive advantages relative to its review peer group (if applicable).
Redeem	The Redeem rating indicates the financial product is no longer considered worthy of investment for any time period and investors should immediately redeem units from the financial product, subject to seeking financial advice. An adverse development has taken place that is considered detrimental to the interests of investors.

Financial Products withdrawn from research process

Capital Raising Closed	As the Trust is closed to new investment, it is no longer included on the Lonsec Recommended List and existing Lonsec research reports and ratings have been withdrawn from the Lonsec website. Going forward, Advisers should not rely on prior research in respect of this product. Lonsec will only be providing further updates should circumstances require. The Trust manager will have to obtain a new Lonsec rating for any new capital raising. Lonsec may also make a recommendation if a roll-over of investor capital is proposed or a liquidity offer is made. An investment in the Trust can be retained.
Discontinued Review	The Discontinued Review status is applied where a fund manager that has approached Lonsec and agreed to tender a financial product for assessment, subsequently elects to discontinue participating in the Review prior to its completion for any reason, other than the financial product being closed or unavailable to retail investors. The Discontinued Review status will be published on the Lonsec website.
Cease Coverage	The Cease Coverage status is applied to financial products where fund managers withdraw from the Lonsec research process after the research process has been completed.
Closed / Wind Up	The Closed / Wind Up status is applied to a financial product when the fund manager advises Lonsec that the financial product is being wound up and the capital is to be returned to investors.

Lonsec

Cromwell Direct Property Fund

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 and 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

December 2021

Analyst

Kevin Prosser

Approved by

Balraj Sokhi