SABANA SHARI'AH COMPLIANT INDUSTRIAL REAL ESTATE INVESTMENT TRUST
(a real estate investment trust constituted on 29 October 2010 under the laws of the Republic of Singapore)

Clarifications relating to the Proposed Merger

This announcement should be read in conjunction with the Joint Announcement (as amended and supplemented by the corrigendum announcement dated 30 July 2020). All capitalised terms used herein but not otherwise defined shall have the meanings ascribed to them in the Joint Announcement.

On 16 July 2020, the boards of directors of ESR Funds Management (S) Limited, as manager of ESR-REIT (the "**ESR-REIT Manager**") and Sabana Real Estate Investment Management Pte. Ltd., as manager of Sabana Shari'ah Compliant Industrial Real Estate Investment Trust ("**Sabana REIT**", and the manager of Sabana REIT, the "**Sabana Manager**") jointly announced the proposed merger (the "**Merger**") of ESR-REIT and Sabana REIT (the "**Joint Announcement**"). The Sabana Manager has since received questions in relation to the Merger and wishes to provide its responses and clarifications to these questions in this announcement.

The board of directors of the Sabana Manager (the "**Board**") comprises only independent directors appointed in accordance with the Securities and Futures Act ("**SFA**") and the listing manual ("**Listing Manual**") of the Singapore Exchange Securities Trading Limited ("**SGX-ST**"). The Board went through a thorough process to evaluate the terms of the Merger. This involved lengthy and careful deliberations with the management team of the Sabana Manager as well as financial advisors that were engaged to evaluate the commercial terms of the Merger. The Merger terms were arrived at after extensive negotiations between the Sabana Manager and the ESR-REIT Manager.

The Board would like to highlight that the Merger is the only formal offer that the Sabana Manager has ever received. In accordance with its fiduciary duties, the Board is proposing the Merger by way of a trust scheme of arrangement ("**Scheme**") for the consideration of the independent unitholders of Sabana REIT (the "**Sabana Unitholders**", and the units in Sabana REIT, the "**Sabana Units**"). The Board believes that independent Sabana Unitholders should have the opportunity to decide and vote on the Merger, taking into account the compelling transaction rationale, and various other factors such as the premium of the gross exchange ratio ("**GXR**") over historical exchange ratios based on the respective unit trading prices, DPU accretion, net asset value ("**NAV**"), the property portfolio of both REITs as well as the challenges of continuing as a smaller standalone REIT in comparison to a potential value uplift from being part of a larger combined REIT (4th largest industrial S-REIT by Singapore industrial GFA market share).[1]

The Sabana Manager believes that a Scheme is a fair and equitable way of effecting the Merger, as it provides a binary outcome (i.e. "all or nothing") of effecting the Merger. The Scheme will be decided upon by the independent Sabana Unitholders at the Scheme Meeting as the Scheme requires the approval by a majority in number of independent Sabana Unitholders representing at least three-fourths (75%) in value of the Sabana Units held by independent Sabana Unitholders present and voting either in person or by proxy at the Scheme Meeting. As an additional protection for the independent Sabana Unitholders, the Scheme will require court sanction before the Scheme can become effective.

As stated in paragraph 10 of the Joint Announcement, the ESR-REIT Manager, its concert parties as well as the common substantial Sabana Unitholders / ESR-REIT Unitholders, including Mr. Tong, Wealthy Fountain Holdings Inc., e-Shang Infinity Cayman Limited and ESR Cayman Limited ("**ESR Cayman**"), will abstain from

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[1] Please refer to paragraph 5(a) of the Joint Announcement.

voting on the Scheme. In addition, the Sabana Manager will abstain from voting on the Scheme pursuant to Rule 748(5) of the Listing Manual of the SGX-ST.

Deloitte & Touche Corporate Finance Pte Ltd has been appointed as the Independent Financial Advisor (the "**IFA**") to advise the independent directors of the Sabana Manager and the trustee of Sabana REIT ("**Sabana Trustee**") on the Scheme, and its opinion will be disclosed in the Scheme Document to be despatched to Sabana Unitholders in due course. **The Sabana Unitholders are advised to carefully consider the details that will be provided in the Scheme Document before deciding on their important vote on the Merger.**

A list of key questions from investors and the Sabana Manager's responses in relation to the Merger are set out below, for Sabana Unitholders' information.

