



Independent Research

November 2006

## SAITeysMcMahon Commercial Office Fund

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## SAITeysMcMahon Commercial Office Fund

### Summary

#### Offer Overview

SAITeysMcMahon Property Limited is the Responsible Entity (RE) for this open-ended unlisted trust that is seeking to raise an additional \$89.05 million to finance the acquisition of an additional five properties. This will bring the portfolio to 8 properties, further diversifying the geographical spread of the Fund. These new properties are located in Auckland NZ, Melbourne, Sydney and Perth in addition to the original three properties located in Brisbane and Melbourne. Excess funds raised (being a total of \$140.8 million) will be used to make further property acquisitions.

#### Evaluation Summary

The Commercial Office Fund's rating is assisted by the forecast stable income returns, the high depreciation benefits associated with some of the properties, and significant growth in the property markets between purchase and this capital raising. Investors should note that the distribution returns are expected to contain a return of capital via increased borrowings (up to a maximum LVR of 70%), therefore distributions will be dependent on increases in capital values of the properties and the ability of the RE to source increased borrowings. The portfolio is nearly 26% leased to the Victorian Police as well as many tenants being well-known public and private companies. The debt is currently fixed for five years, somewhat mitigating interest rate risk. The targeted gearing ratio of 63% of total assets is above the average of 54% for property funds examined recently by PIR. The impact of property specific risk has been reduced from the initial portfolio and should be reduced further as the Fund acquires additional properties.

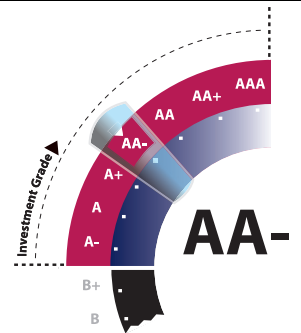
#### Management

SAITeysMcMahon Property Limited (SAITeysMcMahon) is a fund manager specialising in property and has a track record of managing both traditional and non-traditional property assets including office, retail, industrial, healthcare, childcare and agricultural properties. The SAITeysMcMahon group has assets under management in excess of \$3.0 billion.

### Major Considerations

- ▲ A Portfolio of office buildings 97.5% leased (98.7% after rental guarantees) with 100% tax advantaged income for at least the first two years.
- ▲ Largely good tenant covenant, with approximately 26% of leases to government as well as several well-known private and public companies.
- ◀▶ Property investments rely heavily on the capacity of Management, thus any changes to Management can have a substantial (positive or negative) impact on investment performance.
- ▼ Distributions forecast by RE to contain return of capital through increased borrowings equivalent of approximately 4% of current property book value.
- ▼ Reduction in lease expiry and cyclical office market risks dependent on the RE's management skills and its capacity to diversify the portfolio through future acquisitions.

### Overall Investment Rating



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Latest report expiry: 29 May 2006 <sup>1</sup>

### Scheme Details

SAITeysMcMahon Commercial Office Fund	
ARSN 115 845 871	PDS dated 15 June 2006
Fund type	Unlisted Trust
Duration of investment	Open Ended
Unit price	\$1.04
Minimum investment	\$10,000
Distribution frequency	Quarterly
Liquidity	Low
Adviser Commissions	Up to 4%

### Responsible Entity (Manager)

SAITeysMcMahon Property Limited (ABN 90 006 387 435)

### Custodian

Sandhurst Trustees Limited (ABN 16 004 030 737)

### Investment Profile

Number of properties	8		
Property locations	VIC, QLD, NSW, WA, NZ		
Property sector	Office		
Future borrowing commitments	\$39.2m		
Gearing ratio (% of Total Assets)	63.0%		
Gearing ratio (% of Purchase Price)	70.0%		
Purchase price: total funds	90.0%		
Equity sought	\$140.8m	Property Price	\$346.0m
Debt	\$242.2m	Related costs	\$37.0m
Total funds	\$383.0m	Total funds	\$383.0m

### Returns forecast by the Responsible Entity

<b>Year end 30 June</b>	<b>2007</b>
Income return (CPU)	8.4
Tax Advantaged	100%

<sup>1</sup> This report, dated 30 November 2006, expires when the initial offer closes or after 6 months or if there are any material changes in relation to the information contained in this report or any disclosure or offer document issued in relation to this offer. This report was not prepared for inclusion in any offer document and investors must only rely on information contained in the offer document and other associated information. PIR reserves the right to change its opinion, ratings and/or withdraw the report at any time on reasonable grounds.

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Property Investment Research Pty Ltd (PIR) A.B.N. 97 006 425 083 AFS Licence No. 252599

Level 6, 423 Bourke Street Melbourne 3000 Australia (GPO Box 4723 Melbourne 3001 Australia)

Telephone: (03) 9670 7767 Facsimile: (03) 9642 5579 e-mail: propinv@pir.com.au www.pir.com.au

## Conclusion

Qualitative Criteria	Star Ratings Assessment (0 – 5)				
Quality of assets	★	★	★	★	★
Strength of relative property markets	★	★	★	★	★
Quality of income stream	★	★	★	★	★
Potential upside for vehicle	★	★	★	★	★
Diversification	★	★	★		
Investor's initial value	★	★	★	★	★
Level of fees	★	★			
Capital structure and debt management	★	★	★		
Quality of disclosure	★	★	★		
Track record and capacity of Management	★	★	★	★	★

Table i

This offer represents an opportunity to invest in an unlisted trust specialising in investments in the office sector. Most Australian office markets are experiencing falling vacancy rates and solid take-up rates in the wake of strong white-collar employment growth over recent years.

Two of the properties in the initial portfolio are located in the Brisbane CBD, which had a January 2006 vacancy rate of 3.5%, according to the Property Council of Australia (PCA). PIR is advised that recent discussions with the major tenants in these buildings (Queensland Police and SKM) suggest that they will renew their leases. This tends to reduce the Fund's vacancy risk in these Brisbane properties, which are subject to lease expiries in 2006-07.

The initial Melbourne property, 637 Flinders Street, forms part of the World Trade Centre and is fully occupied until 2015 by the Victorian Police under a lease extension negotiated in October 2006. This covenant currently represents approximately 25.5% of the Fund's net income (significantly down from 60% of initial portfolio income). The Melbourne CBD office market has experienced strong take-up levels in recent years and the PCA's January 2006 vacancy fell slightly to 8.3%, well below the historic average of over 14%. However, new supply in the Melbourne CBD and adjoining Docklands precinct is projected to increase over the next two years.

Although Victoria Police has occupied the property for ten years and extended its lease by a further 5 years, there is no guarantee that the lease will be renewed in 2015, however it currently offers a very sound covenant of lease for the next nine years. Given the location away from other supporting office properties, there could be significant

reletting risk if Victoria Police decides not to renew its lease. Since the tenant has extended the lease on terms favourable to the Fund, an upward revaluation is likely on this property. This lease extension pushes back the requirement for a substantial refurbishment, which will be likely in the future. Another consideration is the shift of business to docklands in the general vicinity where this property is located. Over time this may possibly become the favourable locality in the CBD for office locations. In addition Victoria Police also leases a significant amount of adjoining space.

The RE is proposing to acquire additional office properties, which it has already done since the inception of the Fund in late 2005, hence requiring this additional capital raising. This ongoing strategy is expected to reduce the Fund's exposure to tenant and property specific vacancy risk over time, and will result in the Victoria Police Melbourne property continuing to represent a lower proportion of the Fund's total net income.

The additional office properties are proposed to be acquired throughout Australia's capital cities and regional centres, with up to 15% of the gross assets potentially located offshore. The RE has included a purchase of a suburban office building in the growing Newmarket area of Auckland, New Zealand, which represents only 4% of the portfolio by market value. The RE has undertaken to ensure that currency risks are hedged (if this is considered to benefit investors). The enhanced geographical and tenancy diversification of the Fund should also assist in reducing the Fund's exposure to cyclical movements in the office market.

Other additional properties include a Perth CBD office building, which is substantially leased to Wesfarmers (31% by income); a large publicly listed company listed on the ASX. The Perth office market is currently at historic lows in terms of vacancies, fuelled to a large extent by the resources boom. This shortage of supply is being reflected in rising office rents. In September 2006 the Wesfarmers lease had its two yearly market rent review, which resulted in a 44% increase in rent. It is expected that the rents on all the other tenancies in this building will increase by a similar amount.

The number of Melbourne properties in the portfolio has increased with the addition of a property in the heart of Collins Street with 60 individual tenancies and one property in St Kilda Road.

Most of the leases in the properties are subject to annual reviews in line with the Consumer Price Index (CPI) or fixed increases of 3% to 4%. The Victoria Police leases specify market reviews every two years, with a ratcheted increase of 2.5% per annum. The rents for the two Brisbane properties and the Perth property are somewhat below the valuers' assessed market rents at the time of the initial offering, so that short-term lease expiries may provide an opportunity to increase rents. The Melbourne Victoria Police property is over-rented, with an expected reversion to market rent in 2015.

