RAPER CAPITAL

Stuart Nisbett, Chairman
US Masters Residential Property Fund
Level 15, 100 Pacific Highway
North Sydney NSW 2060
Australia

May 13, 2022

Dear Mr Nisbett,

Entities I manage are beneficially interested in 1% of the outstanding shares of US Masters Residential Property Fund (hereafter, 'URF', or 'the Company'). I write today to communicate my complete and total disgust at the terms, and form, of the takeover offer currently being recommended to shareholders.[1] I have seen my fair share of management sins in a multi-decade investment career, but our Board's feeble endorsement of this horrendous transaction surpasses them all. Just as our Company finally rounds into form, management is inexplicably foisting a deeply-discounted bid down our throats, for no apparent reason and with nary a skerrick of supporting financial logic. This shambolic deal fails the most basic test of any change of control transaction – that is, it provides a far inferior outcome to simply maintaining the pre-deal *status quo*. Not only this, the Board has somehow failed to consider other alternative strategies – such as capital structure realignment through preferred share conversion, along with accretive buybacks below stated NAV – that would increase equity value to, at minimum, *a 60-70% premium to the consideration offered in this bid.*

Moreover, the fact that our Board has resorted to all manner of PR kabuki to portray this derisory deal as reasonable only further underlines the total and unmitigated governance disaster on display. If - or when - this deal fails at the upcoming vote, I for one will be happy to see it swept into the dustbin of corporate history where it belongs. Recent trading prices in URF common units and preferred securities suggest I am not alone in this view.

Before proceeding to a discussion of this deal's innumerable failings, we should consider the current, holistic state of our Company. A simple observation demonstrates *there is simply no pressing need to enter any transaction,* let alone one on these abusive terms. As disclosed in the recent March'22 Quarterly Activities Report, after many years of cash burn, URF is finally on the verge of being cashflow breakeven. In fact, the Company specifically guided to being FFO positive in 2H this year, and suggested that most all operating metrics – occupancy, rent payments, same-home FFO, etc. – are at record highs.[2] Compounding the new stability of the run-rate operations, due to changes in the global interest rate environment, the Company's 4%

[1] See 'URF Executes Sale and Purchase Agreement', 28 March, 2022. https://wcsecure.weblink.com.au/pdf/URF/02503329.pdf
[2] See 'Quarterly Report – Q1 2022', 11 May, 2022, p. 9-14 https://wcsecure.weblink.com.au/pdf/URF/02520649.pdf

fixed Term Loan, previously considered an onerous and expensive liability, is now in fact a valuable asset, representing an extremely attractive cost of capital. In sum, then, our Board is endorsing the sell-out of our equity at a time when the URF asset portfolio is in rude health, for perhaps the first time in its long history.

Let us now consider the specifics of the bid our Board enjoins us to accept. URF shareholders would receive 22c per share – *an effective 62% discount to last-reported, post-tax equity NAV*[3] – despite somehow claiming that this price is only an 11% discount to 'unencumbered' gross asset value.[4] In support of this spurious claim, the Board suggests that gross NAV needs to be haircut by a total of $55mm, comprising $28mm of tax payments and $27mm of 'debt yield maintenance' expenses. But both 'adjustments' – inexplicably granted in the buyer's favour – have real value to ordinary unitholders that is being completely ignored in the current bid.

Firstly, regarding the tax issue, whilst it is true that withholding tax is payable on properties as they are sold either piecemeal or *in toto*, if URF were to remain a listed REIT as currently structured, Australian tax residents – the vast majority of the register today – would be able to claim a Foreign Tax Credit against their own income. By deducting this gross amount from the sales price, our Board is essentially depriving the Australian tax resident invested in URF from this valuable credit, over time.

Secondly – and more egregiously – the deduction of yield management expenses from gross NAV as a credit to the buyer is not only disingenuous; it is brainless. 'Yield management expense', more commonly known as 'make whole payments' in fixed income parlance, would only be due if the underlying debt – here, the Global Atlantic term loan – is actually prepaid ahead of term. But the very deal documents clearly state this loan will remain outstanding and be assumed by the buyer.[5] And why wouldn't it? As just described, said funding is now deeply 'in the money' and thus a valuable form of low-cost capital. The buyer group should be paying URF for the right to step into this loan, not the other way around! It would be far more sensible to simply sell the maximum allowable properties each year piecemeal, but leave the bulk of the loan outstanding, whilst reinvesting excess property proceeds into common units trading at a fraction of NAV, than crystallize needlessly this huge excess obligation to the sole detriment of common unitholders.

Thus, properly construed, *the true discount offered to shareholders who accept this transaction is more akin to a 20% discount to gross asset value* (not 11%), and, as mentioned, an abhorrent >60% discount to pre-deal book equity. This of course begs the further question of why? Why are shareholders being press-ganged into accepting such a gargantuan, and permanent, capital impairment, when the operating entity is no longer burning cash, and when historical asset sales have uniformly been conducted at a gross premium to NAV? Why is the board dressing up this transaction as acceptable, and in fact the superior choice, when it is so patently worse than maintaining the pre-deal *status quo*?

