



# Arena REIT Annual Report 2016

For the year ended 30 June 2016



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## About this report

The financial statements in this report cover Arena REIT (the 'Group') comprising Arena REIT Limited, Arena REIT No. 1, Arena REIT No. 2, and their controlled entities. The financial statements are presented in Australian currency.

The Responsible Entity of Arena REIT No.1 and Arena REIT No.2 (the 'Trusts') is Arena REIT Management Limited (ACN 600 069 761, AFSL 465754).

## Important Notice

This report has been prepared by Arena REIT (Arena) comprising Arena REIT Limited (ACN 602 365 186), Arena REIT Management Limited (ACN 600 069 761 AFSL No. 465754) as responsible entity of Arena REIT No.1 (ARSN 106 891 641) and Arena REIT No.2 (ARSN 101 067 878). The information contained in this report is current only as at the date of this report or as otherwise stated herein. This report may not be reproduced or distributed without Arena's prior written consent. The information contained in this report is not investment or financial product advice and is not intended to be used as the basis for making an investment decision. Arena has not considered the investment objectives, financial circumstances or particular needs of any particular recipient. You should consider your own financial situation, objectives and needs, conduct an independent investigation of, and if necessary obtain professional advice in relation to, this report. Past performance is not an indicator or guarantee of future performance.

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This report is for information purposes only and should not be considered as a solicitation, offer or invitation for subscription, purchase or sale of securities in any jurisdiction, or to any person to whom it would not be lawful to make such an offer or invitation.

This report contains forward-looking statements including certain forecast financial information. The words "anticipate", "believe", "expect", "project", "forecast", "estimate", "outlook", "upside", "likely", "intend", "should", "could", "may", "target", "plan", and other similar expressions are intended to identify forward-looking statements. The forward-looking statements are made only as at the date of this announcement and involve known and unknown risks, uncertainties, assumptions and other factors, many of which are beyond the control of Arena and its directors. Such statements are not guarantees of future performance and actual results may differ materially from anticipated result, performance or achievements expressed or implied by the forward-looking statements. Other than as required by law, although they believe there is a reasonable basis for the forward-looking statements, neither Arena nor any other person (including any director, officer, or employee of Arena or any related body corporate) gives any representation, assurance or guarantee (express or implied) as to the accuracy or completeness of each forward-looking statement or that the occurrence of any event, result, performance or achievement will actually occur. You should not place undue reliance on any of the forward-looking statements.



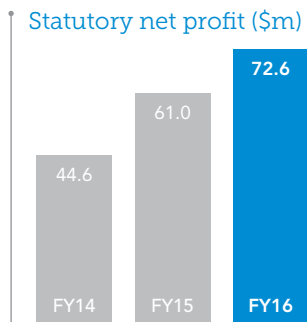
*Arena REIT is an ASX300 listed group that owns, manages and develops specialised real estate assets across Australia.*

*Our objective is to deliver an attractive and predictable distribution to investors with earnings growth prospects over the medium to long term.*

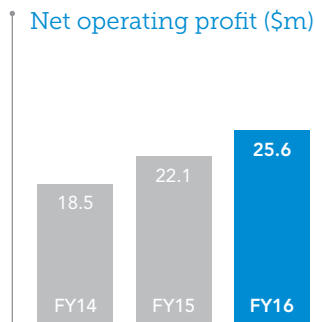
*Since listing on the ASX in 2013, Arena has delivered a three year compound average total return of 33.4% per annum to investors.*

# Financial Highlights

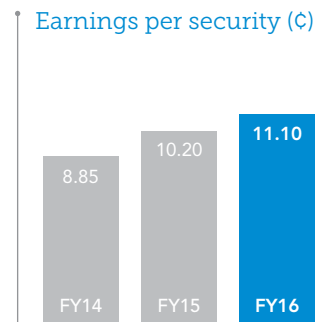
*“Arena has enjoyed another successful year, with our focussed investment strategy, active management of the portfolio and control of borrowing and overhead costs delivering growth in both income and capital value for our investors.”*



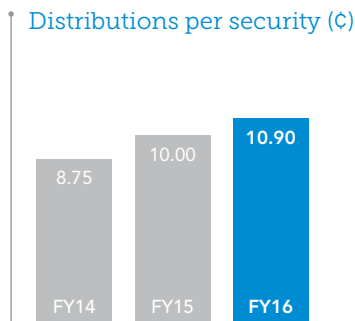
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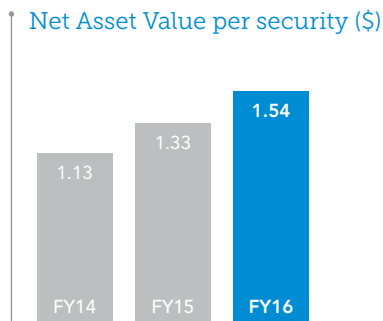
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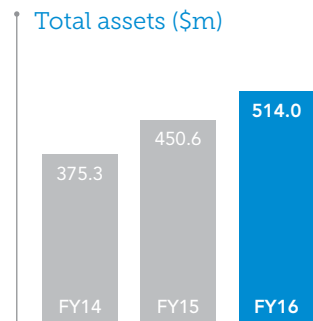
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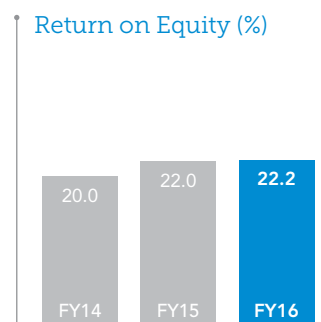
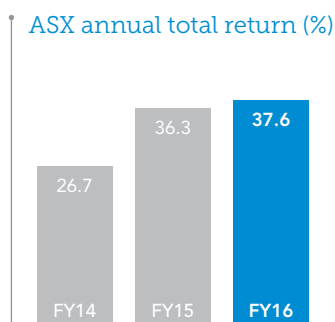
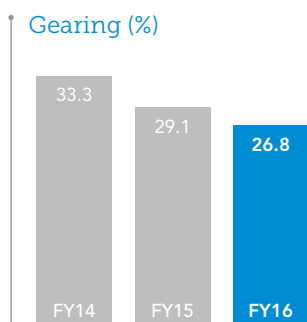
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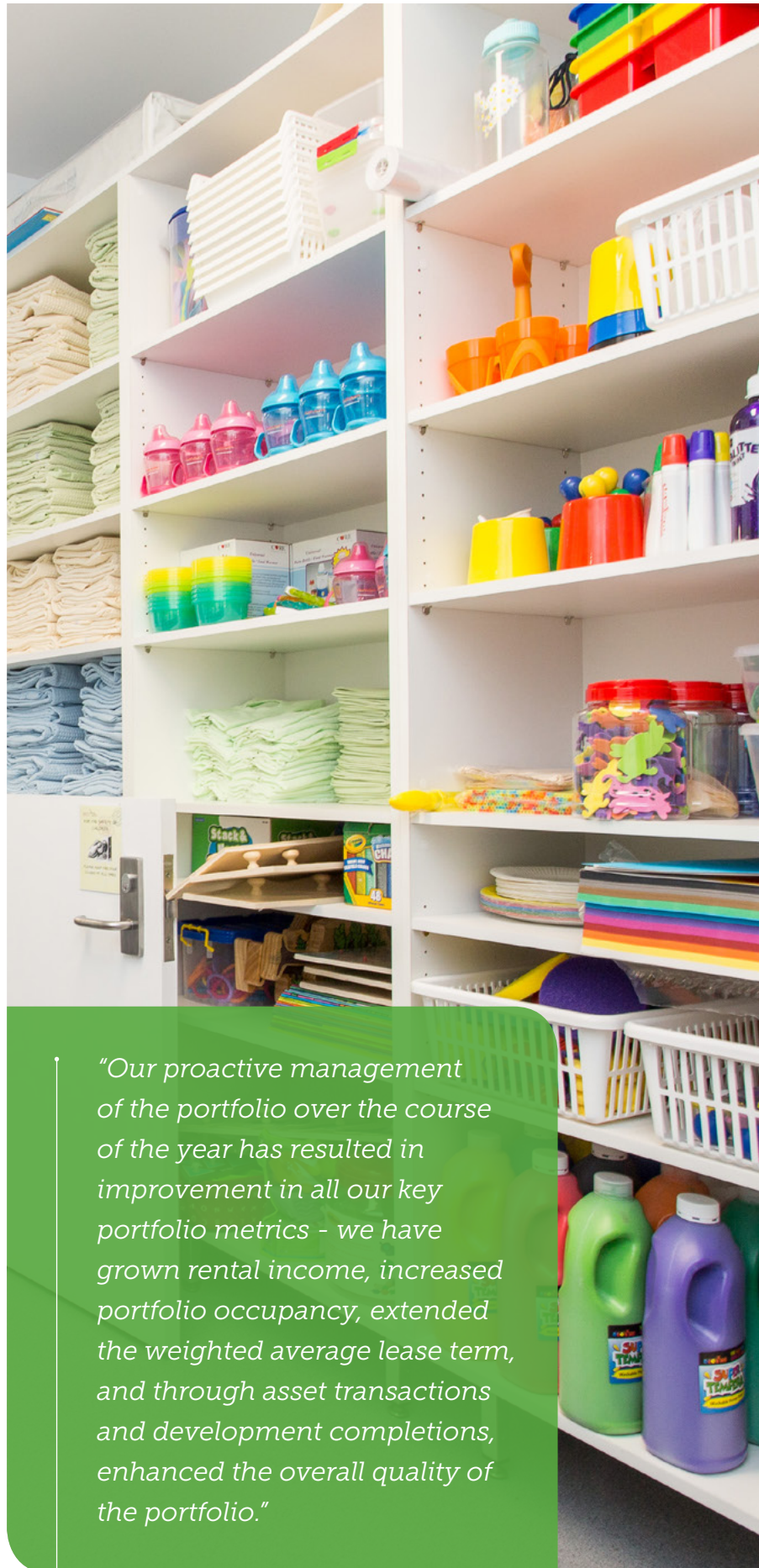


↑14%



## Portfolio Highlights

- ✓ Like for like rental income growth of 3.6% achieved
- ✓ Occupancy increased to 100%
- ✓ Weighted average lease expiry extended to 9.7 years
- ✓ 100% renewal rate achieved on 32 lease option expiries
- ✓ Revaluation uplift of \$51.1 million
- ✓ Weighted average passing portfolio yield firmed 70 basis points to 7.3%
- ✓ Four childcare development projects successfully completed
- ✓ Development pipeline replenished with 14 projects due for completion in the next two years



*"Our proactive management of the portfolio over the course of the year has resulted in improvement in all our key portfolio metrics - we have grown rental income, increased portfolio occupancy, extended the weighted average lease term, and through asset transactions and development completions, enhanced the overall quality of the portfolio."*



David Ross Chairman

## Letter from the Chairman

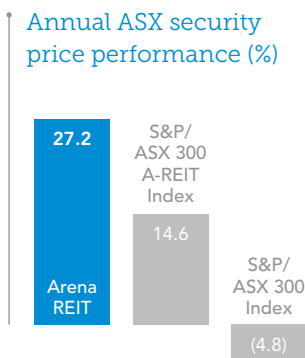
I have pleasure in reporting on another strong year of performance for Arena REIT (Arena).

In June this year we celebrated three years of listing on the Australian Securities Exchange (ASX). Since that time we have successfully grown Arena’s specialised asset base, further diversified the portfolio by both sector and tenant, and through internalisation of management, enhanced the transparency and alignment of our business.

Arena’s investment strategy remains robust. Our focus on providing real estate solutions to sectors that exhibit strong underlying macro and socio-economic drivers has resulted in growing demand for our specialised expertise and opportunities to invest capital.

In childcare, we have benefited from the growth in both population and childcare participation, which has supported our tenant’s operational performance and created opportunities to strategically grow and enhance the quality of the portfolio.

In healthcare, the ageing population and growth in chronic disease have continued to underpin demand for large scale low cost medical care. This has increased investor demand for healthcare property backed by long term leases to established operators.



With interest rates at an historic low in Australia, Arena's strategy of investing in property with relatively long leases on terms which provide opportunity for real growth in income and minimal capital expenditure obligations is attractive to investors. This is reflected in Arena's strong security price performance on the ASX during 2016 and the net asset value per security increasing by 16% over the year.

The weighted average lease expiry (WALE) of Arena's leases has been extended to 9.7 years, with the 100% lease renewal rate during the year again highlighting the merit of investing in specialised sectors where tenants' premises have strategic importance for the operation and value of their business.

Earnings per security grew by 9% for the year, driven in part by Arena's like for like rental income growth of 3.6%. This was achieved through a combination of lease renegotiations, strong market rent reviews which averaged a 5.7% increase, and the structure of Arena's leases where a large proportion have an annual increase of the greater of 2.5% or the growth in the relevant Consumer Price Index (CPI). This rent review structure is advantageous in the current low inflation environment.

A key platform of our strategy continues to be the development of new childcare centres that meet our long-term investment criteria – being in attractive locations and leased on our preferred lease terms to established childcare operators. Our collaborative approach to building value has seen us not only deliver four successful childcare development projects this year, which also contributed to earnings growth, but also add to our growing pipeline of projects for the future.

During 2016, Arena's capital position was also enhanced, with a renegotiation of our borrowing facility extending the average debt maturity and reducing the average cost of debt. The balance sheet remains strong with borrowing at 26.8% of total assets and capacity to fund the existing development pipeline and new investment opportunities.

Operating expenses were largely unchanged compared to the prior year, reflecting efficient cost management despite an increase in the total asset base, reinforcing the benefits of our internalised management structure.

As we head into the 2017 financial year, the management team's focus continues to be on actively managing the existing portfolio and successful execution of development projects.

*"Over the past three years, Arena has delivered a compound average total return of 33.4% per annum, and compound average distribution growth of 11% per annum. In relative terms, this has consistently positioned Arena in the top quartile of A-REITs listed on the ASX."*

As in previous years, I am pleased to advise that we are again forecasting distribution growth, providing distribution guidance of 11.7 cents per security for the 2017 financial year<sup>1</sup>.

In line with Arena's investment strategy, we are also focussed on continuing to seek new opportunities to grow income and mitigate risk – through investment in assets, projects and sectors that offer defensive characteristics and attractive risk adjusted return profiles.

Thank you for your continued support of Arena.

Yours sincerely,



David Ross,  
Chairman

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1. Estimated on a status quo basis assuming no new acquisitions or disposals, developments in progress are completed in line with forecast assumptions, and tenants comply with their lease obligations.



Bryce Mitchelson Managing Director

## Managing Director's Report

Arena's strategy to invest in specialised real estate sectors that exhibit strong underlying demand drivers has underpinned growth in both earnings and valuations. These positive market dynamics, coupled with our proactive management of the portfolio, successful execution of development projects and focus on cost control have contributed to our strong 2016 result and see us well placed as we head into 2017.

### Financial results

I am pleased to advise that Arena has delivered a net operating profit of \$25.6 million, up 16% on the result for 2015. Underpinning this strong result was growth in rental income from both the underlying portfolio and completed development projects, as well as lower net operating and borrowing costs.

Statutory net profit for the year was \$72.6 million, and included unrealised gains from the \$51.1 million increase in property valuations recorded across the portfolio.

On a per security basis, Arena delivered earnings of 11.1 cents and paid an annual distribution of 10.9 cents, reflecting growth of 9% over 2015. This was in line with our upgraded guidance and represents a payout ratio of 98% of net operating profit.

At 30 June, our total assets had increased by 14% to \$514 million, predominantly as a result of the \$51.1 million revaluation uplift on the property portfolio. This uplift also contributed to a \$0.21 increase in Net Asset Value per security to \$1.54 at 30 June 2016.

Importantly, operating expenses were unchanged at \$3.2 million, reflecting efficient cost management over our increased asset base, and reinforcing the benefits being derived from our internalised structure.



*"Our favourable lease structure has provided attractive rental income growth, and our execution of quality childcare development projects continues to deliver earnings accretion and enhance the quality of the portfolio."*

### Capital management

Our proactive approach to capital management has made a positive contribution to 2016 earnings and through the extension of the borrowing facility and new hedging arrangements, we have laid the foundations for a competitive cost of borrowing over the medium term.

#### Borrowing facility renegotiated on favourable terms

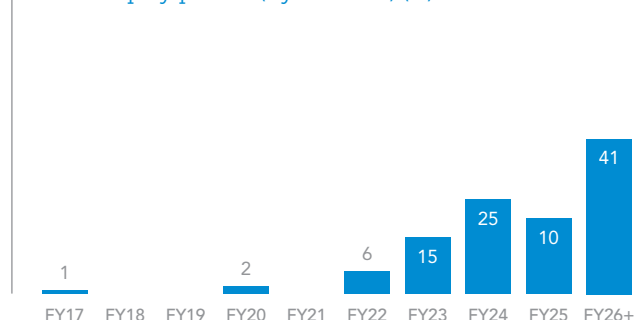
In December 2015 we completed the renegotiation of terms for our \$175 million borrowing facility. As a result, we added a third lender to the syndicate, extended the facility average duration to 3.5 years and reduced the weighted average cost of debt to 3.85% pa at 30 June 2016, down from 4.30% pa at 30 June 2015.

At the end of the 2016 financial year, we had 72% of drawn debt hedged, at a weighted average interest rate of 2.48%.

#### Capacity to fund growth

At 30 June 2016, gearing has decreased to 26.8%, predominantly as a result of the positive impact of revaluations. A further \$37 million is available within the existing debt facility to fund the development pipeline, and the DRP remains open, after raising \$6.2 million this year.

Lease expiry profile (by income) (%)



### Portfolio overview

#### Rent review structure delivering real income growth

Like-for-like rental income increased by 3.6% in FY16, through a combination of annual rent reviews and renegotiated leases.

The majority of rent reviews were subject to a fixed amount or an increase equivalent to the greater of 2.5% or growth in the relevant CPI. In Australia's current low inflation environment, having the 2.5% minimum floor was advantageous, and enabled us to deliver real growth in rental income. This was further buoyed by the positive outcomes received on the 13 market rent reviews completed to date, which recorded an average increase of 5.7%. A further 18 market rent reviews are still in independent determination.

#### Portfolio defensive characteristics enhanced through active management

The portfolio was further strengthened throughout the financial year, with occupancy increased to 100% and the portfolio's weighted average lease expiry (WALE) extended to 9.7 years through the renewal of 32 lease options and the renegotiation of 12 existing leases on new 20 year terms.

The 32 lease option renewals for leases expiring in FY21 reflect a 100% renewal rate, and are a strong indication of the quality of the portfolio's assets and the strength of Arena's tenant relationships. The portfolio management team's focus continues to be on de-risking future income. Only 3.5% of portfolio income is subject to lease expiry over the next five years, and leases on over 75% of portfolio income are not due to expire until 2024 or beyond.

