FINAL TRANSCRIPT

Thomson StreetEvents℠

Conference Call Transcript

FKP.AX - Interim 2011 FKP PROPERTY GROUP Earnings Presentation and Webcast

Event Date/Time: Feb 24, 2011 / 9:00AM AEDT

THOMSON REUTERS

CORPORATE PARTICIPANTS

Peter Brown
FKP Property Group - CEO

David Hunt
FPK Property Group - CFO

CONFERENCE CALL PARTICIPANTS

John Richmond
Merrill Lynch - Analyst

John Freedman
UBS - Analyst

Michael Scott
JP Morgan - Analyst

E Lewin
Macquarie - Analyst

Rohan Sundram
Austock - Analyst

PRESENTATION

Peter Brown - ***FKP Property Group - CEO***

Good morning everybody and welcome to the 2011 half year results for FKP. This morning in our presentation we'll be running through what I believe to be a very strong result. We'll firstly look at the overview of the half year result, followed by the divisional commentary. David Hunt, the Company's CFO will then be running us through the capital management and then I'll be concluding on the strategy and outlook before we open up the presentation for any questions that may arise.

In terms of the overview, as I alluded to, a strong first half performance very much driven by a lift in contributions as predicted from our residential community and our retirements business. The last six months has seen a further strengthening of our balance sheet with of course the issuance of the AUD125 million convertible bond as part of our retirement syndicate refinancing. It sees our gearing at 29% on 31 December with no material debt maturities until June 2012.

The outlook in terms of the residential assets that we have and of course those who have followed us for some time will know that the last few years has been very focused towards the residential asset side of things which includes the retirement of course, which is a subset of the residential assets and the last half year has seen three developments launched in the first half, being LUXE at Woolloomooloo, apartment building in Sydney, The Milton at Milton up in Brisbane and The Rochedale Estates, the large estate that we have in Brisbane.

I talked last year about the real goal, this time last year about the real goal for FKP being restarting the motor and I think what you'll see as we go through this presentation that we're well and truly doing that and we need to continue moving forward.

Our Brisbane assets were largely unaffected by the recent flooding. I can't quite say the same about the Brisbane market. I think it's probably a bit rough to blame all the woes of the Brisbane market on the floods; the floods were probably more of an aberration, but I'll go into that in a fair bit of detail because you will see across the board the one disappointing area for our company has been South East Queensland. However that's been more than made up for what's been a very strong particular residential sector down in Victoria, particularly Melbourne.

Our full year guidance is maintained at 10% to 15% on last year for the underlying profit.

We've talked often about our strategy and for those who have been listening for the last eight years, we've talked about building a national platform from really what was just a company focused only on one market being South East Queensland and I think what you'll see as we go through this result is the real strength of that strategy to transform the Group into a national platform. I probably already alluded to that by talking about the slowness of South East Queensland but the strength of Victoria.

The other side of the strategy of course was the sector diversification and we talked about a few years ago about really seeing residential as being the growth opportunity. It's not to say that we've moved right out of commercial and industrial, we've actually got some very good assets being the Circa development in Norwest and also the Gasworks project up in Newstead in Brisbane and we'll go into that in a bit more detail, but we really did weight our assets and our balance sheet towards the residential market.

When you look at the residential market, you really break it down into apartments, communities or land sales, house and land sales and retirement. So those three sectors are really all part of the same business being the residential business. Then of course we have our funds management business and we'll be talking a bit through that later on in the presentation.

Overseeing it all and over the last eight years, what the key strategy is been to build our recurring income. We've targeted over time a 50% recurring and 50% trading income. Obviously the largest source of our recurring income is through our retirement business.

In terms of the key outcomes, we have an underlying profit after tax of AUD54.6 million and underlying EPS of AUD0.047 per security. Statutory profit after tax by total coincidence coming out at exactly the same as the underlying profit at AUD54.6 million. The recurring income percentage that I just referred to at 77% as I said, very much driven by the retirement business that we have. That number will come under pressure and we expect to reduce, but we expect it to reduce for good reasons as we see the earnings grow on our development site, particularly on our residential development site over the next few years.

Operating cash flow of AUD22.1 million, a distribution that was confirmed at AUD0.014 per security as advised previously to the market. The NTA of FKP being AUD1.24. Gearing, as I said in the opening page, at 29% and that is well below our maximum target gearing level of 35%.

Breaking it down into the divisional contributions and I don't think there are too many surprises in this one, we've talked about the communities and apartments residential business really putting the foot down and getting moving. I talked about restarting the motor. I talked about those assets that are now underway and I will talk further about those that are going to be coming on board. So it sees a huge 171% increase in the residential communities and apartments and we see very strong growth continuing over the next few years in this area.

The retirement operations had a very credible 26% growth in terms of that business and to put that in light and I'll go into a bit more detail on the divisional commentary, to see South East Queensland quite slow, but to see the strength of that result again just shows the strength of this retirement business.

The valuation is steady for the retirement. Commercial and Industrial, we did see a 50% drop. I think that was telescoped to the market. If you remember this time last year, the prior period we had the ENERGEX sale which brought in a fair lump of profit, but I think again, as I said to most investors at the full year, we think we'll more than make up for that profit in terms of the retirement and the communities profit and there's the evidence. We're again fairly confident where we're heading for the full year.

Funds and investment up 11%, corporate overheads relatively steady, so leading us to that underlying profit of AUD54.6 million, a 14% increase. So I think that's again consistent with what we've talked about, the operating profit looking to grow by between 10% and 15% for the full year this year.

