ASX Announcement
4 November 2014

INTERNALISATION PROPOSAL

Creating Enhanced Alignment and Competitive Advantages

- Arena REIT to internalise its management structure subject to certain conditions precedent including ARF investors (Investors) approval.
- Expected uplift in future earnings with FY15 distribution guidance upgraded to 10.0[1] cents per security.
- Independent Expert has concluded that the Internalisation Proposal is "fair and reasonable and in the best interests"[2] of Investors.
- Arena's Independent Directors unanimously recommend that Investors vote in favour of the Internalisation Proposal, in the absence of a superior proposal.
- Meeting Booklet issued today for an Investor meeting scheduled for 5 December 2014.

Arena Investment Management Limited (**Arena**), as responsible entity of Arena REIT (**ARF**) today announced the execution of an Implementation Agreement with Citrus II Investments Pty Ltd (**Citrus II**), the ultimate owner of Arena, to internalise ARF's corporate governance and management functions and to assume the management rights of two unlisted wholesale syndicates, being PHC Darlinghurst Syndicate and Trust (**PHC**) and BSH Joint Venture (**BSH**) (**Internalisation Proposal**).

The independent chairman of Arena, Mr David Ross said, "We are very pleased to have reached an agreement in relation to the internalisation of Arena REIT's governance and management arrangements. The Independent Directors consider that internalisation will better position ARF to continue to deliver attractive returns to investors."

Mr Ross continued, "Since the announcement of the internalisation opportunity with our FY14 results in August, feedback from investors has been supportive and ARF's ASX price increase has reflected this."

Proposal Overview

The Internalisation Proposal will enhance alignment of Board and management with Investors' interests and will be implemented via:

- the distribution to Investors of one fully paid ordinary share in Arena REIT Limited (**ARL**) for each existing stapled security in Arena REIT (**Existing Stapled Security**);
- the stapling of each share in ARL to each Existing Stapled Security to form a new stapled security;

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[1] Assuming the internalisation proposals proceeds, no new acquisitions, developments in progress are completed in line with budget assumptions and tenants comply with all their lease obligations.
[2] Refer KPMG Independent Expert Report dated 24 October 2014, page 3

- the acquisition by ARL of Citrus Investment Services Pty Ltd (**CISL**) (and its wholly owned subsidiaries Arena REIT Management Limited (**ARML**) and Arena Property Services Pty Ltd) from Citrus II; and
- the change of the responsible entity of ARF (and the manager of PHC and BSH) from Arena to ARML.

The key elements of the Internalisation Proposal include:

- **Consideration** - ARF is to pay consideration to Citrus II which implies a purchase price of approximately $10.7 million for the ARF and wholesale funds management (intangible) rights (reflecting 2.8% of Assets Under Management or a multiple of 3.4 times base fees) plus net asset adjustments of approximately $0.8 million in relation to all other operating assets and liabilities of the management business such as intellectual property, IT systems, office equipment, syndicate receivables and other working capital balances. As a consequence, ARF will no longer pay ongoing funds management and transaction fees to an external manager[3]. The consideration will be funded utilising ARF's existing debt facility.
- **Quality Management Team** – Post internalisation, the new ARF Board will comprise the current independent directors and Bryce Mitchelson as Managing Director (current Joint Managing Director of Arena). In addition, other senior staff of Arena including Gareth Winter (CFO) and Rob de Vos (Head of Property) have accepted employment with ARF, subject to the Internalisation Proposal proceeding.
- **No Change in "Social Infrastructure" Strategy** – ARF's existing investment strategy will essentially not change and will remain focussed on investing in social infrastructure style property, including childcare and healthcare assets. ARF will also assume the management rights to two well performing wholesale funds (invested in healthcare assets) and may seek to grow earnings further by leveraging its existing capabilities by providing funds management and property services to other unlisted managed funds.
- **Retain Existing Name & Branding –** ARF will retain the existing Arena brand, investor goodwill and intellectual property built up over the past few years.
- **Other Management Services –** CISL will provide management services to Arena for its remaining unlisted managed funds for a period to no later than 31 December 2016. Certain CISL employees will be retained to provide these services and all costs associated with these management services will be reimbursed to ARF.

The annualised pro-forma FY15 savings in net operating cost cash flows is estimated at $0.8 million, increasing to $1.1 million when potential management fee income is included[4]. Taking into account the interest expense for funding the consideration of $0.4 million, the incremental benefit reduces to $0.7 million. The financial benefits of the Internalisation Proposal are more significant if ARF grows its total assets under management. The cost incurred in presenting the Internalisation Proposal to Investors is estimated at $0.8 million (excluding costs associated with evaluating any alternative proposals).

Following implementation of the Internalisation Proposal, ARF's pro-forma gearing (as at 30 June 2014) is expected to increase to 36.7%, net assets per security will be $1.12 and Net Tangible Assets per security will reduce to $1.07 due to the acquisition of the management rights. The

[3] ARF paid total external funds management and transaction fees of $3.3 million during FY14.
[4] Refer KPMG Corporate Finance Report page 32

proposed change in operating structure also introduces different risks which are explained in the Explanatory Memorandum.