#### Portfolio valuation uplift of \$51.1 million

In accordance with Arena's valuation policy, 39% of the portfolio was independently valued during the 2016 financial year, with assets not valued independently subject to a Directors' valuation. At 30 June 2016, the portfolio recorded a revaluation uplift of \$51.1 million, an increase of 11.5%.

This increase was the result of a combination of rental income growth, proactive portfolio management and a firming in passing yields, with strong transaction evidence in the direct market contributing to the weighted average passing yield on the portfolio firming 70 basis points to 7.3% at 30 June 2016.

## Development projects

Our growing origination and development management capability has enabled us to access attractive development margins on completed developments, as well as identify and secure new projects for the pipeline.

### Completed developments

In the 2016 financial year, we completed four childcare centre developments for a total cost of \$19.1 million, delivering a weighted average yield on cost of 8.7%. Since completion, these centres have been independently valued at \$26.6 million, resulting in an attractive development margin of \$7.5 million.

The centres are now all open and operating, with leases of 15-20 years in place to existing tenants.

#### Developments completed in the 2016 financial year

Project	Tenant	Cost (\$m)	Lease term (years)
Murwillumbah, NSW	Petit Early Learning Journey	2.4	15
Kawana, QLD	Green Leaves Early Learning Centres	3.2	15
Clifton Hill, VIC	Petit Early Learning Journey	6.6	20
Richmond, VIC	Petit Early Learning Journey	6.9	20

### Development pipeline

The development pipeline continues to grow as new opportunities are identified and assessed against our rigorous investment criteria.

As we commence the 2017 financial year we have 14 projects underway or in various stages of planning and negotiation across the portfolio. Six of these projects are integrated on new primary school sites as part of our transaction with the State of Victoria.

Prior to commencement, each project in the pipeline has a pre-commitment in place with an established childcare operator on a long-term lease. Together these projects have a forecast total cost of \$52.0 million and a target weighted average yield on cost of 8%.

## Outlook

As we commence the 2017 financial year, the portfolio's structured rental growth, with its limited exposure to lower inflation expectations, coupled with the progress on the development pipeline, underpin our recently announced distribution guidance of 11.7 cents per security<sup>1</sup>. This reflects forecast distribution growth of 7.4% over the 2016 distribution.

Looking forward, we will continue to monitor the resolution of the proposed Federal Government funding changes for the childcare sector, as well as the impact of increased regulation and additions to supply on tenant profitability.

On behalf of all of the Arena team, I would like to thank you for your continued support over the past twelve months, and look forward to again reporting a positive result for the 2017 financial year.

Yours sincerely



Bryce Mitchelson,  
Managing Director

1. Estimated on a status quo basis assuming no new acquisitions or disposals, developments in progress are completed in line with forecast assumptions, and tenants comply with their lease obligations.

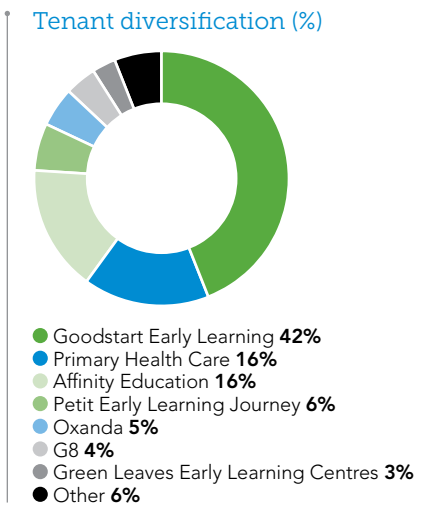
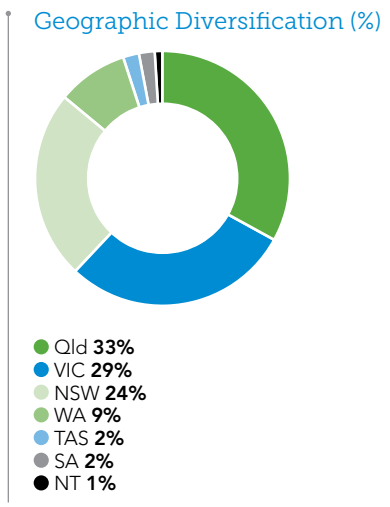
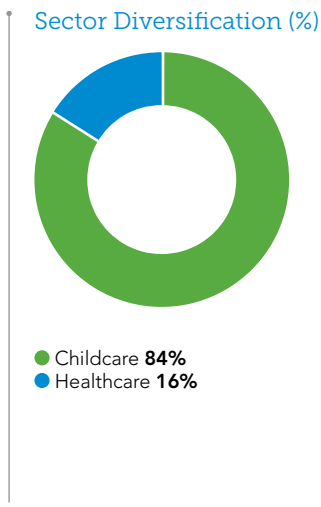
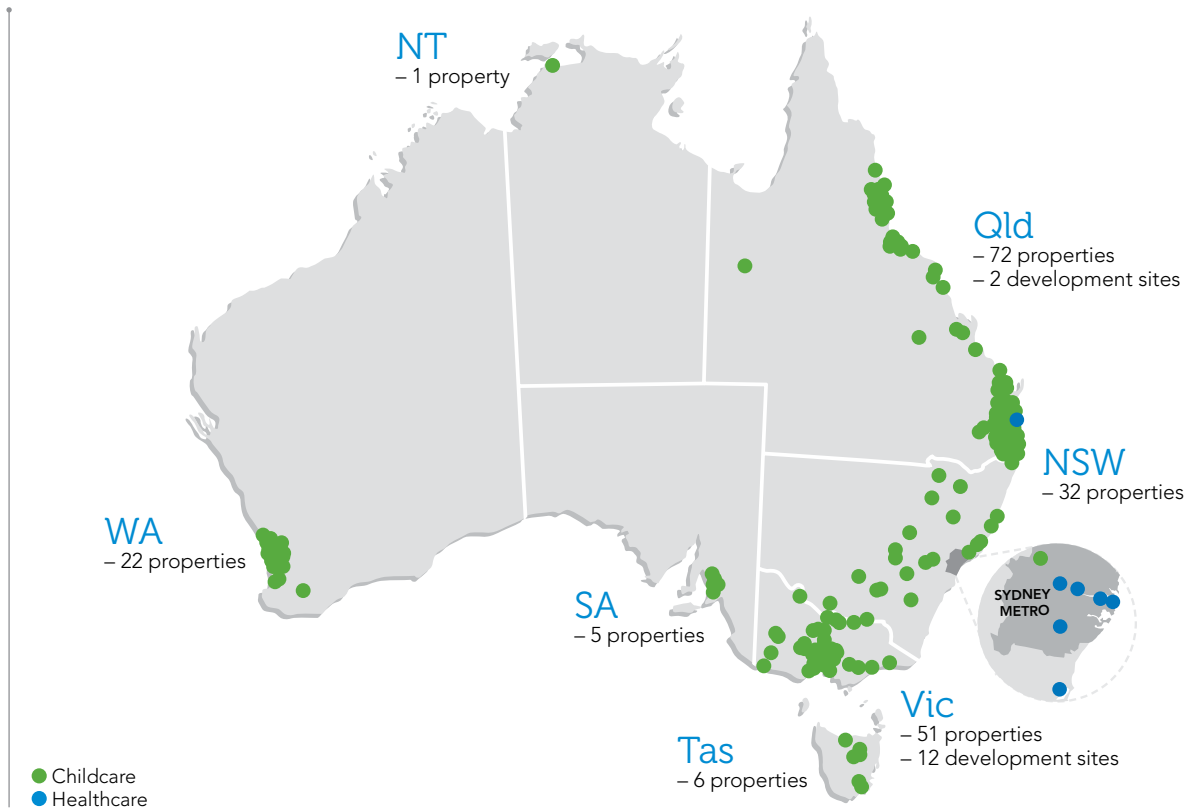


*“Four development projects were completed during the year for a total cost of \$19.1 million. Our growing origination and development management capability has enabled us to access attractive development margins on completed developments, as well as identify and secure new projects for the pipeline.”*

Petit Early Learning Journey, Richmond, VIC

# Portfolio summary

Arena invests in a portfolio of specialised assets in growing sectors that are supported by favourable demographic and economic trends. Our current portfolio of 189 social infrastructure facilities is 100% leased to a diversified tenant base in the growing childcare and healthcare sectors.





**Arena innovation delivers a customised solution for the State of Victoria**

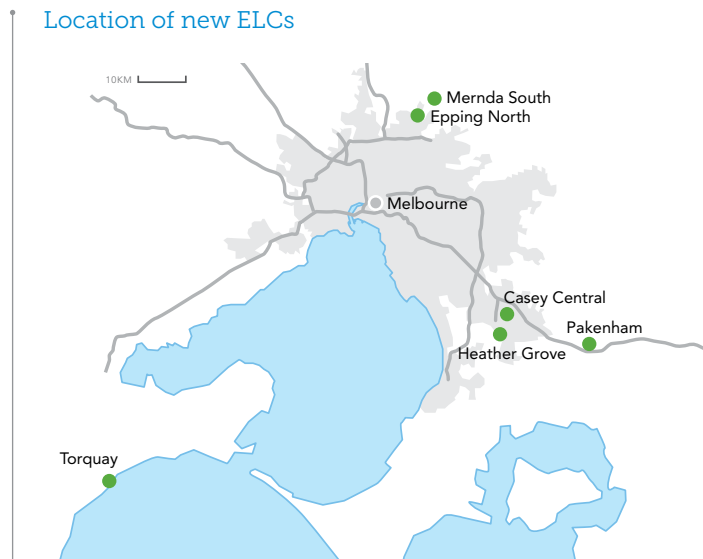
In October 2015 we announced an innovative transaction with the State of Victoria to develop six early learning centres (ELCs) alongside new primary school developments. The transaction involved Arena developing a unique solution to the delivery of integrated childcare centres on new primary school sites.

Arena was granted a 26 year tenure on each site, and has secured YMCA, a well established not-for-profit childcare service provider, to lease the completed centres.

All of the projects are located in areas that are relatively undersupplied with childcare, and have high population growth projections.

The \$15 million in projects began construction in early 2016 and the first five centres are scheduled to open for the commencement of the 2017 school year.

Location of new ELCs





The board of directors (left to right): Dennis Wildenburg, Bryce Mitchelson, David Ross, Simon Parsons and Gareth Winter

## Corporate Governance

The board of directors for Arena REIT Limited and Arena REIT Management Limited work together and take a coordinated approach to corporate governance.



View Arena's key policies and the full Corporate Governance Statement for the 2016 financial year at [www.arena.com.au/about/governance](http://www.arena.com.au/about/governance)

Each Board has a Board Charter which details the composition, responsibilities, and protocols of the Board. In addition, the Boards have a Code of Conduct which sets out the standard of business practices required of directors and staff.

Arena conducts its business in accordance with these charters and codes, as well as other key policies which are published on its website. These include:

- › Arena REIT Continuous Disclosure Policy
- › Arena REIT Diversity Policy
- › Arena REIT Privacy Policy
- › Arena REIT Communications Policy
- › Arena REIT Summary of Risk Management Framework
- › Arena REIT Securities Trading Policy.

In compliance with ASX Listing Rule 4.10.3, Arena has also published on its website a statement disclosing the extent to which Arena has followed the recommendations for good corporate governance set by the ASX Corporate Governance Council (Corporate Governance Principals and Recommendations 3rd Edition) during the reporting period.



# Arena REIT Financial Report 2016

For the year ended 30 June 2016

**PRIMARY**  
HEALTH CARE LIMITED  
**MEDICAL CENTRE**

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## Financial report

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These financial statements cover Arena REIT (the 'Group') comprising Arena REIT No. 1, Arena REIT No. 2, Arena REIT Limited, and their controlled entities. The financial statements are presented in Australian currency.

The Responsible Entity of Arena REIT No. 1 and Arena REIT No. 2 (the 'Trusts') is Arena REIT Management Limited (ACN 600069761). The Responsible Entity's registered office is:

Level 5, 41 Exhibition Street  
Melbourne VIC 3000



Petit Early Learning Journey, Clifton Hill, VIC



# Directors' Report

The directors of Arena REIT Limited ('ARL') and Arena REIT Management Limited ('ARML'), the Responsible Entity of Arena REIT No. 1 and Arena REIT No. 2 (the 'Trusts'), present their report together with the financial statements of Arena REIT for the year ended 30 June 2016. The financial report covers ARL, Arena REIT No. 1 ('ARF1'), Arena REIT No. 2 ('ARF2'), and their controlled entities.

ARF1, ARF2 and ARL are separate entities for which the units and shares have been stapled together to enable trading as one security. The units of ARF1, ARF2 and shares of ARL cannot be traded separately. None of the stapled entities controls any of the other stapled entities, however for the purposes of statutory financial reporting the entities form a consolidated group.

The financial report combines the results of ARF1, ARF2 and ARL. The comparative information presented is that of ARF1 and ARF2 for the entire period and ARL from 12 December 2014.

## Directors

The following persons held office as directors of ARL during the whole of the financial year and up to the date of this report:

- David Ross (Chairman) (Independent, non-executive)
- Simon Parsons (Independent, non-executive)
- Dennis Wildenburg (Independent, non-executive)
- Bryce Mitchelson (Executive)

The following persons held office as directors of ARML during the whole of the financial year and up to the date of this report:

- David Ross (Chairman) (Independent, non-executive)
- Simon Parsons (Independent, non-executive)
- Dennis Wildenburg (Independent, non-executive)
- Bryce Mitchelson (Executive)
- Gareth Winter (Executive)

## Principal activities

Arena REIT invests in a portfolio of investment properties and is listed on the Australian Securities Exchange under the code ARF.

There were no changes in the principal activities of the Group during the year.

## Distributions to securityholders

The following table details the distributions to securityholders declared during the financial year:

	2016	2015	2016	2015
	\$'000	\$'000	cps	cps
September quarter	6,128	5,156	2.6750	2.4375
December quarter	6,158	5,211	2.6750	2.4625
March quarter	6,413	5,803	2.7750	2.5500
June quarter	6,437	5,821	2.7750	2.5500
<b>Total distributions to securityholders</b>	<b>25,136</b>	<b>21,991</b>	<b>10.9000</b>	<b>10.0000</b>

## Directors' Report

### Operating and financial review

The Group operates with the aim of generating attractive and predictable distributions for securityholders with earnings growth prospects over the medium to long term.

The Group's strategy is to invest in property underpinned by relatively long leases and in sectors with supportive macro-economic trends. The Group will consider investment in sectors with the required characteristics, which may include:

- Childcare/early learning services;
- Healthcare – including medical centres, diagnostic facilities, hospitals, aged care and associated facilities;
- Education – including schools, colleges and universities and associated facilities.

### Key financial metrics

	30 June 2016	30 June 2015	Change
Net profit (statutory)	\$72.6 million	\$61.0 million	+19%
Net operating profit (distributable income)	\$25.6 million	\$22.1 million	+16%
Distributable income per security	11.1 cents	10.2 cents	+9%
Distributions per security	10.9 cents	10.0 cents	+9%
Total assets	\$514.0 million	\$450.6 million	+14%
Investment properties	\$491.4 million	\$420.5 million	+17%
Borrowings	\$138.0 million	\$131.0 million	+5%
Net assets	\$357.5 million	\$303.5 million	+18%
NAV per security	\$1.54	\$1.33	+16%
Gearing *	26.8%	29.1%	-230 bps

\* Gearing calculated as Borrowings/Total assets.

### FY16 highlights

- Net operating profit was \$25.6 million, up 16% on the previous year;
- 9% growth in distributable income per security and 9% growth in distributions paid to investors;
- The property portfolio increased with the completion of four purpose-built childcare centre developments and the acquisition of one operational childcare centre;
- Arena commenced the development of six childcare centres in conjunction with the Victorian Government Schools PPP;
- The portfolio occupancy increased to 100%;
- Gearing was 26.8% at 30 June 2016, below the maximum gearing range of 35%-45%;
- NAV per security at 30 June 2016 was \$1.54, an increase of 16% on 30 June 2015. This was primarily due to the increase in investment property values during the period.

## Financial results

	30 June 2016	30 June 2015
	\$'000	\$'000
Rental income	33,316	31,196
Other income	638	480
<b>Total operating income</b>	<b>33,954</b>	<b>31,676</b>
Direct property expenses	(1,003)	(1,306)
Operating expenses	(3,249)	(1,875)
Former responsible entity management fees	–	(1,353)
Finance costs	(4,131)	(5,048)
<b>Net operating profit (distributable income) *</b>	<b>25,571</b>	<b>22,094</b>
Non-distributable items:		
Straight-line rental income	(327)	23
Revaluation gain on investment properties	51,062	39,828
Change in fair value of derivatives	(2,915)	(1,781)
Profit/(loss) on sale of investment properties	(121)	2,232
Stapling and other transaction costs	(242)	(1,438)
Amortisation of security-based payments (non-cash)	(365)	(112)
Other	(42)	120
<b>Statutory net profit</b>	<b>72,621</b>	<b>60,966</b>

\* Net operating profit (distributable income) is not a statutory measure of profit.

## Financial results summary

	30 June 2016	30 June 2015
Net operating profit (distributable income) (\$'000)	25,571	22,094
Weighted average number of ordinary securities ('000)	230,165	216,627
Distributable income per security (cents)	11.11	10.20

- Net operating profit is the measure used to determine securityholder distributions and represents the underlying cash-based profit of the Group for the relevant period. Net operating profit excludes fair value changes from asset and derivative revaluations and items of income or expense not representative of the Group's underlying operating earnings or cashflow.
- The increase in net operating profit during the year is primarily due to:
  - Ongoing annual rent increases on the Group's property portfolio;
  - Commencement of rental income from the four childcare developments completed during the year;
  - The full year effect of acquisitions and developments completed during FY15;
  - A full year of savings in management operating expenses, notwithstanding the 27% increase in total assets since the December 2014 internalisation of management;
  - Lower cost of debt compared to the prior year following the completion of the debt refinance and extension in December 2015.
- Non-distributable items primarily increased due to a higher investment property revaluation gain compared to the prior period.

## Directors' Report

### Investment property portfolio

#### Key property metrics

	30 June 2016	30 June 2015
Total value of investment properties	\$491.4 million	\$420.5 million
Number of properties under lease	189	184
Development sites	14	11
Properties available for lease or sale	–	2
<b>Total properties in portfolio</b>	<b>203</b>	<b>197</b>
Portfolio occupancy	100%	99%
Weighted average lease expiry (WALE)	9.7 years	8.9 years

- The increase in the value of investment properties is primarily due to the addition of:
  - New childcare development expenditure of \$13.7 million;
  - The purchase of an operational childcare centre for \$4.9 million;
  - A net revaluation increment to the portfolio of \$51.1 million for the year.
- Offset by the following investment property disposals during the year:
  - Two vacant childcare centres with a book value of \$1.15 million were sold during the year.

