

Investor Update

1. Introduction

Abacus Wodonga Land Fund and Abacus Wodonga Mortgage Fund (together, the **Wodonga Fund**) were established in June 2005 by Abacus Funds Management Limited to undertake a staged land subdivision project in Wodonga (the **Project**).

Since this time, a great deal of progress has been made and we set out below a summary of the key achievements. However, more recently the global financial crisis has had a significant impact on the Project with credit conditions deteriorating significantly. In particular, it has become increasingly difficult to obtain senior debt funding on acceptable terms for real estate development projects. In addition, there has been a downturn in the Australian economy, increased unemployment and lower consumer confidence. These and other factors have unfortunately impacted adversely on the likely returns for investors in the Wodonga Fund, to the extent that investor capital may be at risk. This is described in more detail below.



2. Project Review

The Wodonga Fund

Pursuant to a Product Disclosure Statement dated 29 June 2005, investors subscribed \$10 million to the Abacus Wodonga Land Fund (the **Land Fund**) and \$10 million to the Abacus Wodonga Mortgage Fund (the **Mortgage Fund**). For every \$1.00 subscribed, investors received one \$0.50 unit in each fund, representing two separate investments with different terms and conditions.

The Land Fund owns the underlying land and is undertaking the Project.

The \$10 million raised by the Mortgage Fund was on-lent to the Land Fund at 12%pa. This loan is the only asset of the Mortgage Fund. This has generated a 12%pa return on the invested capital in the Mortgage Fund.

Distributions from the Mortgage Fund have been paid to investors six-monthly since inception, providing investors with a 6%pa return on their total capital invested in the Wodonga Fund.

The Project

Utilising the proceeds of the capital raising and additional debt, the Land Fund has acquired approximately 173 hectares of land in Wodonga, Victoria.

Known as "White Box Rise", the Project is planned to ultimately provide approximately 1,000 residential lots around a town centre with sites for a primary school, supermarket and shops, community centre, aquatic centre, specialised aged care facility, service station and a bulky goods facility. It was initially expected that the Project would be a staged development over a term of approximately eight years, with completion due in 2013.

Planning approval for the Project was obtained and the infrastructure development for the initial stages of the Project has been completed, comprising 178 residential lots and a 13 lot display village plus the neighbourhood centre, school site, service station and community centre. The residential display village has been completed and comprises 13 lots. The Land Fund does not itself construct homes or commercial developments; rather, it sells developed land.

The first residential lots other than the display homes became available for sale in November 2008. This was later than originally anticipated due to delays in the town planning approval process. However, since November 2008, the Project has progressed well, with the following results achieved:

- As at 30 September 2009, 85 residential lots had been sold and settled for a total value of approximately \$9.1 million. In addition, a further 34 contracts had been entered into (but not settled) for a total value of approximately \$3.0 million.
- The shopping centre site was sold in January 2009 for \$5 million. Construction is due to commence in December 2009. The shopping centre will include a supermarket and a variety of retail stores.
- The school site was sold in November 2008 for \$3.2 million. Construction is expected to commence in December 2009.
- A community centre is also being developed by the council in conjunction with the new school.
- State government and the local council have confirmed that funding is available to build a new aquatic centre.

In light of the difficult economic environment over the past year, we have been very pleased with the value of the land sales achieved. However, the slowdown in the Australian economy, negative consumer sentiment and increased local competition have caused the value and rate of sales to be lower than originally anticipated. This has resulted in reduced revenues and increased holding costs, and has extended the anticipated Project life.



3. 2009 Annual Accounts Summary

The Mortgage Fund earned a profit attributable to members of \$1.2 million for the full year ended 30 June 2009.

A distribution of \$1.2 million (6 cents per unit) was declared and provided for in respect of the full year ended 30 June 2009. Distributions paid and payable represent a 12% annualised return for the year ended 30 June 2009.

The Land Fund reported a net loss attributable to members of \$4.4 million for the full year ended 30 June 2009. The loss is largely the result of the write-down in the value of the underlying property by \$5.8 million to \$54.5 million to reflect the current market conditions. No distribution was paid.