The Fund is projected to offer investors a high tax advantaged component of 100% over several years. This is partly attributable to high depreciation benefits associated with 637 Flinders Street, Melbourne. The RE has made allowance for significant ongoing capital expenditure and lease incentives across the initial portfolio, particularly for the Flinders Street property, and for the additional properties. Expenditure in excess of \$13 million over six years is to be funded from additional debt.

In addition, the RE, in the financial model provided to PIR, shows that distributions will be supported by increased borrowings, which are forecast by the RE to rise by 11% (\$26.7m) from \$238.8 million in 2006 to \$265.5 million in 2012. As the increased borrowings reduces, so does the amount of capital gain an investor can expect to receive at the end of an investment period; it is in effect a return of capital to investors. Furthermore, it is this capital gain that amortises the up front expenses that an investor pays in any unlisted fund. The RE has assured PIR that any increased borrowings to Fund income distributions will not exceed an LVR of 70%.

The increase in borrowings reduces the amount of capital gain that investors can expect to realise at the end of their

investment. However, this should be viewed in light of the value of the portfolio and this increased borrowing represents less than 8% of the portfolio purchase price or 1.3% p.a. of capital gain. Whilst this does increase the risk to investors of not receiving their full amount of equity back at a later date, the risk is somewhat ameliorated by the fact that many of the properties were purchased approximately 18 months ago (the purchase date of many of the properties is significantly earlier than their inclusion in the Fund or the date of this report). Over the last 18 months, yields on office properties have contracted significantly; increasing the value of many of these properties in the interim. Assuming that all rents in the Perth building increase by the same amount as the Wesfarmers market rent review, and that yields remain constant, the 44% rental increase should see that property alone increase in value by \$21 million.

Capital growth in a commercial property investment comes from either increased rental income or a reduction in the yield other investors are willing to pay for a property. Currently yields on commercial properties in Australia are at a relatively low level, especially when viewed in relation to the 10 year government bond rate.

Both the RE's and PIR's financial forecasts take additional borrowing into account. This method of funding capital expenditure by increasing borrowings in future years is a common method observed by PIR in recent times, as RE's struggle to offer returns to investors in a property market characterised by decreasing yields on properties. The method of using capital to fund distributions is not as yet a common occurrence, but sometimes used to provide yields to investors above the yield from the properties after taking into account expenses. The result is a lower expected capital gain over the forecast period as investors have accessed this capital gain over the forecast period via distributions.

Both these methods rely on increasing property values and income to enable increased borrowings to be maintained within allowable ratios. Investors should note that if property values fail to increase (or in fact decrease) then the result may be significantly decreased distributions, possibly coupled with a lack of planned capital expenditure. In addition it will significantly increase the level of borrowings and in the event of a reduction in property values, may trigger loan defaults due to increased Loan to Valuation Ratios.

The PDS indicates that the Fund's gearing ratio is expected to vary over time as new acquisitions are made, with a maximum Loan to Value Ratio (LVR) of 85% of the value

of new acquisitions (considered an extremely high level of gearing for a securitised property fund), which will occur at times when new properties are added to the portfolio before additional equity is raised, reducing to the targeted ratio of 65% to 70% LVR as new application money is received.

The additional acquisitions (five properties), which represent 63% of the total portfolio by market value (eight properties) have been facilitated partly by equity subscribed by the RE's Diversified Property Fund (DPF) and partly by debt financing. The equity raised under this offer will be used to reduce the gearing ratio to the targeted 70% of the valuation of the properties and to fund the acquisition of new properties. This gearing ratio is equivalent to 62% of total assets of the Fund and is higher than the average for unlisted property funds. However, it is not unusual for unlisted trusts to have LVRs of 65% to 70% as their portfolios expand and equity inflows replace debt financing. The RE has reorganised the borrowings of the Fund subsequent to the debt arrangements of the initial portfolio and the average interest rate for the portfolio has been fixed for five years at 6.68%, nearly identical to the interest rate of the initial portfolio at 6.67%.

For most purposes investors should regard the Fund as an investment with low liquidity. However, the RE has undertaken to make withdrawal offers twice a year equal to 5.0% per annum of the net value of the Fund, on a pro rata basis if the withdrawal requests exceed 5%. Provision has also been made for reinvestment of distributions. These facilities should provide investors with some flexibility in the future management of their investment in this Fund, although this facility should not be relied upon as a guarantee of liquidity.

#### **UPDATE REPORTS**

PIR may from time to time produce a report on a property investment vehicle as an update report. These reports are normally undertaken after the initial report as a result of the RE acquiring further assets (in the case of property trusts), changing a loan book (mortgage funds) or as part of an ongoing assessment of a property securities fund/or listed vehicle. Readers should note that each evaluation is based on the material available and observations made at the time of evaluation of the fund and its underlying fundamentals in the context of the investment environment at that time.

All reports expire after six months or upon any material change. If a fund has received an update report, the rating is done on a point in time basis, and as such, the new

In summary, this is an unlisted trust specialising in (although not exclusive to) the Australian office sector. The portfolio is nearly fully leased, with a low vacancy ratio of 2.5% (1.3% after vendor rental guarantees). 26% of the portfolio is leased to the Victorian Government and many other tenants are considered to offer a solid covenant of lease. The weighted average purchase yield of the properties in the portfolio is 7.92%. This is aided by the relatively high yield of 9.85% on the Initial Melbourne property, which represents 21% of the portfolio by market value. That yield was reflective of the risks inherent in the tenancy profile of that property at the time of purchase only having a 4 year lease to a single tenant. The lease extension has markedly changed the risk profile of that property for the better and a much lower market yield is expected for that property if it was to be revalued in the current market.

In the environment of firming (decreasing) property yields experienced over recent years, the RE's forecast initial return of 8.4 cents per unit (supported by increased borrowings) is reasonable, however it may not be sustainable as additional properties are added and does rely on continued property value growth to fund capital distributions. The 100% tax advantaged component is expected to be attractive to investors. Risks associated with interest rate movements have been mitigated. Investors are dependent upon the expertise of an experienced manager for reduction of vacancy risk, which is intended to be partly addressed through additional future acquisitions diversifying the portfolio.

rating may not necessarily match a rating given in the previous report. Should the investment environment have altered from the time of the previous evaluation, a change in rating (up or down) may be enacted.

Ratings may vary due to movements in property markets, composition of a fund's assets or changes to a Manager's strategy or capacity or movements in the risk free rate. A change in a fund's rating should be viewed as PIR's view on the fund in question at the time the report is completed. The rating does not necessarily relate to previous ratings ascribed to the fund by PIR, and should be viewed in context of current market conditions. PIR reserves the right to change its opinion, ratings and/or withdraw the report at any time on reasonable grounds.

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## Key Assessment Issues

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For prospective investors in the Commercial Office Fund, key assessment issues include:

- The open-ended nature of the Fund, which permits further diversification of the portfolio through additional acquisitions, with up to 15% of assets potentially located offshore (expected by PIR to be primarily in New Zealand). Future performance of the Fund will depend upon the nature of these acquisitions.
- The forecast stable income returns and high tax advantaged component of 100% for several years.
- Reliance on capital growth to offset increased borrowings being utilised to boost investor income distributions.
- The very positive short to medium-term outlook for Australia's office sector (especially in Perth and Brisbane), which has been experiencing falling vacancy rates, influenced by strong growth in white-collar employment. High construction costs may contribute to further shortages in some locations by reducing the likelihood of future additional supply, although additional supply is proposed and / or underway for Perth and Brisbane.
- Reasonable expectation for capital appreciation of the initial portfolio, based on the forecast performance of the Brisbane and Melbourne office sub markets and opportunities presented by short-term lease expiries in the Brisbane properties.
- The need for expenditure on capital improvements and lease incentives across the initial portfolio, to be funded from debt. PIR has reviewed the independent technical due diligence reports for the three initial properties and it appears that the RE has made sufficient allowance for this expenditure in its financial forecasts. PIR has not, however, viewed any such documents for the additional properties currently being added to the portfolio.
- The need for increased debt to ensure that distributions are maintained at the forecast and proposed levels.
- There is an alignment of the RE's interests with those of investors, through the participation of the DPF as a 50% equity partner and the incentive of performance fees.
- The availability of six monthly withdrawal opportunities is expected to create some measure of flexibility for investors.

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## Income Returns

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PIR has examined the financial projections of the RE based on the valuations and supporting evidence and is satisfied that, based on forecasts as presented, the Fund is able to generate sufficient returns to enable SAITEYSMcMAHON to continue to distribute the proposed 8.4 cents per unit, subject to best practice corporate governance being undertaken by the RE's directors, staff and consultants. This, however, will be the result of supporting distributions through increased borrowings largely funding capital expenditure items, resulting in essentially a return of capital.