### Capital management

#### Equity

- During the year, 3.7 million securities were issued at an average price of \$1.69 to raise \$6.2 million of equity pursuant to the Distribution Re-investment Plan (DRP);
- A fully underwritten placement to institutional and professional investors was completed in the prior year, raising \$25 million through the issue of 16.25 million stapled securities at a price of \$1.60.

#### Bank facilities & gearing

- Arena REIT completed a refinancing of its syndicated debt facility during the year to extend the facility term to December 2018 (50% of facility) and December 2020 (50% of facility);
- The balance drawn increased by \$7 million to fund acquisitions and development capital expenditure;
- Gearing was 26.8% at 30 June 2016 (30 June 2015: 29.1%);
- The Group was fully compliant with all bank facility covenants throughout FY16 and as at 30 June 2016. At 30 June 2016 the Loan to Valuation Ratio was 31.2% (Covenant: 50%) and the Interest Cover Ratio was 6.2 times (Covenant: 2.0 times).

#### Interest rate management

- During the year the Group managed its interest rate risk in accordance with its interest rate risk management policy. The swap portfolio average term was extended due to near term swap expiry;
- As at 30 June 2016, 72% of Arena REIT borrowings are hedged for a weighted average term of 4.0 years (2015: 69% for 3.5 years). The average swap fixed rate at 30 June 2016 is 2.48% (2015: 2.62%);
- The Group will manage its interest rate swaps to deal with near term expiry and as debt is drawn in accordance with its interest rate risk management policy.

## FY17 outlook

The Group has provided market guidance for FY17 distribution of 11.7 cents per security, which represents an increase of 7.4% on FY16.

The distribution outlook assumes a status quo basis, with no new acquisitions or disposals, developments in progress are completed in line with budget assumptions and tenants comply with their lease obligations.

## Significant changes in state of affairs

In the opinion of the directors, other than the matters identified in this report, there were no significant changes in the state of affairs of the Group that occurred during the financial year.

## Matters subsequent to the end of the financial year

No matter or circumstance has arisen since 30 June 2016 that has significantly affected, or may significantly affect:

- (i) the operations of the Group in future financial years; or
- (ii) the results of those operations in future financial years; or
- (iii) the state of affairs of the Group in future financial years.

## Likely developments and expected results of operations

The Group will continue to be managed in accordance with its existing investment objectives and guidelines.

The results of the Group's operations will be affected by a number of factors, including the performance of investment markets in which the Group invests. Investment performance is not guaranteed and future returns may differ from past returns. As investment conditions change over time, past returns should not be used to predict future returns.

## Material business risks

The material business risks that could adversely affect the achievement of the Group's financial prospects are as follows. The Responsible Entity has in place a Risk Management Policy and Framework under which it identifies, assesses, monitors and manages these risks.

### Concentration risk

The Group's property portfolio is presently 84% invested in childcare centres and childcare centre development sites and 16% in healthcare assets. Adverse events to the childcare sector or healthcare sector may result in a general deterioration of tenants' ability to meet their lease obligations and the future growth prospects of the current portfolio. As at 30 June 2016, 74% of the portfolio by income (excluding developments) is leased to the largest three tenants (Goodstart Early Learning Ltd with 42%, Primary Health Care Limited with 16% and Affinity Education Group with 16%). Any material deterioration in the operating performance of these tenants may result in them not meeting their lease obligations which could reduce the Group's income.

### Tenant risk

The Group relies on tenants to generate its revenue. Tenants may be not for profit companies limited by guarantee, private entities or listed public companies. If a tenant is affected by financial difficulties they may default on their rental or other contractual obligations which may result in loss of rental income and loss in value of the Group's properties. Typically, tenants are required to provide an unconditional and irrevocable bank guarantee, which must not expire until at least six months after the ultimate expiry date of the lease, for an amount generally equivalent to six months' rent (plus GST) as security for their performance under the lease.

Refer to note 9(d) for further details on tenancy risk for the portfolio.

## Directors' Report

### Information on directors

The directors at the date of this report are:



#### David Ross, Independent Non-Executive Chairman

David has over 30 years' experience in the real estate and investment management sectors.

He held senior positions with Lend Lease Corporation over a period of 10 years, including Global and US Chief Executive Officer Real Estate Investments, Chief Executive Officer Asia Pacific and Chief Executive Officer of General Property Trust. He was also Chief Operating Officer of Babcock and Brown, responsible for the Group's corporate and administrative support functions globally.

David holds a Bachelor of Commerce, a Property Valuation qualification and is a Fellow of the Australian Institute of Company Directors (FAICD).

**Other current directorships:** Arena Investment Management Limited.

**Former directorships in last 3 years:** None.



#### Simon Parsons, Independent Non-Executive Director

Simon has over 30 years' experience in the commercial property industry. He is presently Managing Director of Parsons Hill Stenhouse Pty Ltd, a commercial property practice.

Simon is a Fellow of the Royal Institution of Chartered Surveyors (RICS), a Fellow of the Australian Institute of Company Directors (FAICD), and is a member of the RICS Oceania Property Board.

Simon holds a Master of Science (Real Estate) and a Master of Social Science (Env & Planning).

**Other current directorships:** Arena Investment Management Limited.

**Former directorships in last 3 years:** None.



#### Dennis Wildenburg, Independent Non-Executive Director, Chairman of Board Audit Committee

Dennis has over 30 years' experience in the financial services and funds management industry including senior management, Board and compliance committee roles.

Dennis is a member of the Institute of Chartered Accountants in Australia.

**Other current directorships:** Investa Wholesale Funds Management Limited; Arena Investment Management Limited.

**Former directorships in last 3 years:** None.



#### Bryce Mitchelson, Executive Director

Bryce is Managing Director of Arena and joined Arena in May 2009.

Bryce has more than 20 years' experience in listed and unlisted property funds management as well as property investment, development, valuation and real estate agency.

Bryce holds a Bachelor of Economics (Accounting), Bachelor of Business (Property) and Graduate Diploma of Applied Finance and Investment.

**Other current directorships:** None.

**Former directorships in last 3 years:** Arena Investment Management Limited.



### Gareth Winter, Executive Director and Company Secretary

Gareth was appointed Chief Financial Officer of Arena in March 2012, and Executive Director of Arena REIT Management Limited in December 2014. Gareth was formerly a partner at PricewaterhouseCoopers and has over 20 years' professional experience.

Throughout his professional career Gareth specialised in advising the listed and unlisted property and infrastructure funds management sector on corporate finance, capital management, risk management, transaction structuring and financial systems and reporting.

Gareth is a member of the Institute of Chartered Accountants in Australia and holds a Bachelor of Commerce.

**Other current directorships:** None.

**Former directorships in last 3 years:** None.

### Meetings of directors

The number of meetings of the Responsible Entity's board of directors and of each board committee held during the year ended 30 June 2016, and the number of meetings attended by each director were:

	ARL Board		ARML Board		Audit Committee		Remuneration & Nomination Committee	
	A	B	A	B	A	B	A	B
David Ross	11	11	22	22	11	11	4	4
Simon Parsons	11	10	22	21	11	10	4	4
Dennis Wildenburg	11	11	22	22	11	11	4	4
Bryce Mitchelson	11	11	22	22	*	*	*	*
Gareth Winter	*	*	22	22	*	*	*	*

A - Number of meetings held during the year.

B - Number of meetings attended.

\* = Not a member of the relevant committee.

### Remuneration report

This remuneration report presents Arena REIT's remuneration arrangements for Key Management Personnel (KMP) for the year ended 30 June 2016. The report has been prepared and audited in accordance with the requirements of the Corporations Act and Regulations.

#### 1. Overview

##### 1.1 Governance

The directors have appointed a Remuneration and Nomination Committee (the "Committee") to advise the Board on remuneration policy and practices. The Committee is comprised of independent directors and is chaired by Mr David Ross. The Committee will, as required, appoint remuneration advisers to review and advise on aspects of a remuneration policy and associated frameworks. The Committee engaged Ernst & Young (EY) to advise on the establishment of remuneration policy and structure that is consistent with market practice in the A-REIT sector. EY did not provide any remuneration recommendations in respect of KMP.

## Directors' Report

### Remuneration report (continued)

#### 1.2 Key Management Personnel (KMP)

KMP are persons identified as having authority and responsibility for planning, directing and controlling the activities of Arena REIT. There has been no change in KMP since the end of the reporting period.

	Position	FY16 KMP	FY15 KMP
<b>Non-Executive Directors</b>			
David Ross	Non-Executive Chairman Chair – Remuneration & Nomination Committee Member – Audit Committee	Yes	Yes
Simon Parsons	Non-Executive Director Member – Remuneration & Nomination Committee Member – Audit Committee	Yes	Yes
Dennis Wildenburg	Non-Executive Director Chair – Audit Committee Member – Remuneration & Nomination Committee	Yes	Yes
<b>Executive KMP</b>			
Bryce Mitchelson	Managing Director	Yes	Yes
Gareth Winter	Executive Director & Chief Financial Officer	Yes	Yes
Robert de Vos (from 12 December 2014)	Head of Property	Yes	Yes

#### 1.3 Remuneration Policy

The Directors of Arena REIT have adopted a remuneration policy that recognises the need to attract, motivate and retain employees to deliver sustainable and superior business performance. The remuneration policy is underpinned by the following principles:

- Remuneration is externally competitive in terms of quantum, mix and design to support the attraction and retention of employees and takes into account the relative size and nature of the Arena REIT business, its ability to pay and the role and experience of employees;
- The remuneration framework supports the delivery of Arena REIT's business strategy;
- Remuneration is made up of fixed and variable reward;
- Variable reward will be used to recognise performance in both the short term and longer term and will depend on performance against key targets and objectives.

#### 2. Non-Executive Director Remuneration Framework

Each non-executive director of Arena REIT is paid an amount determined by the Board to a maximum aggregate amount approved by securityholders of \$650,000 per annum.

Fees are set to ensure non-executive directors are remunerated fairly for their services, recognising the level of skill, expertise and experience required to perform the role. Non-executive directors do not receive any equity based payments, retirement benefits or incentive payments.

Annual fees in respect of FY16 (inclusive of applicable superannuation) were:

Board Fees		Audit Committee Fees		Remuneration & Nomination Committee Fees	
Chairman <sup>1</sup>	Member	Chairman	Member	Chairman	Member
\$180,000	\$91,000	\$10,000	\$5,000	\$10,000	\$5,000

1. The Board fee received by the Chairman of the Board fee is inclusive of all Committee fees.



## Remuneration report (continued)

### 3. Executive KMP Remuneration Framework

In FY16, Executive KMP remuneration comprised:

- total fixed remuneration (TFR);
- short term incentive (STI); and
- long-term incentive (LTI).

The FY16 Total Maximum Remuneration (TMR) mix for the Executive KMP is set out in the table below:

Executive KMP	Position	TFR	Variable Performance Based Remuneration	
			STI	LTI
Bryce Mitchelson	Managing Director	50%	25%	25%
Gareth Winter	Chief Financial Officer	60%	20%	20%
Robert de Vos	Head of Property	55%	25%	20%

#### 3.1 Total Fixed Remuneration

TFR consists of base salary, employer superannuation contribution, salary sacrifice benefits and other non-monetary benefits. TFR is set based on the role responsibilities, experience and qualifications of the individual, and with reference to market data of comparable organisations. TFR will generally be reviewed on an annual basis.

#### 3.2 Short Term Incentive Plan (STI)

The short term incentive is a performance based component of remuneration and is designed to reward annual performance and focus Executive KMP on meeting business plan objectives. Executive KMP participation in the STI is at the discretion of the Board.

The STI opportunity for each Executive KMP is based on the STI proportion of their TMR mix. The actual award is based on the achievement of the specific Key Performance Indicators (KPIs) for each Executive KMP.

STI objectives for each Executive KMP take into account their respective role and the objectives of the organisation to which they are expected to contribute. The link between the organisations objectives and the Executive KMP's incentive plans is designed to align Executive KMP to Arena REIT's objectives and includes, where relevant, stretch targets.

FY16 performance was measured across two categories of KPIs:

- Financial – target Distributions per Security and Distributable Income per Security;
- Non-financial – linked to non-financial metrics specific to each role eg. strategy development and execution, business performance, risk management, people, stakeholder management and relationships and specific personal objectives.

STI's are paid in cash following the end of the relevant financial year following Board approval. Taking into consideration circumstances over the course of the financial year, the Board has discretion to reduce, cancel or increase STI payments.

#### 3.3 Long Term Incentive Plan (LTI)

The LTI Plan is an equity based incentive scheme designed to align the interests of key management personnel and investors over the long term and retain high performing individuals. Executive KMP participation in the LTI is at the discretion of the Board.

The LTI opportunity for each Executive KMP is based on the LTI proportion of their TMR mix. The actual benefit delivered to the Executive KMP will depend on the quantum of rights granted, the extent to which the performance hurdles are achieved and security price performance. The LTI will be satisfied through the issue of one fully paid ordinary stapled security for each Right that vests.

## Directors' Report

### Remuneration report (continued)

#### 3.3.1 LTI - Performance Rights

Arena REIT's ongoing LTI Plan is in the form of Performance Rights. The vesting of each grant of Performance Rights is subject to the achievement of threshold and stretch performance hurdles measured over a 3 year period. The number of Performance Rights granted is based on the value of the LTI award opportunity divided by an independent valuation of the fair value of a Performance Right as at the grant date. The fair value and the face value of each grant of Performance Rights on the relevant grant date is set out in Section 5 of this report.

Under the LTI Plan grants for FY16 there are two independent hurdles to the vesting of Performance Rights, each with a 50% weighting:

##### *Hurdle 1: Relative total shareholder return (TSR)*

Relative TSR performance is determined based on Arena REIT's total ASX return (assuming reinvestment of distributions) ranked against the members of the comparator group over the performance period.

The comparator group in respect of the FY16 Performance Rights grant are the members of the S&P/ASX 300 A-REIT Index.

The Relative TSR vesting schedule is as follows:

Arena REITs TSR ranking	Proportion of TSR Hurdle Performance Rights that vest
Below 50 <sup>th</sup> percentile	0%
50 <sup>th</sup> to 75 <sup>th</sup> percentile	50% at the threshold plus progressive pro-rata vesting between 50% and 100% (ie on a straight-line basis)
At or above the 75 <sup>th</sup> percentile	100%

Relative TSR was selected as a performance condition because:

- It aligns Executive KMP rewards with Arena REIT securityholder returns;
- The effects of market cycles are reduced as it measures Arena REIT's performance relative to its peers, which are presently considered to be the A-REIT members of the S&P/ASX 300 Index.

##### *Hurdle 2: Distributable Income per Security (DIS)*

The DIS hurdle is based on a target range to be assessed in the final year of a three year performance period. DIS is determined in accordance with Arena REIT's Distribution Policy.

The DIS vesting schedule is as follows:

Arena REITs DIS (in year 3 of the performance period)	Proportion of DIS Hurdle Performance Rights that vest
Below the Target Range	0%
In the Target Range	50% plus progressive pro-rata vesting between 50% and 100% (ie on a straight-line basis)
Above the Target Range	100%

DIS was selected as a performance condition (for STI and LTI) because:

- It aligns Executive KMP rewards with Arena REIT securityholder returns;
- DIS is a key performance indicator referenced by the Board in preparing the annual budget and business plan and in measuring Arena REIT's underlying performance.

The Board retains discretion to adjust the conditions and/or the performance outcome used for assessing whether the performance related conditions have been satisfied to ensure that executive KMP are neither advantaged nor disadvantaged by matters that affect the conditions, for example the timing of a material equity raising or excluding the effects of one-off/non recurrent items.

## Remuneration report (continued)

### 3.3.2 LTI - Recognition Rights

Executive KMP received a once-off grant of Recognition Rights in FY15 to recognise their commitment to the Arena REIT internalisation and reward ongoing effort to deliver Arena REIT's business performance.

Recognition Rights are subject to an employment retention period ending on 30 June 2017. The Board considered the Recognition Rights to be an important incentive for Executive KMP to remain with the business during Arena REIT's transition to an internalised management structure.

### 3.3.3 Other LTI Plan Terms

Other key terms of the LTI Plan are:

- Participants do not receive distributions or dividends on unvested LTI awards during the performance period;
- No payment for Performance Rights or Recognition Rights is required;
- No payment is required on the issue of stapled securities in respect of a vested Performance Right or Recognition Right;
- In the event of termination of employment, the following treatment applies to unvested awards:
  - Dismissal for cause or resignation: unvested awards will lapse unless the Board determines otherwise;
  - In all other circumstances: unvested awards will remain on-foot subject to the original performance conditions and vesting period. The Board will have discretion to pro-rate awards which remain on foot (eg to reflect the portion of the performance/vesting period that has elapsed). The Board may lapse an award in full and also allow accelerated vesting (pro-rated for time and performance) in special circumstances subject to termination benefit rules);
- In the event of an actual or proposed change of control event that the Board in its discretion determines should be treated as a change of control, a pro-rata number of unvested grants vest at the time of the relevant event, based on the performance period elapsed and the extent to which performance hurdles have been achieved at the time (unless the Board determines another treatment in its discretion);
- The LTI Plan restricts Executive KMP from entering into transactions (through the use of derivatives or otherwise) that would have the effect of limiting the economic risk from participating in the LTI Plan.

## 4. Performance and Variable Remuneration Outcomes

Arena REIT's remuneration policy assesses variable remuneration outcomes in the context of performance and change in securityholder wealth. The Remuneration and Nomination Committee is responsible for assessing performance against KPIs and determining the STI to be paid and the extent to which the LTI vests. To assist in this process the Committee receives detailed financial reports, data capable of independent confirmation and individual performance assessments.

## Directors' Report

### Remuneration report (continued)

#### 4.1 Performance Indicators

The table below summarises information on Arena REIT's key financial and performance metrics over the five year period to 30 June 2016.