Traditionally FKP tends to be skewed towards the second half and we see no real change to that this year. Probably the biggest driver of the skew towards the second half in the current year will be the RVG valuation numbers which actually are only calculated at full year, not at half year. So that in itself is a skew. So roughly speaking, we see where we're sitting now the underlying profit sort of repeating itself in the second half and then having the RVG numbers coming in on top of that to get us a stronger number for the full year to get to where our guidance is.

In terms of the divisional commentary, well the two graphs on this slide 8 really tell the story. I don't think it's a surprise to anyone of seeing that graph at the top being Victoria and seeing the strength of the Victorian market, be it good judgment or luck or really it's about being the diversified property group that we are, it just so happens that our largest project is down in Victoria which of course is Point Cook and our first apartment development launched is also in Victoria. So it sees us sitting in a very strong position in terms of taking advantage of that growth.

But I think what these two graphs do show is that there is a solid underlying demand that continues in this country, particularly up and down the east coast. We've seen the Victorian market very strong. What is particularly pleasing to me about the Victorian market, when you see a graph going off the edge and moving away from the others, it always sort of rings alarm bells that are we heading for crash. But what we're actually seeing in terms of say our sales at Point Cook and our sales at Aerial to some extent, is a smoothing or a slowing of that sales rate without coming crashing down. So what we're looking for there is a nice soft return to sort of steadier levels and I think we sit very well in terms of maintaining that.

New South Wales we're seeing some good early signs and we feel quite positive that we have in New South Wales two assets in particular that we think can take advantage of that, one being the LUXE apartments that were launched just before Christmas and the other being the Mulgoa land bank of 600 lots, that's in our Norwest joint venture and that's actually civil works have started and we see that being launched in the new financial year.

So we think we're in a good position to take advantage of what we believe will be an upswing in the New South Wales residential market and we are seeing some early signs of that in our land bank at Kellyville and also at Norwest at the moment. It's been quite solid.

South East Queensland's been slow. It's fair to say, in terms of a lot of commentary that's been made about the impacts of flood and so on, the way I think I would describe the South East Queensland market from pretty much across the board, be it retirement, communities or apartments, is it was slow going into the floods. If you look at the statistics, as we went through the GFC, it would seem that Queensland was the only state that technically went into a recession. It came off a huge growth span and I think there was a very strong slowdown ahead of the floods. What have the floods done? I don't think the floods have done an awful lot to the market. What it has the potential to do is see a bit more money going in.

But the one think I like about South East Queensland in the medium term is that there is so much money being pumped into infrastructure and public works in that South East Queensland quarter. To drive around, see bridges, tunnels, all sorts of things going everywhere and the old adage in development is that development follows infrastructure. So the fundamentals are good. It's off a very low base. We think that market will come back. We can't tell you exactly when that will. We're quite happy with where our Victorian and New South Wales assets are currently sitting to offset any shortage that we get out of South East Queensland but in the medium term we are still very strong in terms of South East Queensland. I'll go through in a few further slides, whilst it is very slow, it's not that grim. We've seen improved revenue receipts coming from our Peregian Springs, as you can see on that slide and we've actually seen of recent some good pickup in terms of our Rochedale estate.

Consistent with what I'm saying about the South East Queensland market, if you look at the launch of Rochedale which occurred about August/September last year, we went in and we had a number of builder sales there but we really weren't bowled over in the rush of retail sales being people coming in and buying lots through our sales office. That's really consistent, what I was saying about the slowness before the floods hit Brisbane. Quite ironically, the month of January, as in last month, we saw 12 sales come through the door in Rochedale, which is more than we'd actually made in the four months prior to that. We've seen a continuation of interest coming into February, so that gives us a lot of confidence in terms of where we're sitting with this exposure in South East Queensland.

In terms of the community and apartments being the driver of profit, I think the two key points to take out of this slide 9 is very much along the lines of the contracts in hand and you can see that whilst we've settled quite a bit, we've got enough contract coming in to see that we've actually go with around about that 500 sort of number in terms of contracts in hand on 11 February. I think the one that really excites me, if you like, on this slide is when you look at the average margins. If you compare where we were last year in terms of the average margins of - including interest, let's say, of 20%, to see that growth into 28% is very exciting. It's of course very positive to see property price growth and we often talk about property price growth, particularly in the retirement business

But I think what this stat actually shows is how that goes to the bottom line and it is very important. So when you look at our development inventory, across the board there really is nothing that gives us any concern other than the ability to go out and make sales. We're very happy with the margins that are sitting and in fact we're seeing improved margins almost across the board and we see that continually, not probably at the same rate, but we do see further margin growth going forward.

Obviously we expect to see the growth continue in this sector. Both sale prices and lot numbers of Saltwater Coast being the biggest driver in this profit number, having continued to exceed initial expectations, so the average sale price is around that AUD300,000, it's hard to generalize because we are actually moving to smaller lots across the board as the whole industry is. The half saw the settlement of all the units in the A2 apartment delivery at Rosebery, so it was nice to be able to call settlements and have all those apartments sold prior to actual settlement. As I said at the beginning, the pipeline of deposits remains strong.

In terms of the outlook for the Group, I talked about restarting the motor. I think we're well and truly doing that. It's a very strong pipeline. We have another six to seven years in terms of the current pipeline. It takes the pressure off any restocking issues. It will become an issue in two or three years' time if we haven't done any restocking, but it's nice to be in a position where we don't have to be going and buying things but we can look at opportunities as they arise on a case-by-case matter.