The weighted average lease term remaining by income, as calculated by PIR, is 3.6 years, compared to 4.7 years of the initial portfolio, which was heavily influenced by 60% of the initial net income being derived from the single-tenanted Melbourne property, where the lease expired in July 2010.

Although the RE published a two-year forecast in the initial PDS, PIR has had access to the RE's financial forecasts for the Portfolio until 2012. Stable rental returns from the portfolio are projected by the RE, partly

as a result of the properties being fully leased, with a reasonable expectation of lease renewals or brief letting-up periods over the short to medium term in the Brisbane properties.

The fact that the RE is deferring some of its annual management fees over the first four years and using additional borrowings to fund costs such as letting-up allowances and leasing commissions has also contributed to the RE's forecast stable income returns. This is a common occurrence in recent times with the property market, which is currently seeing contracting yields and RE's endeavouring to enhance the yield to investors. Interest rates are also fixed for a weighted average of five years.

PIR has undertaken a cash flow analysis for a standardised six-year period as part of the financial rating model process. PIR's financial modelling assumptions have been based on the RE's assumptions in the expected case, while varying the costs associated with lease expiries in the upside and downside scenarios.

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In order to maintain distributions equal to or in excess of 8.4 cents per unit, future acquisitions should ideally offer yields in excess of 8.0%. The RE has not been able to source such properties for the additions to the portfolio that are the subject of this equity raising. The weighted average yield on the additional properties is 7.3%. Given that the management fees and expenses are projected to be around 1% per annum to investors, then the net yield, prior to an allowance for vacancies and capital expenditure, is around 6.3%, which is below the borrowing rate for the Fund. In essence this makes investors more reliant on capital gain for returns from those properties than the initial portfolio, however if the office rental markets continue to improve then these properties can become cashflow positive for the Fund and thus for investors.

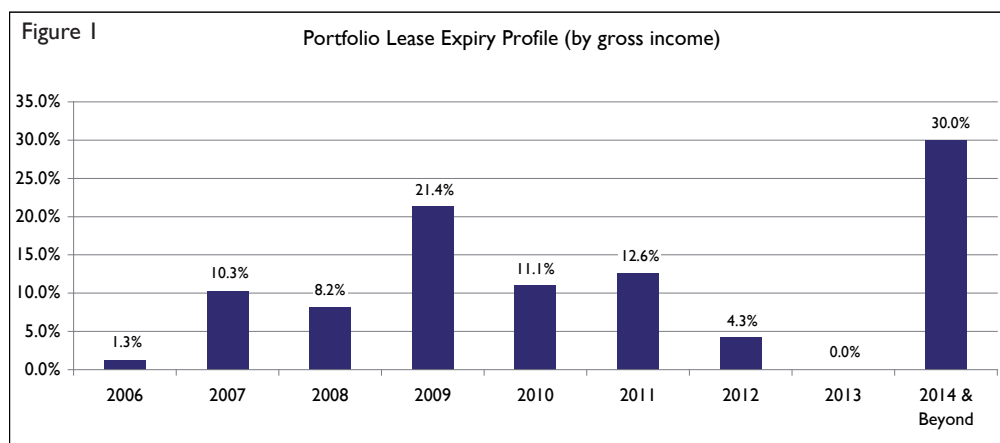
In the initial offering, the income projections did not require increased borrowings (a return of capital to

investors) to support distributions. The weighted average yield on the initial portfolio of three properties was 9.0%, which was heavily supported by the Flinders Street property, which was 56% of the portfolio, having been purchased at a yield of 9.85%, which was reflective of the level of income risk inherent in that property. The use of gearing was earnings accretive to investors. The weighted average yield of the entire portfolio was 8.12%.

That said, in the current property investment market, characterised by tightening yields, the ability of the RE to further source reasonable quality properties offering those yields may offer a challenge over the short to medium term. This emphasises the need for the RE to use its skills in property selection, to negotiate advantageous buying terms and to manage the risks of ownership. PIR believes that the RE has demonstrated these skills in the past, although there is no guarantee that this will continue.

<b>Financial forecasts and projections (PIR expected case)</b>					
<b>Year ended 30 June</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>
Net Property Income	28,358,697	29,839,357	31,141,872	32,532,732	33,908,567
Increased Borrowings	2,772,318	2,388,428	2,136,933	1,444,279	446,047
<b>Total Income</b>	<b>31,131,015</b>	<b>32,227,786</b>	<b>33,278,805</b>	<b>33,977,011</b>	<b>34,354,614</b>
RE fees	2,768,630	3,378,814	3,987,180	4,340,484	4,467,720
Interest Expense	16,476,807	16,911,964	17,332,422	17,662,978	17,900,622
Other expenses	346,079	397,508	419,703	434,048	446,772
<b>Total Expenses</b>	<b>19,591,515</b>	<b>20,688,286</b>	<b>21,739,305</b>	<b>22,437,511</b>	<b>22,815,114</b>
<b>Net Operating Income</b>	<b>11,539,500</b>	<b>11,539,500</b>	<b>11,539,500</b>	<b>11,539,500</b>	<b>11,539,500</b>
Available For Distribution	11,539,500	11,539,500	11,539,500	11,539,500	11,539,500
Distribution to New Investors	7,192,500	7,192,500	7,192,500	7,192,500	7,192,500
New Equity Invested	89,050,000	89,050,000	89,050,000	89,050,000	89,050,000
<b>Return On Equity</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>
Tax Advantage	100.0%	100.0%	100.0%	100.0%	100.0%
<b>After-tax Distribution</b>					
<b>46.5 % Tax rate</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>
<b>31.5 % Tax rate</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>
<b>15 % Tax rate</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>	<b>8.08%</b>

Table ii



This report does not form any part of any offer document

## Capital Returns

PIR's estimate of the Current Realisable Value of the Fund indicates that, excluding income distributions and the impact of taxation benefits, an overall growth rate of 2.4% per annum in the capital value of the property portfolio would be required for 100% equity to be returned to investors at the end of a standardised six-year investment period.

Current Realisable Value	Standardised 6 year term
Growth rate required to return \$1 at end of period:	2.4% p.a

Table iii

PIR's cash flow analysis indicates that capital appreciation of 4.7% per annum may be achieved over a six-year period. Under the expected case scenario, PIR has adopted a weighted terminal capitalisation rate of 8.12%,

with the downside scenario being 3.08% and the upside being 6.12%. The prospect for capital appreciation of the portfolio is enhanced by the low vacancy rates in the Brisbane and Perth market and the RE's proposed capital enhancement of the properties. However, the proposed strategy of returning capital through increasing borrowings over the term of the Fund, borrowing against potential increased capital value, has resulted in a reduced expected realisable capital gain for investors.

The percentages in Table iv 'Application and Sources of Funds' provide benchmarks and replace the former NTA calculation, the true meaning of which has dissolved with the increased application of accounting convention. For further analysis and benchmark comparisons of transaction and establishment costs, subscribers should visit [www.pir.com.au](http://www.pir.com.au).

Application of Funds overall	\$000	%	Source of Funds	\$000	%
Contract purchase price	\$345,975	89.8%	Equity	\$140,800	36.5%
Transaction costs (property acquisition costs e.g. stamp duty, legals and due diligence)	\$17,278	4.5%	Debt	\$242,183	63.0%
Initial payments to RE /advisers/ underwriter	\$17,855	4.6%	Net Rent in Advance	\$2,284	0.5%
Other offer/establishment costs	\$4,039	1.1%			
Cash/contingency	\$119	0.0%			
<b>Total Funds Employed</b>	<b>\$385,267</b>	<b>100.00%</b>	<b>Total</b>	<b>\$385,267</b>	<b>100.00%</b>

Table iv

### Debt

The RE arranged two non-recourse loan facilities with the Bank of New Zealand Australia. Interest rate swap arrangements were negotiated to provide a weighted average fixed interest rate of 6.68% for five years. Those loan facilities permit a gearing ratio of up to 85% of the value of the properties at the time of acquisition, to be reduced to a 65% to 70% range.

The LVR range is expected to vary as new application monies are received and new properties are added to the Trust. The current proposed gearing ratio (assuming the successful raising of the additional equity of \$89.05m) of 70% LVR is equivalent to 63% of total assets, which is above the average of 54% for unlisted trusts examined recently by PIR. However, it is not unusual for unlisted trusts to have LVRs of 65% to 70%.

There is no guarantee that equally favourable interest rates will be available for future loan facilities negotiated by the RE to fund additional acquisitions or to refinance these loan facilities in 2010 and 2011. PIR has assumed a benign interest rate environment on renewal of these debt facilities and a renewal at the current interest rates.

In total the RE has forecast to increase borrowings by \$27 million over the six year period to the end of June 2012. This strategy is heavily reliant on growth in capital value to ensure that borrowings do not raise the LVR over 70%.

