

## FOLKESTONE EDUCATION TRUST RESULTS FOR THE YEAR ENDED 30 JUNE 2016

Folkestone Investment Management Limited as Responsible Entity of the Folkestone Education Trust ("FET" or the "Trust") provides the results of the Trust for the year ended 30 June 2016.

### KEY HIGHLIGHTS FOR THE YEAR

- Statutory profit of \$106.8 million, an increase of 20.5% from \$88.6 million in the previous corresponding period ("pcp")
- Distributable income of \$34.5 million, an increase of 16.2% on pcp
- Distribution of 13.4 cents per unit ("cpu"), an increase of 4.7% on pcp
- NTA per unit of \$2.14, an increase of 17.6% from 30 June 2015
- Total Unitholders' return<sup>1</sup> for the year to 30 June 2016 of 34.8%
- New debt facilities were entered into with ANZ and HSBC resulting in the Trust having an average debt maturity of 4 years
- Development pipeline of 18 centres with a total value of \$103.4 million. Six development sites commenced operations during the year with a completion value of \$26.3 million

### FINANCIAL SUMMARY

The tables below summarise the Trust's results in comparison to the pcp:

INCOME SUMMARY	JUNE 16	JUNE 15	VAR. %
Total Operating Revenue (\$m)	62.1	54.7	13.5
Total Operating Expenses (\$m)	27.6	25.0	10.4
Distributable Income (\$m)	34.5	29.7	16.2
EPU <sup>2</sup> (cpu)	14.0	13.3	5.3
Distribution (cpu)	13.4	12.8	4.7
Statutory Profit (\$m)	106.8	88.6	20.5

BALANCE SHEET SUMMARY AS AT	JUNE 16	JUNE 15	VAR. %
Total Assets (\$m)	753.6	654.5	15.1
Investment Properties <sup>3</sup> (\$m)	719.5	627.3	14.7
Borrowings <sup>4</sup> (\$m)	200.4	193.2	3.7
Net Assets (\$m)	531.8	445.0	19.5
Gearing <sup>5</sup> (%)	26.6	29.5	(2.9)
Units on Issue (m)	248.2	245.2	1.2
NTA per Unit (\$)	2.14	1.82	17.6

<sup>1</sup> Total return includes distributions and change in unit price for the year. Source: UBS Australian A-REIT Month in Review – June 2016.

<sup>2</sup> Distributable income dividend by weighted average number of Units.

<sup>3</sup> Includes \$1.7 million of transaction costs in relation to properties contracted and not settled.

<sup>4</sup> Borrowings as at 30 June 2016 include loans of \$193.0 million and bank overdraft of \$7.4 million.

<sup>5</sup> Gearing is calculated by borrowings / total assets.

## PORTFOLIO PERFORMANCE

Key portfolio performance criteria in comparison to the pcp:

AS AT 30 JUNE	JUNE 16	JUNE 15	VAR. %
Value of Investment Properties (\$m)	717.8	627.0	14.5
Current Annual Property Income (\$m)	53.8	50.5	6.5
Average Lease Income Increase (y-o-y) (%)	2.8	2.4	0.4
Property Yield – Freehold Properties (%)	7.0	7.8	(0.8)
Property Yield – Leasehold Properties (%)	13.7	13.3	0.4
Property Yield – Total <sup>6</sup> (%)	7.3	8.0	(0.7)
Occupancy Rate (%)	99.5	99.7	(0.2)
Weighted Average Lease Expiry (yrs) (by income)	8.2	7.9	3.8

## PROPERTY SUMMARY

The Trust's property portfolio as at 30 June 2016:

PROPERTY PORTFOLIO	NO. OF PROPERTIES	CARRYING VALUE (\$m)	CURRENT ANNUAL INCOME (\$m)
Australia – Childcare	334	612.2	46.4 <sup>7</sup>
New Zealand – Childcare	51	61.8	4.5 <sup>8</sup>
<b>Total Childcare</b>	<b>385</b>	<b>674.0</b>	<b>50.9</b>
Medical Centre	1	11.4	0.7
<b>Total Improved Properties</b>	<b>386</b>	<b>685.4</b>	<b>51.6</b>
Development Sites (Settled)	8	32.4	2.2 <sup>9</sup>
<b>Total Properties</b>	<b>394</b>	<b>717.8</b>	<b>53.8</b>

## TRUST PERFORMANCE

FET paid distributions to investors of 13.4 cpu for the year, an increase of 4.7 per cent from the prior year.

FET provided a total return of 34.8 per cent for the year to 30 June 2016, outperforming the S&P/ASX 300 A-REIT Accumulation Index ("Index") return of 24.6 per cent for the same period. FET has also significantly outperformed the Index over three years at 32.8 per cent per annum (v 18.5 per cent per annum) and five years at 37.4 per cent per annum (v 18.0 per cent per annum).