Key Questions, Responses and Clarifications

A. Conflict of interest

1. Are there any conflicts of interest?

The Board and the management of the Sabana Manager would like to reiterate that there are strict controls in place to mitigate against any potential conflict of interest resulting from ESR Cayman's interests in Sabana REIT and ESR-REIT and their respective managers. These controls include:

- The Board is comprised **entirely of independent directors**, with no representation of directors from either the ESR Cayman or the ESR-REIT Manager.
- There is **no overlap of management teams** between the Sabana Manager and the ESR-REIT Manager.
- All decision-making for the business strategy and operations of Sabana REIT is made solely by the Board and the management team of the Sabana Manager, and the Sabana Manager has its own decision-making process which is independent of ESR Cayman or ESR-REIT.
- Since ESR Cayman's acquisition of the Sabana Manager, information barriers have been in place between the Sabana Manager and the ESR-REIT Manager and between Sabana Manager and ESR Cayman, to ensure that any information relating to Sabana REIT's business strategy or operations is not made privy to ESR-REIT (and vice versa) or shared with ESR Cayman.
- The offices of ESR Cayman, Sabana Manager, and ESR-REIT Manager are separately located in three different physical locations.

B. Transaction-related

2. Why is Sabana REIT selling its assets at a discount to NAV?

- The transaction is a **unit-for-unit merger**. This is **not a sale of assets.**
- The Merger allows Sabana Unitholders to receive consideration units in ESR-REIT and stay invested in an enlarged REIT and enjoy the potential upside post-Merger as elaborated below.
- A merger into an enlarged REIT ("**Enlarged REIT**") **offers the best opportunity for re-rating and for reducing the NAV discount in the long term** as part of a larger, more liquid and scalable REIT that is backed and supported by a developer-sponsor.
- The discount to NAV in respect of the Merger is reflective of Sabana REIT's unit trading price at the time of the Joint Announcement, which is similar to historical REIT mergers that had largely been priced at around the market price (and implied price-to-NAV ("**P/NAV**")) of the respective REITs (as seen in the table below) at the time of announcement of those mergers.

Merger[1]	Target	Implied price based on scheme consideration (S$)	Last traded price prior to announcement (S$)	Last reported NAV per unit prior to announcement (S$)	P/NAV based on scheme consideration[2]	Last traded P/NAV[3]	Difference between P/NAV based on scheme consideration vs. last traded P/NAV
ART-AHT	AHT	1.087	0.975	1.016	1.07x	0.96x	0.11x
CMT-CCT	CCT	2.124	2.130	1.860[4]	1.14x	1.15x	(0.00x)
ESR-REIT-VIT	VIT	0.960	0.890	0.760	1.26x	1.17x	0.09x
FLT-FCOT	FCOT	1.680	1.670	1.629	1.03x	1.03x	0.01x
OUECT-OUEHT	OUEHT	0.747	0.735	0.750	1.00x	0.98x	0.02x
ESR-REIT-Sabana REIT	Sabana REIT	0.377	0.360	0.512	0.74x	0.70x	0.03x

Notes:

(1) ART refers to Ascott Residence Trust, AHT refers to Ascendas Hospitality Trust, CMT refers to Capitaland Mall Trust, CCT refers to Capitaland Commercial Trust, VIT refers to Viva Industrial Trust, FLT refers to Frasers Logistics & Industrial Trust, FCOT refers to Frasers Commercial Trust, OUECT refers to OUE Commercial REIT, OUEHT refers to OUE Hospitality Trust.

(2) Based on the issue price used in the respective REIT merger announcements and reported target NAV prior to announcement.

(3) Based on the last "unaffected" price (i.e. prior to the relevant announcement date) and reported target NAV prior to announcement.

(4) Based on unadjusted CCT NAV per unit as at 31 December 2019, being the last reported NAV per unit prior to the CMT-CCT merger announcement.

