INSIGHT
MAGAZINE

BUILD TO RENT: AN EMERGING CLASS IN AUSTRALIA

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CROMWELL
PROPERTY GROUP

Contact
1300 268 078 (within Australia)
+61 7 3225 7777 (outside Australia)
invest@cromwell.com.au
www.cromwell.com.au

Dear reader,

Welcome to the first print edition of Insight magazine for 2024! Thank you for subscribing to the hardcopy version of our quarterly publication – this year, we will continue to bring you the most relevant, engaging, and insightful content in a timely manner.

Insight #45 is a short form edition to start the year, with a full version of Insight #46 delivered in April.

In this edition, Stuart Cartledge of Phoenix Portfolios looks at an emerging asset class in Australia – Build to Rent; we examine the release of Cromwell's most detailed, comprehensive ESG report to date – the FY23 ESG Report – which details our scope 3 emissions inventory for the first time; and we provide ASX A-REIT market and direct property market updates for the December 2023 quarter.

Keep an eye out for the next edition of Insight in April – and thank you for your continued support of Cromwell Property Group.

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CROMWELL RELEASES ANNUAL ESG REPORT

DETAILS FULL SCOPE 3 INVENTORY

In January, Cromwell released its most detailed, comprehensive ESG report to date. This report serves as a snapshot of how the business is progressing towards meeting our environmental, social, and governance commitments over the short and long-term.

The report was developed in collaboration with all relevant disciplines across the global business, and aligns with major reporting standards, including the Sustainability Accounting Standards Board and the Global Reporting Initiative. It has been designed to provide transparency through qualitative and quantitative data, while showcasing the Group's effort to deliver tangible positive impacts, citing case studies from across the business.

Most significantly, in line with the organisation's desire for greater transparency, this recent report details Cromwell's full scope 3 emissions inventory disclosure for the first time.

What ESG progress means for investors

Increasingly, ESG reporting is being used by investors as another way to track an organisation's activities and keep businesses accountable for their actions. Some investors use ESG results to determine poor performers, associating the factors that cause companies to receive low ESG ratings with weak financial results; some investors seek out high ESG performers, expecting exemplary ESG outcomes to drive superior financial results.

ESG reports are a key source of ESG performance information relied on by investors and stakeholders to make informed decisions about an organisation's impacts. Investor and stakeholder expectations around ESG disclosure are increasing and reporting standards are rising to respond to that expectation.

Indeed, the term "ESG" was first mentioned in the United Nations Global Compact "Who Cares Wins" report in 2004 and has now become synonymous with the ability to demonstrate good corporate citizenship. Industry trends, as well as independent studies, indicate that investors are now wanting to see tangible ESG results.

> ESG reports are a key source of ESG performance information relied on by investors and stakeholders to make informed decisions about an organisation's impacts.

A 2022 Ernst & Young Global Corporate Reporting Survey, released in November that year, found that 78% of investors want companies to focus on environmental, social, and governance activity, even if it hits short-term profits.

These days, a company's risk profile is raised in the eyes of investors if it fails to consider ESG risks adequately and disclose its approach to them. Among other things, this makes it difficult for a company to access capital and can over time, render it 'un-investable' to investors, many of whom now have ESG or green mandates.

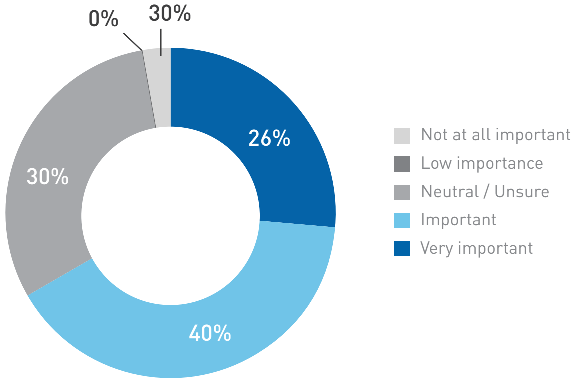
ESG and our tenants

As a commercial real estate investor and property manager, meeting the diverse needs of our tenants remains a high priority.

Through regular, ongoing engagement and detailed annual surveys, our tenants have outlined that helping meet their own ESG requirements and ambitions needs to be a key priority for Cromwell as the building owner. By helping meet these needs, we significantly increase tenant retention across our portfolio – and attract new long-term blue-chip tenants.

Cromwell's October 2023 Tenant Satisfaction Survey Portfolio results showed that 66% of respondents rate sustainability as important or very important in their organisation's decision to lease; and almost 60% of respondents are already at net zero, considering net zero, or already working to become net zero organisations.

How important is sustainability in your organisation's decision to lease?



Source: Tenant Satisfaction Survey 2023

For instance, over the past 12-24 months, state and federal government departments have put increased emphasis on restricting leasing properties that can't demonstrate a credible net zero pathway for the building.

With government tenants making up a significant percentage of our Australian leasing pool, Cromwell has committed to ensuring that we take necessary steps in improving our ESG performance to retain these crucial tenants.

> In this way, we satisfy current tenant needs – and future-proof existing buildings – to increase tenant retention, improved rental yields, and deliver for our investors.

The significance of understanding scope 3 emissions

Scope 3 emissions – also known as 'value chain' emissions – are indirect greenhouse gas emissions both upstream and downstream of an organisation's main operation. Consequently, for this reason, they are also traditionally the most challenging emissions scope to calculate and address for many businesses as they are not directly controlled by the organisation.

Regardless, the UN Global Compact has found that scope 3 emissions generally make up more than 70% of an organisation's total emissions footprint and it is accepted that understanding them is critical to identifying the greatest reduction hotspots, avoiding future value chain risks associated with the transition to a zero-carbon economy, and mitigating against greenwashing.

Group Head of ESG Lara Young said that reducing scope 3 emissions, and including this emission scope in net zero carbon targets, is critical to ensuring legitimate net zero targets that deliver tangible change. Addressing scope 3 emissions, she said, can deliver substantial business benefits by providing a clear transparency, understanding, governance, and oversight of an organisation's full value chain and the evidence of the positive impacts delivered.

"Despite the industry challenges of data quality and availability for scope 3 emissions, the Group is proactive with joint venture partners in Oceania – and its supply chain partners, clients, and tenants globally – to collate scope 3 data via the roll-out its green lease initiative and ESG schedules," said Ms. Young.

