development projects update

7 february 2013

by mirvac

ARTIST'S IMPRESSION OF 8 CHIFLEY SQUARE, SYDNEY, NSW

DEVELOPMENT PROJECTS UPDATE

The regular review of development projects nationally, as at 31 December 2012, has been completed and provides evidence that specific micro markets are not recovering as expected.

Spring and Summer 2012 residential sales have been weaker than expected. Feasibility assumptions for unsold stock and projects that Mirvac will continue to develop in specific markets, have been revised to reflect continued subdued sale prices and rates.

In addition, where it is considered to be appropriate, certain projects will be sold as englobo lots to generate cash rather than investing additional capital into underperforming projects.

Financial impacts:

- A provision of $273.2m or 5.9cpss
- FY13 operating EPS guidance of 10.7 to 10.8cpss unchanged
- FY13 DPS guidance of 8.5 to 8.7cpss unchanged
- Balance Sheet gearing of 23.8%[1]
- Net Tangible Asset ('NTA') of $1.64pss [2]

1) Net debt (at foreign exchange hedged rate) excluding leases/(total tangible assets - cash), based on management accounts as at 31 December 2012 which forms the basis of the financial statements and is subject to independent Auditor's review and Board approval.
2) NTA per stapled security, based on ordinary securities including EIS securities and based on management accounts as at 31 December 2012 which forms the basis of the financial statements and is subject to independent Auditor's review and Board approval.

QUARTERLY NATIONAL REVIEW OF ALL PROJECTS

Mirvac has conducted its regular quarterly review of all markets and projects

Queensland - Sales activity over the past six months has remained weak. Substantial discounting is prevalent in sub-markets where Mirvac has exposure. The recent floods are expected to further reduce confidence.

Western Australia - Despite the low to mid price point market showing early signs of recovery, the high end market in Perth remains weak, with oversupply a concern for potential buyers.

Victoria - A thorough review has concluded that despite declining fundamentals generally, no provisions relating to market conditions are required. Mirvac has no active exposure to weak greenfield locations and the only apartment exposure is Yarra's Edge which continues to perform in line with expectations.

New South Wales - The Sydney market remains Mirvac's most robust exposure. Both greenfield and apartment exposures through Elizabeth Hills, Harold Park, Chatswood and Rhodes are performing to expectations.

Provision by State [1]:

Queensland = 72%

Western Australia = 27%

1) Remaining 1% relates to projects outside of Queensland and Western Australia.

PROJECTS IMPACTED

Impacted projects to be managed in three ways:

Continue to Develop

Management to continue to develop projects over time, with forecast sales prices, sales rates and holding costs updated to reflect revised market expectations.

Englobo Sales

Where considered appropriate, selected underperforming projects to be sold as englobo lots to generate cash and avoid investing additional capital into those projects. As a result of englobo sales, $476m of future cash commitments will no longer be required and $89m[1] is expected from englobo sales proceeds.

Repricing of Unsold Stock

Unsold completed stock has been repriced and sales rates have been updated to align with recent market evidence over the past six months, and the reassessed speed and quantum of a recovery.

1) Proceeds from englobo sales expected to be delivered over FY13, FY14 and FY15.