### Taxation

**Income tax:** There are significant taxation benefits available to investors by way of a tax advantaged component that represents a percentage of 'tax deferred' income. This tax advantaged component is due to allowable deductions, such as building allowance and depreciation of the property, plant and equipment and certain establishment costs.

Australian investors can expect to receive an income stream that is tax advantaged to 100% for the first two years of the investment and for several years beyond (based on the RE's financial forecasts and assuming no change to the property portfolio).

**Capital Gains Tax:** Tax paid on accumulated tax deferrals as well as on increase in property value (net of sale costs). PIR understands that under current law the taxable income

of the Fund will include any capital gains made on the sale of assets owned by the Fund. The cost base used in calculating such capital gain will be reduced by any amounts already claimed as a deduction.

The taxation implications of investing in the Fund may vary according to the investment structure adopted by investors and potential changes to the Taxation Act.

**It is strongly recommended that investors seek/obtain professional and independent financial and taxation advice before choosing to purchase units in this or any investment property vehicle.**

## Risk and Total Returns

PIR's assumptions for the upside and downside scenarios are intended to indicate a 'range of reasonable likelihood' for outcomes. PIR has had regard to the RE's financial forecasts, to the valuers' assumptions in respect of rentals, lease renewals, letting-up periods, rental growth and lease incentives and the technical due diligence consultants' recommendations in respect of capital expenditure.

Alternative assumptions (where warranted) are in accordance with the standard PIR methodology. Whilst no forecasting can be guaranteed to be correct, providing differing assumptions can create both positive and negative outcomes within the PIR framework.

Risk is measured by the deviation in returns from those generated by the expected case scenario. For the upside and downside scenarios, alternative assumptions have been employed in accordance with the standard PIR methodology. Table v indicates a range of IRR's with results in downside and upside cases effectively being one standard deviation from expected figures.

PIR's modelling process produces an expected Internal Rate of Return (IRR) of 8.69% after tax for investors with

a marginal tax rate of 46.5% and 0% gearing by individual investors. This analysis assumes there is no change in the portfolio in the form of redevelopment, forced or other deleterious sale or expansion not assumed in the company's current forecasts during the six-year horizon.

PIR's analysis indicates that investors on a 15% marginal tax rate can potentially achieve a marginally higher IRR of 10.51% after tax. The corresponding expected after-tax IRR for taxpayers in the 31.5% bracket is 9.74%. There is no variation between the tax brackets due to the impact of the 100% tax-advantaged income and of the capital expenditure amounts influencing the cost base used in calculation of capital gains tax.

Forecasting future investment performance is problematic at best and relies on a number of assumptions about future events that may or may not necessarily occur. Changes in even one of the variables affecting investment market performance may have a significant and decisive impact on future outcomes. This report provides no more than a general guide to possible future market conditions and must not be relied on in isolation.

Trust estimated after-tax IRRs	Downside	Expected	Upside
46.5% tax rate	5.38%	8.69%	11.36%
31.5% tax rate	6.29%	9.74%	12.52%
15% tax rate	6.95%	10.51%	13.36%

Table v

## Assumptions

PIR assumptions	Downside	Expected	Upside
Weighted average letting-up period (months)	6	4	2
Weighted average rental growth p.a	3.6%	4.6%*	5.5%
Weighted average terminal capitalisation rate	8.38%	8.12%	7.87%

\* Heavily influenced by the Perth property; expected increase of 8%p.a. for model purposes

Table vi

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## Offer Structure

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The Fund is an unlisted, open-ended fund structured as a unit trust with a Responsible Entity, constitution, compliance plan, custodian, and public offer for units achieved by way of Product Disclosure Statement. The prime responsibility of the Responsible Entity is to safeguard the interests of investors and to manage the Fund to ensure that it achieves its objectives. It is intended that the Fund will acquire further properties that meet the RE's investment criteria. The Fund allows for the participation of all types of Australian investors, including superannuation funds. The RE has progressively settled the property portfolio since June 2005 and borrowed loan funds. Minimum subscriptions to the Fund are \$10,000 with further subscriptions from \$1,000.

The acquisition of the initial portfolio was facilitated partly by equity of \$42.3 million subscribed by the RE's DPF and partly by debt.

This offer is being exclusively marketed via the financial planning network of Discovery Investment Services Corporation Limited as sponsor. The custodian appointed to hold the assets of the Fund is Sandhurst Trustees Limited, a trustee company that has operated for over one hundred years.

The PDS indicates that distributions may be reinvested and that investors may increase their investment in the Fund at any time. As new units are issued in the future, there may be some dilution of the original unit holders' ownership in the Fund, unless they take these opportunities to increase their participation.

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## Liquidity and Exit Mechanism

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The Commercial Office Fund has a Constitution that governs the rights of unit holders and the ongoing operation of the Fund. Under its Constitution, the Fund has a maximum life expectancy of 80 years.

Investors should regard an investment in the Fund as illiquid and the RE will only satisfy a withdrawal request if the Fund is 'liquid' as that term is defined in the Corporations Act. The RE, however, intends to make withdrawal offers every six months for an amount, which does not exceed 5% per annum of the net asset value of the Fund.

The withdrawal price of a unit is expected to be 5% less than the issue price, this amount reflecting the Service Fee incorporated into the original unit price of \$1.00. This fee covers transaction costs. It is anticipated that withdrawal offers will be funded by the issue of new units, but, should a property need to be sold to fund a withdrawal offer, the 5% fee could increase to take account of additional transaction costs associated with the disposal of the property.

The unit price was fixed at \$1 until 30 September 2006. After that it may vary as the underlying value of the Fund's assets changes over time. The unit price will be calculated by dividing the net value of the Fund's assets (less transaction costs and accrued income) by the number of issued units. Net asset value will usually be based on the most recent independent valuation of the properties, but may be determined by the RE. This disadvantage of

using an ageing valuation for any unit redemption may be that the net asset value may not fully reflect the underlying value of the assets.

The withdrawal offers available on a six-monthly basis are expected to provide some flexibility for investors, but PIR still considers that the Fund offers a low level of liquidity, since its underlying assets are properties (not securities).

The regular withdrawal offers proposed by the RE are in addition to any partial withdrawal offers that may be made, should any of the significant assets of the Fund be sold. Under the Fund's Constitution, SAITeysMcMahon, as Responsible Entity for the DPF, has first right of refusal to acquire each of the properties of this Fund, prior to offering them on the open market. The RE has advised PIR that its current intention is to acquire further additional properties and to hold the initial portfolio for the foreseeable future.

Commercial office markets tend to be cyclical, so that it is possible that the RE's current strategy may alter. Should the RE decide that it is in the best interests of investors to dispose of the portfolio, there are various options available, including the acquisition of the properties by SAITeysMcMahon or one of its associated entities, disposal of the properties on the open market or by listing of the units on a secondary market. The management of the RE has demonstrated active asset management of its property portfolios in the past, although past performance is not a guarantee of future performance.

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## Fees

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The Responsible Entity and others are entitled to several fees, which have been included in the financial forecasts. The principal fees are outlined below:

- The RE is entitled to an upfront Service Fee of 5% of the application money paid to acquire units in the Fund, from which commissions will be paid to advisers (including up to 2% payable to Discovery Investment Services as sponsor). This Service Fee is expected to cover the transaction costs associated with the proposed withdrawal offers in most instances (refer to *Liquidity And Exit Mechanism*).
- An upfront acquisition fee of 3% of the acquisition price of any property purchased.
- The RE is entitled to an annual management fee of 1.0% of the gross value of the Fund's assets. The RE has indicated that it will defer this fee over the first four years (paying 0.70% in year one, 0.80% in year two, 0.85% in year three and 0.95% in year four). The deferred fees are to be recouped if SAITEysMcMahon is terminated as RE of the Fund or on a pro-rata basis on disposal of any of the properties. At the time the deferred fees are recouped, they will be calculated as a percentage of the value of the assets at the time the fee is paid.
- The RE is entitled to a performance fee of 2% of the gross sale price of a property on disposal (less selling expenses), provided the net sale price exceeds the purchase price plus costs of acquisition and capital

improvements. Should the net sale price exceed this amount by 50% or more, an additional 2% fee would be paid. These fees would also be paid if the Fund is merged with or acquired by another managed investment scheme.

- Should SAITEysMcMahon be removed as Responsible Entity for the Fund, a removal fee of 3% of the gross assets would be paid to the RE.
- The RE is entitled to be reimbursed for the ongoing administration expenses of the Fund. These costs include an ongoing fee of up to 0.05% payable to the Custodian, Sandhurst Trustees Limited, for its role in holding the assets of the Fund.