"Cromwell has committed to positively contributing to the communities in which we operate, and that goal involves supporting tenants and investors with achieving their net zero targets and evolving ESG needs."

"Cromwell's FY23 ESG report is the first time that Cromwell will publicly disclose scope 3 emissions, and this will place the Group among the minority of industry peers that publicly disclose this data. This outcome is a testament of the Group's capability and desire for full transparency."

Progressing on our ESG commitments

The FY23 ESG Report shows that Cromwell made notable advancements toward our ESG commitments during FY23 – including the development and implementation of our updated ESG Strategy; preparing a globally aligned approach to decarbonising the business to meet our targets of net zero scope 1 and 2 emissions by 2035, and all scope 1, 2, and 3 emissions by 2045.

This activity is supported by emissions abatement cost modelling for our Australian and European portfolios to facilitate emissions reductions and associated decarbonisation costs.

The report also highlights the progression the business has made in the past 12 months regarding specific ESG results. Among our key achievements, emissions intensity (scope 1, 2, and 3) was reduced by 12% in Australia, compared to the previous financial year; European assets recorded reductions of 22%.

The Cromwell Direct Property Fund was third in the Australian NABERS Sustainable Portfolio Index (SPI) – the highest ranked geographically diversified fund in Australia – and Cromwell's Australian investment portfolio was fourth in the same index.

Cromwell Polish Retail Fund (CPRF) achieved a five-star rating and a Cromwell record-high overall score of 90 points, ranking 11th out of 32 European retail non-listed peer funds and 17th out of 87 in the European Retail category.

And, significantly, Cromwell's Australian gender pay gap decreased by 44% since it was first calculated in FY21.

Lara Young said that, among other metrics, these key achievements highlighted the progress the organisation is making.

"We know that ESG is not just about carbon emissions. While reducing emissions is crucial, this cannot be at the expense of biodiversity, social value, or natural capital. These topics are all interlinked and the Group recognises we cannot be successful if focusing on each in isolation," said Ms. Young.

CASE STUDY

McKell Building: Electrification of property assets

One of the largest, and most involved ESG-led projects this year was the electrification of the McKell Building in Sydney's CBD.

The multi-million-dollar project has involved converting the building's existing commercial gas-fired heating system to an electric heat-recovery reverse cycle heating, ventilation, and air conditioning (HVAC) system.

Cromwell's Head of Property Operations, Tessa Morrison, said the upgrade of the 24-storey building has been designed to help 'future-proof' the asset by replacing outdated, 1970s-era infrastructure with modern, energy saving equipment.

"The McKell building is a 1970s-constructed building with an existing NABERS 5.5 Star energy rating, so while it is already significantly energy efficient, we are undertaking this project to reduce emissions and drive further energy efficiencies," said Ms. Morrison.

"This is the first time that a multistorey, 25,000sqm commercial building in the Sydney CBD has undergone an electrification upgrade – and we're excited to have engaged experienced mechanical air conditioning contractor Velocity Air to help deliver the project."

Efficiencies in the new reverse cycle HVAC system will mean that hot air removed as part of the building's air conditioning process will be recycled back into the system for use elsewhere, including heating the building's water.

Looking long-term

Through its data informed approach, Cromwell is working to focus on the broad spectrum of the ESG agenda, while prioritising the most relevant aspects. Cromwell recognises that the industry needs to remain pragmatic, but also strike a balance with a wholistic systems view.

Cromwell's key long-term targets remain:

- Net zero operational emissions (scope 1 & 2) by 2035.
- Entire portfolio (scopes 1, 2, & 3) including tenant and embodied carbon by 2045.
- Significantly reduce our gender pay gap year on year.
- Achieve 40:40:20 gender diversity at all levels.
- Integrate ESG into risk register and business strategy, including objectives and key results.

"Cromwell recognises the ESG challenges that the property industry faces; however, we also recognise the opportunity to deliver tangible positive impacts. The Group has a global in-house ESG team and dedicated Australian and European teams supporting all Cromwell ESG targets and activities," said Ms. Young. ■

BUILD TO RENT: **AN EMERGING CLASS IN AUSTRALIA**

Stuart Cartledge
Managing Director
Phoenix Portfolios

In October 2023, Phoenix Portfolios participated in an Investor Day, hosted by listed REIT, Mirvac Group, that focused on "Living Sectors". Aside from the joy of wearing a high-vis jacket, those with an eye for detail will notice the badge, clearly indicating that the occupant of the jacket is a "Young Worker".

In this article we share with you some of the lessons learned by that young worker from the day.

Australia has a housing crisis. We may have had an inkling of this one before the tour, but with an estimated 1,000,000 new immigrants expected to arrive in Australia over the next 3 years, requiring approximately 400,000 dwellings, we're going to have to get cracking with the government's new housing targets.

The chart below puts these figures into the context of what has been delivered in the past. The key takeaway for us, is that the Australian Government may well be having another Utopia moment.

With demand likely to remain robust, and rental markets as tight as a drum, the opportunity for an entity such as Mirvac Group to deliver product into this environment is compelling.

What is "Build to Rent"?

