AUSTRALIAN PROPERTY OPPORTUNITIES FUND

QUARTERLY UPDATE 31 DECEMBER 2016

The Australian Property Opportunities Fund (**APOF I** or **the Fund**) is pleased to provide this update for the December quarter 2016 (**4Q 2016**).

KEY HIGHLIGHTS

- Announced a distribution of $0.0249 per Unit.
- 3 assets independently re-valued during the quarter resulting in a $18.9m, or 11%, uplift in value.
- Portfolio occupancy steady (currently at 97%).
- The Fund's weighted average lease expiry (WALE) remained strong at 4.8 years.

PORTFOLIO UPDATE

ASSET MANAGEMENT

Occupancy at Oxford Village remained steady during the quarter at 98%. As reported last quarter, four tenants have renewed their leases and are in the initial stages of planning their refurbishment works, with construction due to start next quarter. These tenancy refurbishments will rejuvenate the western side of the centre by creating brighter, more inviting stores. A new tenant, Mister Dee's Kitchen, opened in November 2016 and has reported solid initial trading conditions. The majority of the central plant upgrade works were completed in December 2016. The upgrade included the installation of two new chillers and a new building management system. We expect to see a significant reduction in energy consumption and running costs over the coming months.

The occupancy rate at 390 St Kilda Road declined marginally from 100% to 96% during the quarter. The decrease was due to the termination of one tenant for failure to pay rent and two tenants vacating on lease expiry. One new lease was executed during the quarter and the leasing team are confident of filling the remaining vacancies. There are some small improvements planned for the property, which are in their initial design phases, including building signage and a lobby upgrade. We reported last quarter that an end of trip facility may be included, however, after further analysis a lobby upgrade was viewed as more beneficial to the property.

Lake Innes continued to record increasing sales, up 9.7% on the prior year. Coles progressed refurbishment plans with their works scheduled to start next quarter. The plans include relocating the trolley bay outside of the supermarket, which will provide Coles with more selling space, and updating store design. The centre's occupancy rate was unchanged from the prior quarter at 99%.

At Lynbrook Village Shopping Centre, sales increased slightly over the year. Occupancy remained at 97%. The leasing team continued to focus on renewals and secured lease extensions with three tenants. The competitive landscape shifted during the quarter. Woolworths opened a supermarket at nearby Casey Central, while Coles closed their nearby Hampton Park store late in the quarter. Management are monitoring the overall affect on sales at our Lynbrook centre, however, initial figures have indicated only minimal changes.

At Windsor Riverview, two lease renewals during the quarter saw the lease expiry profile improve, while the occupancy rate remained at 95%. A new lease was agreed with the medical centre over an expanded area. The expansion includes incorporating a second tenancy into the practice and creating consultation rooms on the second level. Efforts to increase engagement with the local

Windsor Riverview – new logo

community continued, with marketing focused on local schools and charities. One marketing activity undertaken during the quarter was a public competition to design a new logo for 'Windsor Riverview', with a prize awarded for the best design. The winning logo has been used to create new branding and signage for the centre.

Noosa Village occupancy increased to 100%, following a new short-term lease. We began lifecycle replacement of the centre's air conditioning system during the quarter given the age of some of the equipment. Three package units have been replaced to date and the remaining four units will be replaced over the next twelve months. A minor refurbishment of the centre is also in the early design phase and includes repainting of the external façade, updating centre signage and modernising design features.

CAPITAL MANAGEMENT

The Fund announced a distribution of $0.0249 per Unit during the quarter, representing a 6.2% annualised distribution yield. During the period, the Fund had three assets, representing over 60% of the portfolio's value, independently re-valued. This resulted in an $18.9m, or 11%, uplift in each of these asset values and a firming in the weighted average capitalisation rate across those three assets of 50bps, from 7.25% to 6.75%. The Fund's gearing ratio will decline to approximately 40% as a result of the positive revaluations.