The total of the Service Fee and the acquisition fee represents an upfront payment to SAITEysMcMahon of 5.0% of the purchase price of the initial properties, which is broadly in line with current PIR industry averages of 4.9%. The ongoing Management Expense Ratio (MER), made up of the RE's annual fee plus expense recoveries, is not expected to exceed 1.0% of the average gross assets in the first year, but the RE has indicated it would rise to 1.3% as the deferred management fee reduces to zero in year five. This is high compared with the average MER of 0.6% for funds examined recently by PIR.

The performance fee generally aligns the interests of the RE with that of investors and provides a strong incentive for the RE to maximise the performance of the Fund. This is generally in line with industry practice.

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## Capacity of Manager

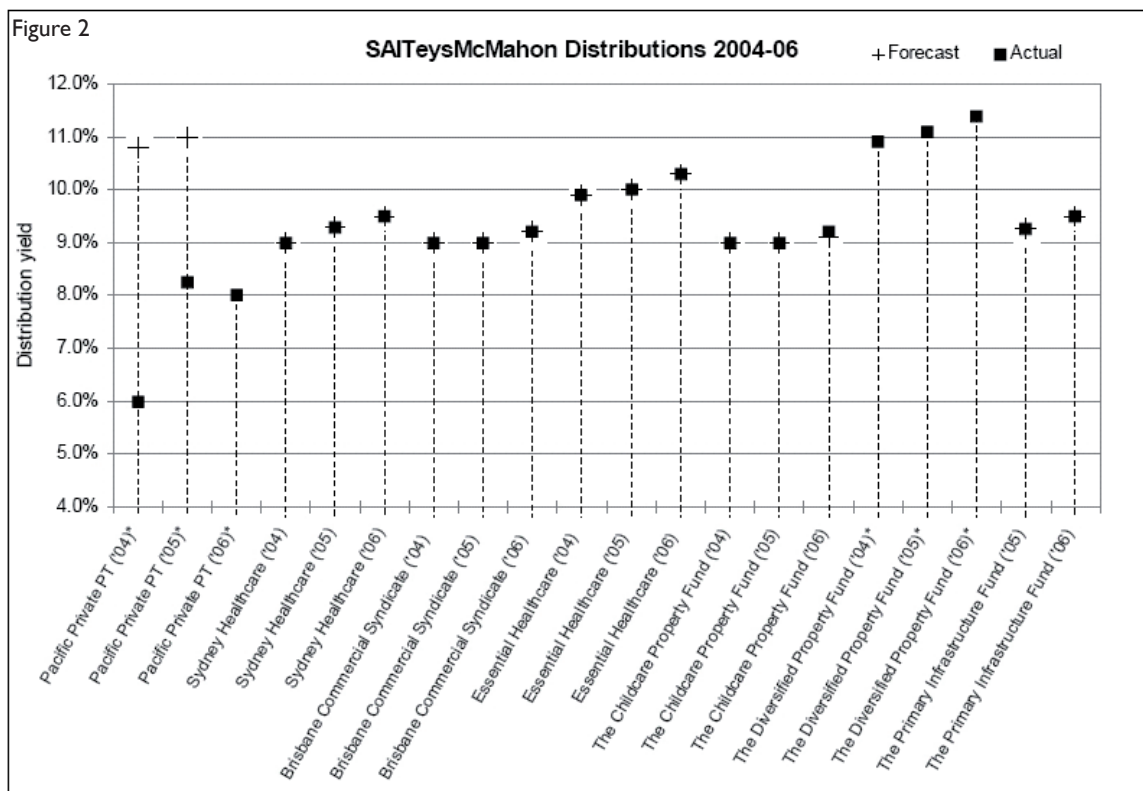
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The RE of the Fund is SAITEysMcMahon Property Limited. SAITEysMcMahon specialises in structuring commercial property trusts and funds. As at 30 September 2006, SAITEysMcMahon managed assets in excess of \$3 billion. Apart from the Pacific Private Property Trust, the RE's syndicates and unlisted trusts have generally performed in line with expectations.

PIR conducted a compliance review of the Responsible Entity on 27 October 2005. The review concluded that

SAITEysMcMahon has further improved its compliance management system and corporate governance framework recently and that overall the entity has a well managed compliance system that will support the continued growth and expansion of the business.

The custodian, Sandhurst Trustees Limited, is a long established trustee company, which is owned by the Bendigo Bank.



Key management personnel are as follows:

Directors of the Responsible Entity

**Grant Ross (Managing Director):** Mr Ross is the managing director of SAITeysMcMahon and sits on SAITeysMcMahon’s investment review committee. He holds a Master of Applied Finance (Melbourne University), Master of Enterprise Innovation (Swinburne University) and Bachelor of Science with Honours (Monash University).

**Graham Brewer (Director):** Mr Brewer is a director of SAITeysMcMahon. With over 27 years’ experience in the property investment industry, Mr Brewer has been actively involved in senior positions with public and private companies in the management of property investment portfolios. He sits on SAITeysMcMahon’s investment review committee and is a fellow of the Australian Property Institute, a registered valuer, and a former councillor of the Victorian division of the Property Council of Australia.

**Greg McMahon (Executive Director):** Mr McMahon is an executive director of SAITeysMcMahon and until recently was a partner of the law firm, McMahon Clarke Legal. He is recognised as one of Australia’s leading managed investment lawyers. He is a past president of the Australian Direct Property Investment Association. Mr McMahon holds a Bachelor of Laws with Honours, Bachelor of Commerce and Graduate Diploma of Applied Finance and Investment.

**David Hinde (CEO):** Mr Hinde is Chief Executive Officer for SAITeysMcMahon and is responsible for overseeing all aspects of the organisation’s strategic development. Mr Hinde has 17 years experience in funds management and was the Managing Director of Becton Property Group’s funds management division prior to joining SAITeysMcMahon. Mr Hinde has also held management positions at MCS Property (now CentromCS) and Lend Lease.

Key Management of the Responsible Entity

**Brad Dichiera (Fund Manager – Commercial Office Fund):** Mr Dichiera has a Bachelor of Commerce from the University of Melbourne and over ten years’ experience in the property industry. For the last six years, Mr Dichiera was with Lend Lease, working in various roles; most recently as Asset Analyst, where he worked primarily on major retail developments and acquisitions for the General Property Trust and the Australian Prime Property Fund.

Directors of SAITeysMcMahon Group

**Robert Appleby (Non-Executive Chairman):** Mr Appleby is the chairman of SAITeysMcMahon. With over 40 years’ experience in the real estate industry, he has been a principal of his own real estate business for over 36 years. He holds a certificate in financial markets from the Securities Institute of Australia.

**Peter Scully (Director):** Mr Scully is a director of SAITeysMcMahon and is the founder of the SAI Group. He has over 30 years' experience as a financial strategist. He lectures for The Executive Connection on personal lifestyle, financial planning and estate planning. He holds a Graduate Diploma in Business Administration from Swinburne University.

**Judy MacMahon (Director):** Ms MacMahon is a director of SAITeysMcMahon, responsible for new business, marketing and distribution. She has over 25 years' experience in property, finance, venture capital and merchant and investment banking.

**Matt Kilbride (General Counsel & Head of Compliance):** Mr Kilbride has over 16 years' experience in legal and compliance roles both in major law firms, such as Blake Dawson Waldron, and within the financial services industry, in entities such as Perpetual Funds Management, AMP Wholesale Investments, Invesco and Equity Trustees. His responsibilities within SAITeysMcMahon include management of the compliance function, where he heads a team of four in performing this function. He holds a Bachelor of Laws, Bachelor of Economics and a Graduate Diploma of Company Secretarial Practice.

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## Property and Location Analysis

Australian office markets are experiencing falling vacancy rates and solid take-up levels in the wake of strong growth in white-collar employment. CBD markets have generally experienced the strongest recovery, reflecting a migration of tenants from suburban markets. The average CBD vacancy fell to 6.5% over the six months to July 2006, according to the PCA, while non-CBD vacancy fell to 8.0%. For the first time in 15 years, no Australian CBD office market has a vacancy level over 10%, indicating very strong demand. This may eventually translate into rental growth, which has been lacklustre over the past few years.

The vacancy rate in Melbourne's CBD decreased by 0.8 percentage points to 7.5% over the six months to July 2006. The decrease was a strong result considering it was accompanied by a record addition of supply to the market of 187,832m<sup>2</sup>. Melbourne has traditionally had a high vacancy rate of over 14% (including significant vacancies of lower grade properties).

Further supply is forecast in 2007 with over 35,000m<sup>2</sup> of new space due to be completed and so far a further 52,000m<sup>2</sup> scheduled for completion in 2008 and beyond.

In the Brisbane CBD market, high construction costs and a shortage of suitable sites (since there has been significant residential development – 15 projects since 2000) may tend to delay the next construction cycle. This is expected to see further growth in rental rates, as vacancy levels remain relatively low over the next few years.