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[3] Being 59c per share on 18 March, 2022. See 'Weekly NAV Estimate', 24 March, 2022. https://wcsecure.weblink.com.au/pdf/URF/02502416.pdf

[4] As discussed in transaction Press Release, ibid., p.1: 'On an unencumbered, post-tax basis, the purchase price represents an 11% discount to the 31 December 2021 book value.'

[5] See ibid., p. 1: 'The Transaction is subject to and conditional upon…consent to the Buyer assuming the Fund's existing loan by the lender, Global Atlantic Financial Group…'

Examining the use of proceeds of this transaction begets yet more incredulity. *The sole beneficiary of this transaction is the URF Preferred shareholder,* who will be paid out at par (plus accrued) if this deal is consummated.[6] To be clear, I have nothing against the Preferred shareholders as a class. But to subscribe to a value-destructive transaction to the benefit of only one class of shareholders – for which there is absolutely no pressing financial need – is negligent at best and a violation of the Directors' duty of care at worst. The Board has a fiduciary duty to protect the rights of *all* shareholders, not one class over another – and especially not when there are multiple other avenues to realign the capital structure to the benefit of all.

This leads us to an examination of the second irredeemable flaw in this transaction: not only is this deal worse than what exists currently, *it will be far, far inferior to what could exist from as soon as January next year*. As the Board is no doubt aware, the Preferred share coupons will 'step up' from 6.375% to 8.5% per annum, from January 1, 2023 – unless of course they are converted to equity at the sole option of the Responsible Entity.[7] Whilst this remains a discretionary decision for the Board, it makes little sense to incur a further 2.125% per annum interest cost (amounting to ~$4.3mm per year) when the entity has just made it to FFO positive territory. Instead, the Board should simply convert the Preferreds to ordinary units and equalize the capital structure once and for all.

This alternate strategy – maintenance of the *status quo*, followed by capital structure equalization in six months or so – is indisputably a far superior outcome than accepting this deeply-discounted bid. To illustrate, *even on the same abusive terms currently being proffered by our Board, common unitholder recovery in this scenario jumps to ~35c, a full 60% higher than the consideration due under the current bid*:[8]

	Current	Post pref conversion	Notes
Purported deal proceeds (A$ mm)	285.4	285.4	FX at deal announcement, 0.75
Pref share claim	199.1	0	assume full conversion to equity
Net residual value for unitholders	**86.3**	**284.9**	incl 500k deal break fee
Units outstanding	401	809	Maximum 408mm new units on conversion
Value per common unit (A$)	**$0.22**	**$0.35**	current implied value much higher ref 0.69 FX

Crucially, this static assessment accords no value for the accretive actions management could concurrently undertake, such as a buyback of common units at a huge discount to NAV – an action that *as recently as last Quarterly Report was on the agenda for excess capital, in the amount of $20mm*.[9] At current prices, $20mm would be enough to retire ~10% of the pro-forma (post-converted) shares outstanding.

Why then abandon that plan, in favour of this horrific deal now? Is it perhaps because the Responsible Entity, having waived basically all fees for managing URF, and without meaningful

[6] In accordance with the Preferred share prospectus. See ibid., p. 1.
[7] The Preferred shares are convertible into common units, solely at the discretion of the Responsible Entity. See prospectus, p. viii (and Section 11.8), https://www.usmastersresidential.com.au/wp-content/uploads/2018/01/URF-PDSCPU.pdf
[8] Raper Capital estimates based upon URF transaction disclosures.
[9] See 'Quarterly Report – Q4 2021', p.7. https://wcsecure.weblink.com.au/pdf/URF/02493464.pdf

ownership of the common units, has simply no incentive to do what is patently right and in the best interest of common shareholders?

As it stands, it seems quite clear many other unitholders share this view. Since this transaction was announced, over 10% of the float has traded at prices north of the announced deal price.[10] I have personally spoken with over 20% of the register – a hugely significant block given the fragmented nature of the ownership base – all of whom have expressed similar anger at the announced deal and a willingness to vote against this transaction on its merits. No doubt other, smaller retail shareholders are likewise incensed, and I expect that to be reflected at the shareholders' vote.

The path forward, therefore, is quite clear: either renegotiate this transaction into something more acceptable to common unitholders or move on from it entirely and focus on the alternate playbook for value creation outlined herein. Offering unitholders a true, unaffected 11% discount to last reported NAV – that is, without deducting the withholding tax and debt yield management expenses – would constitute a bare minimum for most of the register, I believe. This would imply a gross asset sales price of ~$564mm (USD) and *a look-through per unit price of ~41c* (referencing the same 0.75 AUD/USD FX rate as was utilized in the press release announcing the deal). Of course, at today's FX rates (0.69), *the implied minimum acceptable value to shareholders would be 48 cents* on equivalent terms.

While it is late in the day, the Board still has a chance to emerge from this debacle with an acceptable outcome for all involved. I encourage you to grasp this chance – for if not amended, this deal as currently structured is simply destined to fail at the shareholder vote, and the Responsible Entity's purgatorial stewardship of this asset will be compelled to continue.

I remain at your and the Board's disposal to discuss any and all of the items enclosed.

Yours sincerely,

Jeremy Raper

[10] See trading volume and price history here: https://finance.yahoo.com/quote/URF.AX/history?p=URF.AX