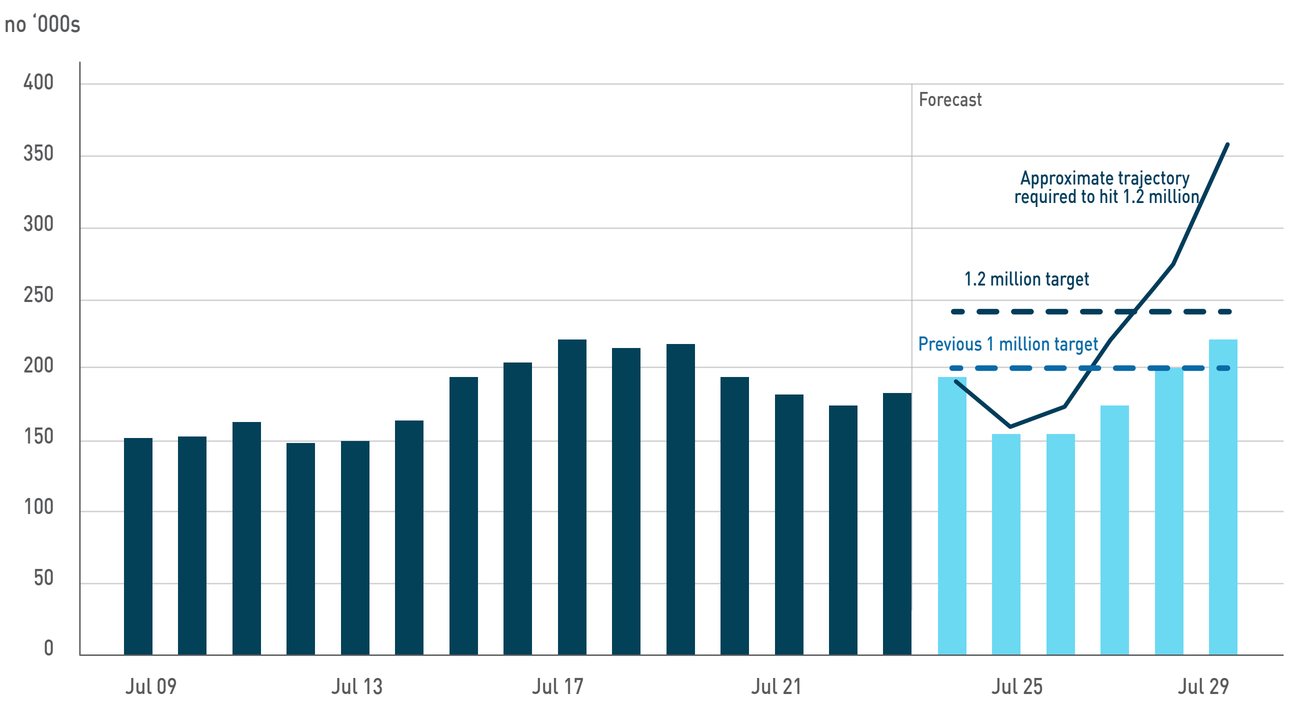
Build to Rent (BTR) is the creation of residential dwellings, typically apartments, which instead of being strata titled and sold to individuals, remain institutionally owned, professionally managed, and represent high quality rental accommodation, often including a higher level of amenity than competing product. Furthermore, a resident has security of tenure, not just through a lease, but because the entire building forms part of a long-term residential community.

An investor in BTR benefits from typically high occupancy rates, with multiple tenants delivering low volatility of income and stable valuations.

An investor in BTR benefits from typically high occupancy rates, with multiple tenants delivering low volatility of income and stable valuations. Well-designed buildings should certainly benefit from relatively low maintenance capital requirements, at least initially, and certainly do not suffer from the requirement to incentivise tenants with expensive fit outs that plague the office leasing market.

While BTR may be a relatively new concept in Australia, it is a mature property sub-sector in offshore markets, particularly in the US, where it is referred to as "multi-family".

Australian dwelling completions and national housing accord targets



Source: ABS, Oxford Economics September 2023

Mirvac is pioneering BTR in Australia

The BTR sector is embryonic in Australia, representing less than 0.5% of housing stock across the country. This compares with a ~12% penetration in the US and around 5.4% in the UK. The opportunity set is therefore large.

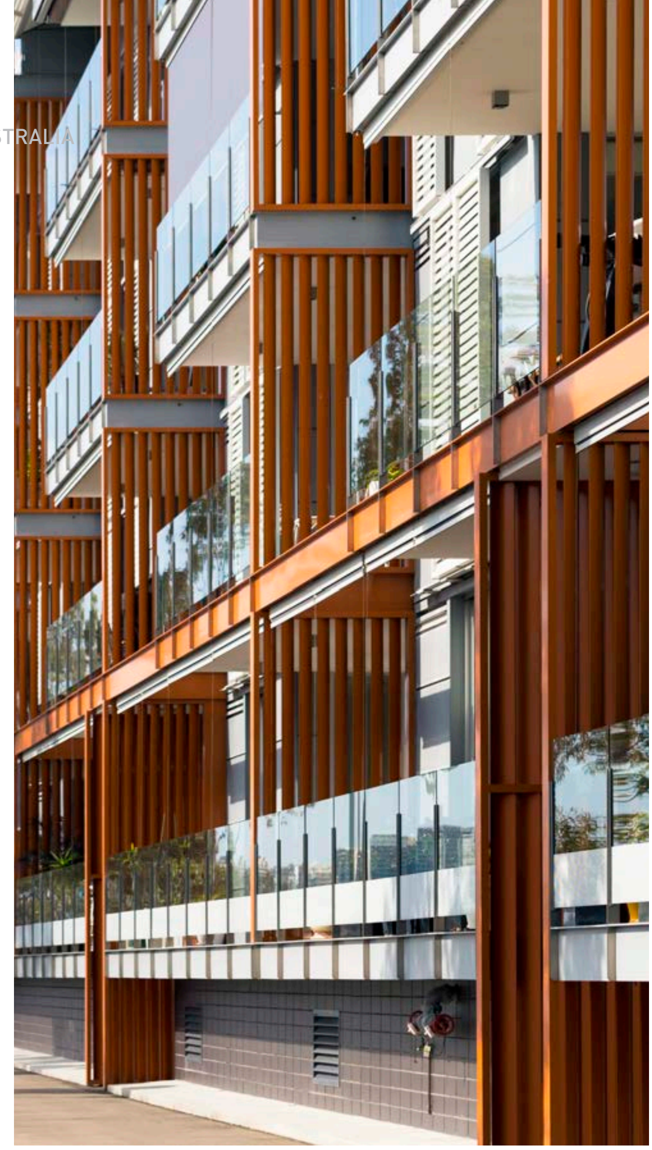
For MGR, the BTR sector capitalises on the company's 50-year residential track record of asset design and creation and has facilitated MGR to pioneer the sector in Australia. MGR has branded its BTR product with the "LIV" name, and delivered LIV Indigo, its first project in Sydney Olympic Park back in September 2020. That project is now 94% occupied. LIV Munro, opposite Queen Victoria Market in Melbourne's CBD is the second completed project which opened at the end of last calendar year and is now 70% occupied. LIV Munro is pictured above.

The tour showed investors around LIV Munro enabling us to get a feel for the amenity, including pool, gym, dining areas, podcasting rooms and rooftop BBQ and relaxation facilities and to meet the on-site staff responsible for the community experience. We were impressed.

We also visited LIV Aston, a project under construction on the corner of Spencer Street and Flinders Street West, also in Melbourne's CBD. Hard hat required! With a total of 474 apartments, the construction project was on time and budget and is expected to compete before the end of the current financial year. This project is almost adjacent to another, yet to be competed, BTR project currently being developed by Lendlease. It will be interesting to see these projects go head-to-head when they are both operational.