Income Statement Summary

Year ended 30 June 2009 (A\$ millions)	Land Fund	Mortgage Fund
Total Revenue	13.2	1.2
Total Expenses (including tax)	17.6	-
Net (Loss) Profit after Tax	(4.4)	1.2

Balance Sheet Summary

As at 30 June 2009 (A\$ millions)	Land Fund	Mortgage Fund
Total Assets	58.9	10.6
Total Liabilities	54.3	0.6
Net Assets	4.6	10.0
Net Asset Value (NAV) per Unit (\$)	\$0.23	\$0.50

The combined NAV as at 30 June 2009 for the Wodonga Fund is \$0.73 (ie one unit in the Land Fund and one unit in the Mortgage Fund).

Full Financial Reports for the Land Fund and the Mortgage Fund are available from the Abacus Property Group website www.abacusproperty.com.au

4. Current Wodonga Fund Issues

Despite the good progress made over the past year, there are a number of significant issues facing the Wodonga Fund that will impact adversely on the future returns to investors. These issues include:

- The consequences of the longer than expected Project life.
- Difficulties in securing bank finance.
- The capital structure of the Wodonga Fund.

4.1 Extended Project Life

The original expectation was a Project life of around 8 years from 2005 to 2013. The Project is now likely to have a Project life of up to 14 years (ending 2019) due to the following factors:

- Delays in achieving the requisite town planning consents.
- Increased competition in the local market leading to slower than expected sale rates (ie 25 lots per quarter expected now compared with 50 lots per quarter in the original Project feasibility).
- The global financial crisis and the flow-on impact of reduced consumer confidence and reduced credit availability.

The longer Project life will negatively affect investor returns as a result of increased holding costs. This will have the effect of reducing and delaying distributions.

4.2 Bank Finance

As at 30 September 2009, the Land Fund had drawn \$18.1 million under a first mortgage debt facility. The key terms of the facility include:

- A maximum 55% loan to valuation ratio (LVR). The bank accepted mortgage valuation at April 2009 was \$49.8 million (comprising the realisable value of the developed lots plus the value of the remaining undeveloped land), potentially allowing a maximum drawdown under the facility of \$27.4 million. While the debt balance of \$18.1 million is less than the \$27.4 million facility limit, the facility does not permit re-draws.
- Two year term expiring on 30 June 2010.
- A facility margin of 2.5% which, combined with a fixed interest rate of 7.05%pa, has created an average cost of debt of 9.55%pa.
- The Fund previously had a covenant requirement to sell 15 lots per quarter at not less than 90% of valuation. The bank has agreed to a reduction in the value of lots available for sale by approximately 15% in line with the

latest required valuation but increased the number of sales from 15 to 18 in any quarter. These changes to the Fund's borrowing arrangements resulted in the effective interest rate being increased from 8.55%pa to 9.55%pa. Currently the Land Fund is exceeding the minimum quarterly sales rate.

- All proceeds from the sale of lots are to be applied to the repayment of bank debt and interest on the bank loan.

The key implications of the first mortgage debt facility for investors are:

- The application of all sale proceeds to the repayment of principal and interest means that no sales proceeds are available to fund the Project and its holding costs, nor are they available to repatriate capital (or pay interest/dividends) to Abacus or to investors. This has necessitated further calls on the Abacus mezzanine loan facility to fund the Project.
- The interest payable by the Land Fund to the Mortgage Fund (12%pa) can be funded only by further advances on the Abacus mezzanine loan facility at a 14%pa interest rate (plus a 1%pa line fee on any undrawn funds on the \$30 million facility limit).
- Interest on the outstanding balance of the Abacus mezzanine loan is accruing (and compounding) at 14%pa (plus a 1%pa line fee on any undrawn funds on the \$30 million facility limit) in priority to investor capital.
- The current average cost of the bank debt (9.55%pa) is higher than originally forecast. Additionally, the facility's requirement that all sales proceeds be applied to the reduction of the bank debt will result in the Land Fund being overhedged (ie the amount of hedging to secure fixed interest rates exceeds the actual loan balance), creating a negative cash flow after the outstanding principal balance falls below \$20m.

Both the pricing and conditions of the bank facility (including the requirement to apply all sales proceeds against outstanding principal) are consistent with now prevailing market terms.

The current facility expires on 30 June 2010 and, unless market conditions demonstrably improve, it is likely that the terms of a replacement facility will be similar.

Finally, a pre-condition of any refinancing will be obtaining a new mortgage valuation. Were this valuation to indicate a lower valuation per lot than the previous valuation, then the carrying value of the property in the Land Fund would need to be reviewed and another write down may be required.