FET's market capitalisation increased from \$515 million at 30 June 2015 to \$663 million at 30 June 2016.

<sup>6</sup> Includes all properties within the portfolio including those completed during the year.

<sup>7</sup> Includes head-lease rent on leasehold properties of \$1.18 million.

<sup>8</sup> Based on NZD rent of \$4.7 million at an exchange rate of 1.0451 as at 30 June 2016.

<sup>9</sup> Site rent charged on 6 development sites. Site rent to commence on 1 site following receipt of Development Approval. 1 site does generate site rent during the construction phase.



## PROPERTY PORTFOLIO

Key highlights in relation to the property portfolio during the year were as follows:

- 61 of 69 five year options were renewed, effectively increasing the term remaining on these leases from 5 to 10 years. The remaining 8 properties are currently being reviewed by management with negotiations underway on a number of the assets to provide the best outcome to the Trust;
- market rent reviews were negotiated in respect of 65 leases achieving an overall increase of 5.5% over the previous year's rental. This growth is further supported by the continued rise in daily fees per place. Of these, 51 reviews were subject to a cap of 5.0 per cent over the previous year's rent and achieved an average 4.6 per cent increase on 41 Australian assets, and a 5.0 per cent increase on 10 New Zealand assets, with the remaining 14 reviews not subject to a cap achieving an average 8.3 per cent increase;
- the WALE of the portfolio increased from 7.9 years at 30 June 2015 to 8.2 years at 30 June 2016 due to new centre completions and lease extensions;
- acquired four existing childcare centres (value of \$12.8 million) of which two settled in FY16;
- settled the disposal of six properties totalling \$9.5 million at an average yield of 7.0 per cent and a 25.3 per cent premium to carrying value at 30 June 2015;
- six centres developed by FET commenced operations with a completion value of \$26.3 million; and
- four development sites settled with a total completion value of \$24.7 million.

## PROPERTY VALUATIONS

During the year, a total of 351 childcare properties and one commercial property in the portfolio were revalued. Of these, 125 properties were independently revalued as part of the Trust's three year independent rolling valuation cycle and 227 were Director's valuations. The Director's valuations were adopted utilising the parameters drawn from the current independent valuations to ensure a consistent valuation methodology across the portfolio.

The outcome is an overall increase of \$72.8 million over the previous carrying values. This result is a function of on-going yield compression in the marketplace driven by continued market recognition and investor appetite for this asset class, combined with growth in income from annual and market rental increases.

The largest increases of the freehold independent valuations occurred in Victoria (17.6 per cent), South Australia (16.8 per cent), New South Wales (16.0 per cent), and Queensland (11.3 per cent). The overall passing yield achieved on the freehold independent valuations was 6.9 per cent, a 90 basis points improvement on the passing yield on these same assets as at 30 June 2015.

Overall yield compression achieved on the portfolio for the year to 30 June 2016 was 70 basis points on 30 June 2015, reducing the overall yield from 8.0 per cent at 30 June 2015 to 7.3 per cent at 30 June 2016.



## ACQUISITIONS

FET's pipeline consists of development sites as well as the purchase of existing centres. The total pipeline value is now \$109.9 million that comprises development sites (\$103.4 million) and further existing centre acquisitions (\$6.5 million) where the sites are owned by FET or a contract of sale/exclusivity agreement has been executed.

### *Development Sites*

At 30 June 2015, FET owned 12 development sites. During the year, FET settled four more development sites with an aggregate completion value of \$24.7 million. Six development sites commenced childcare operations with a completion value of \$26.3 million. All completions were on time and on/under budget and yielded an overall development margin of approximately 16%.

During FY16, FET contracted a further ten development sites, all with committed leasing arrangements, with a completion value of \$46.9 million with settlement of the sites due to occur in FY17. In addition, two development sites at North Manly and Frenchs Forest, which will not proceed to development due to unexpected planning constraints, have been sold with the proceeds exceeding all costs incurred by FET in relation to these sites.

DEVELOPMENT SITES	NO. OF PROPERTIES	UPON COMPLETION VALUE (\$m)
Settled as at 30 June 2015	12	66.2
Settled FY16	4	24.7
Less completed development sites FY16	(6)	(26.3)
Less sold development sites FY16	(2)	(8.1)
<b>Net Settlements as at 30 June 2016</b>	<b>8</b>	<b>56.5</b>
New Sites Contracted / Heads of Agreement executed	10	46.9
<b>Total "Upon Completion"</b>	<b>18</b>	<b>103.4</b>

The current development pipeline of 18 sites when complete, will generate a net rental income of approximately \$7.2 million, an increase of approximately 14 per cent on FET's existing lease income (excluding site rent payable during the construction period) and have an upon completion value of \$103.4 million. FET receives a site rental during the construction period on its accruing investment.