Alongside the three projects referred to above, MGR has another 2 projects under construction, one in Melbourne and the other in Brisbane, which will bring their collective exposure to BTR to approximately 2,200 apartments across 5 projects.

> With a total of 474 apartments, the construction project was on time and budget and is expected to compete before the end of the current financial year.

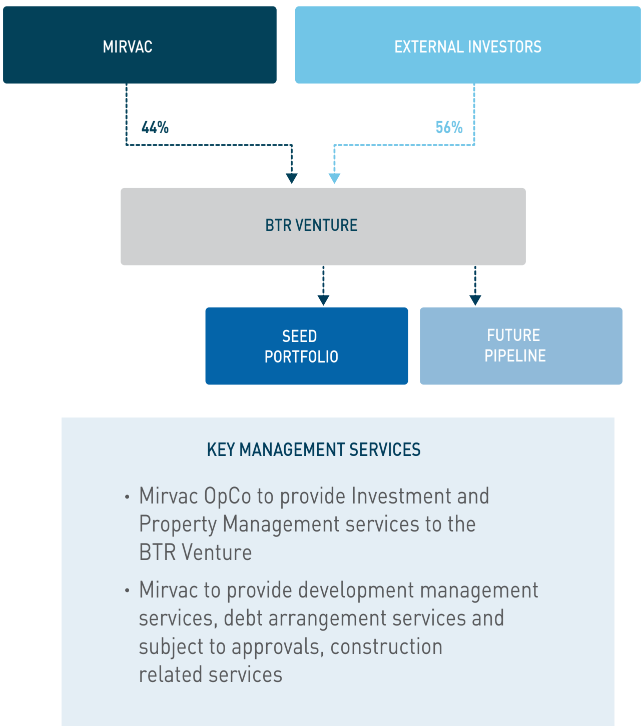


Financial metrics are interesting

Financial modelling for BTR is made a little tricky by some big movements in construction costs over the last few years, which ordinarily would lower returns, combined with some offsetting and also significant market rental increases in the residential sector. For MGR, the end result is a stabilised yield on cost of 4.5% – 5.0%. Along with rental growth, maintenance costs and ancillary income, the investment return (Internal Rate of Return) is estimated to be around 7% – 7.5%.

MGR's investment in the sector is structured in a joint venture as shown in the diagram below.

STRUCTURE SUMMARY



External investors sit alongside MGR, and enjoy investment returns that benefit from MGR's active management and can take comfort that MGR's interests are very much aligned with theirs.

In addition to the returns on capital invested in the joint venture, MGR also earns funds management, development management and asset management fees across the platform. This fee stream is more volatile but adds to the returns that MGR shareholders enjoy.

Phoenix assumes that MGR is able to build out its current pipeline of BTR opportunities and will be able to identify future projects to reach its medium term target of 5,000 apartments on the platform. Importantly, we also assume that the company will be able to continue to partner with external investors to deliver a solid outcome for all stakeholders.

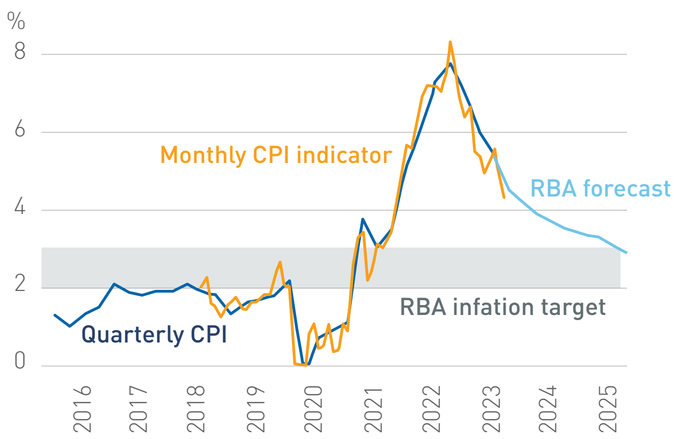
We expect the BTR market to get more competitive, but with penetration rates so low and the demand for housing so high, we forecast a solid runway for the foreseeable future. The only sad thing about the day, was the discovery that BTR is typically targeting the affluent renters, aged between 25 and 39. The "young worker" on this tour is more likely a target for the over 55 land lease portfolio, which we will write about in subsequent articles. ■

DIRECT PROPERTY UPDATE

DECEMBER 2023 QUARTER

Peta Tilse
Head of Retail Funds Management
Cromwell Funds Management

Consumer Price Index (annual % change)



Source: RBA, ABS, CBA, Macrobond

Economy

Over the December quarter, interest rates were reasonably volatile both in terms of short and longer-term rates. The RBA increased interest rates by 25 basis points (bps) in November, taking the cash rate to 4.35%; its highest level since the end of 2011. The justification for the move was to bring inflation to target within a reasonable timeframe (i.e. by end-2025), rather than risk a prolonged overshoot and upwards shift to inflation expectations.

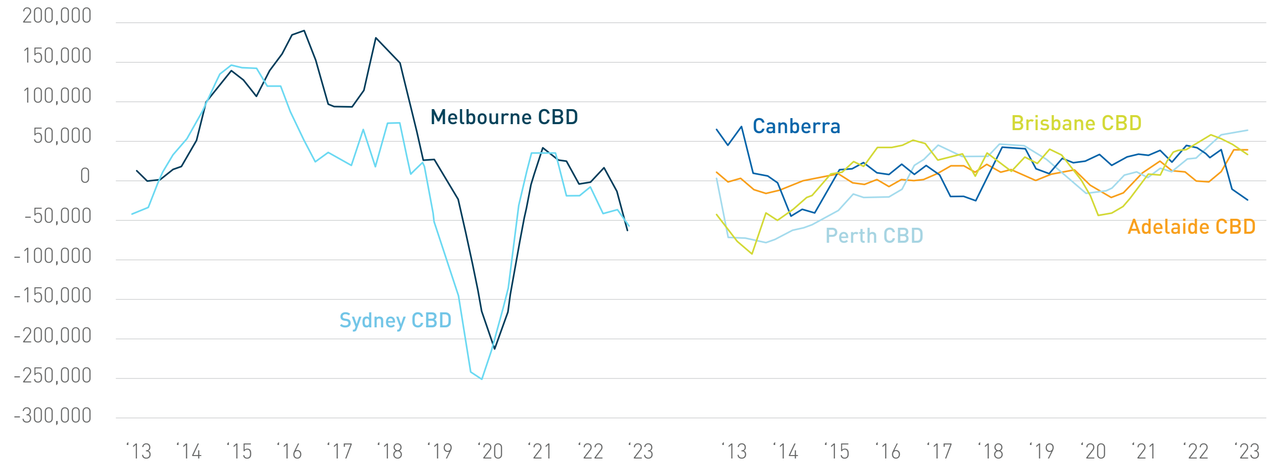
Subsequently, softer than expected inflation offshore and in Australia, together with dovish comments from central banks, helped take some of the heat out of bond yields through to December. Australian government 10-year bond yields decreased by 52bps over the quarter to 4.0%.

