ELITE COMMERCIAL REIT

(a real estate investment trust constituted on 7 June 2018
under the laws of the Republic of Singapore)
(Managed by Elite Commercial REIT Management Pte. Ltd.)

RESPONSE TO QUERIES BY SECURITIES INVESTORS ASSOCIATION (SINGAPORE)

The Board of Directors of Elite Commercial REIT Management Pte. Ltd. (as Manager of Elite Commercial REIT) wishes to announce the following responses to the queries raised by Securities Investors Association (Singapore):

<u>Question 1</u>

For the financial year ended 31 December 2022, income available for distribution was £23.1 million, a 5.8% decrease compared to the previous year. Distribution per unit experienced a greater decline of 11.4%, from 5.43 pence to 4.81 pence. The net asset value per unit dropped by 14.8% to £0.52. Some key financial highlights are reproduced below (page 3):

(Adapted from annual report)

In the letter to unitholders, it was said that "… executed well on its strategies… the REIT managed to withstand challenges throughout the year, the manager also delivered a set of resilient results in FY 2022…"

However, net asset value per unit has decreased from £0.65 in 2020 to £0.61 in 2021, and further to £0.52 in 2022. The portfolio value has also dropped from £500.1 million in 2021 to £466.2 million. The total net fair value losses in the past two years add up to £(69.6) million.

Details of the properties can be found in the Portfolio overview/profiles sections on pages 40 to 63.

(i) Can the manager help unitholders better understand the reasons for the decline in portfolio value even though the properties are underpinned by robust leases (triple net lease), strong tenant profile, good location and primarily freehold tenures?

Manager's Response: The portfolio valuation in the UK is derived based on income capitalisation method, which takes into account the net operating income and market-derived capitalisation rate as at the time of valuation. Besides the 12 assets which are vacant and vacating as at 31 December 2022, the income profile of the other assets remains largely unchanged. However, the impact from other macroeconomic factors, such as the Bank of England's interest rate hikes, has been considered by our valuer in the 31 December 2022 valuation.

The market value of the investment properties as at 31 December 2022 was based on independent professional valuations undertaken by Knight Frank LLP. The decline in portfolio value is mainly attributed to widely reported market factors, including the impact of rising interest rates on financing cost, which has resulted in weaker demand for real estate investment and declining transaction volumes. The impact of rising construction costs on refurbishment and redevelopment projects has caused values for vacant and vacating assets to be impacted as well.

(ii) Out of the 155 properties owned by the REIT, how many of them have a carrying value above its purchase price?

Manager's Response: As stated in the portfolio valuation as at 31 December 2022, 29 (or 18.7%) of the assets in the REIT's portfolio have a carrying value above its purchase price. Based on the income capitalisation method of property valuation, with the normal passing of time, the amount of income that could be derived from the assets is pro-rated accordingly. Depending on the macroeconomic conditions and comparative transactions in the market at the time of valuation, the market-derived capitalisation rate could impact the independent valuer's opinion of the assets' carrying values.

(iii) In particular, the valuations of Sidlaw House, Dundee and John Street, Sunderland have dropped by 70% and 64% from £6.0 million to £1.8 million and from £1.41 million to £0.5 million respectively. Is there a material risk that the carrying values of the properties have been overstated? What measures can the independent directors undertake to enhance the transparency and reliability of the asset valuations, and thereby provide greater assurance to unitholders and the capital market?

Manager's Response: As stated in the response to part (i), the valuation was based on independent professional valuations undertaken by Knight Frank LLP and the valuation exercise is based on the income capitalisation method and takes into consideration the macroeconomic conditions and the income profile of the assets as at the date of valuation. In addition, Knight Frank LLP has made assessments based on a collation and analysis of appropriate comparable investment and rental transactions, together with evidence of demand within the vicinity of the subject properties. Hence, it is common for asset valuation to fluctuate based on the remaining lease tenure of the assets and the existing macroeconomic conditions at the time of valuation.