The short term focus is very much on maximizing the demand at Saltwater Coast and taking advantage of what is a very solid market. It is a quite unique market for those who are not aware of Saltwater Coast in that it is in a peninsula, so we tend not to have a lot of competition, which is quite unusual in a Melbourne market where there is no shortage of land supply typically speaking.

Delivery of the first lots of The Rochedale Estates, we have over 50 sales to builders and as I said, we're moving towards above 20 sales in terms of retail. By far the majority of those have been seen in this calendar year, so hopefully a sign of stronger market to come up in this South East Queensland market.

We did talk in terms of The Rochedale Estates looking to come into this year. With the wet weather that we've had, we actually expect those settlements to come into next financial year, however again, showing the strength of the FKP operating platform yet again, we're still holding our profit guidance in terms of the full year, even though we're not at this present stage expecting the settlements for Rochedale to come into this year.

The other focus of course is on the launch of Mulgoa Rise, 600 lots near Penrith in Sydney. We expect to see a very good result there on the back of - as our Norwest development sort of comes to its end and also our Kellyville development comes to the end. So we look at the margins that we expect there and we see strong margins in terms of the earnings to come from that New South Wales development.

We want to continue our work on the Sunshine Coast market share. As quiet as the Sunshine Coast has been, what's been positive is not only have our revenue numbers actually increased, but we've also seen our market share markedly increase. So again, it's evidence of the quality of the offering that we make and also the teams that we have in place making our sales. So it is good to see that we have well and truly more than the lion's share of the market for that Sunshine Coast market in that region, which of course is north of the Maroochy River.

So the table really shows what we're working. We talked about restarting the motor really from a communities estate and Mulgoa is the last one to get going. So what it leads to is this year we're feeling fairly comfortable with our projections and where we're going and we've made a good part of our sales to meet our numbers already this year. Going into next year we have all these estates really on full cylinders with Mulgoa coming in to add to that.

In terms of the apartments outlook, we've got a pipeline of more than 1700 apartments. I talked earlier about the margins, we're very happy with where the margins are heading for those. The Mill and the Gasworks have been broken up. They were of course very large projects, so what we've effectively done is de-risk those to some extent and we'll see more work coming leading to launches of both those projects in the next sort of six month term.

The short term focus is on continuing construction work at Aerial at Melbourne in Camberwell. Last time I looked I think we're zeroing in on about a bit over 110 apartments sold of the 141 that we have here and we're seeing good, steady one or two a week go through. At this stage we expect construction to be completed at around about May next year, should be a little bit earlier and that will see settlements coming in to the next financial year.

So when I talk about going into the next financial year with these communities all started up and all firing. It's a great comfort for me to sit here and know that in the second half of next year the Aerial profit, which is a very sizeable profit I should add, will be landing into the second half of next year. So it really will just continue the growth of FKP. Then the short term focus then will be on The Milton and LUXE projects, both of which have been launched. If you break those down, LUXE is 77 apartments. We've sold 21 of those apartments. To say - if you asked me to describe how it's gone, they haven't run out the door, which is probably a sign that we're not too cheap but there's been good steady progress and we're seeing that. We're looking for that project to settle in to a steady rate of sales on a per week basis, much as we saw on Aerial and looking to move towards that goal of getting the 21 up to 40 in the next couple of months. Which would then see a launch probably around the middle of this calendar year of that construction project.

The Milton of course is a much bigger project. It consists of 298 units and effectively we're 25% pre-sold. It's a very credible result in terms of what's been quite a tough market as I've said in South East Queensland and really it's about just keeping the head down and working away on those sales. There's obviously been a bit of a hiccup there with the floods, everyone just holding off a little bit but we're looking to see a recovery back to a steady rate. So I think a very credible result and a bit like Peregian. If you look at - this is in the western suburbs - the inner western suburbs of Brisbane. If you look at the total amount of units sold, I think our percentage of those units is well over 80%, so we're more than taking a lion's share, but of course we're looking for that whole market to improve going forward.

We'll then be looking for The Mill and the Gasworks launches over the next six months. Very different markets in terms of Brisbane, so we'll be looking to launch those, which is really we'll see the completion of that restarting of the motor that of course I talked about last year. In terms of the retirement, well this slide's really about the retirement being a specialized class of residential and that graph really shows the correlation if you like to residential. There is a strong correlation and if for no other reason the funding of most retirement sales and virtually all retirement sales, is made by the liquidation of the family home so there has to be a correlation. It does tend to come out a little bit quicker than residential because there is a stronger needs base in terms of buying in the retirement sector. To explain that, if you want to buy an investment unit it's very much discretionary. How do you feel about the world? What are your personal finances like? What tends to happen with retirement is there's concern for a future. There might be an accident. There might be a burglary down the road, your own house. You want safety. You want security. You want community. So there is a stronger needs growth.

I think we feel very comfortable despite aberrations that you may see right now in South East Queensland on the sales and that will be shown on the next slide. We feel very comfortable in the strength of this market, because the one thing any of us can't do is not grow old and it has to happen and so the demand is very certain in terms of this sector going forward.