Metric	FY16	FY15	FY14	FY13	FY12
Net Profit (Statutory) (\$million)	72.6	61.0	44.6	17.2	15.7
Distributable Income (\$million)	25.6	22.1	18.5	11.2	8.5
Distributable Income per Security (cents)	11.11	10.20	8.85	8.20	6.40
Distributions per Security (cents)	10.90	10.00	8.75	8.00	6.50
Net Asset Value per Security (\$)	1.54	1.33	1.13	1.02	1.00
ASX Security Price (\$)	1.99	1.54	1.20	1.02	n/a <sup>1</sup>
Gearing (%)	26.8	29.1	33.3	10.4	41.7
Annual Total Shareholder Return (TSR) (%)	37.6	36.3	26.7	n/a <sup>1</sup>	n/a <sup>1</sup>
Annual TSR of ASX-300 A-REIT Index (%)	24.6	20.2	11.1	n/a <sup>1</sup>	n/a <sup>1</sup>

1. Arena REIT listed on ASX in June 2013. Prior data is not available or relates to a period when the fund was unlisted.

#### 4.2 FY16 STI Performance Measures

A key measure of Arena REIT's performance and contributor to STI performance assessment is the annual underlying profit and distribution.

STI Financial Objective	Result
<b>Underlying Profit Performance:</b>	
• Deliver a minimum FY16 Distribution of 10.7cents per security (7% growth on FY15)	• Actual FY16 Distribution of 10.9 cents per security (9% growth on FY15)
• Deliver FY16 distributable income above 10.9 cents per security (7% growth on FY15)	• Actual FY16 distributable income of 11.11 cents per security (9% growth on FY15)

#### STI Non-Financial Objectives

The Committee set each Executive KMP relevant objectives and KPIs in relation to strategy development and execution, progression of developments, business performance, risk management, people, stakeholder management, funding and liquidity. The achievement of KPIs was assessed by the Committee in the determination of each Executive KMP's STI award.

#### 4.3 FY16 STI Awards

As a result of the performance assessment, the Board awarded STI's in respect of FY16 as set out below.

Executive KMP	STI Award (\$)	Award as a % of STI Opportunity <sup>1</sup>
Bryce Mitchelson	208,250	85%
Gareth Winter	107,667	95%
Robert de Vos	122,715	90%

1. Any STI opportunity not awarded is forfeited.

## Remuneration report (continued)

### 4.4 LTI Performance Measures

No assessment of Performance Rights vesting conditions was required in FY16. No Performance Rights or Recognition Rights were eligible for exercise during FY16.

LTI Year	Measurement Period	LTI Performance Measure	Performance Hurdle	Result	Vesting Outcome
FY15	12 December 2014 to 30 June 2017	Relative TSR	Ranking greater than 50 <sup>th</sup> percentile of the members of the S&P ASX 300 A-REIT Accumulation Index		N/A
	FY17	Distributable Income per Security	Target range of 11.0 cents to 12.0 cents		
FY16	FY16 – FY18	Relative TSR	Ranking greater than 50 <sup>th</sup> percentile of the members of the S&P ASX 300 A-REIT Accumulation Index		N/A
	FY18	Distributable Income per Security	Target range of 11.5 cents to 12.5 cents		

### 4.5 LTI Grants

LTI Grants to Executive KMP during FY16 are set out in the table below.

Executive KMP	Maximum LTI Award as % of TFR	Type	Grant Date	Vesting Date	Rights Granted	Fair value per Right <sup>2</sup>
Bryce Mitchelson <sup>1</sup>	50%	Performance Rights	1 July 2015	30 June 2018	247,475	\$0.99
Gareth Winter <sup>1</sup>	33%	Performance Rights	1 July 2015	30 June 2018	114,478	\$0.99
Robert de Vos	36%	Performance Rights	1 July 2015	30 June 2018	110,192	\$0.99

1. Grants were subject to securityholder approval received at the AGM held on 19 November 2015.

2. Fair Value per Right was determined by an independent valuation. Refer to Note 20 of the financial report for further information on the valuation inputs.

## Directors' Report

### Remuneration report (continued)

#### 4.6 Remuneration Summary (Statutory)

The table below shows details of the remuneration in respect of the KMP measured in accordance with the requirements of accounting standards.

\$		Short Term Benefits			Equity Based Payments		Long Term	Post Employment	Total	
		Salary & Fees	STI	Non-Monetary Benefits	Performance Rights <sup>2</sup>	Recognition Rights <sup>2</sup>	Long Service Leave <sup>3</sup>	Super-annuation		
<b>Non-Executive Director</b>										
	David Ross	FY16	148,521	–	–	–	–	31,479	<b>180,000</b>	
		FY15 <sup>1</sup>	82,104	–	–	–	–	14,804	<b>96,908</b>	
	Simon Parsons	FY16	92,237	–	–	–	–	8,763	<b>101,000</b>	
		FY15 <sup>1</sup>	49,308	–	–	–	–	4,684	<b>53,992</b>	
	Dennis Wildenburg	FY16	88,901	–	–	–	–	17,099	<b>106,000</b>	
		FY15 <sup>1</sup>	44,832	–	–	–	–	11,928	<b>56,760</b>	
<b>Executive KMP</b>										
	Bryce Mitchelson	FY16	470,692	208,250	10,361	137,776	37,307	9,351	19,308	<b>893,045</b>
		FY15 <sup>1</sup>	252,635	111,791	6,468	30,732	20,488	5,590	9,392	<b>437,096</b>
	Gareth Winter	FY16	320,692	107,667	9,201	63,765	17,279	3,282	19,308	<b>541,194</b>
		FY15 <sup>1</sup>	173,334	60,914	5,786	14,234	9,489	2,522	8,728	<b>275,007</b>
	Robert de Vos	FY16	280,692	122,715	9,201	59,992	15,708	1,680	19,308	<b>509,296</b>
		FY15 <sup>1</sup>	141,881	69,220	5,786	12,490	8,627	2,037	10,227	<b>250,718</b>

1. Remuneration disclosed for FY15 is for the period from 12 December 2014 (being the date the KMP commenced employment with Arena REIT) to 30 June 2015.
2. Represents change in accounting accrual. Entitlement subject to vesting conditions.
3. Represents change in accounting accrual. Entitlement subject to legislated minimum period of employment.

#### 4.7 Executive KMP Remuneration Mix

The following table summarises the relative proportions of total remuneration based on the FY16 Remuneration Summary.

Executive KMP	TFR	STI	LTI
Bryce Mitchelson	56%	23%	21%
Gareth Winter	64%	20%	16%
Robert de Vos	61%	24%	15%

Variation between TMR and actual total remuneration mix occurs as a result of non-vesting of opportunities and timing differences between the granting of an LTI and the accounting recognition of the LTI expense which is generally amortised over the relevant vesting period.

## Remuneration report (continued)

### 5. Interests in Securities

Interests in Arena REIT securities held by Directors and Executive KMP is set out below.

#### Ordinary Securities

Ordinary Securities	Balance 30 June 2015	Acquired	Disposed	Received as Remuneration	Balance 30 June 2016
<b>Independent Directors</b>					
David Ross	200,000	–	–	–	200,000
Simon Parsons	200,000	–	–	–	200,000
Dennis Wildenburg	150,000	–	–	–	150,000
<b>Executive KMP</b>					
Bryce Mitchelson	753,907	–	–	–	753,907
Gareth Winter	75,000	–	–	–	75,000
Robert de Vos	26,235	1,706	–	–	27,941

#### Performance Rights and Recognition Rights

Executive KMP	Grant Year	Opening Balance	Rights Granted	Rights Vested	Rights Lapsed	Closing Balance	Fair Value at Grant Date <sup>1</sup>	Face Value at Grant Date <sup>2</sup>
<b>Bryce Mitchelson</b>								
Performance Rights	FY16	–	247,475	–	–	247,475	\$245,000	\$388,536
Performance Rights	FY15	151,596	–	–	–	151,596	\$142,500	\$224,362
Recognition Rights	FY15	77,869	–	–	–	77,869	\$95,000	\$115,246
<b>Gareth Winter</b>								
Performance Rights	FY16	–	114,478	–	–	114,478	\$113,333	\$179,730
Performance Rights	FY15	70,213	–	–	–	70,213	\$66,000	\$108,128
Recognition Rights	FY15	36,066	–	–	–	36,066	\$44,000	\$55,542
<b>Robert de Vos</b>								
Performance Rights	FY16	–	110,192	–	–	110,192	\$109,090	\$173,001
Performance Rights	FY15	63,830	–	–	–	63,830	\$60,000	\$98,298
Recognition Rights	FY15	32,787	–	–	–	32,787	\$40,000	\$50,492

1. Fair value determined by independent valuation.

2. Number of Rights granted multiplied by the security price on the relevant grant date. If Rights vest (subject to performance and vesting conditions), the actual security price on the date of issue of securities may be higher or lower than at the relevant grant date. The value of the unvested Rights may be nil if the relevant vesting conditions are not met and the Rights lapse or are forfeited.

## Directors' Report

### Remuneration report (continued)

#### 6. Service Agreements

Executive KMP Service Agreements detail the individual terms and conditions applying to the employment of the Executive KMP. Key employment terms in addition to the remuneration arrangements set out in this report are set out below:

	Managing Director	Other Executive KMP
<b>Contract Term</b>	Ongoing	Ongoing
<b>Termination by the Executive KMP</b>	Nine months' notice. Unvested STI or LTI entitlements lapse unless the Board determines otherwise.	Six months' notice. Unvested STI or LTI entitlements lapse unless the Board determines otherwise.
<b>Termination by Arena REIT without cause or mutually agreed resignation</b>	Nine months' notice or equivalent payment in lieu of notice based on TFR. Any unvested STI and LTI awards will be governed by the applicable STI or LTI plan rules summarised above.	Six months' notice or equivalent payment in lieu of notice based on TFR. Any unvested STI and LTI awards will be governed by the applicable STI or LTI plan rules summarised above.
<b>Termination by Arena REIT for serious misconduct</b>	No notice period or termination payment unless the board determines otherwise.	No notice period or termination payment unless the Board determines otherwise.
<b>Post-employment restraints</b>	Restrained from soliciting suppliers, customers and staff for a maximum of nine months post-employment.	Restrained from soliciting suppliers, customers and staff for a maximum of six months post-employment.

#### Indemnification and insurance of officers and auditors

During the year, the Group has paid insurance premiums to insure each of the directors, and officers of the Group against liabilities for costs and expenses incurred by them in defending any legal proceedings arising out of their conduct while acting in the capacity of the Group other than conduct involving a wilful breach of duty in relation to the Group.

The contract of insurance prohibits disclosure of the nature of the liability covered and the amount of the premium.

The Group has not, during or since the end of the financial year indemnified or agreed to indemnify an auditor of the Group or of any related body corporate against a liability incurred in their capacity as an auditor.

#### Non-audit services

Details of the non-audit services provided to the Group by the Independent Auditor during the year ended 30 June 2016 are disclosed in note 5 of the financial statements.

#### Fees paid to and interests held in the Group by the Responsible Entity or its associates

Fees paid to the Responsible Entity and its associates out of Group property during the year are disclosed in note 18 to the financial statements.

#### Interests in the Group

The movement in securities on issue in the Group during the year is disclosed in note 14 to the financial statements.



## Corporate governance statement

The board of directors for Arena REIT Limited and Arena REIT Management Limited work together and take a coordinated approach to the corporate governance of the Group.

Each Board has a Board Charter which details the composition, responsibilities, and protocols of the Board. In addition, the Boards have a Code of Conduct which sets out the standard of business practices required of the Group's directors and staff.

Arena conducts its business in accordance with these policies and code, as well as other key policies which are published on its website. These include:

- Arena REIT Continuous Disclosure Policy;
- Arena REIT Diversity Policy;
- Arena REIT Privacy Policy;
- Arena REIT Communications Policy;
- Arena REIT Summary of Risk Management Framework;
- Arena REIT Securities Trading Policy.

In compliance with ASX Listing Rule 4.10.3, Arena has also published a statement disclosing the extent to which the Group has followed the recommendations for good corporate governance set by the ASX Corporate Governance Council (3rd Edition) during the reporting period on its website, [www.arena.com.au/about/governance](http://www.arena.com.au/about/governance).

## Environmental regulation

The operations of the Group are not subject to any particular or significant environmental regulations under a Commonwealth, State or Territory law.

## Rounding of amounts to the nearest thousand dollars

The Group is an entity of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191, relating to the 'rounding off' of amounts in the Directors' report. Amounts in the Directors' report have been rounded to the nearest thousand dollars in accordance with that Instrument, unless otherwise indicated.

## Auditor's independence declaration

The Auditor's independence declaration as required under section 307C of the Corporations Act 2001 is set out on page 34.

This report is made in accordance with a resolution of directors.



David Ross, **Chairman**

Melbourne, 25 August 2016

# Auditor's independence declaration



## Auditor's Independence Declaration

As lead auditor for the audit of Arena REIT for the year ended 30 June 2016, I declare that to the best of my knowledge and belief, there have been:

1. no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and
2. no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Arena REIT which comprises the stapled entities Arena REIT No. 1, Arena REIT No. 2 and Arena REIT Limited and the entities they controlled during the period.

A handwritten signature in black ink, appearing to read 'Elizabeth O'Brien', is written above the printed name.

Elizabeth O'Brien  
Partner  
PricewaterhouseCoopers

Melbourne  
25 August 2016

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Liability limited by a scheme approved under Professional Standards Legislation.

# Consolidated statement of comprehensive income

	Notes	Consolidated	
		30 June 2016 \$'000	30 June 2015 \$'000
<b>Income</b>			
Property rental	9(c)	32,989	31,219
Management fee income		429	488
Interest		167	112
Revaluation of investment properties	9	51,062	39,828
Profit/(loss) on sale of direct properties		(121)	2,232
<b>Total income</b>		<b>84,526</b>	<b>73,879</b>
<b>Expenses</b>			
Direct property expenses	9(c)	(1,003)	(1,306)
Former Responsible Entity's management fee	18	–	(1,353)
Employee benefits expense		(2,526)	(1,214)
Administration and other expenses		(1,128)	(2,211)
Net loss on fair value of derivative financial instruments		(2,915)	(1,781)
Finance costs	3	(4,333)	(5,048)
<b>Total expenses</b>		<b>(11,905)</b>	<b>(12,913)</b>
<b>Net profit for the year</b>		<b>72,621</b>	<b>60,966</b>
Other comprehensive income		–	–
<b>Total comprehensive income for the year</b>		<b>72,621</b>	<b>60,966</b>
<b>Total comprehensive income for the year is attributable to Arena REIT stapled group investors, comprising:</b>			
Unitholders of Arena REIT No. 1		59,155	55,354
Unitholders of Arena REIT No. 2 (non-controlling interest)		14,175	5,626
Unitholders of Arena REIT Limited (non-controlling interest)		(709)	(14)
		<b>72,621</b>	<b>60,966</b>
<b>Earnings per security:</b>		<b>Cents</b>	<b>Cents</b>
Basic earnings per security in Arena REIT No. 1	6	25.70	25.55
Diluted earnings per security in Arena REIT No. 1	6	25.70	25.55
Basic earnings per security in Arena REIT Group	6	31.55	28.14
Diluted earnings per security in Arena REIT Group	6	31.55	28.14

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes.

# Consolidated balance sheet

	Notes	Consolidated	
		30 June 2016 \$'000	30 June 2015 \$'000
<b>Current assets</b>			
Cash and cash equivalents	7	9,446	10,888
Trade and other receivables	8	969	7,163
<b>Total current assets</b>		<b>10,415</b>	<b>18,051</b>
<b>Non-current assets</b>			
Receivables	8	1,062	1,189
Property, plant and equipment		219	121
Investment properties	9	491,439	420,532
Intangible assets	10	10,816	10,730
<b>Total non-current assets</b>		<b>503,536</b>	<b>432,572</b>
<b>Total assets</b>		<b>513,951</b>	<b>450,623</b>
<b>Current liabilities</b>			
Trade and other payables	11	15,124	15,297
Provisions		250	212
<b>Total current liabilities</b>		<b>15,374</b>	<b>15,509</b>
<b>Non-current liabilities</b>			
Derivative financial instruments	13	3,030	398
Provisions		467	451
Interest bearing liabilities	12	137,587	130,774
<b>Total non-current liabilities</b>		<b>141,084</b>	<b>131,623</b>
<b>Total liabilities</b>		<b>156,458</b>	<b>147,132</b>
<b>Net assets</b>		<b>357,493</b>	<b>303,491</b>
<b>Equity</b>			
Contributed equity - ARF1	14	197,224	191,845
Accumulated profit	15	99,187	61,900
Non-controlling interests - ARF2 and ARL		61,082	49,746
<b>Total equity</b>		<b>357,493</b>	<b>303,491</b>

The above consolidated balance sheet should be read in conjunction with the accompanying notes.

## Consolidated statement of changes in equity

	Consolidated			
	Contributed equity	Accumulated profit	Non-controlling interests - ARL & ARF2	Total equity
	\$'000	\$'000	\$'000	\$'000
<b>Balance at 1 July 2014</b>	183,221	25,991	28,990	238,202
Profit for the period	–	55,354	5,613	60,967
<b>Total comprehensive income for the year</b>	<b>–</b>	<b>55,354</b>	<b>5,613</b>	<b>60,967</b>
<b>Transactions with owners in their capacity as owners:</b>				
Arising on stapling	(13,000)	–	13,000	–
Contributions of equity, net of transaction costs	19,980	–	4,361	24,341
Securities issued under DRP	1,644	–	216	1,860
Employee - LTI Performance Plan	–	–	112	112
Distributions to securityholders	–	(19,445)	(2,546)	(21,991)
<b>Balance at 30 June 2015</b>	<b>191,845</b>	<b>61,900</b>	<b>49,746</b>	<b>303,491</b>
<b>Balance at 1 July 2015</b>	191,845	61,900	49,746	303,491
Profit for the period	–	59,155	13,466	72,621
<b>Total comprehensive income for the year</b>	<b>–</b>	<b>59,155</b>	<b>13,466</b>	<b>72,621</b>
<b>Transactions with owners in their capacity as owners:</b>				
Securities issued under DRP	5,379	–	788	6,167
Employee - LTI Performance Plan	–	–	350	350
Distributions to securityholders	–	(21,868)	(3,268)	(25,136)
<b>Balance at 30 June 2016</b>	<b>197,224</b>	<b>99,187</b>	<b>61,082</b>	<b>357,493</b>

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

# Consolidated statement of cash flows

	Consolidated		
	Notes	30 June 2016 \$'000	30 June 2015 \$'000
<b>Cash flows from operating activities</b>			
Property rental receipts		33,460	31,761
Property management receipts		477	432
Payments to suppliers		(3,898)	(4,464)
Finance costs paid		(4,018)	(4,911)
Interest received		165	112
<b>Net cash inflow from operating activities</b>	23	<b>26,186</b>	22,930
<b>Cash flows from investing activities</b>			
Cash arising on stapling		–	1,510
Acquisition of subsidiaries		(995)	(4,862)
Net proceeds from sale of investment properties		7,139	14,938
Payments for investment properties and capital expenditure		(21,579)	(28,973)
Other stapling cash flows		–	(1,027)
<b>Net cash (outflow) from investing activities</b>		<b>(15,435)</b>	(18,414)
<b>Cash flows from financing activities</b>			
Proceeds from equity placement		–	25,000
Payment of transaction costs from issue of securities		(28)	(658)
Distributions paid to securityholders		(18,325)	(19,227)
Loan establishment costs paid		(491)	(112)
Capital receipts from lenders		10,500	41,000
Capital payments to lenders		(3,849)	(43,578)
<b>Net cash (outflow)/inflow from financing activities</b>		<b>(12,193)</b>	2,425
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(1,442)</b>	6,941
Cash and cash equivalents at the beginning of the financial period		10,888	3,947
<b>Cash and cash equivalents at the end of the financial period</b>	7	<b>9,446</b>	10,888

The above consolidated statement of cash flows should be read in conjunction with the accompanying notes.