### *Existing Centres*

In FY16, FET settled the acquisition of two operating centres with a value of \$6.4 million. A further two operating centres are contracted with a value of \$6.5 million and are due to be settled in the first half of FY17.

FET continues to target new opportunities based on our demographic led strategy, with a key focus on selecting high quality real estate supported by sound childcare demand and supply fundamentals. FET's acquisition programme is a key component of its strategy of enhancing the quality of the property portfolio and increasing earnings.



FET has also considered and assessed a number of stand-alone investment opportunities together with a portfolio of assets in Victoria & ACT and another portfolio in NSW, neither of which met FET's investment criteria.

## DISPOSALS

FET's capital and portfolio management strategy includes the selective sale of centres with proceeds redeployed to new asset purchases and/or developments.

FET settled the sale of six operating centres in the year ending 30 June 2016 totalling \$9.5 million. The sales achieved a 25.3 per cent premium to 30 June 2015 carrying value with an average passing yield of 7.0 per cent. This compares to the average yield on the same properties at 30 June 2015 of 8.8 per cent, an improvement of 180 basis points.

Subject to market conditions, it is expected that FET will dispose of a small number of centres during FY17.

## CAPITAL MANAGEMENT

### *Debt Funding*

In June 2016, the Trust successfully refinanced its \$227 million debt facility with Australia and New Zealand Banking Group Limited ("ANZ") and Hongkong and Shanghai Banking Corporation Limited ("HSBC") after the completion of a competitive process.

This replaced the previous \$193 million syndicated debt facility with National Australia Bank Limited ("NAB") and Australia and New Zealand Banking Group ("ANZ") which was due to mature in June 2017 and a separate facility of \$34.3 million with ANZ, assumed as part of the Folkestone Social Infrastructure Trust merger in January 2015, that was due to mature in July 2017.

The key feature of the new bilateral facilities is its two tranche structure split over three and five year terms. One tranche (\$113.5 million or 50 per cent) will mature in June 2019 and the second tranche (\$113.5 million or 50 per cent) will mature in June 2021, resulting in an increased weighted debt maturity of 4 years. Key covenants regarding LVR and ICR remain unchanged.

As at 30 June 2016, FET currently has \$193 million of drawn debt and undrawn capacity of \$34 million, which will be utilised to assist in funding future acquisitions and developments. Gearing as at 30 June 2016 is 26.6 per cent, which is below the targeted long term range of 30 - 40 per cent.

### *Hedging*

As part of FET's interest rate management policy, additional hedging positions were taken out, extending the hedge profile to June 2021, supplementing FET's existing positions from FY17 to FY20.

For FY17, 66 per cent of the drawn debt or \$127 million is now hedged at an average rate of 3.27 per cent per annum. The average hedging position over a five year period to June 2021 is 53 per cent hedged also at an average rate of 3.27 per cent per annum.



The hedging arrangements have been restructured by combining the existing positions with new longer-term positions, at lower rates. This strategy provides the benefits of lower overall hedged rates whilst avoiding any dilution of capital and NTA per Unit, which would result from breaking the existing hedges.

### **Cost of Debt**

As at 30 June 2016, based on the new debt arrangements, FET's cost of debt is 4.5 per cent per annum (30 June 2015: 4.6 per cent per annum), which is based on prevailing interest rates, existing swap arrangements and bank margins. The all-in-cost of debt is 4.8 per cent per annum (30 June 2015: 5.0 per cent per annum) which includes the amortisation of borrowing costs.

### **OUTLOOK AND DISTRIBUTION FORECAST**

The FY17 forecast distribution is estimated to be **14.2 cpu**, an increase of 6.0 per cent on the FY16 level of 13.4 cpu. The forecast is based on continued tenant performance. FET will continue to pay quarterly distributions, one month in arrears.

FET continues with its strategy to be recognised as the leading provider of childcare accommodation and together with quality operating partners, focusing on providing a healthy and safe environment for future generations. Investors benefit from predictable and secure long term cash-flows with the opportunity for capital growth.

FET is committed to active management of its portfolio to capitalise on future growth prospects. Unitholders should note that any investment opportunity is assessed with respect to its consistency with the Trust's characteristics and overall investment objectives.

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### **FURTHER INFORMATION**

#### **Folkestone Education Trust**

The Folkestone Education Trust is the largest Australian ASX listed (ASX:FET) real estate investment trust (A-REIT) that invests in childcare properties. [www.educationtrust.folkestone.com.au](http://www.educationtrust.folkestone.com.au)

#### **About Folkestone**

Folkestone (ASX:FLK) is an ASX listed real estate funds manager and developer providing real estate wealth solutions. Folkestone's funds management platform, with more than \$1 billion under management, offers listed and unlisted real estate funds to private clients and select institutional investors, while it's on balance sheet activities focus on value-add and opportunistic (development) real estate investments. [www.folkestone.com.au](http://www.folkestone.com.au)