Strong results in a challenging market. It's a very complex slide this one. There's a lot of numbers. I'll touch on the important ones. Probably the first one to note is that the actual portfolio turnover. For those who spoke to me at the full year when we announced 10% for the last full year I think it was, as it was for the half year, turnover, I was actually expecting to see it move up so I would have thought we'd be sitting here looking at about 11%. We've seen it come down to 9%. That's been very much driven by South East Queensland. There has been a falling off in terms of the sales in South East Queensland. However, again just showing the strength of the diversified model in the terms of geography, that's been more than made up by South Australian villages, which we've seen very strong price gains. It's fair to say that with me GFC, right till today, and South Australia really hasn't missed a beat.

So what that means is despite the issues we've had in South East Queensland, we've actually seen the average DMF capital gain transaction, as you'll see in the middle of that chart, increasing by 5%. So if you move to the next one, the average DMF capital gain transactions moved 8% up from AUD80,000 to AUD86,000. So what that means is the cash generated from that is up 14% to AUD24.2 million from the prior corresponding period of AUD21.2 million. Again, what's driving that is obviously the price point that we're selling, being an average transaction point of AUD250,000, which is a combination of the mix that sold together with the price growth that's coming through the whole sector. It's seeing better contracts come through in terms of the DMF rate and the capital gain and of course if you see the bottom - towards the bottom of that chart - you see the average age of residents are moving slightly up to 82.8. As I alluded to there's no getting away from it, everyone gets older, which really is the strength of this market.

So moving forward onto the outlook side, you can see the scale that we have. On our balance sheet we have 6200 existing units with a pipeline of 800. We managed for RVG just under 4000 with a pipeline of 600, leading to a bit over 10,000 units, a pipeline of 1500 being a total developed parcel of 11,500. As we look forward we think South East Queensland will be solid in the medium term. It will pick up for all the reasons I said before, but in the meantime we see the strong performance coming out of the other states, more than mitigating the impact of the slowdown that we're seeing up in Queensland. We continue to look at our pipeline to develop and we expect to deliver approximately 35 new units by June 2011. That of course carries with it the benefit of having extra stock but also development profit along the way. We also will be continuing our refurbishment plan. The division of profit contribution for the full year now is expected to be 10%. That is slower than what we forecast in terms of our full year forecasts at our full year result last year, where we said we thought tax would increase by 20%. It is lower and a lower that can be really hung on the slower South East Queensland market. But again, a very credible result in terms of retirement, particularly given the slowness that we've experienced in South East Queensland.

Commercial industrial breaks down into the trading business and also the recurring business and very much it's been about the Gasworks project up in Brisbane and also the Circa project as well as the sell down of our current inventory. We've been very successful in terms of the sell down of that current inventory. The profit has come down substantially, which really is a result of that Energex project. The recurring side, really what we've been doing is if you look at where we sit, we've always talked about being able to add value to our property trust assets. With the successful refurbishment of Bridge Street we've now disposed of that at what we believe to be a very good price. We've also more recently disposed of the Indooroopilly Junction Shopping Centre, which really fell into the non-core sector as opposed to carrying out any major refurbishment work. We're now working in terms of the repositioning of our office tower in Chatswood in Sydney, where the expiry comes up in 30th of June of this year. We're looking at strategic trust asset disposals for the other trust assets, where we believe we've pretty much maximized the value we can add to that. The two most likely in our sights at the present time are our Spring Street office building and our Lonsdale Street office building in Melbourne, Spring Street being in Sydney. So what that means is that with Bridge Street and Indooroopilly and potentially Spring Street and Lonsdale Street, it really sees us in the second half expecting our debt to come down as we head towards 30 June, below that 29% number that you see in these results.

Funds management, well we continue to work in terms of our Core Plus. The investors have been very clear that they're really looking for liquidity. They were closed end funds, which were designed to provide liquidity in a fairly short time period. We're probably fast tracking that but not in any sort of fire sale way and we've been very happy with the progress. We believe the investors are very happy with the progress that's been made on those Core Plus businesses, particularly with Harris Street, Chandos Street and William Street sales that have all come through, being all Sydney fringe office buildings.

Investment wise RVG, we've seen a pretty strong pick up in the sales coming through RVG, albeit off a fairly low base so we've seen our resales up 16% on the prior half year. Discussions continue with RVG. It's fair to say that there probably are a couple of investors in RVG fairly unhappy with how things have been going with RVG and how that's been managed and that's been voiced, I think both publicly and privately so we continue to work with those investors to get a good outcome. Just so it's very clear, as you can see from that box we have a AUD130 million investment in RVG. Now that is our units that we have in the trust, which is about 19% holding of the trust so it is a 19% holding. We do the asset management for the Australian assets of RVG. We have no value on that asset management contract on our balance sheet. We also share the fund management with Macquarie. We have no value on our balance sheet for that fund management that we have with Macquarie, but for all intents and purposes it really is a fund that's managed by Macquarie because it's totally staffed by Macquarie staff and it's all operated out of Macquarie's office. So really our exposure, our investment in RVG is that AUD130 million, which is against what we see as very strong retirement assets and we feel quite comfortable with the quality of those assets and that investment that we have.

Occupancy in the US unfortunately has continued to decline in terms of the US. We'd like to see a turnaround. We're sort of quite happy to see GPT sell their seniors business at a good price, so we would be looking to divest that at the appropriate time. I think it's important to get occupancy up a little bit higher and then take advantage of what we expect to be a recovering US market prior to liquidation. We've also seen the first contribution from Port Bouvard, our extension into Western Australia with the first tranche of 20 settlements coming in terms of Oceanique.

With that I'll move onto the capital management and hand it over to David.