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# Notes to the consolidated financial statements

## 1. General information

These financial statements cover Arena REIT (the 'Group') comprising Arena REIT No. 1, Arena REIT No. 2, Arena REIT Limited, and their controlled entities. Arena REIT is listed on ASX and registered and domiciled in Australia.

The Arena REIT Stapled Group (the 'Group') now comprises Arena REIT No. 1 ('ARF1'), Arena REIT No. 2 ('ARF2') and Arena REIT Limited ('ARL'), following the stapling of ARL (the 'Aggregation'). The Responsible Entity of ARF1 and ARF2 is Arena REIT Management Limited (the 'Responsible Entity'). The stapling occurred in conjunction with the internalisation of corporate governance and management rights of the Group approved by securityholders in December 2014.

The financial statements were authorised for issue by the directors on 25 August 2016. The directors have the power to amend and reissue the financial statements.

## 2. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

### (a) Basis of preparation

These general purpose financial statements have been prepared in accordance with Australian Accounting Standards and interpretations issued by the Australian Accounting Standards Board and the *Corporations Act 2001*. Arena REIT is a for-profit unit trust for the purpose of preparing the financial statements.

The financial report has been prepared on an accruals and historical cost basis except for investment properties, financial assets at fair value through profit or loss, derivative financial instruments which are measured at fair value, and assets held for sale which are recognised at fair value less costs to sell. Cost is based on the fair value of consideration given in exchange for assets. Comparative information is reclassified where appropriate to enhance comparability.

### Compliance with International Financial Reporting Standards

The financial statements of the Group also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board.

### Going Concern

As at 30 June 2016, the Group had a net working capital deficiency of \$4.96 million. This deficiency is due to working capital management within the Arena stapled group, and the difference in the timing of drawdowns from the Group's debt facility and the timing of capital expenditure on developments and asset acquisitions. The Group has \$37 million of unused debt facility which can be drawn to fund cashflow requirements.

After taking into account all available information, the directors of the Group have concluded that there are reasonable grounds to believe:

- The Group will be able to pay its debts as and when they fall due; and
- The basis of preparation of the financial report on a going concern basis is appropriate.

### (i) New and amended standards adopted by the Group

There were no new accounting standards adopted during the year which had a significant impact on the reported performance of the Group or required disclosures within the financial statements.

### (b) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Chief Operating Decision Maker.

The Board as the Chief Operating Decision Maker is responsible for making strategic decisions about the Group, assessing the financial performance and financial position of the Group, determining the allocation of resources, and risk management.



## 2. Summary of significant accounting policies (continued)

### (c) Principles of consolidation

#### (i) Stapled entities

The units of ARF1, ARF2 and the shares of ARL are combined and issued as stapled securities in the Arena REIT Stapled Group. The units of ARF1, ARF2 and shares of ARL cannot be traded separately and can only be traded as a stapled security. This financial report consists of the consolidated financial statements of the Arena REIT Stapled Group, which comprises ARF1, ARF2, and ARL and its controlled entities.

AASB 3 Business Combinations requires one of the stapled entities in a stapling structure to be identified as the parent entity for the purpose of preparing consolidated financial reports. In accordance with this requirement, ARF1 has been identified as the parent entity in relation to the stapling with ARF2 and ARL.

The consolidated financial statements of the Arena REIT Stapled Group incorporate the assets and liabilities of the entities controlled by ARF1 at 30 June 2016, including those deemed to be controlled by ARF1 by identifying it as the parent of the Arena REIT Stapled Group, and the results of those controlled entities for the year then ended. The effects of all transactions between entities in the consolidated entity are eliminated in full.

Non-controlling interests in the results and equity are shown separately in the Statement of Comprehensive Income and Statement of Financial Position respectively. Non-controlling interests are those interests in ARF2 and ARL which are not held directly or indirectly by ARF1.

Securityholders approved the stapling effective from 12 December 2014 and this is the date the consolidation has occurred for financial reporting purposes.

#### (ii) Subsidiaries

Subsidiaries are all entities (including structured entities) over which the group has control. The group controls an entity when the group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power to direct the activities of the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the group. They are deconsolidated from the date that control ceases.

The acquisition method of accounting is used to account for business combinations by the group (refer to note 2(f)).

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the transferred asset. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the group.

Non-controlling interests in the results and equity of subsidiaries are shown separately in the consolidated statement of comprehensive income, statement of changes in equity and balance sheet respectively.

#### (iii) Changes in ownership interests

When the Group ceases to have control, joint control or significant influence, any retained interest in the entity is remeasured to its fair value with the change in carrying amount recognised in profit or loss. The fair value becomes the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to profit or loss.

If the ownership interest in a joint venture or an associate is reduced but joint control or significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income are reclassified to profit or loss where appropriate.

### (d) Presentation of members interests in ARF2 and ARL

As ARF1 has been assessed as the parent entity of the Group, the securityholders interests in ARF2 and ARL are included in equity as "non-controlling interests" relating to the stapled entity. Securityholders interests in ARF2 and ARL are not presented as attributable to owners of the parent reflecting the fact that they are not owned by ARF1, but by the securityholders of the stapled group.

## Notes to the consolidated financial statements

### 2. Summary of significant accounting policies (continued)

#### (e) Parent entity financial information

Parent entity information has been prepared on the same basis as the rest of the financial report.

#### (f) Business combinations

The acquisition method of accounting is used to account for all business combinations, regardless of whether equity instruments or other assets are acquired. The consideration transferred for the acquisition of a subsidiary comprises the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred also includes the fair value of any asset or liability resulting from a contingent consideration arrangement and the fair value of any pre-existing equity interest in the subsidiary.

Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are, with limited exceptions, measured initially at their fair values at the acquisition-date. On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net identifiable assets.

The excess of the consideration transferred and the amount of any non-controlling interest in the acquiree over the fair value of the net identifiable assets acquired is recorded as goodwill. If those amounts are less than the fair value of the net identifiable assets of the subsidiary acquired and the measurement of all amounts has been reviewed, the difference is recognised directly in profit or loss as a bargain purchase.

Where settlement of any part of cash consideration is deferred, the amounts payable in the future are discounted to their present value as at the date of exchange. The discount rate used is the entity's incremental borrowing rate, being the rate at which a similar borrowing could be obtained from an independent financier under comparable terms and conditions.

Contingent consideration is classified either as equity or a financial liability. Amounts classified as a financial liability are subsequently remeasured to fair value with changes in fair value recognised in profit or loss.

#### (g) Revenue

Rental income from operating leases is recognised as income on a straight-line basis over the lease term. Where a lease has fixed annual increases, the total rent receivable over the operating lease is recognised as revenue on a straight-line basis over the lease term. This results in more income being recognised early in the lease term and less late in the lease term compared to the lease conditions. The difference between the lease income recognised and the actual lease payments received is shown within the fair value of the investment property on the consolidated balance sheet.

When the Group provides lease incentives to tenants, the cost of the incentives are recognised over the lease term, on a straight-line basis, as a reduction in rental income.

Contingent rents based on the future amount of a factor that changes other than with the passage of time, are only recognised when contractually due.

Interest income is recognised in the consolidated statement of comprehensive income using the effective interest rate method.

Distribution income is recognised when the right to receive a distribution has been established.

Management service fees earned from managed investment schemes or trusts are calculated based on the agreed percentage of funds under management and agreed percentages of schemes or trust acquisitions and disposals. Management fees are recognised on an accrual basis.

Performance fees earned from managed funds are recorded when the Group has a legal or constructive right as a result of past events, and it is probable that an inflow of resources will occur and the amount can be reliably estimated.

## 2. Summary of significant accounting policies (continued)

### (g) Revenue (continued)

Deferred management fees and performance fees are measured at the present value of the Responsible Entity's best estimate of the amount receivable at the end of the reporting period. The discount rate used to determine the present value reflects current market assessments of the time value of money and the risks specific to the asset.

Other income is recognised when the right to receive the revenue has been established.

All income is stated net of goods and services tax (GST).

### (h) Expenses

All expenses are recognised in profit or loss on an accruals basis.

### (i) Employee benefits

#### (i) Short-term obligations

Liabilities for wages and salaries, including non-monetary benefits that are expected to be settled wholly within 12 months after the end of the period in which the employees render the related service are recognised in respect of employees' services up to the end of the reporting period and are measured at the amounts expected to be paid when the liabilities are settled. The liabilities are presented as current employee benefit obligations in the balance sheet.

#### (ii) Other long-term employee benefit obligations

The liabilities for long service leave and annual leave that are not expected to be settled wholly within 12 months after the end of the period in which the employees render the related service. They are therefore measured as the present value of expected future payments to be made in respect of services provided by employees up to the end of the reporting period. Consideration is given to expected future wage and salary levels, experience of employee departures and periods of service.

The obligations are presented as current liabilities in the balance sheet if the entity does not have an unconditional right to defer settlement for at least twelve months after the reporting period, regardless of when the actual settlement is expected to occur.

#### (iii) Security-based payments

For information relating to the Group's Long Term Incentive Plan, refer to note 20.

Employees may receive remuneration in the form of security-based incentives, whereby employees render services as consideration for equity-based incentives (equity-settled transactions). The Group did not have any cash-settled security-based incentives in the financial year.

The cost of equity-settled transactions is recognised, together with a corresponding increase in reserves in equity, over the period in which the performance and service conditions are fulfilled. The cumulative expense recognised for these transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and for awards subject to non-market vesting conditions, the Group's best estimate of the number of equity instruments that will ultimately vest in respect of the relevant rights. The income statement expense or credit for a period represents the movement in cumulative expense recognised as at the beginning and end of that period and is recognised in employee expenses.

If the terms of an equity-settled transaction are modified, the minimum expense recognised is the expense as if the terms had not been modified, if the original terms of the award are met. An additional expense is recognised for any modification that increases the total fair value of the transaction, or is otherwise beneficial to the employee as measured at the date of modification.

If an equity-settled award is cancelled, it is treated as if it vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. This includes any award where non-vesting conditions within the control of either the Group or the employee are not met. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award.

## Notes to the consolidated financial statements

### 2. Summary of significant accounting policies (continued)

#### (j) Income tax

##### (i) Trusts

Arena REIT No.1 and Arena REIT No.2 (the Trusts) are not subject to Australian income tax provided their taxable income is fully distributed to securityholders.

##### (ii) Companies

The income tax expense or revenue for the period is the tax payable on the current period's taxable income based on the applicable income tax rate for each jurisdiction adjusted by changes in deferred tax assets and liabilities attributable to temporary differences and to unused tax losses.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax liabilities are not recognised if they arise from the initial recognition of goodwill. Deferred income tax is also not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Current and deferred tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

##### (iii) Tax consolidation legislation

Arena REIT Limited and its wholly-owned Australian controlled entities have implemented the tax consolidation legislation. As a consequence, these entities are taxed as a single entity and the deferred tax assets and liabilities of these entities are set off in the consolidated financial statements.

The head entity, Arena REIT Limited, and the controlled entities in the tax consolidated group account for their own current and deferred tax amounts. These tax amounts are measured as if each entity in the tax consolidated group continues to be a standalone taxpayer in its own right.

In addition to its own current and deferred tax amounts, Arena REIT Limited also recognises the current tax liabilities (or assets) and the deferred tax assets arising from unused tax losses and unused tax credits assumed from controlled entities in the tax consolidated group.

All current tax balances are transferred from the controlled entities in the group to Arena REIT Limited. As there is no tax sharing agreement in place the current tax receivable or payable is transferred from each controlled entity to Arena REIT Limited as a contribution to (or distribution from) wholly owned entities.

#### (k) Distributions

The Group distributes income adjusted for amounts determined by the Group. Provision is made for any distribution amounts declared, being appropriately disclosed and no longer at the discretion of the entity, on or before the end of the reporting date but not distributed at the end of the reporting period. The distributions are recognised within the balance sheet and statement of changes in equity as a reduction in accumulated profit/(losses).

## 2. Summary of significant accounting policies (continued)

### (l) Earnings per security (EPS)

#### (i) Basic earnings per security

Basic earnings per security is calculated by dividing:

- the profit attributable to the securityholders, excluding any costs of servicing equity other than ordinary securities;
- by the weighted average number of ordinary securities outstanding during the financial year.

#### (ii) Diluted earnings per security

Diluted earnings per security adjust the figures used in the determination of basic earnings per security to take into account:

- the effect of interest and other financial costs associated with dilutive potential ordinary securities;
- the weighted average number of additional ordinary securities that would have been outstanding assuming the conversion of all dilutive potential ordinary securities.

### (m) Cash and cash equivalents

For the purpose of presentation in the consolidated statement of cash flows, cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short term, highly liquid investments with original maturities of three months or less from the date of acquisition that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

### (n) Receivables

Receivables may include amounts for dividends, interest and trust distributions. Dividends and trust distributions are accrued when the right to receive payment is established. Interest is accrued at the end of each reporting period from the time of last payment. Amounts are generally received within 30 days of being recorded as receivables.

Collectability of trade receivables is reviewed on an ongoing basis. Debts which are known to be uncollectible are written off by reducing the carrying amount directly. An allowance account (provision for impairment of trade receivables) is used when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 30 days overdue) are considered indicators that the trade receivable is impaired. The amount of the impairment allowance is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. Cash flows relating to short term receivables are not discounted if the effect of discounting is immaterial.

The amount of the impairment loss is recognised in the statement of comprehensive income within other expenses. When a trade receivable for which an impairment allowance had been recognised becomes uncollectible in a subsequent period, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against other expenses in the statement of comprehensive income.

### (o) Assets held for sale

Assets are classified as held-for-sale when a sale is considered highly probable and their carrying amount will be recovered principally through a sale transaction rather than through continued use. Assets classified as held-for-sale are presented separately from the other assets in the consolidated balance sheet.

Assets classified as held-for-sale are measured at the lower of their carrying amount and fair value less costs to sell. Changes to fair value are recorded in the consolidated statement of comprehensive income.

An impairment loss is recognised for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell. A gain is recognised for any subsequent increases in fair value less costs to sell of an asset (or disposal group), but not in excess of any cumulative impairment loss previously recognised. A gain or loss not previously recognised by the date of the sale of the asset (or disposal group) is recognised at the date of derecognition.

## Notes to the consolidated financial statements

### 2. Summary of significant accounting policies (continued)

#### (o) Assets held for sale (continued)

Assets (including those that are part of a disposal group) are not depreciated or amortised while they are classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal group classified as held for sale continue to be recognised.

#### (p) Property, plant and equipment

Property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost may also include transfers from equity of any gains or losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. The carrying amount of any component accounted for as a separate asset is derecognised when replaced. All other repairs and maintenance are charged to profit or loss during the reporting period in which they are incurred.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in profit or loss.

#### (q) Investment properties

Investment property is real estate investments held to earn long-term rental income and for capital appreciation. Investment properties are carried at fair value determined either by the Directors or independent valuers with changes in fair value recorded in the statement of comprehensive income.

Land and buildings (including integral plant and equipment) that comprise investment property are not depreciated. The carrying amount of investment properties may include the cost of acquisition, additions, refurbishments, redevelopments, improvements, lease incentives, assets relating to fixed increases in operating lease rental in future periods and borrowing costs incurred during the construction period of qualifying assets.

#### (i) Valuation basis

The basis of the valuation of investment properties is fair value, being the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The Directors may determine the requirement for a valuation at any time but has adopted a valuation program that provides for each property to be independently valued by suitably qualified valuers at least once every three years. Changes in market conditions may necessitate more frequent independent revaluations of properties.

Valuations are derived from a number of factors that may include a direct comparison between the subject property and a range of comparable sales evidence, the present value of net future cash flow projections based on reliable estimates of future cash flows, existing lease contracts, external evidence such as current market rents for similar properties, and using capitalisation rates and discount rates that reflect current market assessments of the uncertainty in the amount and timing of cash flows.

#### (r) Intangible assets - Goodwill

Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill is not amortised but it is tested for impairment annually, or more frequently if events or changes in circumstances indicate that it might be impaired, and is carried at cost less accumulated impairment losses. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose. The units or groups of units are identified at the lowest level at which goodwill is monitored for internal management purposes, being the operating segments.

## 2. Summary of significant accounting policies (continued)

### (s) Impairment of assets

Goodwill and intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment, or more frequently if events or changes in circumstances indicate that they might be impaired. Other assets are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at the end of each reporting period.

### (t) Financial instruments

#### (i) Classification

The Group's investments are classified as at fair value through profit or loss. They comprise:

- Financial instruments held for trading

Derivative financial instruments such as futures, forward contracts, options and interest rate swaps are included under this classification. The Group does not designate any derivatives as hedges in a hedging relationship.

- Financial instruments designated at fair value through profit or loss upon initial recognition

These include financial assets that are not held for trading purposes and which may be sold. These are investments in exchange traded debt and equity instruments, unlisted trusts and commercial paper.

Financial assets designated at fair value through profit or loss at inception are those that are managed and their performance evaluated on a fair value basis in accordance with the Group's documented investment strategy. The Group's policy is for the Responsible Entity to evaluate the information about these financial instruments on a fair value basis together with other related financial information.

#### (ii) Recognition/derecognition

Financial assets and financial liabilities are recognised on the date it becomes party to the contractual agreement (trade date) and recognises changes in fair value of the financial assets or financial liabilities from this date.

Investments are derecognised when the right to receive cash flows from the investments have expired or the Group has transferred substantially all risks and rewards of ownership.

#### (iii) Measurement

##### *Financial assets and liabilities held at fair value through profit or loss*

At initial recognition, financial assets are initially recognised at fair value. Transaction costs of financial assets carried at fair value through profit or loss are expensed in the profit or loss.

The fair value of financial assets and liabilities traded in active markets is subsequently based on their quoted market prices at the end of the reporting period without any deduction for estimated future selling costs. The quoted market price used for financial assets held by the consolidated entity and the Group is the current bid price and the quoted market price for financial liabilities is the current asking price.