REAL ESTATE MARKET UPDATE

RETAIL

While Australian retail turnover continues to grow, the rate of growth has slowed over the last two years. Growth reached a peak in October 2014 at 5.7% p.a. and by October 2016 had slowed to 3.7% p.a. The slowdown is largely attributable to food price deflation. The slowdown in the food category was partially offset by accelerating growth in clothing, footwear, personal accessories and department stores. Clothing recorded 5.7% year on year growth in October 2016.

Overall, retail competition remains strong, particularly within specific sectors. This has resulted in several chains entering into voluntary administration during 2016. Retail chains which closed during the year included Dick Smith, Payless Shoes, Pumpkin Patch, Masters and Howards Storage World. This underlines the importance of tenant selection and having a portfolio with a high proportion of non-discretionary income. Across the portfolio, there was only one store vacancy as a result of the above closures which was Dick Smith at Windsor Riverview, with this tenancy now leased to a well trading toy store. This is a reflection of the detailed analysis and hard work the team has undertaken to build a defensive portfolio.

Sydney and Melbourne markets continued to record low single digit rental growth, predominantly driven by the CBD precincts and bulky good categories. Rents remained broadly stable in South East Queensland, Perth, Adelaide and Canberra.

The quarter saw the continued trend of yield compression for retail assets.

OFFICE

Office sector lead indicators were mixed in 2016, however, business confidence remained positive. Firmer confidence was reflected in job advertisements, with the growth in advertisements accelerating to 6.1% over the 12 months to November 2016. The turnaround in job advertisements is a positive sign for employment growth after the momentum in the Australian labour market subsided during the second half of 2016.

Higher commodity prices benefited the Brisbane and Perth office markets. Brisbane CBD has shown some signs of recovery to date.

Leasing enquiry and activity was robust in the Melbourne CBD. Positive leasing activity and evidence of increasing demand for space, continued to exert upward pressure on effective rents. Confirmation is expected of a prime gross effective rent increase by 4.0% over Q4, equating to an increase of 10.5% over 2016.

The volume of leasing activity, completions and stock withdrawals has made calculating Sydney's physical market indicators more challenging in Q4. A reduction of Sydney CBD leasing incentives is expected, along with a prime gross effective rent increase of 6.0% in Q4 and 17.6% over 2016.

Yield compression was less pronounced in Q4, with the most significant compression occurring in the Melbourne CBD. The tighter end of the Melbourne CBD prime equivalent yield range is now only slightly softer than the Sydney CBD.

INDUSTRIAL

Investment demand remained buoyant, although there was an apparent lack of stock for sale on-market in 2016. While transaction dollar volumes are expected to have remained near record highs, these were most likely supported by a few, large, off-market transactions during the year.

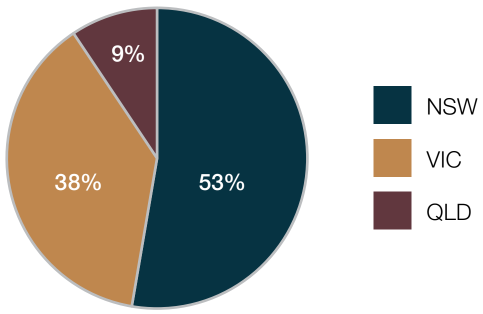
Prime rents were generally flat during the quarter. This overall trend was impacted to a small degree by pockets of growth in South Sydney and North Sydney and weakness in Perth. Over the year, strong growth was recorded in South Sydney (8.1%), North Sydney (3.6%) and South East Melbourne (4.0%). Other markets were broadly flat, to mildly negative, over the year.

FUND STATISTICS

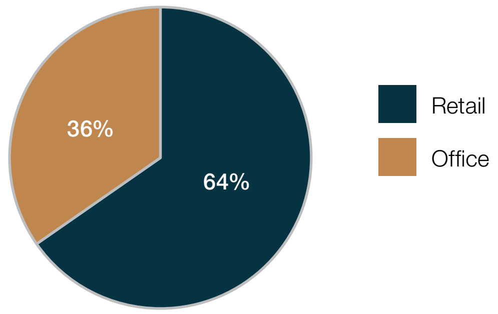
PORTFOLIO SUMMARY	OCCUPANCY (%)	VALUE ($M) [1]
Oxford Village, Darlinghurst NSW	98	82.9
390 St Kilda Road, Melbourne VIC	96	81.0
Windsor Riverview Shopping Centre NSW	95	51.7
Lynbrook Village, Lynbrook VIC	97	34.6
Noosa Village, Noosaville QLD	100	26.8
Lake Innes Village, Port Macquarie NSW	99	27.5
Total	97	304.5