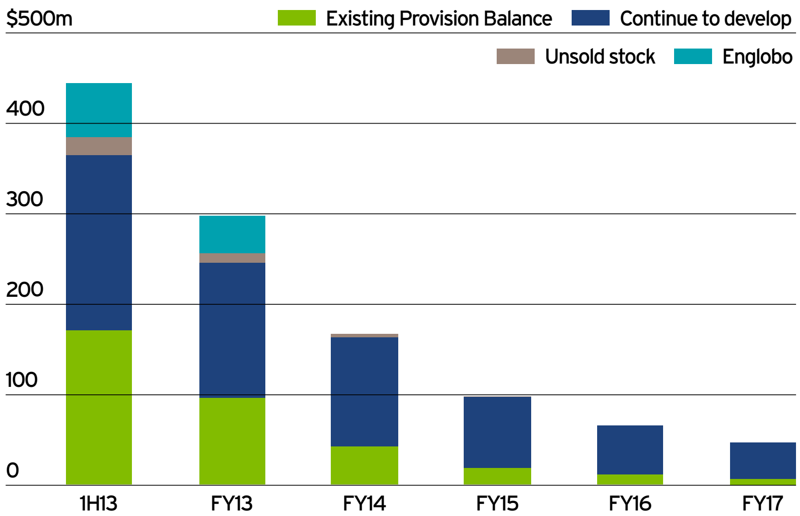
PROJECTS IMPACTED

Project	Product Line	State	Provision	Acquisition Date
Gainsborough Greens	Masterplanned Communities	QLD	$58.6m	Oct 06
Waterfront, Newstead – Site Balance	Apartments	QLD	$51.4m	Apr 08
Beachside Leighton, Stage 2	Apartments	WA	$43.0m	Aug 06
Mackay	Commercial	QLD	$30.0m	Nov 07
Hope Island	Masterplanned Communities	QLD	$15.9m	Jan 07
Hamilton	Apartments	QLD	$13.4m	Jan 10
Burswood	Apartments	WA	$12.3m	Feb 03
Mariner's Peninsula, Townsville	Apartments	QLD	$11.6m	Jun 06
Waterfront, Newstead - Park	Apartments	QLD	$8.6m	Apr 08
Brookwater	Masterplanned Communities	QLD	$8.4m	May 06
Other [1]	–	–	$20.0m	–
Total			**$273.2m**	

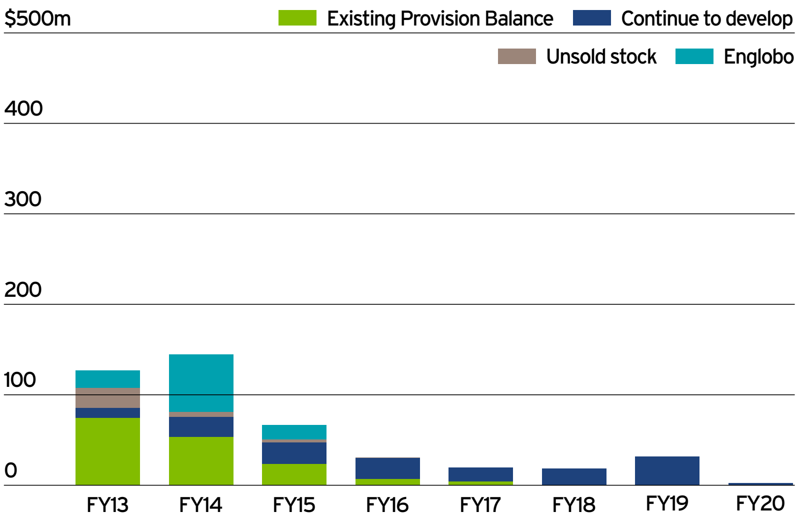
1) Remaining 1% relates to projects outside of Queensland and Western Australia.

PROVISION ROLL OFF [1]

Provision Balance Profile



Provision Release Profile



1) Based on forecast revenue, market conditions, expenditure and interest costs over project life.

WHAT HAS OCCURRED

Historical context:

- Acquisitions made predominantly in a market with high expected growth - average age of provisioned projects is 6.8 years (average acquisition date FY07)
- Large capital commitments due to projects being '100% on Balance Sheet'
- Capitalised interest is 20.6% of gross provisioned inventory

Ramifications:

- Requirement to extend timeframe assumptions and reduce revenue expectations due to ongoing market weakness
- Compounding interest and holding costs over life of project have contributed to deteriorated returns

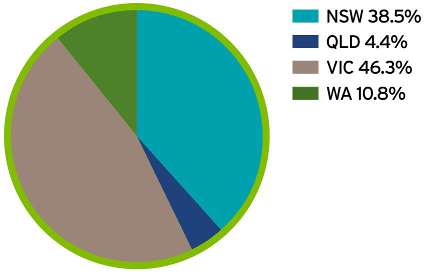
LOOKING FORWARD

- Centralised capital allocation decision making
- Average age of non impaired projects is 2.5 years – purchased consistent with current market assumptions
- Pro-actively increasing the number of capital efficient projects:

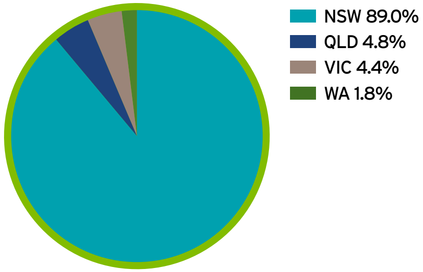
Projects controlled in capital efficient structures	
FY07	11%[1]
FY12	30%[2]
FY15	45%[2]

- Capitalised interest is 6.8% of gross inventory from non provisioned projects
- Forecast development operating EBIT focused on robust NSW market

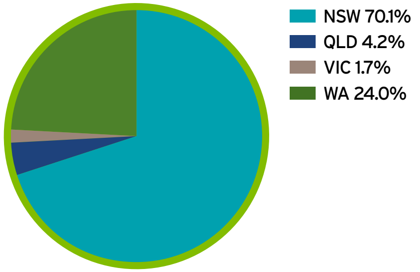
FY13



FY14



FY15



1) Represents capital structures (such as JVs and Investments and Associates) other than 100% inventory on Balance Sheet.
2) Forecasted capital represents the development capital held within JV, Investments and Associates structures along with recent inventory acquisitions, acquired under capital efficient terms.

SUMMARY

- FY13 EPS guidance of 10.7 to 10.8cpss is unchanged
- Mirvac remains on track to achieve FY14 target of >10% ROIC using post provisioned EBIT and pre provisioned inventory balance
- Balance Sheet gearing within the target range at 23.8% [1]
- Mirvac remains compliant with all debt covenants

1) Net debt (at foreign exchange hedged rate) excluding leases/(total tangible assets - cash), based on management accounts as at 31 December 2012 which forms the basis of the financial statements and are subject to independent Auditor's review and Board approval.

additional information

by mirvac

NET REALISABLE VALUE

- Mirvac undertakes comprehensive and regular reviews of the carrying value of Inventories and JV and Associates. Inventory is required to be carried at the lower of cost and Net Realisable Value ("NRV"). NRV for the purposes of inventories provision is the difference between costs accumulated to date, plus all future costs (including interest and cost to sell) less forecast net revenue. Any future loss is booked as a provision immediately rather than progressively over the life of the project.
- Englobo projects are assessed on the basis of expected current market/saleable value of the project (which differs to the NRV build out scenarios previously adopted).

CAPITALISED INTEREST POLICY

- Mirvac assesses and allocates capitalised interest on a stage-by-stage basis within a project and accounts for the stage separately (not project wide)
- Mirvac allocates interest to stages by the gross value of WIP irrespective of whether the project is in provision or not (therefore not burdening other profitable projects)
- Capitalisation of interest occurs when a stage is active
- Capitalisation ceases when a stage is practically complete, where a stage is inactive or deemed on-hold
- Projects recently announced as on-hold (Mariners Peninsula, Townsville and Foreshore, Hamilton) have commenced expensing interest
- All future interest costs (capitalised and/or expensed on gross value) are factored into NRV calculations

HYPOTHETICAL PROFIT MAKING DEVELOPMENT PROJECT – TREATMENT OF CAPITALISED COSTS

Project Metrics			Total
Sales revenue			120
Land			(20)
Cost of property development and construction			(60)
Sales & marketing expenses			(10)
Interest costs			(10)
Total project return			**20**

Cash Flow	Year 1	Year 2	Year 3
Sales revenue			120
Land	(20)		
Cost of property development and construction	(20)	(40)	
Sales & marketing expenses	(5)		(5)
Interest costs	(3)	(5)	(2)
Net cash flow	**(48)**	**(45)**	**113**

P&L	Year 1	Year 2	Year 3
Sales revenue			120
COGS			(80)
Gross margin	–	–	**40**
Sales & marketing expenses	(5)	–	(5)
EBIT	**(5)**	–	**35**
Interest and finance charges paid/payable	–	–	(2)
Interest capitalised in current and prior years expensed this year	–	–	(8)
Total finance costs	–	–	**(10)**
Operating net profit	**(5)**	–	**25**

Balance Sheet	Year 1	Year 2	Year 3
Cost of acquisition	20	20	–
Development costs	20	60	–
Borrowing costs capitalised during development	3	8	–
Gross inventory	**43**	**88**	–

During construction all interest costs are capitalised to inventory. These are released in the P&L on settlement through ‘Borrowing costs capitalised during development’.

