

Arena REIT

(ASX CODE: ARF)

Annual results to 30 June 2013

Positioned for earnings growth

30 August 2013

arenainvest.com.au



Presenters



Bryce Mitchelson

Joint Managing Director

- Joined Arena in 2009.
- Previously held senior positions with Centro Properties Group and Heine Management Limited.



James Goodwin

Joint Managing Director

- Joined Arena in 2011.
- Previously held senior positions with Becton Property Group, Centro Properties Group and Freehills.



Vin Harink

Senior Portfolio Manager

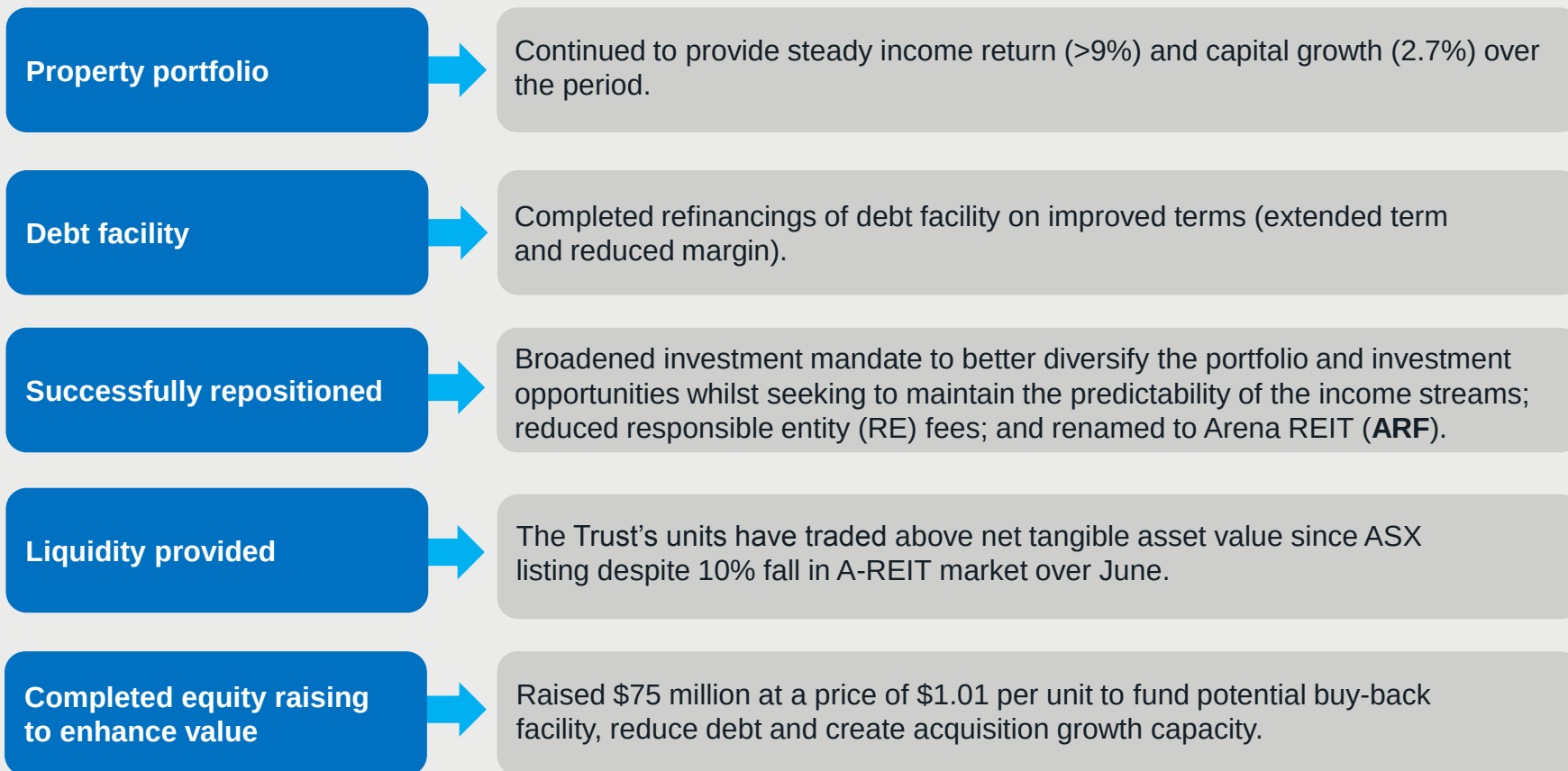
- Joined Arena in 2009.
- Previously CEO of Austock Property Funds Management.