David Hunt - ***FKP Property Group - CFO***

Thanks Peter and good morning. Firstly I will provide you an update on financing that occurred during the period. In December FKP announced the successful completion of the inaugural issue of its AUD125 million senior unsecured convertible bonds, which settled in January. The convertible bonds have a fixed coupon of 8% payable half yearly for a term of five years. The initial conversion price of the convertible bond is AUD1.014, representing a 20% premium to the reference price in December. This initiative diversifies the Group's sources of capital and extends the debt maturity profile.

AUD100 million of the convertible bond proceeds will be used to repay the current AUD375 million retirement facility, which expires in March this year. Term sheets have been executed for a new three year AUD275 million senior retirement facility, which has similar pricing and covenant metrics to the current facility. As reported in August, one of the three syndicate members will exit the retirement facility. During the period the Group completed the refinance of the AUD130 million Wilbow development facility and executed a new AUD80 million project facility for Aerial.

The group has no major refinances within the next 12 months. Management are well progressed on the refinance of the development MOF, which has a June 2012 expiry. Management expect to refinance this facility before the end of 2011. The group has and will continue to diversify its sources of debt. As a result of the convertible bond and project finance initiatives, FKP has reduced its reliance on senior bank debt. Project finance will be used to finance both the LUXE and Milton projects.

Turning to capital management metrics, gearing is managed based on the ratio of net debt divided by cash adjusted assets, which remains steady at 29% during the period. This is well below the maximum target gearing level of 35%. Interest coverage ratio has improved to 3.7 times from 3.2 times at 30 June, well above the covenant of 1.75 times. The weighted average debt maturity will increase to two-and-a-half years post the convertible bond and retirement refinancing. This is up from 1.2 years at 31 December.

AUD215 million of new hedges were entered into during the period, which improved the average cost of debt before margins and line fees to 5.96%, down from 6.3% at 30 June. The impact of the convertible bond has increased the cost of debt to 6.1% as floating debt is replaced with marginally higher fixed debt. The group was 71% hedged at 31 December and is currently 90% hedged as a result of the convertible bond. This hedge position is just outside the preferred 12 month range of 60 to 80%, which management expects to be back within by 30 June this year. At

31 December FKP had undrawn lines in cash of AUD220 million and importantly all covenants have been met. Distributions for the period is AUD0.014, which equates to 55% of realised underlying profit. This is within the guidance range of 40% to 60%.

I'll now pass you back to Peter for the strategy and outlook section.

Peter Brown - *FKP Property Group - CEO*

Thanks David. So just to wrap up in terms of the presentation and looking at the strategy and the outlook for the Group going forward, as I've reiterated throughout this presentation, a very positive outlook we believe for our residential communities and apartment buildings going forward. Earnings have been - I think are very well secured as it says at the top there with over 80% of our current apartment and lot sales already in the bag, over 80%, so it does leave us fairly confident going forward. The ongoing favorable supply and demand fundamentals in the residential market I expect will continue to drive the growth. In summary, I see Victoria leveling off a bit but again continuing a good margin provision to the Group going forward. We see some growth coming in New South Wales, which we look to take advantage of through Mulgoa and Woolloomooloo LUXE and in South East Queensland we see a strengthening through to the 2012 financial year, which is probably that medium term outlook that we see growing in terms of this business.

We are the market leader in terms of the retirement business. We have the scale. It is quite predictable and I guess most impressive of all to me in terms of the retirement portfolio, is the robustness of it. To see the weakness in South East Queensland being more than made up for strength in the other states, again just indicates the diversified nature of FKP as it now is. We expect to see the earnings growth to continue into the financial year 2012, which is consistent with how we see the South East Queensland market recovery. Strong base of recurring earnings. We talked about the 50/50 average split. 77% as we sit here today, it will come under pressure and move back towards that 50% and that will be a very positive sign because it'll be the strength of the earnings coming from both our residential communities and apartments business, together with our retirement business going forward.

Sound capital management, the gearing currently at 29%. I alluded to with the two asset sales that have already settled together with a potential couple of other asset sales in the second half of this year, we expect to see the gearing move down towards - probably closer down towards the 26% as we move towards the 30th of June this year, which of course is subject to those extra sales but we do expect it coming down nonetheless. The convertible bond I think really takes the company into a new era in terms of its capital management. It means that the retirement facility now moves down from AUD375 million to AUD275 million and we did see a positive response in terms of that bond. I understand it has been trading quite well post the issue. In terms of the score card for us, well retirement we've talked about reactivation of the development pipeline, and you've seen that with some 35 units expected to be delivered. We do have some big projects, in terms of the retirement pipeline, and there is a lot of work going on trying to get those bigger projects moving as well.

Increased scope with the refurbishment program, that's a program where effectively you look to add value and take some margin on the re-sales before they actually resell.

Communities. The launch of the major developments; the LUXE and Milton. All about restarting that motor. The release of additional stages of our residential community, so it's the continuation down at Point Cook, down at Phillip Island down in Melbourne, at Maitland here in Sydney, it's the finalization of the Kellyville and Norwest and launch of Mulgoa. Together with the realising of what we expect to be growing demand at Rochedale and continued stages and, hopefully, increased revenue and sales numbers at Peregian. So a lot to do with these residential communities and it can be summarized as one word to sell.