More recent data has shown Australia's annual inflation pace slowing quite materially from 4.9% in October to 4.3% in November[1]. While there could be an uptick in Q1 2024 due to base effects and government subsidies rolling off, there was little in the latest data which would give the RBA cause for concern. Goods inflation continued to slow, and services inflation appears to have peaked. While dwelling and rental costs and insurance premiums rose further, dining out and household services eased. Overall, inflation is on track to undershoot the RBA's forecast for the quarter, decreasing the likelihood of a hike in February.

While expectations of further cash rate hikes have diminished, 10-year bond yields remain approximately 40bps higher than a year ago[2], putting pressure on debt costs and access to capital. The macro impact of interest rates continues to be the main challenge facing commercial property, despite bottom-up demand drivers remaining relatively resilient. This is being reflected in higher capitalisation rates (effectively the earnings multiple for property), and in turn putting downward pressure on asset valuations.

1 Monthly Consumer Price Index Indicator, November 2023 (ABS, Jan-24)
2 Capital Market Yields – Government Bonds (RBA, Jan-24)

Net absorption YoY (sqm)



Source: JLL (Dec-23); Cromwell

In further economic data, the labour market remains tight, however there are signs of softer conditions emerging. Unemployment increased to 3.9% in November (latest available data), the highest it has been since May 2022 and slightly above consensus expectations (3.8%)[3]. Hours worked was flat over the month leading to a higher underemployment rate, job ads declined, and there were more applicants per job – all signs of slowing. Positively, the increase in the unemployment rate has been orderly and driven by strong population growth (i.e. supply), rather than job destruction. In fact, annual jobs growth increased to 3.2%, with 104,000 jobs created over the quarter-to-date (65% being full-time), a positive for office space demand.

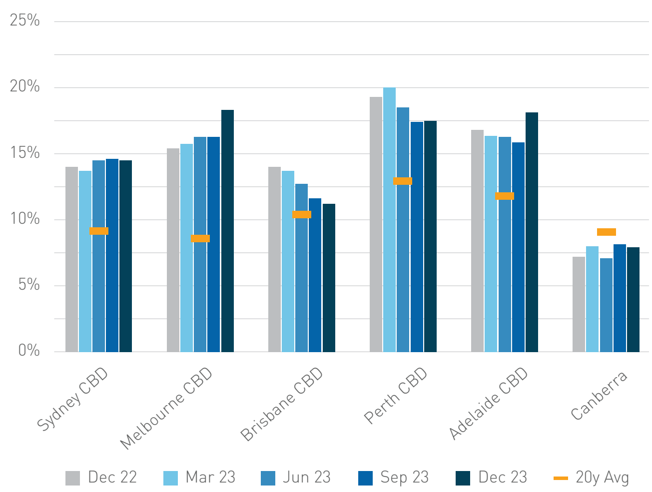
Office

There continues to be mixed demand readings between the major CBDs, largely aligned to the different industry compositions of the markets. According to JLL Research, national CBD net absorption totalled -59,000 square metres (sqm) across the quarter, the weakest result since March 2021. The resource-based markets of Brisbane (+9,000 sqm) and Perth (+7,000 sqm) both continued their run of positive demand, recording the strongest results of the quarter. Melbourne CBD recorded the weakest net absorption on a quarterly and annual basis, due to a couple of substantial A-Grade contractions in the Parliament precinct. It was the first quarter since March 2021 where Prime net absorption was weaker than Secondary net absorption.

> There continues to be mixed demand readings between the major CBDs, largely aligned to the different industry compositions of the markets.

The national CBD vacancy rate increased from 14.2% to 14.9% over the quarter, with the result following a similar pattern as net absorption. Brisbane CBD (-0.4%) recorded the biggest improvement in vacancy rate, while Melbourne CBD (+2.0%) deteriorated materially, due to the occupier contractions seen in the Parliament precinct. While headline vacancy remains elevated compared to the historical long-term average, particularly across Prime stock, the majority of CBD assets remain well-occupied (<10% vacancy).

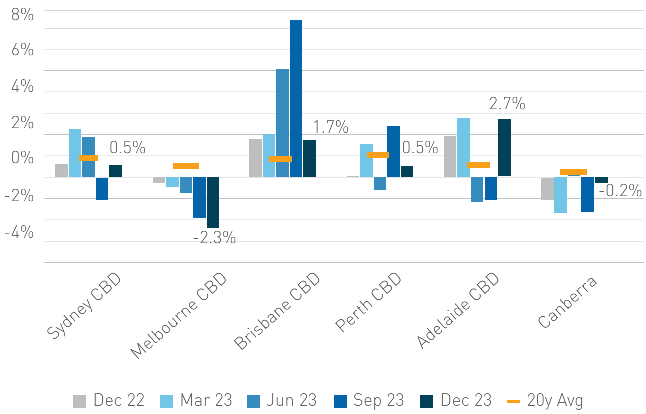
Total vacancy rate



Source: JLL (Dec-23); Cromwell

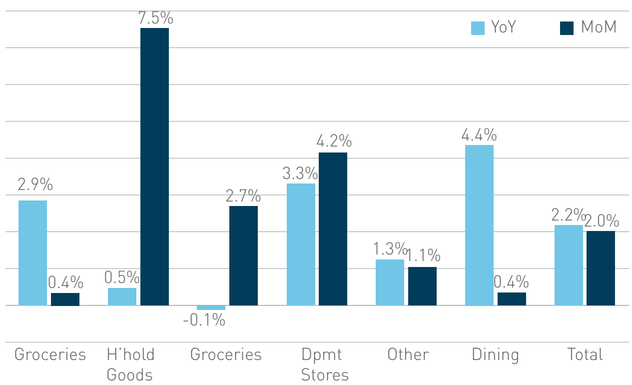
3 Labour Force, Australia, November 2023 (ABS, Dec-23)

Prime net effective rental growth (QoQ)



Sources: JLL (Dec-23); Cromwell

Retail Sales Growth (Nov-23)



Source: ABS (Nov-23); Cromwell

Adelaide joined Brisbane and Perth as CBD markets where net effective rents are higher today compared to pre-pandemic.