Agenda

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1. Key achievements

A landmark year



2. Financial highlights

Solid improvement in earnings and a strengthened financial position

Performance for year ended	FY13	FY12	Change
Statutory net profit (million)	\$17.2	\$15.7	9.8%
Distributable income (million)	\$11.2	\$8.5	31.8%
Distributable income per unit	8.2 cents	6.4 cents	28.1%
Distributions per unit	8.0 cents	6.5 cents	23.1%
Tax deferred component (%)	82.8%	100%	(17.2)%
Return on equity (%)	12.6%	11.8%	+80bps

Financial position	30 June 2013	30 June 2012	Change
Total assets (\$ million)	\$241.3	\$240.2	0.5%
Balance sheet gearing (%)	10.4%	41.7%	(75.0)%
Net asset value (\$ million)	\$210.1	\$132.8	58.2%
ASX market capitalisation (\$ million) ¹	\$218.7	Not applicable	
Net tangible asset value per unit (\$)	\$1.02	\$1.00	2.0%

Notes

¹ Based on closing price of \$1.065 as at 29 Aug 2013

3. FY13 Financial results – income statement

FY13 distributable income increased by 31.8%

\$million	FY13	FY12	Change
Income			
Lease rental income	21.3	21.7	(2.1%)
Other income	0.7	0.8	(12.1%)
Expenses			
Direct property expenses	(0.8)	(1.1)	(21.2%)
Management fees	(2.4)	(2.4)	(1.1%)
Administration expenses	(1.0)	(0.9)	5.7%
Finance costs	(6.6)	(9.6)	(31.4%)
Distributable income	11.2	8.5	31.8%
Straight-line rental income	0.5	0.7	(33.6%)
Revaluation gain on investment properties	5.2	8.7	(40.6%)
Change in fair value of derivatives	(0.1)	(4.2)	(96.7%)
Revaluation gain on securities interest	1.4	1.4	2.2%
Other	(1.0)	0.6	(266.7)%
Net statutory profit	17.2	15.7	9.8%
Distributable income per unit (cents)	8.2	6.4	28.1%
Distributions per unit (cents)	8.0	6.5	23.1%

- Rental income is slightly down due to the sale of the New Zealand portfolio in April 2012. Adjusting for the NZ sale, total Australian portfolio income was up 2.8%.
- FY13 trust expenses includes \$0.2 million of one-off expenses.
- Significant finance cost savings generated from improved financing terms, repayment of debt and close of swaps from New Zealand sale proceeds.
- Revaluation gain based on 47 Independent and 119 Director valuations. Primary driver of valuation increases is growth in underlying rent.
- Distributable income and distributions in-line with May 2013 PDS forecast of \$11.1 million (refer Annexure 4).

3. FY13 Financial results – FFO

FFO increased by 31.8%

\$m	FY13	FY12	Change
Distributable income	11.2	8.5	31.8%
Other adjustments	0.0	0.0	0.0%
Funds from operations	11.2	8.5	31.8%
Interest rate derivative close out costs	(2.1)	(3.3)	(36.4%)
Adjusted funds from operations	9.1	5.2	75.3%
FFO per unit (cents)	8.2	6.4	28.1%
AFFO per unit (cents)	6.7	3.9	71.8%

Notes

FFO and AFFO presented using principles of Property Council of Australia White Paper released in May 2013.

- FFO same as distributable income.
- AFFO reflects the close out of interest rate derivatives.
- FY13 interest rate derivatives close out of \$86 million due to repayment of debt from IPO proceeds. The Trust's interest expense was 100% hedged at 30 June 2013.
- FY12 interest rate derivatives close out – used proceeds from New Zealand portfolio sale.

3. FY13 Financial results – balance sheet

Balance sheet gearing reduced from 41.7% to 10.4%

\$ million	FY13	FY12	Change
Cash	5.0	5.6	(10.2%)
Trade and other receivables	1.9	3.0	(36.7%)
Investment properties	234.9	226.3	3.8%
Indirect investments	0.0	6.4	(100.0%)
Total assets	241.8	241.3	0.2%
Trade and other payables	3.3	3.6	(8.3%)
Distributions payable	3.3	2.6	23.7%
Borrowings	25.0	100.2	(75.0%)
Interest rate swaps	0.1	2.0	(96.5%)
Total liabilities	31.7	108.5	(76.8%)
Net assets / unitholder equity (\$m)	210.1	132.8	58.2%
Number of units on issue (m)	206.3	132.1	+74.2
Net tangible asset value / unit (\$)	1.02	1.00	+0.02
Gearing ratio (%)	10.4%	41.7%	(75.0)%

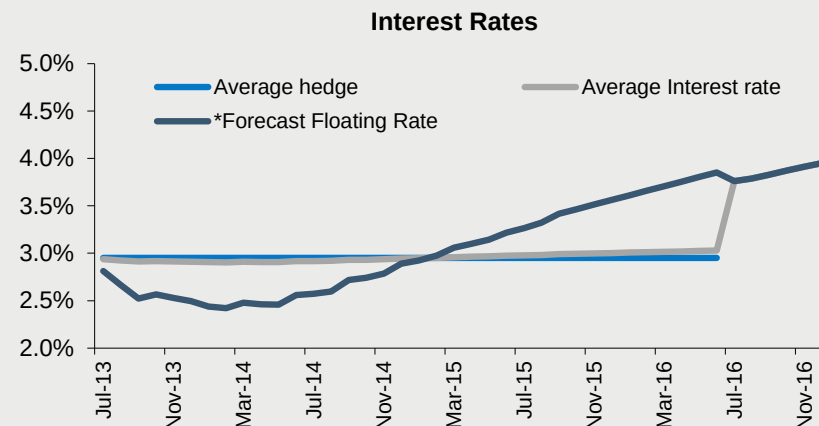
- \$75 million of equity raised in June 2013.
- Investment properties increased through increase in valuation and capex.
- Investment in Australian Education Trust (ASX:AEU) sold in December 2013 for \$7.8 million, 22% above previous year carrying value.
- Borrowings substantially reduced due to:
 - \$5.6 million repaid in January 2013 from sale of AEU units
 - \$71 million repaid using equity raising proceeds (net of costs)
 - \$1.4 million redraw to fund development capex.