[1] As at 30 September 2016, except for Oxford Village, 390 St Kilda Road and Lake Innes Village which have already been independently re-valued at 31 December 2016, resulting in a combined $18.9m, or 11%, valuation uplift. The Fund is currently in the process of finalising its half-yearly property valuation appraisals. An updated property portfolio valuation will be included in the 31 December 2016 half-year financial report, which the Fund anticipates releasing in March 2017.

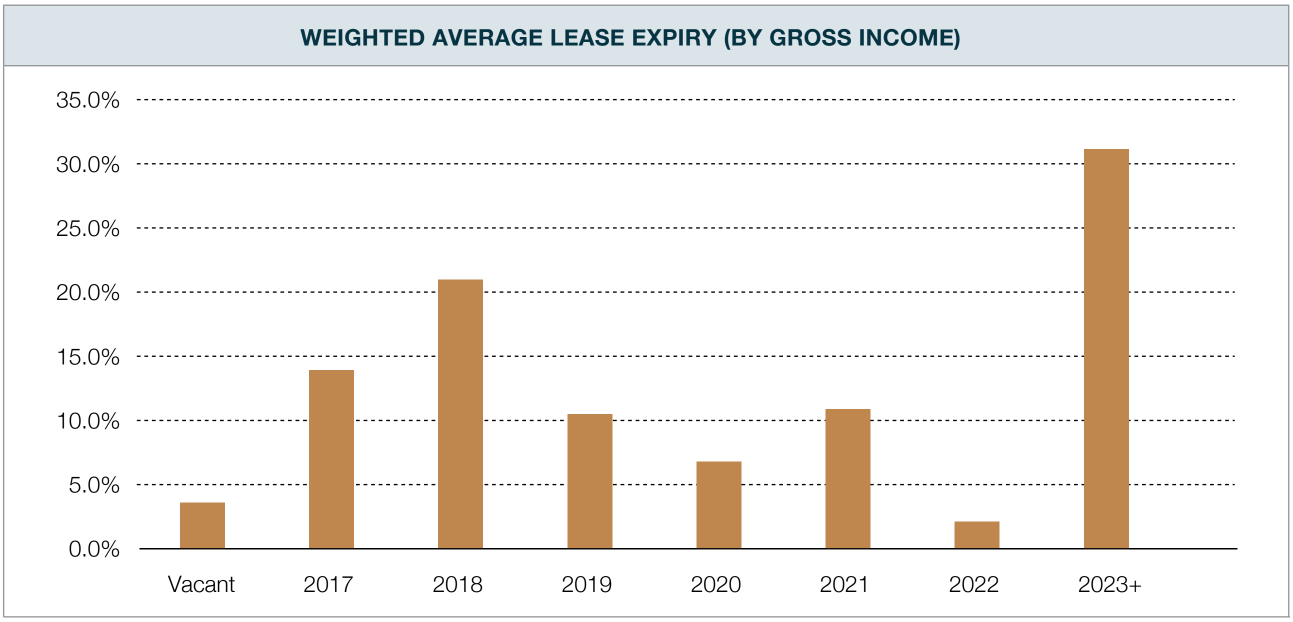
GEOGRAPHY DIVERSIFICATION
(by current value)



SECTOR DIVERSIFICATION
(by current value)



TOP TENANTS (BY GROSS INCOME)	
Wesfarmers (from Coles and Liquorland)	15%
Study Group Australia	11%
Fitness First Australia	4%
Woolworths (including BWS)	3%
Toll Transport	3%



Source: Fort Street Real Estate Capital, JLL

For more information, visit **apof.com.au** or email **info@australianpropertyopportunitiesfund.com.au**.

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