Prime net face rent growth (+0.9%) accelerated slightly compared to the prior quarter (+0.6%), with the Sydney CBD and Canberra the biggest improvers. Prime incentives were relatively stable across every CBD market except Melbourne (+1.0%) and Canberra (+0.3%). This meant that on a net effective basis, Melbourne and Canberra were the only markets where rents headed backwards over the quarter. Adelaide (+2.7%) recorded the strongest net effective rental growth, as Brisbane slowed after two quarters of very strong growth. Adelaide joined Brisbane and Perth as CBD markets where net effective rents are higher today compared to pre-pandemic.

Transaction volume for the quarter ($1.8 billion nationally) was roughly in line with the quarterly average over the rest of the year but was 66% lower than the Q4 average of the past five years[4]. The lack of transaction activity reflects the sharp increase in cost of capital seen over the past 18 months, and the gap between bidder and vendor price expectations which is taking time to align. It also reflects a lack of large transactions, with only one asset greater than $250 million changing hands during the quarter. This has been reflected in the total expansion of national CBD prime average yields to 120bps from peak pricing, with further expansion possible given the inherent lags in the valuation process.

Retail

There was a large rebound in retail sales in November (+2.0%), following a slow start to the quarter in October (-0.4%)[5]. November's monthly growth was the strongest result since November 2021, when activity was boosted by post-lockdown reopening. It is important to note that Black Friday sales had a large positive impact, with spending surging across household goods, department stores and clothing. A decent portion of this spending was likely 'brought forward' from December, so Christmas data (due 30 January 2024) may be weaker.

Consumers remain under pressure, with Westpac's measure of sentiment up in December but still at very pessimistic levels. While real disposable household incomes should improve in the latter half of 2024, elevated inflation and interest rates are expected to dampen per capita discretionary spending for some time yet.

Rental growth at large discretionary shopping centres continues to underperform though is positive. Large Format Retail was the top-performing sub-sector over the quarter, with rental growth benefiting from a lack of new supply across 2022 and 2023. This positive supply-demand dynamic saw Large Format vacancy decline over the quarter, while the other retail sub-sectors recorded slight increases.

It was a slow quarter for retail transactions, with volume totalling less than $1 billion. No large assets changed hands, following the sales of Stockland Townsville and Midland Gate Shopping Centre last quarter. As seen across most commercial property sectors, retail capitalisation rates expanded further over the quarter.

4 Real Capital Analytics, Jan-24
5 Retail Trade, Australia, November 2023 (ABS, Jan-24)

Industrial

Australia's industrial market remains the tightest in the world, with a national vacancy rate of 1.1%[6]. The city-level figures are book-ended by Melbourne (1.6%) and Sydney (0.5%), while Brisbane saw the biggest increase in vacancy rate (+0.8%) over the second half of 2023. Vacancy has been rising in most offshore markets across the year and the trend has now reached Australia, reflecting ongoing supply and a softening of demand. While vacancy is increasing, it remains well below long-term average levels.

Softening of demand is consistent with a slowing global economy (hence lower trade volumes) and an unwinding of some of the e-commerce gains made through the pandemic years. However, net absorption continues to be positive, particularly in Sydney and Melbourne where newly developed stock is being readily taken up by occupiers whose expansion in prior quarters was constrained by limited availability. While the demand cycle is starting to slowly turn, low vacancy helped generate national super prime net face rental growth of 15% year-on-year as at 4Q23 (preliminary data)[6]. Prime incentives remain low compared to historical levels at around 10-15%.

Supply delivered in 2023 was elevated at around double long-term levels. Higher levels of supply are earmarked for completion in 2024, however delays due to planning, infrastructure servicing, and construction will likely see some of this development pushed into the following year (as was seen in 2022 and 2023). Ongoing supply will likely put upwards pressure on the vacancy rate, however solid levels of pre-commitment (already almost 50% across the East Coast) limit the risk of a blowout.

While investors remain relatively positive on the industrial outlook, as with other sectors, transaction activity was nevertheless muted. Volume over the course of 2023 was soft compared to recent record highs, but roughly in line with levels seen in the three years prior to the pandemic.

Outlook

The Australian economy remains in a solid position despite global headwinds. Inflation is slowing, employment is solid and population growth will provide support to demand over the course of the year. The rate hiking cycle is nearing its end, financial stability has been maintained, and distress remains contained.

These factors put the Australian commercial property market in good stead from a demand perspective. Businesses continue to adjust size requirements for occupancy as they live with hybrid working, although in certain markets this is now largely known. Experiential workplaces with clever refurbishments and amenity continue to attract and retain quality tenants; something we continue to see within our assets. Capital continues to view Australia as a favourable investment destination given its attractive demographic profile, growth prospects, and relative social and political stability.

Powerful megatrends such as the need for more sustainable, energy efficient real estate, demographic shifts, and rising demand for segments serving the modern economy such as urban logistics, healthcare and highly amenitised offices will create income growth opportunities. ■

6 Australia's Industrial and Logistics Vacancy Second Half 2023 (2H23), CBRE (Dec-23)

ASX A-REIT MARKET UPDATE

DECEMBER 2023 QUARTER

Stuart Cartledge
Managing Director
Phoenix Portfolios

The S&P/ASX 300 A-REIT Accumulation Index moved substantially higher in the final quarter of 2023, gaining 16.5%. Property stocks meaningfully outperformed broader equities in the quarter, with the S&P/ASX 300 Accumulation Index adding a lessor 8.4%. This outperformance was driven by a large move in bond yields. After hitting a peak of approximately 5.0% during the quarter, the 10 Year Australian Government Bond yield dropped materially, finishing below 4.0%.

Property fund managers earnings are particularly leveraged to movements in bond yields. Given this it is unsurprising that they were major outperformers during the quarter. Charter Hall Group (CHC) had previously materially underperformed as bond rates rose, however recovered strongly, gaining 29.2% over the quarter. Centuria Capital Group (CNI) followed a similar path, rising 32.7% for the quarter. Goodman Group (GMG) as only a marginal outperformer for the period, lifting 18.6%, however had performed stronger earlier in 2023, finishing with a total return of 47.5% for the calendar year. In contrast, despite having a productive period from a business development perspective, property debt fund manager Qualitas Limited (QAL) only added 3.1% as its investment products will not directly benefit from a reduction in interest rates.