4.3 The Capital Structure

In addition to the bank debt described above, the Land Fund is capitalised with:

- \$24.6 million drawn on the Abacus mezzanine loan (as at 30 September 2009); and
- \$20 million of investor capital, split as to \$10 million equity in the Land Fund and \$10 million equity in the Mortgage Fund.



4.3.1 Abacus mezzanine loan facility

As envisaged by the original Product Disclosure Statement, Abacus has provided a second-ranking secured loan facility to the Land Fund to enable it to fund Project costs, including the interest payable to the Mortgage Fund. Funds advanced under this facility attract an interest rate of 14%pa, and any undrawn funds on the \$30 million facility limit attract a line fee of 1%pa.

Since the Project's inception, the Land Fund has drawn \$24.6 million (as at 30 September 2009) on the Abacus mezzanine loan facility to fund capital works, interest payments to the Mortgage Fund, Project management fees, interest and fees accrued on the mezzanine loan and running and holding costs.

It was originally envisaged that the mezzanine loan would be repaid out of land sales and refinancing of the bank debt facility as the capital works increased the value of the Property. However, due to the current state of credit markets and the terms of the first mortgage debt facility, this has not been possible. Consequently, investors now have a \$24.6 million mezzanine debt facility ranking ahead of their position, which accrues interest at 14%pa (plus a 1%pa line fee on any undrawn funds on the \$30 million facility limit).

The original term of this loan expires on 31 May 2010.

4.3.2 Unitholder Capital

(a) Mortgage Fund

In respect of the \$10 million loan to the Land Fund, interest has been funded by the Land Fund borrowing the annual interest cost (approximately \$1.2 million pa) from Abacus under the terms of the mezzanine loan facility.

Pursuant to the Product Disclosure Statement, Abacus agreed to fund (via the mezzanine loan facility) these interest payments until 30 June 2008, and has continued to do so beyond this date in order to assist the Wodonga Fund.

The Mortgage Fund's loan to the Land Fund is due for repayment in May 2010, but the Land Fund will not be able to repay the Loan.

(b) Land Fund

Based on the carrying value of the Property and the Land Fund's balance sheet at 30 June 2009, the current book value of the \$10 million unitholder equity in the Land Fund is \$4.6 million.



5. Changes To The Capital And Fee Structure

In light of the current credit environment and terms of a first mortgage debt facility for a project of this type, Abacus has resolved to make the following changes to the Wodonga Fund's capital structure:

- (i) Abacus will extend the term of its mezzanine loan from 31 May 2010 to 31 May 2015 and reduce the interest rate from 14%pa (plus a 1%pa line fee on any undrawn funds) to 10%pa on the drawn amount only, effective from 1 January 2010.
- (ii) Abacus will extend the term of the loan by the Mortgage Fund to the Land Fund from 31 May 2010 to 31 May 2015. In addition, interest on this loan will be suspended from 1 January 2010. This will mean that distributions will be suspended until the bank debt facility has been refinanced, the Project performance has been reviewed (taking into account the impact of the reduction in the first home owner's grant) and sufficient proceeds are being generated to allow for the resumption of interest payments on the loan. The distribution for the six month period to 31 December 2009 will be paid in February 2010.
- (iii) The annual management fee of 1%pa of the gross assets of the Land Fund payable to each of the Gillon Group and Abacus will be reduced from 1 January 2010 to 0.5%pa each plus a bonus of 0.2%pa each if a minimum number of sales of 18 lots per quarter is achieved. Subject to future Project performance, the revised fees may be reviewed and amended

6. Conclusion

Based on the current state of the capital and real estate markets, our modelling of potential future returns to investors suggests that there are reasonable prospects for Wodonga Fund investors to recoup their capital and, potentially, receive a small return.

There are many factors that could have a positive or negative impact on this outlook, including:

- Sales rates of the remaining residential lots.
- Sales prices for the remaining residential lots.
- The terms of the next first mortgage debt facility.

However, until we see a marked improvement in credit markets, we anticipate that it will be several years before investors start receiving any return of capital.

We are obviously disappointed to be writing to you in these circumstances, particularly given the recent progress that had been made with the underlying land subdivision project at Wodonga. However, in light of uncertain economic and credit market conditions, we believe that the changes to the capital and fee structure outlined above reduce the risks associated with the Project and improve the outlook for future investor returns.

