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RENTAL MANAGEMENT INVESTMENT TRUST

Unique, high income investment in Australia's residential rental property market

DIRECTORS OF THE RESPONSIBLE ENTITY

s 47F [redacted]

MARKET DATA

ASX Code:	RTI
Current Price:	$1:00
Market Capitalisation:	$13.3 million
Enterprise Value:	$14.4 million

CAPITAL STRUCTURE

Shares on Issue:	13.27 million

FINANCIAL SUMMARY

$mill	31 July 2013
Net Debt	1.1
Unitholders Equity	12.4
Total Assets	14.1

MAJOR SHAREHOLDERS

Sterling First Group	14.1%
RMA Consolidation Pty Ltd	13.5%

CORPORATE DETAILS

Unit 23, 397 Warnbro Sound Avenue
Port Kennedy, WA, 6172
Ph: 1300 440 166
www.thetaasset.com.au

KEY POINTS

- RMIT owns 1,700 rental management agreements in WA from which it generates income from sharing (45%) the management fee with an independent property manager.
- The RMIT portfolio has been established through the acquisition of three (soon to be four) agency businesses managing rent rolls. Acquisitions will be the primary source of growth for the portfolio.
- Australia's 10,000 real estate agencies manage In excess of 1.5 million residential properties. Most rent rolls are small and there are considerable opportunities for market consolidation.
- A return to investors of in excess of 9% of FUM is targeted with additional tax deferred benefits expected to flow to investors.
- The Trust, together with its alliance partner Sterling First Group (business development, property management and investment management) is well placed to participate in the consolidation of Australia's highly fragmented rental property management industry.
- Agreements are in place with Sterling First Group to secure rental management agreements to replace the annual churn and to grow the number of rental management agreements through organic growth.
- The average life of an RMA is 8 years, with churn primarily due to the sale of the property by the owner.
- The replacement of the annual churn will be funded from the cash flow of the Trust, thereby preserving the capital base, and additional growth will be funded by a mix of debt and new equity.

INVESTMENT PROPOSITION

RMIT provides investors with a unique exposure to Australia's residential property market through investment in a highly diversified portfolio of rental management agreements (RMAs) that provide a high quality, reliable income stream.

Whilst very low income yields have made residential property ownership an unattractive option for a publicly listed investment vehicle, indirect exposure through investment in rental management agreements, which are linked to property rents and deliver yields comparable with retail, commercial or industrial property are a competitive alternative.

RMIT has been structured solely as an asset holding vehicle. Accordingly, with no operational exposure and a highly diversified portfolio, there will be relatively little risk to investor income. As the churn rate on the portfolio is about 10% to 12.5% per annum, the key risk will be management's ability to replace the churn from cash flows without adversely impacting investor income.

BUSINESS OVERVIEW

Rental Management Investment Trust (RMIT) is in the process of finalising a listing on the ASX having raised $13.3 million in pre-IPO funds. The Trust has been established to provide investors with high yielding exposure to Australia's residential property investment market through the ownership of rental management agreements (RMAs).

Property owners pay a management fee that varies according to property type and location but typically represents between 8% and 10% of the gross weekly rent generated by the property. This fee will be split between the property manager (55%) and RMIT (45%).

In return the property manager will provide a range of services including locating and screening suitable tenants, completion of the Tenancy Agreement and the lodging of rental bonds, collecting rents, pursuing late rent, repairs, periodic inspections and if required, the eviction of tenants.

The RMIT (Investment Trust) model is specifically designed to address major flaws in the publicly listed corporate model by primarily externalising all organic business development and business acquisition activities (with alliance partners) and by allowing the free cash flows to be distributed, unaffected by amortisation charges, to investors. The objective is to deliver a yield to investors in excess of 9.0% pa, which is expected to be boosted by ongoing deferred tax benefits.

The free cash flow to be distributed to unitholders is determined after an amount equal to the annual amortisation (over 8 years) of the cost of acquiring an RMA has been set aside. Accordingly, an internally generated pool of capital is accumulated for reinvestment in new RMAs to replace the annual churn and in this way the capital base is protected against erosion.

RMIT will purchase rental management agreements (organic business development) at 1.75 times the base management fee and it has the first right of refusal over portfolios of rental management agreements acquired through acquisition of rental management businesses at cost plus 0.25 times the base management fee (up to a maximum of 2.5 times the base management fee).

Sterling First Group is RMIT's cornerstone partner and will source RMAs for the portfolio as well as providing property management services. Although Sterling First Group is legally independent, the alliance effectively replicates an otherwise fully integrated property manager with strong growth aspirations.