The fair value of financial assets and liabilities that are not traded in an active market are determined using valuation techniques. Accordingly, there may be a difference between the fair value at initial recognition and amounts determined using a valuation technique. If such a difference exists, the Group recognises the difference in profit or loss to reflect a change in factors, including time, that market participants would consider in setting a price.

Further detail on how the fair values of financial instruments are determined is disclosed in note 21(d).

## Notes to the consolidated financial statements

### 2. Summary of significant accounting policies (continued)

#### (t) Financial instruments (continued)

##### (iii) Measurement (continued)

###### *Loans and receivables*

Loan assets are measured initially at fair value plus transaction costs and subsequently amortised using the effective interest rate method, less impairment losses if any. Such assets are reviewed at the end of each reporting period to determine whether there is objective evidence of impairment.

If evidence of impairment exists, an impairment loss is recognised in profit or loss as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the original effective interest rate.

If in a subsequent period the amount of an impairment loss recognised on a financial asset carried at amortised cost decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down is reversed through profit or loss.

##### (iv) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the consolidated balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

##### (u) Provisions

A provision is recognised when the Group has a legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are measured at the present value of the Group's best estimate of the expenditure required to settle the present obligation at the end of the reporting period. The discount rate used to determine the present value reflects current market assessments of the time value of money and the risks specific to the liability.

##### (v) Borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the consolidated statement of comprehensive income over the period of the borrowings using the effective interest method. Fees paid on the establishment of loan facilities are recognised as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. In this case, the fee is deferred until the drawdown occurs. To the extent there is no evidence that it is probable that some or all of the facility will be drawn down, the fee is capitalised as a prepayment for liquidity services and amortised over the period of the facility to which it relates.

Borrowings are removed from the consolidated balance sheet when the obligation specified in the contract is discharged, cancelled or expired. The difference between the carrying amount of the financial liability that has been extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, is recognised in profit or loss as finance costs.

Borrowings are classified as current liabilities unless the entity has an unconditional right to defer settlement of the liability for at least 12 months after the reporting period.

##### (w) Borrowing costs

Borrowing costs include interest and amortisation of costs incurred in connection with arrangement of borrowings. Borrowing costs are expensed as incurred unless they relate to qualifying assets. Qualifying assets are assets which take more than twelve months to get ready for their intended use or sale. Where funds are borrowed specifically for the acquisition, construction or production of a qualifying asset, the amount of borrowing costs capitalised are those incurred in relation to that borrowing. Where funds are borrowed generally, borrowing costs are capitalised using a weighted average capitalisation rate.



## 2. Summary of significant accounting policies (continued)

### (x) Goods and Services Tax (GST)

Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of the GST incurred is not recoverable from the relevant taxation authority. In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense.

Receivables and payables in the consolidated balance sheet are shown inclusive of GST.

The net amount of GST recoverable from, or payable to, the taxation authority is included with other receivables and payables in the consolidated balance sheet.

Cashflows are presented on a net basis. The GST components of cash flows arising from investing or financing activities which are recoverable from, or payable to the taxation authority, are presented as operating cash flows.

### (y) Use of estimates

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

#### (i) Financial instruments

For certain Group's financial instruments, quoted market prices are readily available. However, certain financial instruments, for example over-the-counter derivatives or unquoted securities, are fair valued using valuation techniques. Where valuation techniques (for example, pricing models) are used to determine fair values, they are validated and periodically reviewed by experienced personnel of the Responsible Entity, independent of the area that created them.

Models use observable data, to the extent practicable. However, areas such as credit risk (both own and counterparty), volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect the reported fair value of financial instruments. For more information on how fair value is calculated please refer to note 21.

For certain other financial instruments, the carrying amounts approximate fair value due to the short-term nature of these financial instruments.

#### (ii) Investment properties

The Group carries its investment properties at fair value with changes in the fair values recognised in profit or loss. It obtains independent valuations at least every 3 years. At the end of each reporting period, the directors update their assessment of the fair value of each property, taking into account the most recent independent valuations. The key assumptions used in this determination are set out in note 2(q) and 9.

#### (iii) Impairment of intangibles - Goodwill

The Group assesses the recoverability of intangibles and goodwill on at least an annual basis. In determining the recoverability of these assets the Group uses a number of assumptions and estimates. The methodology and assumptions used are disclosed in note 10.

#### (iv) Income taxes

The Group may be subject to income taxes in Australia. Certain judgment is required in determining the provision for income taxes. There are many transactions and calculations undertaken during the ordinary course of business for which the ultimate tax determination is uncertain. The Group recognises liabilities for anticipated tax outcomes based on estimates of taxes which may be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred tax provisions in the period in which a determination is made.

## Notes to the consolidated financial statements

### 2. Summary of significant accounting policies (continued)

#### (y) Use of estimates (continued)

##### (v) Deferred disposal and performance fees

The Group may receive management fees on the sale of property by an investment scheme for which it is the responsible entity. Revenue for deferred disposal and performance fees is recognised for finite life schemes when the performance criteria has been met, and for indefinite life schemes, in the period when the decision to sell a property has been made. The amount of this "deferred" management fee is dependent on the sale price of the property. In the calculation of deferred disposal and performance fees, the sale price is assumed to be the most current valuation as reported in the investment scheme.

##### (z) Rounding of amounts

The Group is an entity of the kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191, relating to the 'rounding off' of amounts in the financial statements. Amounts in the financial statements have been rounded off to the nearest thousand dollars in accordance with that Instrument, unless otherwise indicated.

##### (aa) New accounting standards and interpretations

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2016 reporting periods. The Group has not early adopted these standards/interpretations. The Group's assessment of the impact of relevant new standards and interpretations is set out below:

Standard / Interpretation	Impact	Effective annual reporting periods beginning on or after	Expected to be initially applied in the financial year ending
<b>AASB 9 Financial Instruments</b>	<p>The standard addresses the classification, measurement and derecognition of financial instruments. For financial liabilities that are measured under the fair value option, entities will need to recognise the part of the fair value change that is due to changes in their own credit risk in other comprehensive income rather than profit or loss.</p> <p>New hedge accounting rules align hedge accounting more closely with common risk management processes. As a general rule, it will be easier to apply hedge accounting going forward. The new standard also introduces expanded disclosure requirements and changes in presentation.</p> <p>In December 2014, the AASB introduced a new impairment model. The new impairment model is an expected credit loss (ECL) model which may result in the earlier recognition of credit losses.</p> <p>Management does not expect the above changes to have a significant impact on the Group's financial statements.</p>	1 January 2018	30 June 2019
<b>AASB 15 Revenue from contracts with customers</b>	<p>The AASB has issued a new standard for the recognition of revenue. This will replace AASB 118 which covers contracts for goods and services and AASB 111 which covers construction contracts.</p> <p>The new standard is based on the principle that revenue is recognised when control of a good or service transfers to a customer - so the notion of control replaces the existing notion of risks and rewards.</p> <p>Management does not expect this to have an impact on the Group's financial statements.</p>	1 January 2018	30 June 2019

## 2. Summary of significant accounting policies (continued)

### (aa) New accounting standards and interpretations (continued)

Standard / Interpretation	Impact	Effective annual reporting periods beginning on or after	Expected to be initially applied in the financial year ending
<b>IFRS 16 Leases</b>	<p>In February 2016, the AASB issued AASB 16 Leases. The standard provides a single lessee accounting model, requiring lessees to recognise an asset (the right to use the leased item) and a financial liability to pay rentals. The only exemptions are where the lease term is 12 months or less, or the underlying asset has a low value.</p> <p>Lessor accounting is substantially unchanged under AASB 16.</p> <p>Management does not expect the above changes to have a significant impact on the Group's financial statements on adoption.</p>	1 January 2019	30 June 2020

There are no other standards that are not yet effective and that are expected to have a material impact on the entity in the current or future reporting periods and on foreseeable future transactions.

## Notes to the consolidated financial statements

### 3. Finance costs

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
<b>Finance costs:</b>		
Interest paid or payable	3,951	4,730
Loan establishment and other finance costs	181	318
Write-off of loan establishment costs due to refinancing	201	–
<b>Total finance costs expensed</b>	<b>4,333</b>	<b>5,048</b>
Finance costs capitalised (a)	1,172	1,268
<b>Total finance costs</b>	<b>5,505</b>	<b>6,316</b>

(a) Finance costs are capitalised in relation to current property developments. The capitalisation rate used to determine the amount of finance costs to be capitalised was the weighted average interest rate applicable to the Group's outstanding borrowings at the end of each month.

### 4. Income taxes

Under current Australian income tax legislation, ARF1 and ARF2 are not liable to Australian income tax, provided that the members are presently entitled to the income of the Trusts. Trust distributions are subject to income tax in the hands of securityholders.

ARL and its wholly-owned Australian controlled entities have implemented the tax consolidation legislation. ARL as the head entity in the tax consolidated group, accounts for its own current and deferred tax amounts. ARL also recognises the current and deferred tax liabilities (or assets) of the entities in the tax consolidation group. Where appropriate, deferred tax assets and liabilities are offset.

#### (a) Numerical reconciliation of tax expense per the statutory income tax rate to income tax expense recognised

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Profit before income tax	72,621	60,966
Tax at the applicable Australian tax rate of 30% (2015 - 30%)	(21,786)	(18,290)
Profit attributable to entities not subject to tax	21,999	18,294
Deferred tax assets not recognised	(213)	(256)
Other movements	–	252
<b>Income tax expense</b>	<b>–</b>	<b>–</b>

Unrecognised deferred tax assets are \$0.2 million (2015: \$0.3 million). These have not been recognised as it is not probable that future taxable profit will arise to offset these deductible temporary differences.

## 5. Remuneration of auditors

During the year the following fees were paid or payable for services provided by the auditor of the Group:

	Consolidated	
	30 June 2016	30 June 2015
	\$	\$
<b>PricewaterhouseCoopers Australian firm</b>		
<b>Audit and other assurance services</b>		
Audit and review of financial statements	104,000	86,000
Audit of compliance plans	10,000	6,000
<b>Total remuneration for audit and other assurance services</b>	<b>114,000</b>	92,000
<b>Taxation services</b>		
Tax compliance services, including review of income tax returns	31,673	21,156
<b>Total remuneration for taxation services</b>	<b>31,673</b>	21,156
<b>Other services</b>		
Investigating Accountant report and due diligence in respect of the staplings and management internalisation	–	135,648
<b>Total remuneration of PricewaterhouseCoopers</b>	<b>145,673</b>	248,804

## 6. Earnings per security ('EPS')

	2016	2015
	Cents	Cents
Basic EPS in Arena REIT No. 1	25.70	25.55
Diluted EPS in Arena REIT No. 1	25.70	25.55
Basic EPS in Arena REIT Group	31.55	28.14
Diluted EPS in Arena REIT Group	31.55	28.14

The following information reflects the income and security numbers used in the calculations of basic and diluted EPS.

	2016	2015
	Number of securities '000	Number of securities '000
Weighted average number of ordinary securities used in calculating basic EPS	230,165	216,627
Bonus element of security options which are dilutive	–	–
Adjusted weighted average number of ordinary securities used in calculating diluted EPS	230,165	216,627

## Notes to the consolidated financial statements

### 6. Earnings per security ('EPS') (continued)

	30 June 2016	30 June 2015
	\$'000	\$'000
Earnings used in calculating basic EPS for Arena REIT No. 1	59,155	55,354
Earnings used in calculating diluted EPS for Arena REIT No. 1	59,155	55,354
Earnings used in calculating basic EPS for Arena REIT Group	72,621	60,966
Earnings used in calculating diluted EPS for Arena REIT Group	72,621	60,966

### 7. Cash and cash equivalents

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Cash at bank	8,146	10,888
Term deposits	1,300	–
<b>Total cash and cash equivalents</b>	<b>9,446</b>	<b>10,888</b>

Term deposits are used to secure bank guarantees in respect of development properties.

### 8. Trade and other receivables

#### (a) Trade and other receivables - Current

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Trade receivables	75	296
Other receivables	391	6,457
Prepayments	503	410
	<b>969</b>	<b>7,163</b>

Other receivables as at 30 June 2015 includes \$6.2 million of sales proceeds payable to the Group following the auction of 3 childcare properties on 24 June 2015.

## 8. Trade and other receivables (continued)

### (i) Impairment and ageing

The ageing of trade receivables at the end of the reporting period was:

	Gross 2016 \$'000	Impairment 2016 \$'000	Gross 2015 \$'000	Impairment 2015 \$'000
Not past due	75	–	240	–
Past due 0 - 30 days	–	–	22	–
Past due 31 - 60 days	–	–	34	–
Past due 61 - 90 days	–	–	–	–
Past due over 90 days	–	–	–	–
	<b>75</b>	<b>–</b>	<b>296</b>	<b>–</b>

No other class of financial asset is past due.

Any receivables which are doubtful have been provided for.

From time to time, tenant payments are delayed for administrative reasons such as lease assignment. Management have reviewed all receivables for impairment and are comfortable that the balances are due and payable, and that recovery can be obtained. Past history also supports the recoverability of these receivables.

### (b) Receivables - Non-current

	Consolidated	
	30 June 2016 \$'000	30 June 2015 \$'000
Deferred management & performance fees receivable	1,062	1,189

### (i) Impairment and ageing

None of the non-current receivables are impaired or past due but not impaired.

### (ii) Fair values

The fair values and carrying values of non-current receivables are as follows:

	Consolidated 30 June 2016	
	Carrying amount \$'000	Fair value \$'000
Deferred management & performance fees	1,062	1,062

## Notes to the consolidated financial statements

### 9. Investment properties

#### (a) Valuations and carrying amounts

Property Portfolio	Carrying amount		Latest external valuation	
	2016	2015	2016	2015
	\$'000	\$'000	\$'000	\$'000
Childcare properties	391,037	322,822	354,388	287,631
Childcare developments	22,216	30,117	13,570	23,430
Healthcare properties	78,186	67,593	74,128	63,855
<b>Total</b>	<b>491,439</b>	420,532	<b>442,086</b>	374,916

Independent valuations were performed on 35 childcare properties and 7 healthcare properties as at 31 December 2015, and a further 31 childcare properties as at 30 June 2016. The board of directors has reviewed these valuations and has determined they are appropriate to adopt during the financial period ending 30 June 2016. Director valuations were performed on investment properties not independently valued.

The key inputs into valuations are:

- Passing rent;
- Market rent per licensed place (childcare properties);
- Market rents (healthcare properties);
- Capitalisation rates;
- Lease terms.

The key inputs into the valuation are based on market information for comparable properties. The majority of childcare and healthcare properties are located in markets with evidence to support valuation inputs and methodology. The independent valuers have experience in valuing similar assets and have access to market evidence to support their conclusions. Comparable assets are considered those in similar markets and condition.

Investment properties have been classified as Level 2 in the fair value hierarchy.

There have been no transfers between the levels in the fair value hierarchy during the year.

#### (i) Key assumptions - Childcare properties

	30 June 2016	30 June 2015
Market rent per licensed place	\$1,400 to \$3,900	\$1,200 to \$3,300
Capitalisation rates	6.0% to 8.5%	7.0% to 10.75%
Passing yields	5.25% to 10.0%	7.0% to 10.75%

#### (ii) Key assumptions - Healthcare properties

	30 June 2016	30 June 2015
Capitalisation rates	6.5% to 7.5%	7.5% to 8.5%
Passing yields	6.25% to 8.0%	6.5% to 8.5%



## 9. Investment properties (continued)

### (b) Movements during the financial year

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
<b>At fair value</b>		
Opening balance	420,532	355,831
Property acquisitions and capital expenditure	21,277	29,839
Disposals	(1,150)	(5,080)
Revaluations	51,062	39,828
Other IFRS revaluation adjustments	(282)	114
<b>Closing balance</b>	<b>491,439</b>	420,532

### (c) Amounts recognised in profit or loss for investment properties

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Rental income	33,316	31,196
Other rental income (recognised on a straight line basis)	(327)	23
Direct operating expenses from property that generated rental income	(724)	(923)
Direct operating expenses from property that did not generate rental income	(279)	(383)
Revaluation gain on investment properties	51,062	39,828

### (d) Tenancy risk

Set out below are details of the major tenants who lease properties from the Group:

**Goodstart Early Learning Ltd ("Goodstart")** – representing 42% of the Group's investment property portfolio by income. Like most not-for-profit entities, Goodstart is a company limited by guarantee. It therefore does not have "shareholders," rather, each of the member charities (Mission Australia, Benevolent Society, Brotherhood of St Laurence and Social Ventures Australia) is a member of the company. Goodstart's "capital" is loan capital of varying degrees of risk and subordination.

**Primary Health Care Limited ("PRY")** – representing 16% of the Group's investment property portfolio by income. PRY is a listed company and a major operator of medical clinics throughout Australia. PRY has entered into a deed of cross guarantee with its subsidiaries which are parties to the Group's healthcare property leases. The Group also has a parent entity guarantee with PRY to provide security for their performance under the leases.

**Affinity Education Group Limited ("Affinity")** – representing 16% of the Group's investment property portfolio by income. Affinity is a privately held provider of early childhood education, owning and operating over 150 childcare centres throughout Australia. Affinity have provided Arena with a pooled bank guarantee as security against each of the properties leased.

## Notes to the consolidated financial statements

### 9. Investment properties (continued)

#### Other Tenants

Operator	% of Investment Property Portfolio by Income
Petit Early Learning Journey	6%
Oxanda Education	5%
G8 Education	4%

All of the above tenants are childcare centre operators. G8 Education is listed on the Australian Securities Exchange. The other tenants are privately owned with experience operating childcare centres and their lease obligations are typically secured by bank guarantees and cross defaults.

#### (e) Assets pledged as security

Refer to note 12 for information on investment properties and other assets pledged as security by the Group.

#### (f) Contractual obligations

Capital expenditure contracted for at the end of the reporting period but not recognised as liabilities is as follows:

	30 June 2016	30 June 2015
	\$'000	\$'000
Investment properties	14,456	3,521

The above commitments include the costs associated with developments, and the acquisition of childcare properties.

#### (g) Leasing arrangements

Investment properties are leased to tenants under long-term operating leases with rentals payable monthly. Minimum lease payments receivable on leases of investment properties are as follows:

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Minimum lease receivable under non-cancellable operating leases of investment properties not recognised in the financial statements are receivable as follows:		
Within one year	34,015	31,138
Later than one year but not later than 5 years	142,989	130,599
Later than 5 years	201,204	146,760
	<b>378,208</b>	<b>308,497</b>

## 10. Intangible assets

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Goodwill	10,816	10,730
	<b>10,816</b>	10,730

Goodwill represents funds management (intangible rights) acquired by the Group on the management internalisation of Arena REIT in December 2014.