Those with exposure to residential property, particularly smaller capitalisation securities, were major underperformers across the December quarter. AV Jennings (AVJ) lost 9.1%, propelled lower by a heavily discounted, and somewhat surprising equity raise. Aspen Group (APZ) underperformed the index, only up 1.9%, with Peet Limited (PPC) similarly gaining only 4.5%. Performance was more robust for large capitalisation residential property developer Stockland (SGP), up 15.6%, just below the index's strong result.

Office property owners had very mixed results during the period. Leading the way higher was GPT Group (GPT) which rose 22.2% for the quarter. Centuria Office REIT (COF) was also an outperformer, recovering some of its recent underperformance, adding 20.2%. On the other side of the ledger, Australian Unity Office Fund (AOF) lost ground in an absolute sense falling 16.2%, whilst Dexus (DXS) gained only 8.9% after announcing current Chief Investment Officer, Ross Du Vernet will take over from Darren Steinberg as Chief Executive Officer of the company in 2024.

Retail landlords were very strong performers to finish off the year. The major outperformer was Unibail-Rodamco-Westfield (URW), who's share price shot 47.5% higher. As one of the more financially leveraged stocks in the sector, it is a relative beneficiary of lower global interest rates. Scentre Group (SCG) and Vicinity Centres (VCX) were also outperformers, up 21.5% and 20.4% respectively. Both are beneficiaries of more resilient consumer spending than anticipated, with initial indications of spending across the key Christmas period appearing robust.

In general, smaller capitalisation, non-benchmark property owners were substantial underperformers during the quarter. Each of Desane Group Holdings (DGH), 360 Capital REIT (TOT), Newmark Property REIT (NPR) and Gowings Brothers Limited (GOW) had negative absolute returns despite the movement in the Index and bond yields. In many cases this may be more representative of shorter term supply and demand dynamics for shares rather than underlying business underperformance.

Market outlook

The listed property sector is in good shape and provides investors with the opportunity to gain exposure to high quality commercial real estate at a meaningful discount to independently assessed values. While share market volatility may be uncomfortable at times, the offset is liquidity, enabling investors to rebalance portfolios without the risk of being trapped in illiquid vehicles.

Rising interest rates have been a headwind for many asset classes, with property, both listed and unlisted, a particularly interest rate sensitive sector. The August reporting season saw a number of listed stocks come under pressure as short term interest rates hedges are beginning to roll off and higher interest costs are impacting earnings growth and distributions. Long term valuations are driven by "normalised" interest costs, meaning the impact of short term hedges maturing is mostly immaterial. Should the sharp decline in interest rates seen in December 2023 be sustained, these headwinds may dissipate and possibly reverse.

The industrial sub-sector continues to be the most sought after, given the tailwinds of e-commerce growth, the potential onshoring of key manufacturing categories and the decision by many corporates to build some redundancy into supply chains to cope with current disruptions. All of these factors are contributing to ongoing demand for industrial space, which is evident by rapidly accelerating market rents and vacancy rates at historic lows of around 1% in many markets.

We remain cognisant of the structural changes occurring in the retail sector with the growing penetration of online sales and the greater importance of experiential offering inside malls. Recent performance of shopping centre owners has however been strong, with consumers showing resilience. It is interesting to note the juxtaposition of very high retail sales figures despite very low levels of consumer confidence, no doubt impacted by rising costs of living. Importantly, we are also now seeing positive re-leasing spreads in shopping centres, indicating strengthening demand from retail tenants.

The jury is still out on exactly how tenants will use office space moving forward, but demand for good quality well located space remains. Leasing activity is beginning to pick up, and there has also been some transactional activity, albeit at prices typically at discounts to book values. Incentives on new leases do remain elevated and some vacancy in the market is becoming apparent.

We expect to see further downside to asset values in office markets, but elsewhere expect market rent growth to largely offset cap rate expansion, particularly in industrial assets. Listed pricing provides a meaningful buffer to such movements.

OPEN FOR INVESTMENT

CROMWELL DIRECT PROPERTY FUND

Investment Report to 31 December 2023

The Fund's investment portfolio provides exposure to unlisted, direct property throughout Australia. The Fund aims to provide a monthly tax-advantaged income stream and future capital growth potential.

Please visit the Fund webpage for the latest performance figures: www.cromwell.com.au/dpf

KEY STATISTICS

as at 31 December 2023

Unit Price	**$0.9147**[1]
Distribution Yield	**5.2% p.a.**[2]
WALE	**4.2 years**[3]

PERFORMANCE

	1 Year	3 Years	5 Years	Inception (Aug-13)
Fund Performance After fees & costs	(24.1%)	(4.2%)	(0.4%)	5.1%
Benchmark PCA / MSCI Australia Unlisted Retail Quarterly Property Fund Index (Unfrozen)	(4.6%)	6.8%	9.3%	14.9%
Excess Returns After fees & costs	(19.5%)	(11.0%)	(9.7%)	(9.8%)

Past performance is not a reliable indicator of future performance.

FUND UPDATE

- Please refer to page 11 for an overview of what is happening in the real estate market and the market in general.
- The fund currently remains closed to applications until the audited December half-year financials are completed.
- The portfolio continues to experience positive leasing outcomes, with its current weighted average lease expiry being 4.2 years and occupancy sitting at 96.4%.
- The December valuation cycle has been completed, with the portfolio value falling 8.9%, on a gross basis, and the weighted average capitalisation rate expanding by 72 basis points to 6.87%.
- During the quarter, the Fund implemented new hedging which lifted the hedge ratio to 51.7% against drawn balances, and produced a weighted average hedge term of 1.85 years as at 31 December 2023.
- Since inception, the Fund has delivered an annualised return of 5.12% per annum with 12-month performance of -24.06%.
- The Fund's distribution rate will be adjusted to 4.75 cpu as of 1 January 2024 as Cromwell Funds Management continues to navigate a more difficult operating environment.

In addition to the footnotes below, please read the important disclaimer on the final page.

Applications for units in the Cromwell Direct Property Fund are temporarily suspended, with likely reinstatement in early 2024. Please refer to continuous disclosure notice dated 20 November 2023 and 15 January 2024 on our website for further information – www.cromwell.com.au/dpf.