As stated on Page 140 of the Annual Report, the Audit and Risk Committee ("**ARC**") has reviewed the independence and competency of the external valuer and the appropriateness of the valuation methodology applied by the valuer in arriving at the fair value of the investment properties based on their existing use.

The ARC has also reviewed the valuation reports and held discussions with Management and the external auditors in reviewing the reasonableness of the key assumptions and the underlying key data including the yield rates used in the valuation and the comparable market data provided by the valuer. The ARC noted that the valuation report has been prepared in accordance with the Royal Institution of Chartered Surveyors' RICS Valuation – Global Standards (incorporating the International Valuation Standards). The ARC has held discussions with Knight Frank LLP, the valuer for the REIT's portfolio, to understand the basis of key assumptions applied by the valuer.

The Manager is of the view that the carrying values have been stated fairly at the point of valuation.

The Manager provides regular and timely reporting, so that the Unitholders and the wider investing community can be kept abreast on the material matters affecting the business and their investments.

(iv) What is the REIT's current acquisition strategy and how does the board provide guidance on property valuations and market cycles?

Manager's Response: The Manager continues to monitor the macroeconomic as well as local UK real estate market conditions closely when undertaking evaluation of any acquisition opportunity on a case-by-case basis, either from the Sponsors' Right of First Refusal ("**ROFR**") pipeline or from the third-party market. The fundamental criteria for acquisition remain clear that the transaction should deliver sustainable value to Unitholders.

The Manager provides regular and timely reporting, so that the Unitholders and the wider investing community can be kept abreast on the material matters affecting the business and their investments.

(v) Does the board have concerns regarding the REIT's high aggregate leverage of 45.8%, especially with ten assets set to be vacated in 2023? Is an equity fundraising being considered to strengthen the balance sheet?

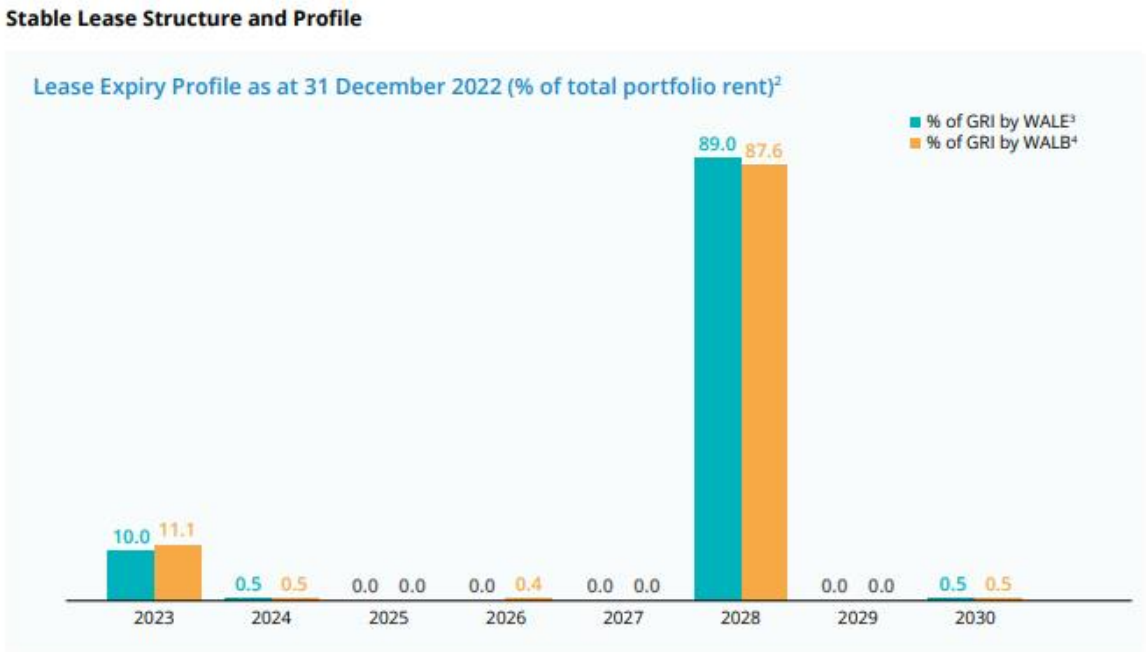
Manager's Response: The Manager is cognisant of the concerns of Unitholders with regard to the aggregate leverage, which was a result of the lower valuation as at 31 December 2022, amidst a rising interest rate and rising inflation environment.