The St Kilda Road office market is considered to be distinct from the Melbourne CBD office market, which now incorporates the Docklands area. In the six months to July 2006, the overall vacancy rate for the St Kilda precinct fell 0.7% to 9.4%. A Grade vacancy rates fell to 12.6%, which is still relatively high and may impede rental growth into the future.

The Sydney CBD office market vacancy rate dropped by 0.3 percentage points to 9.4% over the six months to July 2006, its lowest level in 3 years, indicating a continued recovery in tenant demand. The vacancy drop and strong net absorption come despite the substantial addition of supply over the period.

The Perth CBD has experienced a rapid decline in vacancy rates over the last year, due to increased demand for office space, largely from resources companies, with little new office space of a good quality likely to become available in the next two years. In the six months to July 2006 the vacancy rate for Perth fell dramatically from 5.8% to 3.5%, which is the lowest ever vacancy rate for Perth. Supply constraints look to remain tight (only 8221m<sup>2</sup> of space was added to the market over the period), especially for Premium and A grade offices, especially if the resources sector continues to boom. These conditions have led to strong rental growth and increased the already keen interest of investors in securely leased commercial property investments.

Research on the Auckland office market released early 2006 by CB Richard Ellis, highlighted that CBD office markets found rising secondary vacancies as tenants upgraded into precommitted new built space. It is noted, however, that the easing has occurred from the tightest conditions in 20 years and, relative to long term averages, the current market remains healthy. Rent growth is reflecting the prevailing occupancy trends, with prime CBD rents seeing strong quarterly growth over 2005 with tightening yield gaps between prime and secondary property closing by 180 basis points over the last five years.

### I. 40 Tank Street, Brisbane, QLD

<b>% of Portfolio</b>	9%	<b>Completion Date</b>	1985, refurbished 1996		
<b>Ownership</b>	100%	<b>Purchase Price</b>	\$31,750,000		
<b>Title</b>	Freehold	<b>Vacancy</b>	Nil		
<b>Type</b>	Office/retail	<b>Gross Lettable Area</b>	6,354m <sup>2</sup>		
<b>Location</b>	Brisbane CBD	<b>Total Site Area</b>	2,106m <sup>2</sup>		
<b>Major Tenants</b>		<b>Lease Terms</b>		<b>% Area</b>	<b>% Rental</b>
Queensland Justice & Attorney General		5 years, expiring 30 Sept 2011 (1 x 5 year option)		34%	20%
Queensland Police		5 years, expiring 31 March 2007 (2 x 5 year options)		33%	15%
Kings Parking		10 years, expiring 31 August 2014 (1 x 10 year option)		-	48%
<b>Valuation Date</b>	<b>\$ Value</b>	<b>Valuer</b>	<b>Initial yield</b>	<b>Cap rate</b>	<b>\$/m<sup>2</sup></b>
25 February 2005	\$31,750,000	CB Richard Ellis	7.99%	8.25%	\$4,997/m <sup>2</sup>

Table vii

- Located in the legal precinct in the western corridor of the Brisbane CBD. Nearby buildings include the Brisbane Transit Centre, Commonwealth Law Courts, Roma Street Magistrates Courts and the Queensland Police Department Headquarters.
- A well-presented eleven-storey building, with ground floor retail/office space, 266-bay public parking station on levels one to five and five storeys of upper level office space. Refurbished in 1996, it is serviced by three passenger lifts and one secure passenger lift for the judges from a secure 19-bay parking area on level one. The building has a high parking ratio of one space per 22m<sup>2</sup> of net lettable area (NLA).
- The upper level office floors achieve views to the south-east towards the Brisbane River and offer column-free accommodation, with floor plates over 1,000m<sup>2</sup>.
- Fully occupied, with the office rents reported to be below market by the valuer; CB Richard Ellis. Short-term lease expiries relating to 50% of current net income provide an opportunity for rental growth.
- Most tenancies subject to annual reviews in line with the CPI or fixed annual increases of 3.5% or 4%.
- Western corridor characterised by mix of uses, including secondary retailing, office buildings, hotels and apartment buildings. Access to Roma Street Parklands is available from George Street at the northern end of Tank Street. A dilapidated heritage building and vacant adjoining site are located opposite 40 Tank Street and are for sale, with potential for development as an office, retail, residential or mixed-use complex. To the rear of 40 Tank Street is another vacant site, currently used as an open-air car park.
- Availability of potential development sites near 40 Tank Street may represent a threat to lease renewals if a new office development cycle provides alternative new space suited to the sitting government tenants. However, the building has features specifically designed to accommodate the Queensland Justice and Attorney General's Department (the secure car park and lift) and Queensland Police recently leased ground floor space for terms that would extend its presence beyond some of its other lease expiry dates (it has five separate leases expiring between 2006 and 2009, with options extending as far as 2017).
- PIR has reviewed a copy of a technical due diligence report for 40 Tank Street, prepared in March 2005 by GN Constructions Pty Ltd. SAITeysMcMahon's financial forecasts to 2012 indicate that the RE appears to have made sufficient provision in various allowance for the capital expenditure items recommended in this report (approximately \$1.3 million over the next decade).

2. The Victorian Police Centre, 637 Flinders Street, Melbourne, VIC					
<b>% of Portfolio</b>		25%	<b>Completion Date</b>		1983, refurbished 1995
<b>Ownership</b>		100%	<b>Purchase Price</b>		\$71,000,000
<b>Title</b>		Freehold	<b>Vacancy</b>		Nil
<b>Type</b>		Office	<b>Gross Lettable Area</b>		23,050m <sup>2</sup>
<b>Location</b>		Melbourne CBD	<b>Total Site Area</b>		4,209m <sup>2</sup>
<b>Major Tenants</b>		<b>Lease Terms</b>		<b>% Area</b>	<b>% Rental</b>
Victorian Police – Buildings C & E		17 years, + 5 years; expiring 31 July, 2015		86%	88%
Victorian Police – Building A		16 years + 5 years; expiring 31 July, 2015		14%	12%
<b>Valuation Date</b>	<b>\$ Value</b>	<b>Valuer</b>	<b>Initial yield</b>	<b>Cap rate</b>	<b>\$/m<sup>2</sup></b>
8 August 2005	\$71,000,000	m3property	9.85%	7.75%	\$3,080/m <sup>2</sup>

Table viii

- The World Trade Centre has a total NLA of approximately 66,000m<sup>2</sup> and 660 parking spaces and is located north of Siddeley Street, inland from the Yarra River. To the south-west of the traditional Melbourne CBD grid, offering views to the CBD and to the adjoining Docklands precinct to the north-west, on the other side of the Citylink connection to the Westgate Freeway. The Fund has purchased three of the buildings contained in the Centre, making up approximately 35% of the total.
- Two inter-connected office buildings with one building providing five levels of office accommodation whilst the other building has ten levels of office accommodation. The podium levels offer floor plates from 2,816m<sup>2</sup> to 3,680m<sup>2</sup>, while the tower building has smaller areas of 585m<sup>2</sup> to 677m<sup>2</sup>. Includes three levels of above ground parking for 340 vehicles, reflecting a high parking ratio of one space per 68m<sup>2</sup> of NLA.
- The concourse level connects these buildings with the balance of the World Trade Centre via two pedestrian bridges, and accommodates a gymnasium, sauna and change rooms.
- Extensively refurbished in 1995 for Victoria Police, the building is understood to suit this tenant partly because of its high parking provision and its high level of accessibility to Melbourne's freeway systems. Spencer Street Station, currently being redeveloped for completion in early 2006, is approximately 200 metres to the north, and a tram stop is outside of the building in Flinders Street.
- The World Trade Centre's ownership is to be split between this Fund and Asset 1, the purchaser of the balance of the complex. The World Trade Centre Land Management Deed governs the inter-relationship between the two parts of the complex, addressing issues related to shared services and cost sharing. Asset 1's part of the World Trade Centre is proposed to be upgraded, with potential expenditure of \$30 million. PIR is advised that the RE is undertaking negotiations with Asset 1 that could result in reduced outgoings following the expiry of the Victoria Police lease in 2015.
- The passing net income for the office component at \$256/m<sup>2</sup> is 35% above market income assessed by the valuer, m3property. This has contributed to the high initial yield, creating a steady cash flow for the next four years. The Fund also has the benefit of market reviews every two years, with minimum rental increases of 2.5% per annum. However, in October 2006 the RE negotiated a 5 year lease extension at the same rates.
- The high tax advantaged income of the Fund of 100% per annum for several years is partly the result of depreciation benefits associated with this complex.
- The complex presents as dated and is expected to require substantial refurbishment on expiry of the current lease. PIR has reviewed the Executive Summary of a Technical Review report for the complex prepared in February 2005 by Rider Hunt Terotech. It recommends expenditure of \$15.4 million over the next six years, should Victoria Police vacate on lease expiry in 2015, or \$6 million if the lease is renewed. The RE appears to have made allowance for reasonable expenditure in its financial forecasts, relating to these recommendations.
- Capital expenditure allowances include \$1 million over the next four years for replacement of the carpet, agreed in a variation to the lease in 2005.