The Group tests annually whether goodwill has been impaired on the basis of a value-in-use assessment:

- cash flow projections are based on internal financial budgets covering a 5 year period;
- methodology and key assumptions have been made with reference to, and are supported by, the Independent Expert's Report obtained at the time of internalisation;
- management fee rates used to assess cash flow savings are based on the Arena REIT Constitution and PDS;
- for the purposes of the assessment, growth rates have been set in the range of 2-3% per annum; and
- cash flows have been discounted at a rate of 8.25% per annum.

## 11. Trade and other payables

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Prepaid rental income	2,059	2,161
Investment property acquisition	–	1,722
Sundry creditors and accruals	6,628	5,593
Distributions payable	6,437	5,821
	<b>15,124</b>	15,297

Trade and other payables are non-interest bearing.

## 12. Interest bearing liabilities

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
<b>Non-current:</b>		
<b>Secured</b>		
Syndicated facility	138,000	131,000
Unamortised transaction costs	(413)	(226)
<b>Total secured non-current borrowings</b>	<b>137,587</b>	130,774

## Notes to the consolidated financial statements

### 12. Interest bearing liabilities (continued)

#### (a) Financing arrangements

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
<b>Committed facilities available at the end of the reporting period</b>		
Interest bearing liabilities	175,000	175,000
<b>Facilities used at the end of the reporting period</b>		
Interest bearing liabilities	138,000	131,000

Arena REIT extended the term of its \$175 million debt facility in December 2015 (\$87.5 million for a 3 year term to 31 December 2018 and \$87.5 million for a 5 year term to 31 December 2020). The facilities are available to both ARF1 and ARF2 and the assets of both Trusts are held as security under the facilities.

The interest rate applying to the drawn amount of the facilities is set on a monthly basis at the prevailing market interest rates.

The undrawn amount of the bank facilities may be drawn at any time.

#### (b) Assets pledged as security

The bank facilities are secured by a registered first mortgage over investment property and a fixed and floating charge over the assets of Arena REIT No. 1 and Arena REIT No. 2.

The carrying amounts of assets pledged as security are:

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
<b>Financial assets pledged</b>		
Cash and cash equivalents	6,444	6,966
Trade and other receivables	613	6,718
	<b>7,057</b>	13,684
<b>Other assets pledged</b>		
Investment properties	491,439	420,532
	<b>491,439</b>	420,532

#### (c) Covenants

The covenants over the Group's bank facility require an interest cover ratio of greater than 2.0 times (Actual at 30 June 2016 of 6.2 times) and a loan to market value of investment properties ratio of less than 50% (Actual at 30 June 2016 of 31.2%). The Group was in compliance with its covenants throughout the year.

### 13. Derivative financial instruments

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
<b>Non-current liabilities</b>		
Interest rate swaps	3,030	398
	<b>3,030</b>	<b>398</b>

The Group has entered into interest rate swap contracts under which they receive interest at variable rates and pay interest at fixed rates to protect interest bearing liabilities from exposure to changes in interest rates.

Swaps currently in place cover 72% (2015: 69%) of the facility principal outstanding. The weighted average fixed interest swap rate at 30 June 2016 was 2.48% (2015: 2.62%), and the weighted average term was 4.0 years (2015: 3.5 years).

Periodic swap settlements match the period for which interest is payable on the underlying debt, and are settled on a net basis.

The notional principal amounts and periods of expiry of the interest rate swap contracts are as follows:

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Less than 1 year	–	–
1 -2 years	25,000	15,000
2 -3 years	10,000	25,000
3 -4 years	20,000	10,000
4 -5 years	22,500	20,000
Greater than 5 years	22,500	20,000
	<b>100,000</b>	<b>90,000</b>

### 14. Contributed equity

#### (a) Securities

	Consolidated			
	30 June 2016	30 June 2015	30 June 2016	30 June 2015
	Securities '000	Securities'000	\$'000	\$'000
<b>Ordinary Securities</b>				
Fully paid	231,966	228,290	197,224	191,845

Other contributed equity attributable to securityholders of the Group relating to ARF2 and ARL of \$39.7 million is included within Non-controlling interests - ARF2 and ARL (30 June 2015: \$38.9 million).

## Notes to the consolidated financial statements

### 14. Contributed equity (continued)

#### (b) Movements in ordinary securities

Date	Details	Number of securities	
		'000	\$'000
1 July 2014	Opening balance	211,496	183,221
	Arising on stapling	–	(13,000)
	Issue of securities under DRP (i)	1,169	1,644
10 March 2015	Issue of securities under institutional placement (ii)	15,625	19,980
30 June 2015	Closing balance	228,290	191,845
1 July 2015	Opening balance	228,290	191,845
	Issue of securities under DRP (i)	3,676	5,379
30 June 2016	Closing balance	231,966	197,224

#### (i) Distribution Re-investment Plan (DRP)

The Group has a Distribution Reinvestment Plan (DRP) under which securityholders may elect to have all or part of their distribution entitlements satisfied by the issue of new securities rather than being paid in cash. The DRP first came into operation with the distribution for the quarter-ended 30 September 2014 and remains open at the date of these financial statements.

#### (ii) Institutional Placement

The Group completed a fully underwritten placement to institutional and professional investors in the prior year. \$25 million was raised through the issue of 15,625,000 stapled securities at a price of \$1.60 per stapled security. Settlement of the new stapled securities under the placement occurred 10 March 2015.

#### (c) Capital management

The objectives of the Stapled Group are to generate attractive and predictable income distributions to investors with earnings growth prospects over the medium to long term.

The Group aims to invest to meet the Group's investment objectives while maintaining sufficient liquidity to meet its commitments. The Group regularly reviews performance, including asset allocation strategies, investment and operational management strategies, investment opportunities, performance review, and risk management.

In order to maintain its capital structure, the Group may adjust the amount of distributions paid to securityholders, return capital to securityholders, issue new securities or sell assets to reduce debt.

Consistent with others in the industry, the Group monitors capital through the analysis of a number of financial ratios, including the Gearing ratio.

Gearing Ratio	2016	2015
	\$'000	\$'000
Interest bearing liabilities	138,000	131,000
Total assets	513,951	450,623
Gearing ratio	26.8%	29.1%

## 15. Accumulated profit

	Consolidated	
	30 June 2016 \$'000	30 June 2015 \$'000
<b>Movements in accumulated profit were as follows:</b>		
Opening accumulated profit	61,900	25,991
Net profit for the period attributable to ARF1	59,155	55,354
Distribution paid or payable attributable to ARF1	(21,868)	(19,445)
<b>Closing accumulated profit</b>	<b>99,187</b>	<b>61,900</b>

### Distributions to securityholders

The following table details the distributions to securityholders during the financial year on a consolidated basis, including distributions declared by ARF2 (classified as a non-controlling interest) of \$3.3 million (30 June 2015: \$2.5 million).

Distributions declared	2016 \$'000	2015 \$'000	2016 cps	2015 cps
September quarter	6,128	5,156	2.6750	2.4375
December quarter	6,158	5,211	2.6750	2.4625
March quarter	6,413	5,803	2.7750	2.5500
June quarter	6,437	5,821	2.7750	2.5500
<b>Total distributions to securityholders</b>	<b>25,136</b>	<b>21,991</b>	<b>10.9000</b>	<b>10.0000</b>

## 16. Non-controlling interests

The financial statements reflect the consolidation of ARF1, ARF2 and ARL. For financial reporting purposes, one entity in the stapled group must be identified as the acquirer or parent entity of the others. ARF1 has been identified as the acquirer of ARF2 and ARL, resulting in ARF2 and ARL being disclosed as Non-controlling interests.

Movements in non-controlling interests were as follows:

	ARF2 30 June 2015	ARL 30 June 2015	Total 30 June 2015
<b>Opening balance - 1 July 2014</b>	<b>28,992</b>	<b>-</b>	<b>28,992</b>
Arising on stapling	-	13,000	13,000
Securities issued under DRP	216	-	216
Contributions of equity, net of transaction costs	2,971	1,389	4,360
Net profit for the period attributable to non-controlling interests	5,626	(14)	5,612
Distributions paid or payable attributable to non-controlling interests	(2,546)	-	(2,546)
Increase/(decrease) in reserves (i)	-	112	112
<b>Closing balance - 30 June 2015</b>	<b>35,259</b>	<b>14,487</b>	<b>49,746</b>

## Notes to the consolidated financial statements

### 16. Non-controlling interests (continued)

	ARF2	ARL	Total
	30 June 2016	30 June 2016	30 June 2016
<b>Opening balance - 1 July 2015</b>	<b>35,259</b>	<b>14,487</b>	<b>49,746</b>
Securities issued under DRP	788	–	788
Net profit for the period attributable to non-controlling interests	14,175	(709)	13,466
Distributions paid or payable attributable to non-controlling interests	(3,268)	–	(3,268)
Increase/(decrease) in reserves (i)	–	350	350
<b>Closing balance - 30 June 2016</b>	<b>46,954</b>	<b>14,128</b>	<b>61,082</b>

#### (i) Reserves

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Opening balance	112	–
Security-based benefits expense for the period	350	112
<b>Balance 30 June</b>	<b>462</b>	112

The security-based benefits reserve is used to recognise the fair value of rights issued under the Group's Long Term Incentive Plan.

### 17. Segment information

The Group operates as one business segment being investment in real estate, and in one geographic segment being Australia. The Group's segments are based on reports used by the Chief Operating Decision Maker in making strategic decisions about the Group, assessing the financial performance and financial position of the Group, determining the allocation of resources, and risk management.

### 18. Related party disclosures

#### Subsidiaries

Investments in subsidiaries is set out in note 19.

#### Key management personnel compensation

	30 June 2016	30 June 2015
	\$	\$
Short-term employee benefits	1,869,119	1,011,950
Post-employment benefits	115,265	59,763
Long-term benefits	14,313	10,149
Termination benefits	–	–
Security-based payments	331,827	96,510
	<b>2,330,524</b>	1,178,372

Detailed remuneration disclosures are provided in the Remuneration report.



## 18. Related party disclosures (continued)

### Stapled group

The Arena REIT Stapled Group comprises ARF1, ARF2, and ARL and its controlled entities.

Arena REIT Management Limited (a wholly owned subsidiary of ARL) replaced Arena Investment Management Limited as responsible entity of the Trusts on 12 December 2014.

### Responsible entity

The Responsible Entity or its related parties are entitled to receive fees in accordance with the Group's constitution, from the Group and its controlled entities.

	30 June 2016	30 June 2015
	\$	\$
<b>The following transactions occurred with related parties:</b>		
Acquisition of interests in related parties	–	485,428
Property management income received from other related parties	28,000	7,000
Management fees received by the Group from other related parties	344,234	180,494
Property income received from other related parties	43,163	18,054
Increase/(decrease) in fair value of performance fee receivable by the Group from other related parties	(127,326)	118,968
<b>Amounts receivable:</b>		
Amount receivable from other related parties at the end of the reporting period	52,752	48,341
Deferred management and performance fees receivable at the end of the reporting period	1,061,811	1,189,137
<b>Amounts payable:</b>		
Amounts payable to other related parties at the end of the reporting period	–	–

### Former Responsible Entity

On 11 December 2014, Arena Investment Management Limited ('AIML') retired as Responsible Entity of the funds within the Arena REIT Stapled Group. The former Responsible Entity received the following fees during the year, up to the date of retirement:

	30 June 2016	30 June 2015
	\$	\$
<b>The following transactions occurred with the former Responsible Entity prior to its retirement on 11 December 2014:</b>		
Management fees paid or payable by the Group to the former Responsible Entity	–	1,352,599
Property disposal and performance fees paid or payable by the Group to the former Responsible Entity	–	284,150
<b>Amounts payable:</b>		
Amounts payable to the former Responsible Entity at the end of the reporting period	–	–

## Notes to the consolidated financial statements

### 19. Investments in subsidiaries

The consolidated financial statements incorporate the assets, liabilities and results of the following subsidiaries of ARL:

Name of entity	Country of incorporation	Class of shares	Equity holding	
			2016 %	2015 %
Citrus Investment Services Limited	Australia	Ordinary	100	100
Arena Property Services Pty Limited*	Australia	Ordinary	–	100
Arena REIT Management Limited	Australia	Ordinary	100	100
Arena REIT Operations Pty Limited	Australia	Ordinary	100	–

\* wound-up during the year.

The management function of the Arena REIT Group was internalised in the prior year, taking effect from 12 December 2014. The internalisation process involved the stapling of each share in Arena REIT Limited ('ARL') to each existing stapled security, as well as the acquisition by ARL of Citrus Investment Services Pty Ltd, Arena REIT Management Limited and Arena Property Services Pty Ltd.

### 20. Security-based benefits expense

#### (a) Performance Rights and Recognition Rights Plan (Rights)

The performance rights and recognition rights are unquoted securities. Conversion to stapled securities is subject to service and performance conditions which are discussed in the Remuneration Report.

Performance rights	2016	2015	
	Number	Number	Total Number
Rights issued	535,655	304,987	840,642
<b>Performance rights issued</b>	<b>535,655</b>	<b>304,987</b>	<b>840,642</b>
Number rights forfeited/lapsed in prior years	–	–	–
Number rights forfeited/lapsed in current year	–	–	–
Number rights vested in prior years	–	–	–
Number rights vested in current year	–	–	–
<b>Closing balance</b>	<b>535,655</b>	<b>304,987</b>	<b>840,642</b>

Recognition rights	2016	2015	
	Number	Number	Total Number
Rights issued	–	186,660	186,660
<b>Recognition rights issued</b>	<b>–</b>	<b>186,660</b>	<b>186,660</b>
Number rights forfeited/lapsed in prior years	–	–	–
Number rights forfeited/lapsed in current year	–	(10,000)	(10,000)
Number rights vested in prior years	–	–	–
Number rights vested in current year	–	–	–
<b>Closing balance</b>	<b>–</b>	<b>176,660</b>	<b>176,660</b>

## 20. Security-based benefits expense (continued)

### (b) Rights expense

Total expenses relating to the Rights recognised during the year as part of employee benefit expense was as follows:

	30 June 2016	30 June 2015
	\$'000	\$'000
Performance Rights and Recognition Rights	350	112
	<b>350</b>	<b>112</b>

### (c) Rights valuation inputs

Rights issued were independently valued for the purposes of valuation and accounting using a Black-Scholes or Monte Carlo method, as applicable. The model inputs for the Rights issued during FY16 to assess the fair value are as follows:

#### Performance rights

Grant date	1 July 2015
Security price at grant date	\$1.57
Fair value of right	\$0.99
Expected price volatility	22%
Risk-free interest rate	2.05%

## 21. Financial risk management and fair value measurement

The Group's investing activities expose it to various types of risk that are associated with the financial instruments and markets in which it invests. The most important types of financial risk to which the Group is exposed to are market risk, credit risk and liquidity risk. The exposure to each of these risks, as well as the Group's policies and processes for managing these risks are described below.

### (a) Market risk

Market risk embodies the potential for both loss and gains and includes interest rate risk and price risk. The Group's strategy on the management of investment risk is driven by the Group's investment objective. The Group's market risk is managed in accordance with the investment guidelines as outlined in the Group's Product Disclosure Statement.

#### (i) Cash flow and fair value interest rate risk

The Group's cash and cash equivalents, floating rate borrowings and interest rate swaps expose it to a risk of change in the fair value or future cash flows due to changes in interest rates. The specific interest rate exposures are disclosed in the relevant notes to the financial statements.

The Group economically hedges a portion of its exposure to changes in interest rates on variable rate borrowings by using floating-to-fixed interest rate swaps. By hedging against changes in interest rates, the Group has limited its exposure to changes in interest rates on its cash flows. The portion that is hedged is set by the Board of Directors and is influenced by the hedging requirements set out in the Group's debt facility documents, and the market outlook. The Group ensures the maturity of individual swaps does not exceed the expected life of assets.

## Notes to the consolidated financial statements

### 21. Financial risk management and fair value measurement (continued)

The Group's exposure to interest rate risk at reporting date, including its sensitivity to changes in market interest rates that were reasonably possible, is as follows:

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
<b>Financial assets</b>		
Cash and cash equivalents (floating interest rate)	9,446	10,888
<b>Financial liabilities</b>		
Interest bearing liabilities - floating interest rate	(138,000)	(131,000)
Derivative financial instruments (notional principal amount) - fixed rate interest rate swaps	100,000	90,000
<b>Net Exposure</b>	<b>(28,554)</b>	<b>(30,112)</b>

Sensitivity of profit or loss to movements in market interest rates for derivative instruments with cash flow risk:

	Consolidated	
	2016	2015
	\$'000	\$'000
Market interest rate increased by 100 basis points (2015: 100 bp)	(286)	(301)
Market interest rate decreased by 100 basis points (2015: 100 bp)	286	301
<b>Instruments with fair value risk:</b>		
Derivative financial instruments	100,000	90,000

Sensitivity of profit or loss to movements in market interest rates for financial instruments with fair value risk:

Market interest rate increased by 100 basis points (2015: 100bp)	3,571	3,142
Market interest rate decreased by 100 basis points (2015: 100bp)	(3,571)	(3,142)

The interest rate range for sensitivity purposes has been determined using the assumption that interest rates changed by +/- 100 basis points from year end rates with all other variables held constant. In determining the impact of an increase/decrease in equity to securityholders arising from market risk the Group has considered prior period and expected future movements of the portfolio information in order to determine a reasonable possible shift in assumptions.

## 21. Financial risk management and fair value measurement (continued)

### (b) Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge its obligation and cause the other party to incur a financial loss.

The Group's maximum credit risk exposure at balance date in relation to each class of recognised financial asset, other than equity and derivative financial instruments, is the carrying amount of those assets as indicated in the balance sheet. This does not represent the maximum risk exposure that could arise in the future as a result of changes in values, but best represents the current maximum exposure at reporting date.

	Consolidated	
	30 June 2016	30 June 2015
	\$'000	\$'000
Cash at bank	9,446	10,888
Other receivables	1,528	1,745
Less: Allowance for impairment of trade receivables	–	–
<b>Maximum exposure to credit risk</b>	<b>10,974</b>	12,633

The Group manages credit risk and the losses which could arise from default by ensuring that parties to contractual arrangements are of an appropriate credit rating, or do not show a history of defaults. Financial assets such as cash at bank and interest rate swaps are held with high credit quality financial institutions (rated equivalent A or higher by the major rating agencies). Before accepting a new tenant, the Group endeavours to obtain financial information from the prospective tenant, and rental guarantees are sought before a tenancy is approved. Third party credit risk is secured by corporate, personal and bank guarantees where possible.