4. Capital management

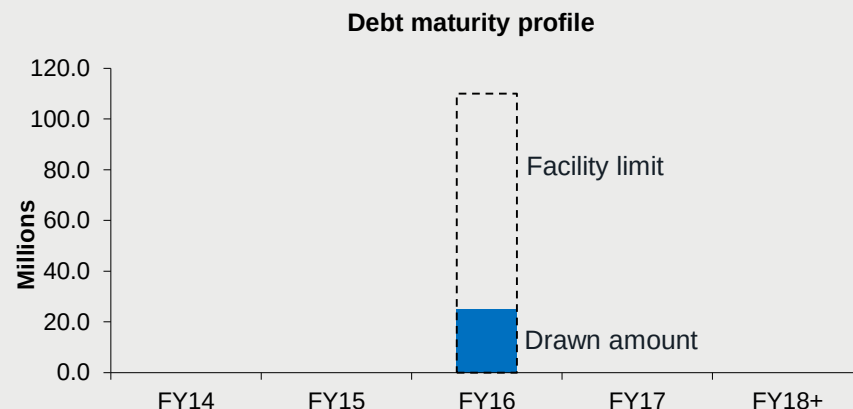
Substantial headroom and redraw capacity to fund acquisitions

As at 30 June	2013	2012
Facility limit	\$110.0m	\$110.0m
Drawn amount	\$25.0m	\$100.2m
Undrawn amount	\$85.0m	\$9.8m
Weighted average duration of debt	3.0 years	2.5 years
Interest rate hedging	100.0%	85.8%
Gearing	10.4%	41.7%
Loan to value ratio	10.8%	44.5%
Loan to value ratio (covenant)	50.0%	55.0%
Interest cover ratio	2.6x	1.9x
Interest cover ratio (covenant)	2.0x	1.5x

- 30 June 2013 debt 100% hedged to June 2016 at a base rate of 2.95%.
- Buy-back facility of \$20 million remains fully available.

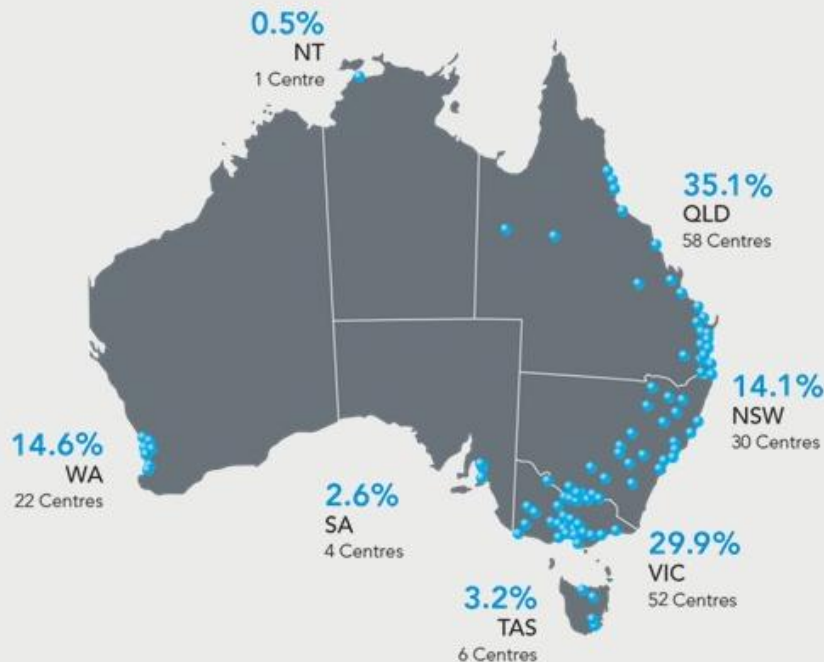


*Forecast floating rate is 30 day FRA as at 20 August 2013



5. Childcare portfolio update – overview

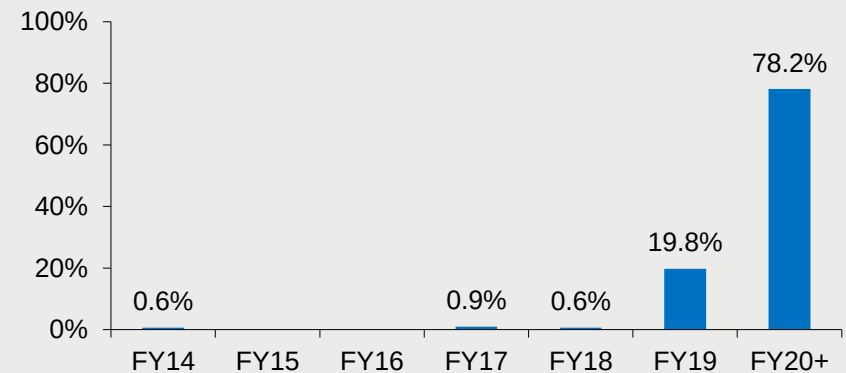
Geographically diverse portfolio of property assets