3. 369 Ann Street, Brisbane, QLD					
<b>% of Portfolio</b>		7%	<b>Completion Date</b>		1988
<b>Ownership</b>		100%	<b>Purchase Price</b>		\$24,250,000
<b>Title</b>		Freehold	<b>Vacancy</b>		Nil
<b>Type</b>		Office	<b>Gross Lettable Area</b>		6,646m <sup>2</sup>
<b>Location</b>		Brisbane CBD	<b>Total Site Area</b>		1,813m <sup>2</sup>
Major Tenants		Lease Terms		% Area	% Rental
Sinclair Knight Merz Pty Ltd		10 years, expiring 30 Sept 2008 (2 x 5 year options)		37%	32%
Sinclair Knight Merz Pty Ltd		7 years & 3 months, expiring 30 Sept 2008		14%	13%
Valuation Date	\$ Value	Valuer	Initial yield	Cap rate	\$/m <sup>2</sup>
14 July 2005	\$24,250,000	JLL	7.34%	7.75%	\$3,649/m <sup>2</sup>

Table ix

- An attractive nine-storey office building located on the corner of Ann and Wharf Streets in the uptown precinct of the Brisbane CBD. Approximately 500 metres from the GPO, 200 metres from Central railway station and 200 metres from the premium Eagle Street precinct. Adjoins St Johns Cathedral and opposite Cathedral Square Park.
- Includes 71 car spaces over two levels, reflecting a high parking ratio of one space per 94m<sup>2</sup> of NLA. Has pedestrian tunnel access to Cathedral Square public car parking station with 700 car spaces. Services include 100% standby power provided by a rooftop generator, with fuel supplied by a 15,000-litre underground storage tank.
- Fully occupied, with global professional services firm, SKM, accounting for 80% of the area and two-thirds of the net income, from five separate leases. Two floors occupied by a variety of smaller tenants, with several lease expiries in 2007.
- Approximately 29% of current net income subject to lease expiries over the next three years and 71% in September 2008. Likelihood of lease renewals considered good in current market, with SKM reported to be interested in occupying any space that becomes vacant.
- Rental reviews annually in line with the CPI or fixed increases of 3% to 4%.
- Some possibility of extending NLA of the building at ground level, perhaps introducing a café – the design features an underutilised 750m<sup>2</sup> plaza area adjoining St Johns Cathedral.
- SKM reported to have undertaken significant internal refurbishment to its tenancy area recently, but GN Constructions Pty Ltd's Property Review dated July 2005 indicates there has been no major fabric refurbishment since completion in 1988. The report recommends \$830,500 in expenditure over the next five years. The RE appears to have made appropriate allowances for capital expenditure in its financial forecasts.

4. Citibank Building, 350 Collins Street, Melbourne, VIC					
<b>% of Portfolio</b>		15%	<b>Completion Date</b>		1969, refurbished 1995
<b>Ownership</b>		100%	<b>Purchase Price</b>		\$55,500,000
<b>Title</b>		Freehold	<b>Vacancy</b>		4%
<b>Type</b>		Office	<b>Gross Lettable Area</b>		17,700m <sup>2</sup>
<b>Location</b>		Melbourne CBD	<b>Total Site Area</b>		1,909m <sup>2</sup>
Major Tenants		Lease Terms		% Area	% Rental
Austock		expiring 21 November, 2010		10.7%	9.0%
Valuation Date	\$ Value	Valuer	Initial yield	Cap rate	\$/m <sup>2</sup>
1 November 2005	\$55,500,000	Ernst & Young	7.51%	7.50%	\$3,123/m <sup>2</sup>

Table x

- A B grade 17 level office building (16 levels of Office accommodation above ground floor retail outlets) well located in the heart of the financial precinct of the Melbourne CBD between Elizabeth Street and Queen Street, opposite 333 Collins. The location is considered very strong, although not as good as the eastern Collins precinct, which is the premium office location. The property has frontage at the rear to Little Collins Street and two basement levels of car parking for 65 vehicles
- The floor plate is long and narrow, with a central core mid way along the site. Floor plates are essentially split with a southern and northern section, with light courts either side of the core. The floors are well suited to small multiple tenancies and in fact do not suit large tenants. Other major tenants are Citibank, Collins Street Business Centre and Australian Pooled Development Financing.
- There are presently more than 60 office tenants in the building. The high number of small tenants has both a negative and positive aspect. There are few Collins Street buildings with the scale and prominence of the subject that can offer very small tenants direct,

off the lobby exposure. Fit-outs are recyclable with very little re-fit cost to either the Lessor or Lessee. There is also a shorter “down time” as a consequence. Small tenancies tend to attract a premium rental over larger tenancies. On the negative side, a large number of tenancies presents a very high management requirement. This building was originally refurbished and let up by Adamco, which had its office in the building. The letting-management was intensive and the results were strong. A less than very good management effort will see occupancy and revenue fall.

- There could be some significant capital expenditure requirements over the next few years, as most of the plant is original and should be reaching the end of its life cycle in the foreseeable future.
- It is noted that 25% of lease income is exposed to lease expiries in the next 6 months and more than 60% over the next 3 years. The RE will need to be very focused and proactive with intensive leasing and management effort applied at the property to maintain income.

5. Wesfarmers House, 40, The Esplanade, Perth, Western Australia					
<b>% of Portfolio</b>		14%	<b>Completion Date</b>		1985
<b>Ownership</b>		100%	<b>Purchase Price</b>		\$47,500,000
<b>Title</b>		Freehold	<b>Vacancy</b>		Nil
<b>Type</b>		Commercial	<b>Gross Lettable Area</b>		11,019m <sup>2</sup>
<b>Location</b>		Perth CBD	<b>Total Site Area</b>		1,823m <sup>2</sup>
<b>Major Tenants</b>		<b>Lease Terms</b>		<b>% Area</b>	<b>% Rental</b>
Wesfarmers Limited		To June 2010, with market rent review in June 2008		38%	31%
Landcorp (West Australian Land Authority)		To June 2009, with 4% p.a. fixed increases		17%	14%
Talbot and Olivier (Togsak Pty Ltd)		To March 2018, with 4% p.a. fixed increases except when market rent reviews every 3 years; rent free until August 2007		12%	13%
<b>Valuation Date</b>	<b>\$ Value</b>	<b>Valuer</b>		<b>Initial yield</b>	<b>Cap rate</b>
December 2005	\$48,000,000	Jones Lang Lasalle		6.74%	7.5%
					<b>\$/m<sup>2</sup></b>
					\$4,356/m <sup>2</sup>

Table xi

- This modern A Grade office building with 12 upper floors of offices, ground floor lobby and secured basement parking for 122 cars over three levels is about 100 metres south of St George’s Terrace and William Street junction, which is generally considered the heart of the Perth CBD.
- The property is on a corner site, opposite an entrance to the station for the new southern railway line due to be finished in 2007 and close to the City Busport.
- The building has a distinctive, white aluminium panel and reflective glass façade and steps up from The Esplanade to the marble finished ground floor foyer facing the four lifts. The building has good quality finishes, good natural light to most of the office areas and good views over the Swan River from most levels. The floor plan allows for a variety of office configurations, somewhat limited by the central lift and amenities core dividing each floor into halves. There are male and female toilets and kitchen areas on each floor.

- Parking provision is good (with two separate areas, one with a rear access to one upper level and the main car park with access from The Esplanade to two levels of parking). As well as 67 tenant bays, there are 55 public bays. The public car park is run by the building manager and is manned.
- The major tenant is a West Australian based major public company that has been associated with the

building for many years. The remaining vacant areas have been let with effect from April 2006 and the property will have tenants from diverse industries and few lease expiries until 2009. The valuer considered that the rents for some tenancies were under current market levels, providing good prospects for rental growth when rents are renegotiated.

6. Kvaerner House, 600 St Kilda Road, Melbourne, VIC					
<b>% of Portfolio</b>		16%	<b>Completion Date</b>		1989
<b>Ownership</b>		100%	<b>Purchase Price</b>		\$58,100,000
<b>Title</b>		Freehold	<b>Vacancy</b>		3%
<b>Type</b>		Office	<b>Gross Lettable Area</b>		16,851m <sup>2</sup>
<b>Location</b>		St Kilda Road, Melbourne	<b>Total Site Area</b>		4,882m <sup>2</sup>
<b>Major Tenants</b>		<b>Lease Terms</b>		<b>% Area</b>	<b>% Rental</b>
Aker Kvaener		3 years, expiring 1 January, 2009		18%	21%
<b>Valuation Date</b>	<b>\$ Value</b>	<b>Valuer</b>		<b>Initial yield</b>	<b>Cap rate</b>
December 2005	\$58,100,000	Ernst & Young		7.32%	8.25%
					<b>\$/m<sup>2</sup></b>
					\$3,448/m <sup>2</sup>

Table xii

- This property is a 15 level A grade office building located on a corner site in the St Kilda Road office precinct. This area is an established suburban office precinct with other developments generally comprising multilevel commercial and residential buildings.
- The building comprises a 15 level building with ground floor retail, 14 upper levels of office accommodation along with a seven level car park

to the rear of the property. Total NLA is 16,850m<sup>2</sup> of office space, with secure undercover parking for 570 vehicles. Office floorplates are of varying sizes, comprising generally good quality accommodation with good natural light.