Commercial and Industrial - it's just the continuation of the non-core assets which we've basically done now. It's probably better to describe the assets that we would be looking to sell as assets that we believe we've added the value to and we believe it's the right time to liquidate, and to realize that value that we've added and to have the capacity to have assets that we think we can add more value to. The approvals are received for the large Gasworks mixed-use project in Brisbane and as well as Circa.

So when you look at - as you saw on the earlier slide, to say that we're geared towards residential is not to say that we've exited from commercial. You have effectively a AUD1 billion end value pipeline coming in the commercial area, being Gasworks and Norwest.

So you know we have - obviously that market hasn't been tearing at the gates of late. But we are seeing some very strong interest in terms of the Gasworks next stage which is roughly 8000 square meters of retail and 8000 square meters of commercial. We also have interest in buying that upfront, in terms of - and then a construction fund for it, very similar to what we had with the Energex project, which is a handy way of realizing profit earlier and de-risking projects as we move forward.

Funds management and investment. Obviously we continue with the sell-down of our Core Plus assets. The RVG investor discussions continue. Really what we want to do is just work with the investors and give them the outcome that they deserve.

Port Bouvard has started delivering contribution. The real opportunity there is on Point Grey development where the massive 2000 plus lot development with a marina, where the approvals are coming through very well and we look for that to start contributing in the next financial year in terms of Port Bouvard. Meanwhile we'll keep working on the sales and settlements of the Oceanique project.

So there is that mix, in terms of the growth assets, and you're seeing the growth, the 14% jump in the half year, mixed with the predictability of our recurring income which shows with the retirement business showing the strength of that portfolio.

So lastly, the assets continuing to perform, I think we've always said our assets are industry best. I've never really heard any argument otherwise. What it's been for us is about actually making those assets work and releasing cash, so that comes down to the sales and that comes down to restarting the motor and getting these assets really working.

The existing assets are sufficient to generate growth in the medium term without further acquisitions. So there really is no pressure to be out there buying right now, but if the right opportunity comes along of course we'd be interested.

The diversity of business provides stability with a 50-50 recurring and trading income target over a five year period, obviously we're well above that at the present time.

The future growth in the retirement and residential communities are both complementary. We saw the fact that there is that strong correlation in between those two sectors, both being residential sectors, and then the momentum will continue for this full year and beyond.

We've retained our profit guidance of 10% to 15%. That sees a second half contribution stronger than the first half as is traditional with FKP. The distribution of AUD0.03 per security which has been forecast is reaffirmed today and, also, the positive outlook we see as continuing into financial year '12.

The strength of that really is on having these community projects going and then the security of knowing that Aerial, the land in the second half of next year which will dump a fair bucket of profit into the business.

Then the challenge then will be, as it is at the moment, to see the likes of the LUXE'S, the Milton's, the Albion's, and the Gasworks launched over the next 12 months, or into construction, so that then the financial year '13, '14 and so on are secured which there will be a huge level of transparency.

So with that I'll conclude the presentation and open it up for any questions.

QUESTION AND ANSWER

Operator

The first question comes from the line of [John Richard] from Merrill Lynch, please go ahead.

John Richmond - ***Merrill Lynch - Analyst***

Thanks so much. I was just wondering on your retirement business, you mentioned the expectation previously to have the turnover reach up to 11%, is that still the expectation over the next sort of 12 months to medium term?

Peter Brown - ***FKP Property Group - CEO***

The big key there John will be the South East Queensland market. We've seen very strong growth, as I've said in the presentation, in terms of New South Wales, Victoria and South Australia and even Tasmania. But that South East Queensland pocket has been - has slowed substantially.

Now it's a big call to say we see it moving to 11% in 12 months. If you had asked me in the sort of 24 months I would be quite comfortable to say we sort of see it moving there. So our target, at this stage, over the next 12 months is to move that 9% back up towards the 10% and then look to go beyond.

When I was talking about moving to 11% at the full year, it really was not probably seeing how hard South East Queensland was going to slow. So I think it's fairer to say we'd see it moving back towards that 11% and potentially higher, given how strong South East Queensland does move in retirement, if it moves very quickly it could even be beyond that 11%, within say an 18 to 24 month period.

John Richmond - ***Merrill Lynch - Analyst***

Great. Was that also part of the reason why, as in South East Queensland, part of the reason behind the flat result in revaluation contribution?

David Hunt - ***FKP Property Group - CFO***

John, yes that's correct. If you look at the sales which were in Queensland they were down probably 25% on prior period, and that reduction in the sales was one of the causes of not seeing the same sort of cash growth as coming through as we expected around the August period.

John Richmond - ***Merrill Lynch - Analyst***

Just on RVG, could you just remind me of the refinancing facility there and the timing of that?

Peter Brown - ***FKP Property Group - CEO***

Yes, RVGs refinance is due on 1 April, so most of the focus in terms of RVG, between us and Macquarie, is on that refinancing at the moment. Substantial progress has obviously been made and we're looking for the banks in the syndicate at RVG to be going to credit within the month of February leading to a refinancing next month.

John Richmond - ***Merrill Lynch - Analyst***

Terrific. Then just with the press speculations with Lend Lease’s discussions with Macquarie's stake in that and your sort of position there and involvement, I guess, in that.

Peter Brown - ***FKP Property Group - CEO***

Probably John the best way to describe it is we have the asset management and you know we're not sellers of the asset management. We own 50% of the fund manager which, as I said earlier, it's something that we don't really have a lot of say in, it's very much run by Macquarie.