Note: Percentages shown by value

Portfolio overview	By Number of Centres
% Freehold	99.5%
% Purpose built	91.3%
% Metropolitan	58.0%
Median age of centre (years)	9

Lease expiry by income



- Lease extension options on 33 childcare centres with leases expiring in FY19 are able to be exercised in FY14 (5 years notice).

5. Childcare portfolio update – overview *continued*

Quality portfolio of high yielding assets

Portfolio overview	June 2013	June 2012	Change
Leased childcare centres	167	170	-3
Available for sale / lease	6	3	+3
Development land	4	4	No change
Total properties	177	177	No change
WALE (years)	8.3	9.1	(0.8)
Tenanted occupancy	96.5%	98.3%	(1.8)%
Passing yield ¹	9.3%	9.5%	(0.2)%
Average places / leased centres	80.7	80.6	+0.1
Property portfolio (\$'000)	234,934	226,292	+8,642
Average Value per place	16,673	16,182	+491
Average rent / leased place	1,546	1,513	+33
Rental growth (like for like)	2.5%	2.9%	+40bps
Avg operator occupancy	72.9%	72.7%	+20bps
Operator gross revenue growth	4.3%	n/a	-%

Notes

¹ Excludes vacant centres and office suites

- Weighted Average Lease Expiry (WALE) fell by less than 1 year due to completion of Mernda on a new 15 year lease and other changes.
- Rental growth FY13 running at CPI (minimum 2.5% increase).
- Operator occupancy improving.
- Operator occupancy cost ratio declining slightly

Property Portfolio Movement	(\$'000)
Portfolio at 30 June 2012	226,292
Property acquisitions	1,007
Property disposals	-290
Revaluation	5,750
Development and other capex	2,041
Maintenance capex	134
Portfolio at 30 June 2013	234,934

5. Childcare portfolio update – valuation summary

Revaluation gain of \$5.75 million

Portfolio overview (as at 30 June 2013)	Number of assets	Carrying value (\$'000)	Rent (pa) \$'000	Passing yield
Queensland	52	72,305	7,080	9.78%
New South Wales	30	32,790	3,121	9.52%
Victoria	52	69,560	6,343	9.12%
Tasmania	6	7,465	727	9.74%
South Australia	4	6,015	544	9.04%
Western Australia	22	34,025	2,906	9.24%
Northern Territory	1	1,085	114	10.48%
Operating childcare centres	167	223,245	20,835	9.33%
Vacant centres (for sale or lease)	6	5,710		
Total childcare centres (A)	173	228,955	20,835	
Murarrie office component		3,430	327	9.54%
Development land and WIP	4	2,549		
Total other property (B)	4	5,979	327	
Total property portfolio (A+B)	177	234,934	21,163	

Valuation type (for 12 months to 30 June 2013)	Number of assets	Change (\$'000)	Change (%)
Independent valuation	47	1,990	3.3%
Director's valuation	119	3,760	2.5%
Total Revalued	166	5,750	2.7%
Not valued	11	-	-
Total childcare centres	177	5,750	2.5%

- 34 properties independently valued at 30 June 2013 resulting in 2.85% increase.
- Additional 13 properties were independently valued as at 31 December 2012.
- Director's valuations based on same passing yield as independent valuations ie.growth due to increase in underlying rent.

5. Childcare portfolio update – general activity

Continuous portfolio remixing

- **New leases** – North Ipswich centre leased after reinstatement following the Brisbane floods.
- Progress with the 5 properties handed back by Goodstart:
 - 1 property subject to unconditional sale contract with settlement in early September 2013
 - 1 property re-leased subject to issue of service approval
 - 3 properties subject to lease or sale.
 - No further centres can be handed back.
- **Post 30 June 2013 event:**
 - Acquisition – Bushland's Beach, Townsville, QLD
 - acquired 16 July 2013 for \$2.75 million on a passing yield of 9.35%
 - purpose built in 2008 with 150 approved places
 - new 15 year lease to entity associated with Kids in Care Group
 - Arena REIT standard triple net lease.



5. Childcare portfolio update – developments

Small development pipeline

- Undertaking development on childcare centres has various advantages:
 - generally better quality centres can be built in selected locations
 - generally larger centres with more flexible configurations
 - Arena REIT standard lease can be adopted.
- Mernda construction completed in May 2013.
- Building pipeline:
 - **Augustine Heights** – construction drawings and costings being finalised for second centre
 - **Maddingley** – construction drawings and costings being finalised
 - **Griffin** – construction drawings and costings being finalised
 - further development properties being negotiated in conjunction with childcare operators.