Withdrawals are limited and cannot be guaranteed. Please note that as per the Update to Cromwell Direct Property Fund dated 29 September 2023, DPF ceased to offer redemptions from 1 October 2023 for a period of 6 months, see Continuous Disclosure Notices for more details. For further information, see Section 7.4 of the PDS.

1. Unit prices are calculated daily. See the PDS for further information and www.cromwell.com.au/dpf for latest pricing.
2. Based on distributions of 4.75 cents per unit p.a. effective from 1 January 2024 and ex-unit price of $0.9147 as at 31 December 2023.
3. Figures as at 31 December 2023. Calculated on a 'look-through' gross passing income basis.

See www.cromwell.com.au/dpf for further information.

OPEN FOR INVESTMENT

CROMWELL PHOENIX PROPERTY SECURITIES FUND ORDINARY UNITS

Investment Report to 31 December 2023

Cromwell Phoenix Property Securities Fund - Ordinary Units.
The Fund is one of the top performing property securities funds in Australia, with underlying investments chosen by Phoenix Portfolios using a 'best ideas' approach.

Please visit the Fund webpage for the latest performance figures: www.cromwell.com.au/psf

KEY STATISTICS

as at 31 December 2023

Status	**OPEN**[1]
Unit Price	**$1.163**[2]
Distribution Yield	**N/A**

PERFORMANCE

	1 Year	3 years	5 years	10 years	Inception (Apr-08)
Fund Performance After fees & costs	9.8%	5.4%	5.6%	9.4%	7.7%
Benchmark S&P/ASX 300 A-REIT Accumulation Index	16.9%	5.9%	6.4%	9.4%	4.8%
Excess Returns After fees & costs	(7.1%)	(0.5%)	(0.7%)	0.0%	2.9%

Past performance is not a reliable indicator of future performance.

TOP TEN STOCK HOLDINGS[3]

- ABACUS GROUP
- CENTURIA INDUSTRIAL REIT
- CHARTER HALL GROUP LIMITED
- GENERAL PROPERTY TRUST
- GOODMAN GROUP
- HOTEL PROPERTY INVESTMENTS
- MIRVAC GROUP
- PEET LIMITED
- SCENTRE GROUP
- STOCKLAND LTD

FUND UPDATE

- Since inception in April 2008, the Fund has delivered an annualised return, net of fees, of 7.7%, outperforming the S&P/ASX 300 A-REIT Accumulation Index by nearly 3.0%.
- The S&P/ASX 300 A-REIT Accumulation Index shot higher over the quarter, adding 16.5%, driven by falling bond rates.
- Unibail-Rodamco-Westfield (URW) along with property fund managers were the major outperformers.
- The Fund's holdings in Charter Hall Group and URW were additive to absolute and relative returns.
- The Fund lost value through its holding in Peet Limited and relative value from an underweight holding in Goodman Group.

In addition to the footnotes below, please read the important disclaimer on the final page.

Phoenix Portfolios Pty Ltd ABN 80 117 850 254 AFSL 300302 (Phoenix) is the investment manager of the Fund. None of CFM, Phoenix nor their related entities, directors or officers makes any promise or representation, or gives any guarantee as to the success of the Fund, distributions, amount you will receive on withdrawal, income or capital return or the taxation consequences of investing.

1. Withdrawals cannot be guaranteed and are subject to the assumptions and risks set out in the Product Disclosure Statement dated 15 November 2023 (PDS).
2. Unit price as at 31 December 2023. Unit prices are calculated daily. See the PDS for further information and www.cromwell.com.au/psf for latest pricing.
3. As at 31 December 2023. Positions in the Fund are subject to change.

See www.cromwell.com.au/psf for further information.

OPEN FOR INVESTMENT

CROMWELL PHOENIX GLOBAL OPPORTUNITIES FUND

Investment Report to 31 December 2023

The Fund invests in a portfolio of internationally listed, predominantly small capitalisation securities, which at the time of their acquisition, are considered to be trading at discounts to their observable net asset values (NAVs).

Please visit the Fund webpage for the latest performance figures: www.cromwell.com.au/gof

KEY STATISTICS

as at 31 December 2023

Status	**OPEN**[1]
Unit Price	**$1.2962**[2]
Distributions	**Annually**

PERFORMANCE

	6 Months	1 Year	2 Years	3 Years	Inception (Dec-19)
Fund Performance After fees & costs	5.0%	14.0%	4.7%	10.5%	10.3%
Benchmark Vanguard Total World Stock ETF	4.8%	21.7%	3.2%	10.0%	9.3%
Benchmark MSCI World Microcap AUD	2.4%	7.0%	(8.2%)	0.5%	4.4%

Past performance is not a reliable indicator of future performance.

FUND UPDATE

- Since inception in December 2019, the Fund has delivered an annualised return of 10.3% net of fees.
- The Fund delivered a net return of 5.7% over the December 2023 quarter, outperforming both large capitalisation and small capitalisation indices.
- Contributing positively to performance over the quarter were positions in:
  - Industrial Logistics Property Trust (NASDAQ:ILPT)
  - Spirit Airlines (NYSE:SAVE)
  - Park Hotels (NYSE:PK)
  - Osaka Steel (TSE:5449)
  - Sun Corporation (TSE:6736)
- Detracting from performance over the quarter were positions in:
  - Melco International Development Limited (SEHK:200)
  - Burelle SA (ENXTPA:BUR)
  - Akita Drilling (TSX:AKT.A)
  - Sotherly Hotels (NASDAQ:SOHO).

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1. Withdrawals cannot be guaranteed and are subject to the assumptions and risks set out in the Product Disclosure Statement dated 26 October 2021 (PDS).
2. Unit prices are calculated monthly. See the PDS for further information and www.cromwell.com.au/gof for latest pricing.

See www.cromwell.com.au/gof for further information.

CLOSED FOR INVESTMENT

CROMWELL PHOENIX OPPORTUNITIES FUND

Please visit the Fund webpage for the latest performance figures: www.cromwell.com.au/pof

CROMWELL PROPERTY TRUST 12

Please visit the Fund webpage for the latest performance figures: www.cromwell.com.au/c12

CROMWELL RIVERPARK TRUST

Please visit the Fund webpage for the latest performance figures: www.cromwell.com.au/crt

CROMWELL PROPERTY GROUP