We are not really looking to sell our 50% of our fund manager. We are committed to the fund. You know it has been mentioned, and it has been publicly said by a couple of investors, that they are unhappy with the management of the fund. A bit like what we did two years ago with our Core Plus Funds, we're talking to them as much as possible and try to get an outcome in terms of how we move forward.

In terms of Lend Lease or Stockland or anyone of interest, I imagine anyone that's looked at retirement would have a great interest in RVG because the assets really are second to none.

John Richmond - ***Merrill Lynch - Analyst***

Yeah, sure. Then just lastly, did you say that you may consider with the proceeds from the next couple of assets sales within the trust and use that to purchase the next stage of the Gasworks?

Peter Brown - ***FKP Property Group - CEO***

Sorry, no. I - probably not, in terms of the Gasworks, but you know the model that you're alluding to is a very attractive model in the future for FKP.

I think if there was an asset that we saw great opportunity not just by making a development profit, but also realizing good capital appreciation into the future, it would be a very attractive proposition to develop it within the trust and to hang onto that.

At this stage that's not our intention on Gasworks, on a few fronts. But effectively we're not looking to take any more weight in the South East Queensland market, in terms of investment assets which is the main driver.

But the model you are alluding to I expect to come into play at some stage in the near future for FKP.

John Richmond - ***Merrill Lynch - Analyst***

Are there any sort of development sites that you're eyeing off at the moment with that in mind?

Peter Brown - ***FKP Property Group - CEO***

Not really. We are very focused on restarting the motor at the moment John. So you know whilst we are selling down some of the assets we believe we've added value to, the whole company is focused on really getting these residential assets up and running, which is really securing the earnings you know over the next five years.

Then I think as we get more comfort there which we - you know I think we're three quarters of the way to doing that, as we get more comfort there then we can start expanding our horizons and looking at those types of opportunities.

John Richmond - ***Merrill Lynch - Analyst***

Excellent. Thank you very much.

Operator

Our next question comes from the line of John Freedman from UBS, please go ahead.

John Freedman - ***UBS - Analyst***

Good morning. Could I just ask what the average debt margin is at the moment, just looking at the page that tells you the average cost of debt ex the margins?

David Hunt - ***FKP Property Group - CFO***

The average margin is around 300, that's including line fees.

John Freedman - ***UBS - Analyst***

Right, okay, thank you. Will that be similar into FY12?

David Hunt - ***FKP Property Group - CFO***

Yes. As we've locked away most of our refinancing for the next 18 months the margins won't change materially.

John Freedman - ***UBS - Analyst***

Okay and you mentioned in the presentation that you'll be putting finance in place for that and so on, what's the sort of cost of debt all in for those sort of projects for you?

David Hunt - ***FKP Property Group - CFO***

If you look at threw your money at say 5.5 to 5.75 and you can do margins with lines fees of 275, all in it would be around that 8.25 to 8.5.

John Freedman - ***UBS - Analyst***

Right, okay, thank you. Can I get some comment just on the expected EBIT split geographically between the states for the residential issue?

David Hunt - ***FKP Property Group - CFO***

The major driver was Point Cook which, as Peter said, that was very strong during the period. So the major driver was the Victorian area which contributed probably around that AUD10 million. The Queensland was still very strong with AUD5 million, the New South Wales we had some smaller projects which were probably around that AUD1 million to AUD2 million.

John Freedman - ***UBS - Analyst***

Okay, that's great. Thank you very much.

Operator

Our next question comes from the line of Michael Scott from JP Morgan, please go ahead.

Michael Scott - ***JP Morgan - Analyst***

Hi guys. Just if I can ask just simply with RVG how confident are you in retaining the management of that fund going forward?

Peter Brown - ***FKP Property Group - CEO***

That's a bit of a tough question Michael. The real issue for us is - and this is probably the point when I did the presentation of why I focused on the investment that we have and what it is on our balance sheet.

We have no value in that management. We believe that we are the best manager of it going forward. We currently own half of the manager and we also have the asset management.

Now it's never been brought into question by anyone, our asset management credentials, and we have a contract which will last for another seven years also, in terms of the asset management of this vehicle. We own close to 20% of the fund, so that's really consistent with us believing that we are probably the suitable fund manager going forward.

However, you know it is not necessarily on our control in this matter. So all we can really do Michael is work with the investors and put our best foot forward to achieve the outcomes that we have.

But the point I'd like to make is that whilst we're you know 50% of the fund manager we don't make any money on that. So we really want, as all the investors do and as a 20% investor, what is best for the fund. Now we have a view that we're best for the fund, but we obviously have to convince other investors of that also.

Michael Scott - ***JP Morgan - Analyst***

With the earnings from RVG over FY10 that was nearly all on accruals basis, just wondering if you could provide some color over the next couple of years whether you expect more cash to come out of that investment.

David Hunt - ***FKP Property Group - CFO***

Our forecast for this year is RVG to contribute around that AUD15 million which we don't expect distributions to come out of RVG, so the cash will be held within RVG to continually manage that business and their development pipeline.

Forecasting forward, we expect just normalized growth coming off that AUD15 million contribution per annum.

Michael Scott - ***JP Morgan - Analyst***

Is the - have you got any idea when that distribution would recommence?

David Hunt - ***FKP Property Group - CFO***

As part of the refinancing which is going through to the banks at the moment, and where the position of the fund will ultimately be with the management. I think that over the next six months you'll have a better position on that, probably August is the best time to talk about distributions for RVG.