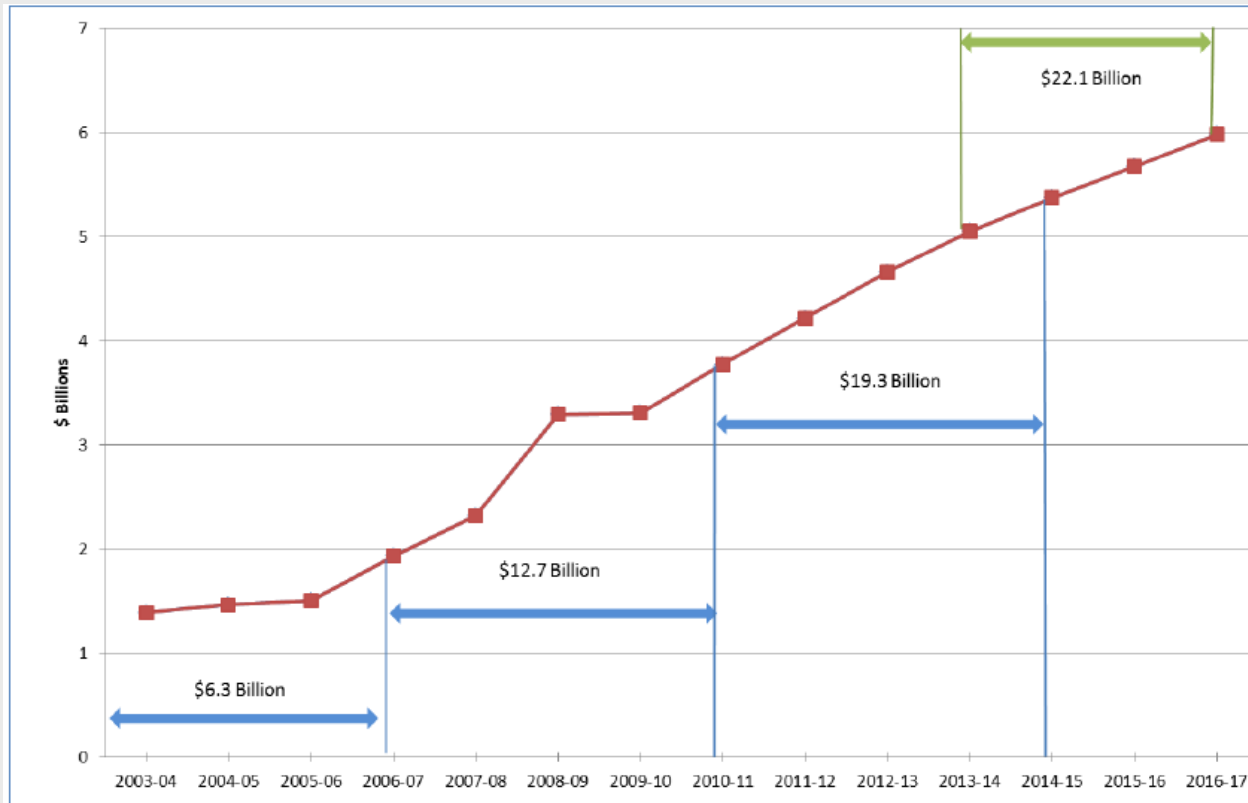
Mernda, Vic



- Approved places – 120.
- Completed April 2013 for a total cost of \$2.6 million (including land).
- Pre-leased to Stoneview.
- Lease commences 17 May 2013 on standard Arena REIT lease terms.
- Valued on completion at \$2.73 million.
- Passing yield of 9.0% on commencement.
- Land 3,260sqm, Building 733sqm.
- 30 car parks.

5. Childcare portfolio update – market update

Government support increasing



Source: DEEWR administrative and forward estimates data.

- 6-8% pa growth in funding over next 4 years.
- Funding expected to increase to \$22.1 billion FY14-17.

5. Childcare portfolio update – market update

Usage of childcare services increasing

- As at 30 September 2012, 23.4% of children in 0-5 age group used accredited childcare/early learning services.
- Demand underpinned by increasing number of children in 0-5 age group (1% pa).
- Number of children using long day care increased 1.3% for the year to September 2012, having increased by 21.2% in the four years to September 2012 and 39.5% in the 8 years to September 2012.
- Average hours per week per child in long day care centres increased 2.2% for the year to September 2012, increasing from 26.1 hours in September 2009 to 27.2 hours at September 2012.
- Average hourly fees for long day care increased 7.3% nationally for the year to September 2012 which is above the average annual increase of 6.9% since September 2004.
- The number of long day care centres increased to 6,192 (2.0% increase in the 12 months to September 2012).

Source: Child Care in Australia, August 2013, Australian Government

5. Childcare portfolio update – market update

Quality of centres improving market wide

Rating NQF	Services	% rating
Exceeding	588	22.9
Meeting	850	33.2
Working towards	1,119	43.6
Significant Improvement required	7	0.3
Total	2,564	

- National Quality Framework introduced in 2012.
- Government has now rated approximately 40% of all accredited long day care centres in Australia.
- Rating related to quality of service, not necessarily quality of building.
- Objective is to improve overall quality of childcare services provided.