The Implementation Agreement sets out the agreed terms and conditions for the implementation of the Internalisation Proposal, including regulatory and other approvals required. The Meeting Booklet includes a summary of the Implementation Agreement and includes details of the conditions of the Internalisation Proposal, exclusivity provisions and the termination rights of the parties.

Internalisation Precedent Conditions

The Internalisation Proposal remains subject to the following key conditions:

- Investor approval of the Internalisation Proposal;
- The Independent Expert does not change their opinion that the Internalisation Proposal is "fair and reasonable and in the best interests of" Investors;
- No superior proposal;
- ASIC issuing a new Australian Financial Services Licence to ARML in an appropriate form; and
- All required consents of financiers being obtained.

Other alternatives considered

In considering the Internalisation Proposal and in forming the view that the Internalisation Proposal is in the best interests of Investors, the Independent Directors have had regard to possible alternatives, and the potential implications of these alternatives for Investors. In particular, the Independent Directors have considered the merits and risks of:

- the prospect that Citrus II (as the owner of Arena) may sell the management rights of ARF to another third party external manager; and
- the potential merger of ARF with another listed A-REIT.

On 29 September 2014, ARF received an indicative, non-binding, conditional proposal for the potential merger of ARF and the ASX-listed Folkestone Education Trust (**FET**) (FET Indicative Offer).

Under the FET Indicative Offer, ARF Investors would have received 0.795 FET units for every Existing Stapled Security. Folkestone Investment Management Limited would have externally managed the merged entity with base management fees of 0.45% of gross assets (with the intention of further reductions as the vehicle grows past certain thresholds) and removal of Arena asset acquisition, disposal and performance fees. Implementation of the FET Indicative Offer would have required a trust scheme or stapling of units, requiring the approval of ARF Investors and possibly also FET investor approval.

The FET Indicative Offer was subject to several conditions including due diligence and final approval from FET independent directors.

The Arena Independent Directors determined that the FET Indicative Offer did not provide ARF Investors with a compelling value proposition compared to the Arena Internalisation Proposal. Moreover, in the event that the Arena Internalisation Proposal is approved by Investors, the ARF Board will retain the ability to pursue strategic initiatives that are in the best interests of Investors.

Independent Expert Report prepared

The Independent Directors appointed KPMG Corporate Finance to prepare an independent expert's report to opine on the Internalisation Proposal. The Independent Expert assessed that the present value of the net financial benefits from the Internalisation Proposal is greater than the consideration to be paid[5] and the consideration is in line with comparable transactions. Their conclusion is that the Internalisation Proposal is "fair and reasonable and in the best interests" of Investors. A full copy of this report is contained in the Meeting Booklet being provided to Investors.

ARF Investor meeting to be held

The Arena Independent Directors have today called an Investor meeting scheduled to be held in Melbourne at 11am (AEST) on 5 December 2014 to consider and vote on three ordinary resolutions, two to give effect to the Internalisation Proposal and the other to vote on the issue to the Managing Director, Bryce Mitchelson, of rights to Arena New Stapled Securities under the Arena Long Term Incentive Plan. Full details in relation to the Internalisation Proposal and Investor meeting are contained in the Meeting Booklet comprising the explanatory memorandum, notice of meeting and prospectus (separately announced to ASX today).

The Arena directors strongly encourage Investors to read the Meeting Booklet and vote on the Internalisation Proposal.

Arena Independent Directors unanimously recommend Investors vote in favour

The Independent Directors of Arena have unanimously recommended that Investors vote in favour of each resolution for the Internalisation Proposal, in the absence of a superior alternative. The Independent Directors consider the potential key benefits of the Internalisation Proposal include:

- expected ongoing net management cost savings contributing to ARF distribution guidance for FY15 being upgraded to 10.0[6] cents per security (up from 9.75 cents per security);
- greater alignment of interests through the new ARF Board and management being accountable only to Investors; and
- a superior outlook for ARF earnings growth per security with the elimination of external management fees which would otherwise be charged on any increases in portfolio valuations, new acquisitions and capital expenditure. An internalised ARF will have operating leverage, meaning, that new acquisitions should not require a material increase in internal management cost which should therefore provide greater contributions to earnings growth per security.

Key Dates

The indicative timetable for the Internalisation Proposal is provided in the Meeting Booklet. If all the conditions precedent are satisfied, the Internalisation Proposal is scheduled to be implemented on 12 December 2014.

[5] Refer KPMG Independent Expert Report page 44
[6] Assuming the Internalisation Proposal proceeds, no new acquisitions, developments in progress are completed in line with budget assumptions and tenants comply with all their lease obligations.

About Arena REIT

Arena REIT (ASX code ARF) is an S&P/ASX 300 listed stapled group with a strategy to invest in sectors such as childcare, healthcare, education and government tenanted facilities leased on a relatively long term basis. ARF owns 178 childcare centres, 11 development sites (with a further 4 under contract) and 7 multi-disciplinary medical centres situated throughout Australia with an aggregate value of over $364 million as at 30 September 2014. Distributions are paid to investors on a quarterly basis.

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The information in this document should be read together with the Meeting Book (containing a Notice of Meeting and Explanatory Memorandum and Prospectus) dated on the date of this document.

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