Michael Scott - ***JP Morgan - Analyst***

Just with impairments, just wondering how confident you are of not seeing any write-downs over the next year.

Peter Brown - ***FKP Property Group - CEO***

Yeah Michael, we took our medicine and it wasn't good for anyone, but we took it. We took it properly and did a lot of work on that. As I sort of mentioned in the main presentation, from a development inventory point of view, there's nothing that's got us worried.

In fact, we're seeing the opposite. We're seeing a lot of our, particularly, land banks getting stronger and stronger in terms of the margins they're going to deliver. In terms of the apartment projects we have, again they're all sitting on a very solid basis you know with sort of an average of around about 20% return on cost and you know in some cases, such as Aerial in Melbourne, you know a fair bit better than that.

Michael Scott - ***JP Morgan - Analyst***

Just finally, could you reiterate your view on selling the retirement portfolio? Is your view that you would sell at book value?

I'm just thinking that - I mean it's a great portfolio, some may see it as the best part of FKP, and if you sell it there is reinvestment risk. Yeah, just wondering if you can comment on that.

Peter Brown - ***FKP Property Group - CEO***

I think, you know - just so it's clear, we're not presently looking to sell our retirement assets from our balance sheet. We're strong believers in them and we believe we can generate a lot more cash out of them, which I think is important that we strive to do, and the biggest generator of cash, of course, is sales, which is why I say it comes down to selling.

In terms of were an offer to be made, and I can say there's no offer that's been made. But, as you'd expect, a company such as us to deal with any large offer that was ever received, you'd have to give it due consideration. Now, the first part of consideration would be, you know, what that offer is, you know. Is it asset value? Is it more? Is it less? What is it?

The second part of it would be it does it make sense for shareholders and I think - I agree with you Michael that it's a very important part of our business and so hence I think if we, as FKP's board, had an offer and decided to sell that, it would need to make a very compelling reason what it was going to use those funds to do in terms - and then ultimately, of course, it would have to get shareholder approval to do that.

So, it's not on the table at the moment. Do I expect that to be on the table in the short term? No I don't. But, as any large part of our business, if an approach was made, we'd have to give it due consideration.

Michael Scott - ***JP Morgan - Analyst***

Great. Thanks guys.

Operator

Our next question comes from the line of [E Lewin] from Macquarie. Please go ahead.

E Lewin - ***Macquarie - Analyst***

Hi guys, a few questions from me. Firstly, in terms of your guidance - now you mentioned that Rochedale settlements were expected to delay into the next year and obviously, you've already talked about a second half skew in strength across the other business units. I'm just wondering where you - if you were able to provide any other clarity on where you expect that to be made up in terms of the full year guidance to be maintained?

David Hunt - ***FKP Property Group - CFO***

I think the major driver is the Point Cook project, where we're expecting probably another AUD5 million plus coming out of that project than what we expected in August and that's been the major contributor of the makeup of the shortfall in the retirement side of the business.

E Lewin - ***Macquarie - Analyst***

Sure and then there's my second question, kind of a standard one just on cash flow and my apologies if this is actually set out in the material somewhere, but the accounts only came through the ASX a few minutes ago. You mentioned operating cash flow of AUD22 odd million and operating profit obviously closer AUD55 and notwithstanding there are obviously non-cash elements in the business, particularly on retirement. I was just wondering why the cash flow number is so low, relative to the profit number.

David Hunt - ***FKP Property Group - CFO***

The business is spending a lot of money on projects at the moment. So we're reinvesting a lot of the cash from the Point Cook project into the developments, which we've got on our books, which we are kicking off at the moment, is the major reason for that.

We also put a slide in the presentation which took our underlying profit down to realize underlying profit and then down to an AFFO level, to give a little bit of guidance to the market, to show that we're covering our distributions as well. So that there has provided extra information on how we are comfortable where the position is.

Excess cash, as we said in August, is important to actually regenerate future projects. That development pipeline is quite strong and that's where we are putting the funds back into.

E Lewin - ***Macquarie - Analyst***

Thank you.

Operator

Our next question comes from the line of Rohan Sundram from Austock. Please go ahead.

Rohan Sundram - ***Austock - Analyst***

Morning guys. Thanks for your time. I've only just jumped on, so apologies if you've already covered it. But did you mention are you expecting any change to development costs going forward in light of the floods and to what extent have you been able to lock in these costs on your projects coming up?

Peter Brown - ***FKP Property Group - CEO***

In terms of development costs, we've pretty well locked away our development costs in Victoria with the lending of a lump sum contract to an external contractor that has a fairly robust balance sheet.

In terms of Point Cook, civil works tend to not be driven by cost inflation the same way that building construction does. You know, you have machines and you have men and women driving machines. So you tend not to have the same sort of risk in terms of escalation. As we come to Sydney, Sydney - the building cost in Sydney is below Brisbane at the moment and has been for the last few years. So we see good opportunity for getting some good prices in Sydney and not a lot of risk in the short term, in terms of the horizon for LUXE and again, the civil projects tend not to be a risk.

Then up in Queensland it's fair to say that Queensland has come off a very strong base and it hasn't really let off, because as the private projects sort of started ceasing, all the Government work has come into play. So you really haven't seen much release in terms of the high cost base in Queensland. So, if anything, we'd be hoping that Queensland may come back a little bit in terms of cost pressure to the building side, because it is a very high base that is has been on.

Operator

Ladies and Gentlemen, that does conclude our conference call for today. Thank you for your participation. You may now all disconnect.