Source: Child Care in Australia, August 2013, Australian Government

Recent market transactions

- Most sales off-market.
- Yields firming - Recent transactions have centres generally trading in the yield range of 7% to 9%, but as low as 6.3% yield.

New Supply

- More new centres being developed; generally built to accommodate more than 90 childcare places.
- Best Practice Guidelines for the Planning and Development of Child Care Facilities presently being put together.

5. Labor and Coalition childcare policies

Both parties support childcare funding

Issue	Labor	Coalition
Affordability	- Retain means tested CCB plus no means tested CCR - Funding for parents on income support	- Proposed Productivity Commission Inquiry into funding - No means testing of CCR - Supports CCB
Availability	- Field trials of flexible childcare (\$5 million) \$190 million in training support - Reviewing the Budget Based Funded childcare program - Commissioned research into how to increase supply/reduce red tape	- Productivity Commission inquiry including consideration of care in the “24 hour economy” - Proposed to re-establish the Federal Planning and Advisory Commission to approve new services on needs basis
Quality	- Retaining National Quality Framework - National Partnership Agreement on Early Childhood Education to provide a minimum of 15 hours \$25 billion over next 4 years	- Productivity Commission inquiry with terms of reference to include national Quality Standards framework - Work with States to improve implementation
Workforce	\$114/week pay rise subsidised by government through EBA - Fair Work Commission to look at wages across sector - Supporting employment/training of appropriately qualified staff	- Productivity Commission Report to include extending support to care provided by nannies - Opposed to deliver pay increases through EBA’s

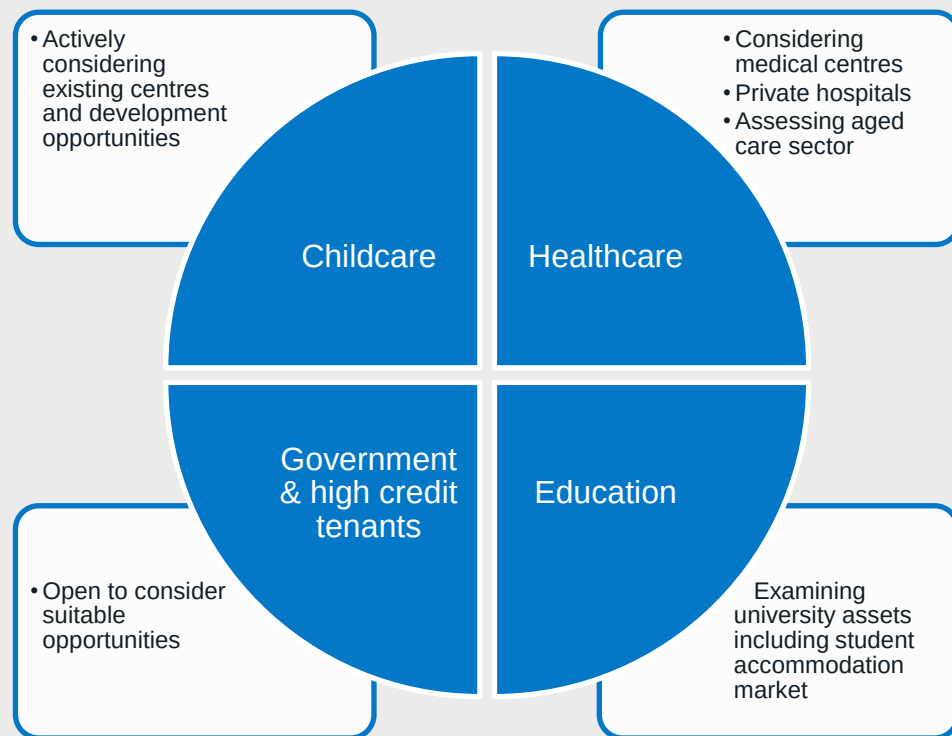
Source: National Foundation for Australian Women, report

CCB – Child Care Benefit
CCR – Child Care Rebate

6. Strategy and FY14 outlook

An active year ahead

- Focused on adding value to and improving quality of the portfolio.
- Seeking to grow and diversify the portfolio gradually over time into sectors such as healthcare, education:
 - quality investment opportunities are relatively scarce
 - selective and disciplined approach required
 - seeking to maintain the predictability of the income streams.
- Diversification benefits from both an underlying tenancy and sector perspective.
- Up to \$83 million acquisition capacity using existing undrawn debt facility.
- FY14 distribution forecast of 8.2 cents per unit (2.5% increase); assuming no acquisitions or developments, and other assumptions detailed in PDS.