RMIT has so far made three rent roll acquisitions covering some 1,700 rental management agreements in Western Australia, whilst a conditional contract has been signed with an agency in Mt Ommaney, Qld, which will add rental management agreements covering another 390 residential properties.

BUSINESS DRIVERS AND GROWTH PROFILE

Over 1 million residential rental properties in Australia are managed by real estate agents. Whilst some agencies manage a relatively large number of properties, most real estate agencies are primarily focussed on sales with property management a secondary concern. Accordingly, the service to landlords and tenants is mixed.

The Australian real estate agency market is highly fragmented with most suburbs around the country supporting several relatively small businesses primarily structured to sell residential properties. It is unclear as to exactly how many agency businesses there are, although it is generally accepted (based on a 2006 ABS survey) that there are about 10,000 of which about one-third are franchised. The rest are mostly independently operated. The franchise groups have clear advantages in terms of marketing and systems. The main national franchise groups are LJ Hooker, Ray White and Century 21, whilst there are many other regional or state based franchise groups.

What is clear is that the industry has shrunk over the past few years as sales activity has contracted. Under pressure from falling income, many individual agents have left the industry as income levels have fallen.

There are estimated to be over 2 million residential rental properties in Australia of which more than 70% are managed by agents. With base management fees varying from about 6.3% (of the underlying rent) in Sydney and Melbourne to nearly 9% in Perth, the fee income pool is about $1.2 billion.

Attempts have been made in the past to consolidate the rental management business with a view to enhancing the level of service with a high degree of consistency. Moreover, returns could be significantly increased through greater investment in systems and better overhead management. However, these attempts have generally met limited success and their growth is ultimately constrained due to some fundamental flaws in the business model.

The two most significant flaws are the high cost of securing new business from an internal business development team and the inability to capitalise those business acquisition costs. Internally driven business development is capital intensive with acquisition costs generally in the order of one year's gross fee income from that property. Some business growth can usually be funded from the cash flow of an established rental management portfolio, however, aggressive growth can only be funded from new equity or debt. And the Catch 22 is that new funding is very difficult to raise where profits are depressed due to the immediate expensing of business acquisition costs and where there is no balance sheet recognition of a valuable asset with a medium term life (typically about 8 years).

With a highly fragmented real estate agency industry where the largest provider of residential rental management services has maybe a 2% national market share and where only the larger groups generate decent margins there are considerable market consolidation opportunities. RMIT's alliance partner is ideally placed to drive this consolidation process with RMIT potentially being the holding vehicle for the underlying rental management agreement assets.

The residential rental property management market is huge; generating over $1 billion annual fee income. However, there are relatively few managers of significant size and the largest group, believed to be Real Estate Corp (ASX:RNC) has less than 2% market share, nationally. Barriers to entry are relatively low although the costs associated with developing and sustaining a high quality service are rising especially as systems and technology increasingly underpin that service. It is expected that the property management industry will progressively consolidate as smaller businesses face the combination of a profit squeeze and increasing technology costs.

The evidence strongly suggests that there are considerable scale benefits for both the property manager and the landlord. Smaller independent and regional agencies look to be the most vulnerable. In the current environment where sales commission income is still under considerable pressure there may be some resistance to selling rent rolls, especially if property management income is rising, but we would expect agencies to more actively exit property management as property sales rates recover.

FINANCIAL SUMMARY

BALANCE SHEET	
($'000)	**31 July 2013**
Current Assets	
Cash & Equivalents	316
	316
Non-Current Assets	
Rental Mgt Agreements	9,742
Pref Shares in Sterling First Group	4,000
Other	
Total Assets	14,058
Current Liabilities	
Payables	53
Provision - Distribution	165
Other	
	218
Non-Current Liabilities	
Financial Liabilities	1,400
Other	
Unitholders' Equity	12,440
Liabilities & Equity	**14,058**

The RMIT and its pre restructure predecessor have been in operations since February 2012 and have made seven quarterly distributions to unitholders as follows:

PRE RESTRUCTURE					POST	
Apr 12	July 12	Oct 12	Jan 13	Apr 13	July 13	Oct 13
2.5¢	2.5¢	2.3¢	2.3¢	2.3¢	2.3¢	2.3¢
10.1%	10%	9.25%	9.25%	9.25%	9.25%	9.25%

Commentary

As RTI is in the process of listing on the ASX, it has yet to produce any trading results. Accordingly, the balance sheet data adjacent was produced for the PDS in support of the Trust's listing.

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