All receivables are monitored by the Group. If any amounts owing are overdue these are followed up and if necessary, allowances are made for debts that are doubtful.

At the end of the reporting period there are no issues with the credit quality of financial assets that are either past due or impaired, and all amounts are expected to be received in full.

## Notes to the consolidated financial statements

### 21. Financial risk management and fair value measurement (continued)

#### (c) Liquidity risk

Liquidity risk is the risk that the Group may not be able to generate sufficient cash resources to settle its obligations in full as they fall due or can only do so on terms that are materially disadvantageous.

The Group monitors its exposure to liquidity risk by ensuring that as required there is sufficient cash on hand or debt facility funding available to meet the contractual obligations of financial liabilities as they fall due. The Group sets budgets to monitor cash flows.

The table below analyses the Group's financial liabilities into relevant maturity groupings based on the remaining period at the end of the reporting period. The amounts in the table are the contractual undiscounted cash flows.

Consolidated	Less than 12 months \$'000	1-2 years \$'000	Greater than 2 years \$'000
<b>30 June 2016</b>			
Trade and other payables	15,124	–	–
Interest rate swaps	625	613	1,373
Interest bearing liabilities	3,347	3,347	146,775
<b>Contractual cash flows (excluding gross settled derivatives)</b>	<b>19,096</b>	<b>3,960</b>	<b>148,148</b>

Consolidated	Less than 12 months \$'000	1-2 years \$'000	Greater than 2 years \$'000
<b>30 June 2015</b>			
Trade and other payables	15,297	–	–
Interest rate swaps	914	434	1,726
Interest bearing liabilities	3,632	90,122	48,317
<b>Contractual cash flows (excluding gross settled derivatives)</b>	<b>19,843</b>	<b>90,556</b>	<b>50,043</b>

#### (d) Fair value estimation

The carrying amounts of the Group's assets and liabilities at the end of each reporting period approximate their fair values.

Financial assets and liabilities held at fair value through profit or loss are measured initially at fair value excluding any transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. Transaction costs on financial assets and financial liabilities at fair value through profit or loss are expensed immediately. Subsequent to initial recognition, all instruments held at fair value through profit or loss are measured at fair value with changes in their fair value recognised in profit or loss.

## 21. Financial risk management and fair value measurement (continued)

### (e) Fair value hierarchy

#### (i) Classification of financial assets and financial liabilities

AASB 13 requires disclosure of fair value measurements by level of fair value hierarchy. The fair value hierarchy has the following levels:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1);
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2);
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The level in the fair value hierarchy within which the fair value measurement is categorised in its entirety is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. For this purpose, the significance of an input is assessed against the fair value measurement in its entirety. If a fair value measurement uses observable inputs that require significant adjustment based on unobservable inputs, that measurement is a level 3 measurement. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgement, considering factors specific to the asset or liability.

The determination of what constitutes 'observable' requires significant judgement by the Responsible Entity. The Responsible Entity considers observable data to be that market data that is readily available, regularly distributed or updated, reliable and verifiable, not proprietary, and provided by independent sources that are actively involved in the relevant market.

The following table presents the Group's financial assets and liabilities (by class) measured at fair value according to the fair value hierarchy at 30 June 2016 and 30 June 2015 on a recurring basis:

Consolidated	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
<b>30 June 2016</b>				
<b>Financial liabilities</b>				
Interest rate swaps	–	3,030	–	3,030
<b>Total</b>	<b>–</b>	<b>3,030</b>	<b>–</b>	<b>3,030</b>
<hr/>				
Consolidated	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
<b>30 June 2015</b>				
<b>Financial liabilities</b>				
Interest rate swaps	–	398	–	398
<b>Total</b>	<b>–</b>	<b>398</b>	<b>–</b>	<b>398</b>

The Group's policy is to recognise transfers into and transfers out of fair value hierarchy levels as at the end of the reporting period. There were no transfers between levels during the year.

The Group did not measure any financial assets or financial liabilities at fair value on a non-recurring basis as at 30 June 2016.

## Notes to the consolidated financial statements

### 21. Financial risk management and fair value measurement (continued)

#### (ii) Valuation techniques used to derive level 2 and level 3 values

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in level 2.

If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3.

The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows based on observable yield curves, taking into account any material credit risk.

#### (f) AFSL financial compliance risk

The Group is exposed to the risk of having inadequate capital and liquidity. Arena REIT Management Limited, a subsidiary of ARL, holds an Australian Financial Services License ('AFSL') and acts as a responsible entity for the Group's managed investment schemes. The AFSL requires minimum levels of net tangible assets, liquid assets, cash reserves and liquidity, which may restrict the Group in paying dividends that would breach these requirements.

The directors regularly review and monitor the Group's balance sheet to ensure ARML's compliance with its AFSL requirements.

### 22. Parent entity financial information

#### Summary of financial information

The individual financial statements for the parent entity show the following aggregate amounts:

Parent	30 June 2016	30 June 2015
	\$'000	\$'000
<b>Income statement information</b>		
Net profit attributable to Arena REIT No. 1	59,155	55,354
<b>Comprehensive income information</b>		
Total comprehensive income attributable to Arena REIT No. 1	59,155	55,354
<b>Balance Sheet</b>		
Current assets	6,330	11,129
Non-current assets	413,253	352,939
<b>Total assets</b>	<b>419,583</b>	<b>364,068</b>
Current liabilities	13,161	12,884
Non-current liabilities	110,010	97,439
<b>Total liabilities</b>	<b>123,171</b>	<b>110,323</b>
<b>Equity attributable to securityholders of Arena REIT No. 1</b>		
Contributed equity	197,224	191,845
Accumulated profit	99,188	61,900
	<b>296,412</b>	<b>253,745</b>



## 23. Reconciliation of profit to net cash inflow from operating activities

	30 June 2016	30 June 2015
	\$'000	\$'000
Profit for the year	72,621	60,966
Amortisation of borrowing costs	103	75
Net increase in fair value of investment properties	(51,062)	(39,828)
Straight lining adjustment on rental income	327	(23)
Net (gain)/loss on sale of direct property	121	(2,232)
Net (gain)/loss on derivative financial instruments	2,915	1,781
Security-based payments expense	350	112
Stapling and other transaction costs	201	1,027
Other	174	(39)
Changes in operating assets and liabilities		
Decrease/(increase) in trade and other receivables	79	890
(Decrease)/increase in trade and other payables	303	150
(Decrease)/increase in provisions	54	51
<b>Net cash inflow from operating activities</b>	<b>26,186</b>	<b>22,930</b>

## 24. Contingent assets and liabilities and commitments

There are no material outstanding contingent assets or liabilities as at 30 June 2016 and 30 June 2015. For details of commitments of the Group as at 30 June 2016, refer to note 9.

## 25. Events occurring after the reporting period

No significant events have occurred since the end of the reporting period which would impact on the financial position of the Group disclosed in the consolidated balance sheet as at 30 June 2016 or on the results and cash flows of the Group for the year ended on that date.

## Directors' declaration

In the opinion of the directors:

- (a) the financial statements and notes set out on pages 35 to 73 are in accordance with the *Corporations Act 2001*, including:
  - (i) complying with Accounting Standards, the *Corporations Regulations 2001* and other mandatory professional reporting requirements, and
  - (ii) giving a true and fair view of the Group's financial position as at 30 June 2016 and of its performance for the financial year ended on that date, and
- (b) there are reasonable grounds to believe that the Group will be able to pay its debts as and when they become due and payable, and
- (c) Note 2(a) confirms that the financial statements comply with International Financial Reporting Standards as issued by the International Accounting Standards Board.

The directors have been given the declarations by the managing director and chief financial officer required by section 295A of the *Corporations Act 2001*.

This declaration is made in accordance with a resolution of the directors.



David Ross, **Chairman**

Melbourne, 25 August 2016

# Independent auditor's report



## **Independent auditor's report to the securityholders of Arena REIT**

### ***Report on the financial report***

We have audited the accompanying financial report of Arena REIT (the Group), which comprises the consolidated balance sheet as at 30 June 2016, the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration for Arena REIT (the consolidated entity). The consolidated entity comprises of the stapled entities Arena REIT No. 1, Arena REIT No. 2, Arena REIT Limited, and the entities they controlled at year's end or from time to time during the financial year.

### ***Directors' responsibility for the financial report***

The directors of the Group are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 2, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with International Financial Reporting Standards.

### ***Auditor's responsibility***

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the consolidated entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***Independence***

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*.

### ***Auditor's opinion***

In our opinion:

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**PricewaterhouseCoopers, ABN 52 780 433 757**  
Freshwater Place, 2 Southbank Boulevard, SOUTHBANK VIC 3006, GPO Box 1331, MELBOURNE VIC 3001  
T: 61 3 8603 1000, F: 61 3 8603 1999, [www.pwc.com.au](http://www.pwc.com.au)

Liability limited by a scheme approved under Professional Standards Legislation.

## Independent auditor's report (continued)



- (a) the financial report of Arena REIT is in accordance with the *Corporations Act 2001*, including:
  - (i) giving a true and fair view of the consolidated entity's financial position as at 30 June 2016 and of its performance for the year ended on that date; and
  - (ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.
- (b) the financial report and notes also comply with International Financial Reporting Standards as disclosed in Note 2.

### **Report on the Remuneration Report**

We have audited the remuneration report included in pages 9 to 18 of the directors' report for the year ended 30 June 2016. The directors of the Group are responsible for the preparation and presentation of the remuneration report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with Australian Auditing Standards.

### **Auditor's opinion**

In our opinion, the remuneration report of Arena REIT for the year ended 30 June 2016 complies with section 300A of the *Corporations Act 2001*.

A handwritten signature in cursive script, appearing to read 'PricewaterhouseCoopers', written in black ink.

PricewaterhouseCoopers

A handwritten signature in cursive script, appearing to read 'Elizabeth O'Brien', written in black ink.

Elizabeth O'Brien  
Partner

Melbourne  
25 August 2016

## ASX additional information

### Additional Securities Exchange Information as at 1 August 2016

There were 231,965,539 fully paid ordinary securities on issue, held by 4,220 securityholders. There were 126 holders holding less than a marketable parcel.

The voting rights attaching to the ordinary securities, set out in section 253C of the *Corporations Act 2001*, are:

- (i) on a show of hands every person present who is a securityholder has one vote; and
- (ii) on a poll each securityholder present in person or by proxy or attorney has one vote for each security they have in the Group.

### Distribution of securityholders

Number of securities held	Number of securityholders	Total securities held	% of total securities on issue
1-1,000	502	241,762	0.10
1,001-5,000	689	2,025,705	0.87
5,001-10,000	699	5,610,154	2.42
10,001-100,000	2,215	68,000,927	29.32
100,000 and over	115	156,086,991	67.29
<b>Total</b>	<b>4,220</b>	<b>231,965,539</b>	<b>100.00</b>

### Substantial securityholders

Name of substantial securityholder	Number of securities
Australian Unity Funds Management Limited	27,677,037
Commonwealth Bank of Australia	15,907,988
The Vanguard Group, Inc	16,352,388

## ASX additional information (continued)

## Twenty largest securityholders

Holder Name	Number of securities	Fully paid (%)
HSBC Custody Nominees (Australia) Limited	32,292,720	13.92
BNP Paribas Noms Pty Ltd <DRP>	31,436,097	13.55
J P Morgan Nominees Australia Limited	27,870,318	12.02
Citicorp Nominees Pty Limited	13,665,657	5.89
National Nominees Limited	13,451,656	5.80
Perpetual Nominees Limited <PNL1 A/C>	5,969,753	2.57
Perpetual Nominees Limited <INV1 A/C>	4,400,556	1.90
Sandhurst Trustees Ltd <AIMS PSF A/C>	2,665,937	1.15
Navigator Australia Ltd <MLC Investment Sett A/C>	932,766	0.40
RBC Investor Services Australia Nominees Pty Limited <BKCUST A/C>	829,482	0.36
Keith David Kirk	722,195	0.31
HSBC Custody Nominees (Australia) Limited - A/C 2	581,259	0.25
Netwealth Investments Limited <WRAP Services A/C>	572,717	0.25
Taverners No 11 Pty Ltd <Brencorp No 11 Unit A/C>	561,794	0.24
Arkwright Developments Pty Limited <The Findlay A/C>	550,000	0.24
Mr Jiebo Huang	547,030	0.24
Norcad Investments Pty Ltd	495,050	0.21
Austral Capital Pty Ltd <Austral Equity Fund A/C>	484,104	0.21
Mr Philippe Denis Georges Perez	470,251	0.20
Karen Arnott	400,000	0.17
<b>Totals</b>	<b>138,899,342</b>	<b>59.88</b>

# Investor Information

## ASX listing

Arena REIT is listed on the Australian Securities Exchange (ASX) under the code ARF.

## Arena REIT securities

A stapled security in Arena REIT comprises:

- › one security in Arena REIT Limited;
- › one security in Arena REIT No.1; and
- › one security in Arena REIT No.2;

stapled and traded together as one security.

## Accessing information on Arena

The Arena website [www.arena.com.au](http://www.arena.com.au) provides access to the latest announcements, financial reports, presentations and teleconferences released by Arena. It also provides information on Arena's Board and management team, as well as access to information on your investment via the Investor Centre.

## Receiving information electronically

By electing to receive information from Arena electronically, you will receive secure and environmentally friendly email notifications of ASX announcements, distribution and annual tax statements, annual reports and upcoming events.

If you wish to register for electronic communications you can log in and update your details online, download the form from the Investor Centre [www.arena.com.au/Investor-Centre](http://www.arena.com.au/Investor-Centre) or call 1800 008 494 to request a form.

## Managing your investment online

You can manage your holding online by registering at the Investor Centre on the Arena website. To register, please call 1800 008 494 and request an online password. Once received, go to the Investor Centre at [www.arena.com.au/Investor-Centre](http://www.arena.com.au/Investor-Centre) and click on 'Investor Login' to register.

## Distribution payments

Arena makes distribution payments on a quarterly basis, typically within six weeks of the quarter end. Details of the 2016 financial year distributions are provided in the table below.

### FY16 distributions

Quarter ended	Payment date	Distribution amount (cps)
30 September 2015	12 November 2015	2.675
31 December 2015	11 February 2016	2.675
31 March 2016	12 May 2016	2.775
30 June 2016	11 August 2016	2.775

To ensure timely receipt of your distribution, please consider the following:

### Direct credit

Arena encourages investors to receive distribution payments by direct credit to their nominated bank account. If you wish to register for direct credit or update your payment details you can log in and amend your details online, download the form from the Investor Centre [www.arena.com.au/Investor-Centre](http://www.arena.com.au/Investor-Centre) or call 1800 008 494 to request a form.

### Dividend and distribution reinvestment plan

The dividend and distribution reinvestment plan (DRP) is currently in operation and allows investors to reinvest their distribution payments automatically into additional securities, without brokerage or other transaction costs. Participation is optional and investors can join, vary their participation or withdraw from the DRP at any time. Please visit the Investor Centre [www.arena.com.au/Investor-Centre](http://www.arena.com.au/Investor-Centre) for further details and an election form.

### Tax File Number (TFN) notification

You are not required by law to provide your TFN, Australian Business Number (ABN) or exemption status. However, if you do not provide your TFN, ABN or exemption, withholding tax at the highest marginal rate for Australian resident members may be deducted from distributions paid to you. If you wish to update your TFN, ABN or exemption status, you can log in and amend your details online, download the form from the Investor Centre [www.arena.com.au/Investor-Centre](http://www.arena.com.au/Investor-Centre) or call 1800 008 494 to request a form. If you are a chess holder, please contact your sponsoring broker.

## Investor Information (continued)

### Annual tax statement and 2016 tax guide

An annual tax statement is dispatched to investors in August each year. To assist in completion of your tax return, Arena also publishes an annual tax guide each year. The 2016 tax guide is available for download from the Investor Centre [www.arena.com.au/Investor-Centre](http://www.arena.com.au/Investor-Centre).

### Investor feedback or complaints

If you have any complaints or feedback, please direct these in writing to:

**Arena Investor Relations**

Locked Bag 32002  
Collins Street East  
Melbourne VIC 8003  
Telephone: 1800 008 494  
Email: [complaints@arena.com.au](mailto:complaints@arena.com.au)

If you make a complaint and do not receive a satisfactory outcome, you can contact the Financial Ombudsman Service Limited (FOS), of which Arena is a member, on the details below. FOS is an external dispute resolution scheme approved by the Australian Securities and Investments Commission (ASIC). Please note that FOS will not deal with complaints that have not first been referred to Arena for resolution.

FOS can be contacted at:

**Financial Ombudsman Service**

GPO Box 3  
Melbourne VIC 3001  
Telephone: 1800 367 287  
Email: [info@fos.org.au](mailto:info@fos.org.au)

### Arena calendar\*

#### February

- › Interim results released
- › Distribution paid for quarter ended 31 December

#### May

- › Distribution paid for quarter ended 31 March

#### August

- › Annual results released
- › Distribution paid for quarter ended 30 June
- › Annual tax statements dispatched

#### September

- › Annual Report released
- › Notice of Annual General Meeting dispatched

#### November

- › Distribution paid for quarter ended 30 September
- › Annual General Meeting

\*The dates listed above are indicative only and subject to change.

### Privacy policy

Arena is committed to ensuring the confidentiality and security of investors' personal information. Arena's privacy policy, detailing how we handle personal information, is available on the Arena website [www.arena.com.au](http://www.arena.com.au)



# Corporate Directory

## **Arena REIT Limited**

ACN 602 365 186

## **Arena REIT Management Limited**

ACN 600 069 761 AFSL 465754

## **Registered Office**

Level 5, 41 Exhibition Street  
Melbourne VIC 8003

**Phone:** +61 3 9093 9000

**Fax:** +61 3 9093 9093

**Email:** [info@arena.com.au](mailto:info@arena.com.au)

**Website:** [www.arena.com.au](http://www.arena.com.au)

## **Directors**

David Ross

Simon Parsons

Dennis Wildenburg

Bryce Mitchelson

Gareth Winter (ARML only)

## **Company Secretary**

Gareth Winter

## **Auditor**

### **PricewaterhouseCoopers**

Freshwater Place  
2 Southbank Boulevard  
Southbank VIC 3006

## **Registry**

### **Boardroom Pty Limited**

Level 12, 225 George Street  
Sydney NSW 2001

## **Investor inquiries and correspondence**

### **Arena REIT**

Locked Bag 32001  
Collins Street East  
Melbourne VIC 8003

**Telephone:** 1800 008 494

**Website:** [www.arena.com.au](http://www.arena.com.au)

**Email:** [info@arena.com.au](mailto:info@arena.com.au)

## **Stock exchange listing**

Arena REIT stapled securities are listed on the  
Australian Securities Exchange (ASX)