7. Investment case

Compelling return and risk profile

- ✓ Knowledgeable and experienced fund manager.
- ✓ Portfolio with stable cash flow:
 - landlord favourable leases – long and net rent basis
 - strong underlying demand for childcare services
 - relatively low gearing.
- ✓ Tenant and concentration risks mitigated through active management.
- ✓ Potential diversification into healthcare and other sectors with similar investment characteristics.
- ✓ Relatively high income distribution yield circa 7.8% p.a. (based on trading price \$1.05/unit) with quarterly distributions.
- ✓ Potential for earnings growth through either:
 - buy-back of units if conditions of the facility are satisfied
 - new investments.

8. Questions



9. Annexures



Annexure 1 - about Arena

Specialist property fund manager

- One of Australia's leading property funds management companies managing approximately \$1.0 billion in funds on behalf of over 15,000 investors.
- Manages 211 commercial property investments in Australia and New Zealand, and invests in traditional property sectors such as office, industrial and retail, as well as growing specialised sectors like social infrastructure (eg childcare, healthcare).
- Manages 1 ASX listed property trust (Arena REIT), 4 unlisted managed investment schemes and 2 joint venture vehicles.
- Majority Independent Board chaired by David Ross, and joined by Dennis Wildenburg and Simon Parsons.
- Highly skilled and experienced investment management team.
- Backed by Morgan Stanley. Morgan Stanley Global Real Estate Investing has been active in Australia since 2004, with operations including several high-quality asset management platforms in the real estate space. Current platforms include Investa Property Group with expertise in office, residential, industrial and funds management, Grand Hotel Group, a hotel ownership and management platform, Arena Investment Management and Retire Australia.

Annexure 2 – detailed profit and loss statement

\$m	FY13	FY12	Variance
Property rental	21.8	22.5	(3.1%)
Interest	0.1	0.2	(39.7%)
Fair value gains on financial assets at fair value through profit or loss	1.4	1.4	2.3%
Distribution income	0.3	0.6	(50.0%)
Revaluation of investment properties	5.2	8.7	(40.6%)
Profit on sale of direct properties	0.0	0.8	(98.8%)
Other operating income	0.3	0.0	2109.5%
Total net investment income	29.1	34.2	(14.9%)
Expenses			
Direct property expenses	(0.9)	(1.1)	(21.2%)
Responsible entity's fees	(2.4)	(2.4)	(1.1%)
Custodian fees	(0.1)	(0.1)	(1.4%)
Consulting and legal fees	(0.5)	(0.5)	8.2%
Other administration expenses	(0.4)	(0.4)	16.0%
Net foreign exchange loss	0.0	(0.2)	(105.4%)
Net loss on change in fair value of derivative financial instruments	(0.1)	(4.2)	(96.7%)
Finance costs	(7.5)	(9.7)	(22.7%)
Total expenses	(11.9)	(18.5)	(35.9%)
Net profit/(loss) for the year	17.2	15.7	9.8%

Annexure 3 – cash flow statement

\$m	FY13	FY12	Variance
Cash flows from operating activities			
Property rental receipts	21.0	21.3	(1.1%)
Payments to suppliers	(4.8)	(5.0)	(4.4%)
Finance costs paid	(6.4)	(8.6)	(26.1%)
Interest received	0.1	0.2	(39.7%)
Other receipts from operations	1.1	0.6	76.0 %
Net cash inflow from operating activities	11.0	8.4	31.3 %
Cash flows from investing activities			
Acquisition of development properties	(1.8)	0.0	100.0 %
Acquisition of investment property	(1.1)	0.0	100.0 %
Proceeds from sale of investments	7.8	0.0	100.0 %
Proceeds from sale of investment properties	0.3	13.6	(97.8%)
Payments for capital expenditure	(0.1)	(0.0)	480.7 %
Net cash inflow from investing activities	5.0	13.6	(63.0%)
Cash flows from financing activities			
Net proceeds from issue of units	71.5	0.0	100.0 %
Distributions paid to unitholders	(10.2)	(8.3)	24.0 %
Loan establishment costs	(0.6)	(1.0)	(41.7%)
Proceeds from borrowings	1.5	0.9	70.5 %
Repayment of borrowings	(76.7)	(10.0)	665.6 %
Termination of derivatives	(2.1)	(3.3)	(36.8%)
Net cash (outflow) from financing activities	(16.6)	(21.7)	(23.4%)
Net increase/(decrease) in cash and cash equivalents	(0.6)	0.3	(272.3%)
Cash and cash equivalents at the beginning of the financial year	5.6	4.9	13.6 %
Effects of exchange rate changes on cash and cash equivalents	0.0	0.3	(100.0%)
Cash and cash equivalents at the end of the year	5.0	5.6	(10.2%)

Annexure 4 - FY13 actual results compared to PDS

	FY13	FY13	Variance
\$m	Actual	PDS forecast	%
Income			
Net property income	20.8	20.8	(0.1%)
Other income	0.6	0.6	2.3 %
Expense			
Management fees	(2.4)	(2.4)	(1.1%)
Other operating expenses	(0.8)	(0.7)	21.2 %
EBIT	18.2	18.3	(0.7%)
Net interest and borrowing costs	(7.3)	(7.6)	(4.5%)
Net operating profit excluding fair value adjustment	10.9	10.7	1.9 %
Non-distributable income and expense			
- Straight-lining of rent income	(0.5)	(0.4)	24.2 %
- Write-off of capitalised borrowing costs	0.8	0.8	5.8 %
Net operating profit available for distribution	11.2	11.1	0.5 %
Weighted average number of units on issue (million)	135,544	135,700	(0.1%)
Underlying EPU cents (based on operating profit)	8.2	8.1	1.6 %
Distribution (¢ per unit)	8.0	8.0	0.2 %

Annexure 5 - typical Arena childcare lease

Lease term and option

- Initial term: 15 years.
- Option term(s): 2 terms of 5 years each.
- Exercise of option: The tenant is required to give the landlord notice of its intention to exercise the option not less than 5 years prior to the expiration of the initial term.