The Manager seeks to bring down the gearing to a more comfortable level of below 40% over time. Strategies to do so includes disposal of non-core or non-income producing assets and using the proceeds to pare down debts, issuing perpetual securities (which can be accounted as Equity, subject to certain conditions) or traditional equity fundraising.

The Manager will assess the options and consider the prevailing market conditions to derive an optimal strategy for reducing aggregate leverage.

Question 2

The lease expiry profile of the REIT is shown below:



(Source: Annual Report)

(i) Can the manager confirm that the tenant(s) accounting for 11.1% of the total REIT's portfolio based on FY2022's gross rental income (by WALB) will be vacating the properties?

Manager's Response: The Manager has previously announced that a total of 10 assets that would be vacating in FY 2023. These 10 assets constitute 7.8% of the 11.1% stated in the above chart. The remaining 3.3%, as at 31 December 2022, are existing leases which are in discussions for potential renewals or extensions.

(ii) Two assets are currently vacant and 10 more assets are expected to be vacated in FY2023. Can the manager provide details of the ten properties expected to be vacated in FY2023, and explain the strategy for leasing them out given the current weak market sentiment?

Manager's Response: For the 10 assets that are expected to be vacated in FY 2023, the Manager continues to actively explore a variety of alternative options for these assets subject to market demand and conditions of the respective areas. These include:

- Negotiating for reasonable dilapidations settlement
- Potential re-letting as an office or other uses
- Disposal with vacant possession or following re-letting
- Seeking consent for alternative uses (conversion or redevelopment)

To ensure the best outcomes, we actively formulate asset management strategies specific to each asset, with the focus on maximising value outcomes and minimising holding costs. This involves consultation with our network of local advisors who assist in any future re-letting, conversion or redevelopment and/or disposal strategies.

Eight of the 10 assets were returned to the REIT on 31 March 2023. Below is the summary update for the 10 assets:

	Asset	**Dilapidation Settlement**	**Lease Extension**	**Re-letting/ Repositioning/ Disposal**
1	Ladywell House, Edinburgh	In Progress	6-months to July 2023	Marketing agent appointed
2	Hilden House, Warrington	Agreed	6-months to September 2023	Marketing agent appointed
3	Cardwell Place, Blackburn	Agreed	-	Marketing agent appointed
4	Leeds Road, Bradford	Agreed	-	Marketing agent appointed
5	Victoria Road, Kirkcaldy	In Progress	-	Marketing agent appointed
6	Openshaw Job Centre, Manchester	Agreed	-	Marketing agent appointed
7	Lindsay House, Dundee	In Progress	-	Marketing agent appointed
8	Crown Buildings, Caerphilly	In Progress	-	Marketing agent appointed
9	Crown House, Burton On Trent	In Progress	-	Marketing agent appointed
10	St Paul's House, Chippenham	In Progress	-	Marketing agent appointed

The Manager is cognisant of the local market leasing conditions of the market and will rely on expert local knowledge to implement suitable strategies to maximise value and minimise holding costs.

(iii) What is the estimated capital expenditure required to renovate and/or reposition the assets that are currently vacant or expected to be vacated in FY2023?

Manager's Response: In theory, the dilapidations claims represent the estimated capital expenditure required for each individual assets as assessed by the Landlord's independent surveyor. In practise, tenants do have the right to dispute or negotiate these claims. The Manager do not expect the capital expenditure budget to exceed the proceeds generated from the dilapidations settlements.