- Weighted average lease expiry of 3.2 years by net income. The property is currently leased to 14 tenants. Vacancy level by area is currently 3%

7. 235 Pyrmont Street, Pyrmont, Sydney, NSW					
<b>% of Portfolio</b>		12%	<b>Completion Date</b>		1989
<b>Ownership</b>		100%	<b>Purchase Price</b>		\$43,000,000
<b>Title</b>		Freehold	<b>Vacancy</b>		Nil
<b>Type</b>		Office	<b>Gross Lettable Area</b>		10,239m <sup>2</sup>
<b>Location</b>		Sydney Fringe CBD	<b>Total Site Area</b>		2,050m <sup>2</sup>
<b>Major Tenants</b>		<b>Lease Terms</b>		<b>% Area</b>	<b>% Rental</b>
John Holland		To Nov 2010		42.1%	40.2%
Roadshow Films Pty Ltd		To Dec 2008 + 3-yr option		19.9%	18.6%
<b>Valuation Date</b>	<b>\$ Value</b>	<b>Valuer</b>		<b>Initial yield</b>	<b>Cap rate</b>
31 December 2005	\$43,000,000	Savills (NSW) P/L		7.34%	7.50%
					<b>\$/m<sup>2</sup></b>
					\$4,200/m <sup>2</sup>

Table xiii

- The property is located on a corner site at the intersection of Pyrmont and Allen Streets in the Pyrmont area of Sydney (close to Darling Harbour) approximately one kilometre from the Sydney CBD. Pyrmont is an inner suburb located approximately 1 kilometre by road from the central business district

of Sydney. It is an established area comprising medium and high-density residential development; Darling Harbour tourist precinct and Convention Centre; Star City Entertainment and Casino Complex; Novotel Hotel and Goldsbrough Apartment Hotel; and a number of commercial office buildings.

*This report does not form any part of any offer document*

- 235 Pymont Street is a B-grade office building, which was reconstructed in 1989 behind its original heritage façade. An air bridge provides a pedestrian walkway direct from Level 2 of the building across Pymont Street and leading to the Light Rail and Monorail stations within a short two-minute walk.
- The building features ground floor foyer area and retail space (Level 1) with seven upper levels of office accommodation. The NLA is approximately 10,239m<sup>2</sup> over seven strata lots. A central atrium enhances natural light for Levels 4 – 7. Level 8 comprises a small commercial office suite of approximately 410m<sup>2</sup> with terrace area (accessed via stairs from Level 7) together with rooftop plant area. In addition there are 30 strata car-parking bays in the adjacent property at 320-360 Harris Street, which are isolated via security screening from the remaining car-parking bays in the building.
- The laneway (Camden Lane) at the rear of 235 Pymont Street forms part of the common property on the Strata Plan 39122, with adjacent properties having rights of way access.
- Tenants include John Holland, Festival Records, Landmark Education, Roadshow Films Pty Ltd, L’Oreal Australia and Microstream.
- The valuation by Savills, dated 31 December 2005, notes that capital expenditure of approximately \$2.45 million may be required over the next 10-year period.

8. 414-416 Khyber Pass Road, Newmarket, Auckland, New Zealand					
<b>% of Portfolio</b>		4%	<b>Completion Date</b>		2005
<b>Ownership</b>		100%	<b>Purchase Price</b>		A\$15,100,000
<b>Title</b>		Freehold	<b>Vacancy</b>		9%*
<b>Type</b>		Office	<b>Gross Lettable Area</b>		5,295m <sup>2</sup>
<b>Location</b>		Auckland Suburbs	<b>Total Site Area</b>		1,002m <sup>2</sup>
<b>Major Tenants</b>		<b>Lease Terms</b>		<b>% Area</b>	<b>% Rental</b>
AXON Computer Systems		9 years, expiring 27 February 2014		34%	32%
Cock & Bull		10 years, expiring 31 July, 2015		16%	21%
<b>Valuation Date</b>	<b>\$ Value</b>	<b>Valuer</b>	<b>Initial yield</b>	<b>Cap rate</b>	<b>\$/m<sup>2</sup></b>
19 April 2006	NZ\$17,700,000	CBRE	8.08%	8.50%	\$3,343/m <sup>2</sup>

\* Covered by rental guarantee until May 2008

Table xiv

- It is located on the corner of Khyber Pass and Kingdon street, close to both the Lion Brewery and Broadway, the main retail precinct of Newmarket. Newmarket is located within 5 kms of the heart of the Auckland CBD.
- A new 6 level suburban A-grade office building completed in 2005, comprising a ground level entry foyer off Kingdon Street and a ground level restaurant/pub with access off Khyber pass. This is well located with supporting establishments nearby.
- There is ample public carparking located opposite the site.
- There is good public transport via bus to the surrounding suburbs and the CBD.
- Being new, there are good depreciation benefits for this building.
- Located on a small site, there is good natural light to two sides but this does not always penetrate to the rear of the floors. The floorplates are of an adequate size.
- AXON computer systems occupy the upper two floors.
- The vacant space, which comprises approximately one third of a floor, has a rental guarantee at market rates from the vendor for up to two years from the date of settlement while the space remains vacant. There exists the possibility that an existing tenant will require this space due to expansion over this period. Otherwise it may be a difficult space to let, due to configuration and lack of good natural light.
- The purchase price was NZ\$18 million.

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## Due Diligence

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PIR was engaged by **SAITeys McMahon Property Limited** to undertake this investment evaluation for a fixed fee established prior to commencement of work on the investment evaluation. Property Investment Research Pty Ltd (PIR) advises that in the compilation of this report, a full due diligence on this offer has not been conducted. Investors would be well advised to consult the offer document, conduct their own inquiries, and receive professional advice. This report was not prepared to form any part of any offer document.

PIR has relied upon information contained in the Product Disclosure Statement dated 15 June 2006. PIR has carried out its own independent inquiries by:

- inspecting the properties;
- holding discussions with representatives of the Responsible Entity; and
- reviewing the PDS dated 15 June 2006.

PIR has received copies of the valuations, tenancy schedules, building due diligence reports, as well as the PDS and the RE's electronic financial analysis. PIR has received copies of the Constitution and the Compliance Plan, which have been registered by the Australian Securities and Investment Commission (ASIC).

PIR has received copies of the following documents:

- Product Disclosure Statements – various, due diligence folders;
- Australian Financial Services Licence No 233191 effective 18 June 2004;
- PIF Breaches Register;
- Certificate of Currency – Chubb. 9 March 2005;
- Charter – Investment Review Committee; and
- Financial model provided by SAITeysMcMahon Property Limited.

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## Explanation of Investment Rating

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The Investment Rating Financial Model (patent pending) provides a single measure of the overall investment merit of this vehicle for various investor profiles. It incorporates the level of expected returns (IRRs) from the investment and adjusts these for both illiquidity and risk associated with this investment, presenting them across the three main marginal tax rates. The Investment Rating is based on the premium of the estimated risk-free, after-tax IRR adjusted for illiquidity over the prevailing 10-year bond rate. This measure enables the valid comparison of an investment with any other for nine (tax rate and risk tolerance) investor profiles. This facilitates the task of tailoring investment selection to the needs of the individual investor. Further, it provides ratings in which the advisers and investors can have unprecedented confidence. The ratings presented in the risk tolerance/tax rate matrix are only a representative sample of those available on PIR's unique individually tailored on-line investment selection system.

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Except when investor gearing is involved, a lower marginal investor tax rate would normally attract a higher rating because investors on higher tax rates (nearly) always pay more tax. An investment which rates AA- for a 46.5% tax rate investor may be relatively better for that investor profile than for a 15% taxpayer for which the rating is AA+. A high rating for a higher marginal investor tax rate is generally less common than the same rating for a lower marginal investor tax rate.

For ease of comprehension, the Investment Rating uses symbols similar to those applied by credit rating agencies. These ratings should not, however, be confused or compared with those used by credit rating agencies. The seven published Investment Ratings from lowest to highest are: A- A A+ AA- AA AA+ AAA. Projects with ratings below A- are not considered investment grade.

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Richard Cruickshank, Managing Director.

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