Rent

- Annual rent increases are typically the greater of CPI and 2.5%.
- Market reviews at tenth anniversary and on the commencement date of each further term are subject to floor of 0% increase and a cap at 7.5% on leases to Goodstart and no cap on other leases.

Operating expenses and outgoings

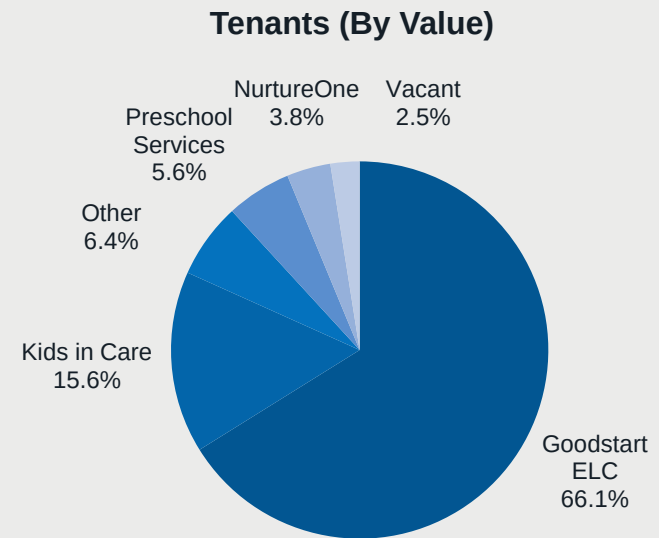
- Tenants are responsible for all, or substantially all of, the statutory and operating outgoings and costs including land tax, insurance and repairs and maintenance, including of a capital or structural nature.

Other terms

- Provision of confidential centre operating metrics on quarterly basis (occupancy, daily rates, profitability).
- Majority of tenants provide a bank guarantee for 6 months rent plus GST.
- The tenant may not assign, transfer, mortgage, or charge its interest, or grant any sublease or license without Arena's consent (not to be unreasonably withheld).
- The landlord may transfer its interest in the land at any time without the tenant's consent.

Annexure 6 - major childcare operators (long day care)

- Low concentration with Goodstart having an 11% market share.
- 3 types of operators: not-for-profit, profit and government.
- Increase acquisition activity, particularly by G8 Education.
- Pressure on costs due to stricter staff qualification levels and higher staff-to-child ratios.



Significant operators

Goodstart Early Learning

- Not-for-profit
- 655 centres (ex ABC)
- All centres leased
- Some government support

G8 education

- 3% of market
- For profit
- More than 200+ centres
- Largest listed operator
- Has doubled number of operated centres in past 2 years

KU Children's Services

- 2% of market
- Not-for-profit
- 150+ centres

Annexure 7 - useful links and references

- Goodstart Early Learning website: www.goodstart.org.au
- G8 Education website: www.g8education.com
- Mychild Government website: www.mychild.gov.au
 - Report - Child Care in Australia, August 2013:
www.mychild.gov.au/pages/ResourcesReports.aspx
- Australian Children's Education and Care Quality Authority: www.acecqa.gov.au
- National Quality Framework: [//deewr.gov.au/national-quality-framework-early-childhood-education-and-care](http://deewr.gov.au/national-quality-framework-early-childhood-education-and-care)
- Australian Bureau of Statistics:
www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/4102.0Main+Features50Jun+2010
- The Australian Institute, The trouble with childcare March 2013:
www.tai.org.au/file.php?file=media_releases/PB%2049%20Trouble%20with%20childcare.pdf
- National Foundation for Australian Woman: www.nfaw.org/election-2013-compare-and-contrast-child-care/
- Liberal Party Proposed Terms of Reference for Productivity Commission Inquiry into Childcare:
www.liberal.org.au/latest-news/2012/11/19/tony-abbott-joint-press-release-terms-reference-proposed-productivity
- Productivity Commission Report into Child Care: www.pc.gov.au/projects/study/education-workforce/early-childhood/report

For further information

Please contact:



James Goodwin

Joint Managing Director
Ph. 0421 275 525
james.goodwin@arenainvest.com.au



Investor and Adviser Services

Ph. 1800 008 494
info@arenainvest.com.au
www.arenainvest.com.au



Bryce Mitchelson

Joint Managing Director
Ph. 0408 275 375
bryce.mitchelson@arenainvest.com.au

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