(iv) It was mentioned in the letter to unitholders that "vacancy holding costs" are expected to increase. Considering the expected increase in vacancy holding costs, what strategies are available to the manager to maintain or increase the total income available for distribution?

Manager's Response: The Manager focuses on efficient settlement of dilapidations claims and early engagement with local agents to determine if assets should be repositioned, in order to be re-let, or disposed of, in order to maximise value and minimise hold costs.

Potential tailwinds to maintain or increase the total income available for distribution includes:

- Majority of the REIT's existing assets will benefit from the rent escalation in April 2023, which would increase the revenue for the REIT.
- Potential recycling of capital from vacant and vacating assets to pare down debt and lower interest costs for the REIT.
- Value-enhancing acquisitions that complement the REIT portfolio.

(v) Can the manager provide a restatement of its track record and collective experience of the manager (including the directors) in the UK market? In addition, could the manager explain the challenges faced in leasing out Sidlaw House and John Street, given that both properties have been vacant for nine months and twelve months respectively?

Manager's Response: The Chief Investment Officer of the Manager, Jonathan Edmunds, has about 20 years of real estate experience and an extensive investment and asset management track record in the UK. The Manager subcontracts property management work to ERES UK Ltd, who is part of the sponsor group. ERES UK Ltd currently employs a team of three experienced asset managers, two of whom have more than 15 years each of relevant UK real estate office market experience. JLL, a globally recognised real estate consultancy, supports the REIT with rent collection, asset inspection and preparation of property reports.

Below is the summary update for the 2 assets:

	Asset	**Dilapidation Settlement**	**Re-letting/ Repositioning/ Disposal**
1	John Street, Sunderland	Agreed	Disposal in progress
2	Sidlaw House, Dundee	In Progress	Marketing agent appointed

The regional sub-markets where these assets are located has seen weaker demand for commercial real estate, resulting in challenges faced in re-letting these assets.

<u>Question 3</u>

As disclosed in the corporate governance report, the internal audit function of the group is outsourced to Ernst & Young Advisory Pte. Ltd. The internal auditor adopts the Standards for the Professional Practice of Internal Auditing set by the Institute of Internal Auditors. The internal auditor is independent of management and reports directly to the chairman of the audit and risk committee (ARC).

It was further disclosed that the internal auditors completed review of the overall control environment, cash and bank management, network security and sustainability reporting.

(i) What were the key findings and recommendations by the internal auditor for FY2022?
(ii) How was the internal audit carried out for these foreign subsidiaries?
(iii) What is the level of oversight by the ARC on the actions taken by management to follow up on the recommendations?

Manager's Response:
The scope of work that was covered by the internal auditor for FY2022 includes (i) General Control Environment, (ii) Cash and Bank Management, (iii) Network Security, and (iv) Sustainability Reporting.

As part of the evaluation process, the internal auditor will assign the following priority ratings for findings identified during the internal control review:

Priority	Definition
High	A finding, which as a material impact on internal control, finance or operations and is time sensitive to the organisation. It requires the immediate attention of department and senior management. There should be a priority action for its resolution.
Moderate	A finding of moderate significance to the organisation. It requires the attention of the responsible department management within a reasonable timeframe (generally less than 3 months). There should be an agreed program for its near term resolution.
Low	A finding of lesser significance. It does not warrant immediate attention; however, there should be an agreed program for ultimate resolution (generally within 6 months).

No findings and recommendations were raised for (i) General Control Environment and (ii) Cash and Bank Management segments of review.

There were no findings on the other two segments which are assessed as High.

The internal audit focused on the REIT as a whole and was performed through interviews and review procedures conducted both physically and virtually, where applicable.

The internal findings and recommendations were presented at the respective ARC sessions. ARC members note the findings and ensure that the recommendations and corresponding management actions are completed in a timely manner.

BY ORDER OF THE BOARD
Shaldine Wang
Chief Executive Officer

Elite Commercial REIT Management Pte. Ltd.
(Company registration no. 201925309R)
as manager of Elite Commercial REIT

24 April 2023

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