Upon the completion of construction interest costs are expensed directly to the P&L

Upon Settlement capitalised acquisition (land) and development (construction) costs are released in the P&L through ‘COGS’.

HYPOTHETICAL PROVISIONED DEVELOPMENT PROJECT – TREATMENT OF CAPITALISED COSTS

Project Metrics	Total
Sales revenue	100
Land	(25)
Cost of property development and construction	(50)
Sales & marketing expenses	(10)
Interest costs	(25)
Total project return	**(10)**

Cash flow	Year 1	Year 2	Year 3	Year 4	Year 5
Sales revenue					100
Land	(25)				
Cost of property development and construction	(5)	(10)	(15)	(20)	
Sales & marketing expenses	(5)				(5)
Interest costs	(3)	(5)	(7)	(8)	(2)
Net cash flow	**(38)**	**(15)**	**(22)**	**(28)**	**93**

P&L	Year 1	Year 2	Year 3	Year 4	Year 5
Sales revenue					100
COGS					(75)
Gross margin	–	–	–	–	**25**
Sales & marketing expenses	(5)	–	–	–	(5)
EBIT	**(5)**	–	–	–	**20**
Interest and finance charges paid/payable					(2)
Interest and finance charges paid/payable - provision release					2
Interest capitalised in current and prior years expensed this year – provision release					(23)
Interest capitalised in current and prior years expensed this year – provision release					3
Total finance costs	–	–	–	–	**(20)**
Operating net profit	**(5)**				
Inventory impairment		(5)			
Statutory net profit	**(5)**	**(5)**	–	–	–

Balance sheet	Year 1	Year 2	Year 3	Year 4	Year 5
Cost of acquisition	25	25	25	25	–
Development costs	5	15	30	50	–
Borrowing costs capitalised during development	3	8	15	23	–
Gross inventory	**33**	**48**	**70**	**98**	–
Provision for loss	–	(5)	(5)	(5)	–
Net inventory	**33**	**43**	**65**	**93**	–

This is the same project but it has suffered from a 2 year delay in construction, increasing interest costs and resulting in a negative project return.

In year 2 when the construction delays become apparent, an inventory impairment is taken to reflect the reduced net realisable value of the project.

Gross margin is not affected by interest (project delay impact) Impairment in this example relates to increased finance costs from time delay. If the impairment related to increased development costs causes the margin to be negative then the impairment is applied to make gross margin zero through COGS provision and COGS interest provision, released on settlement.

The Inventory is not written down at the time of the impairment but a provision for loss is added to the balance sheet. This provision is released against interest costs upon settlement.

GLOSSARY

Term	Meaning
COGS	Cost of Goods Sold
CPSS	Cents Per Stapled Security
DPS	Distribution Per Stapled Security
EBIT	In the current reporting period, Mirvac has revised its definition of Earnings Before Interest and Taxes (EBIT). Mirvac considers interest income from joint ventures and interest income from mezzanine loans to be part of a business's operations and should therefore form part of operating revenue. Prior to FY11, interest income from joint ventures and interest income from mezzanine loans were shown as part of interest revenue. All historical EBIT figures in this presentation have been re-stated to reflect the current definition of EBIT for comparability.
EIS	Employee Incentive Scheme
Englobo	Group of land lots that have subdivision potential
EPS	Earnings Per Stapled Security
FY	Financial Year
JV	Joint Venture
MGR	Mirvac Group ASX code
MPT	Mirvac Property Trust
NRV	Net Realisable Value
NTA	Net Tangible Assets
ROIC	Return on Invested Capital. EBIT divided by average invested capital.
WIP	Work In Progress

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