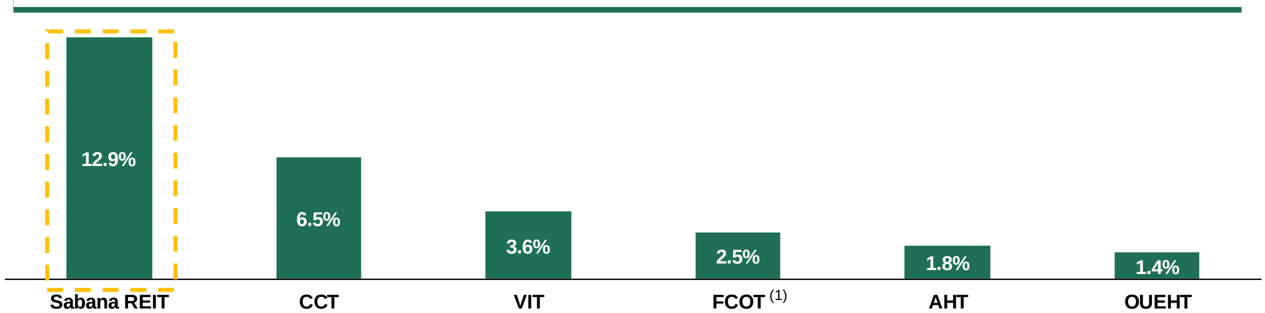
- While NAV per unit is a pertinent evaluation consideration, it should not be the only factor when considering the merits of the Merger and Sabana Unitholders should also take into consideration the following merits of the Merger (details of which are set out in the Joint Announcement):

  (i) **<u>Pro forma DPU accretion of 12.9% is the highest</u>** among prior S-REIT mergers; and

  (ii) a **<u>compelling transaction rationale</u>** for Sabana Unitholders, which is particularly relevant and important in the current uncertain environment, namely:

  - creation of a sizeable and liquid industrial real estate investment trust in Singapore;
  - enhanced portfolio diversification, strength, and resilience;
  - improved growth outlook with greater capacity for Asset Enhancement Initiatives ("**AEIs**") and / or potential asset redevelopment; and
  - enhanced balance sheet flexibility, better access to capital and lower cost of funding.

Pro-forma DPU accretion



Source: Based on DPU accretion reported in the respective merger documents.
Note: CCT refers to Capitaland Commercial Trust, VIT refers to Viva Industrial Trust, FCOT refers to Frasers Commercial Trust, AHT refers to Ascendas Hospitality Trust, OUEHT refers to OUE Hospitality Trust.
Chart excludes Croesus Trust, Accordia Golf Trust and Saizen REIT transactions as these are privatisations / asset sales (and not REIT mergers), whereby the target unitholders do not stay invested in the merged REIT.
(1) FCOT pro forma DPU accretion is based solely on the impact of the FLT-FCOT merger and does not include the impact of the proposed asset acquisition.

3. Why sell now, when the unit price is low during the COVID-19 pandemic, which results in a low offer price?

- The transaction is a **<u>unit-for-unit merger</u>**. This is **<u>not a sale of assets</u>**.
- When COVID-19 pandemic subsides and the economy begins to recover, Sabana REIT wants to be well-positioned to take advantage of any opportunities that may become available, including the recovery in the demand for logistics / industrial space as global trade and economy pick up.

- As such, Sabana REIT needs to better position its portfolio to tap on such opportunities whether by way of AEIs, redevelopments and / or the repositioning of properties to make it more attractive for tenants. Such strategic initiatives require funding.

- It will be more challenging and slower for Sabana REIT to do so as a standalone sub-scale REIT as compared to leveraging the support of the Enlarged REIT platform to execute these strategies.

- The greater scale resulting from the Merger would also allow Sabana REIT to be more resilient amidst the COVID-19 situation, to emerge stronger post pandemic and to execute the necessary strategies at lower cost of funding in order to tap on available opportunities.

  - Sabana Unitholders that choose to stay invested in the Enlarged REIT post-Merger will still get to enjoy the recovery and any potential future upsides not available in an asset sale.

- Additionally, given that this is a **unit-for-unit merger**, **the relevant metric is the GXR**, which is a relative price metric (ESR-REIT unit price versus Sabana REIT unit price). As such, despite the COVID-19 period, the Sabana Manager believes that it is a good time for Sabana REIT to carry out the Merger, given that **the implied GXR of the scheme consideration is at a premium to historical GXRs**. To illustrate, the current Merger terms imply a GXR of 0.940x, which is higher than the historical GXRs laid out in the table below:

	Sabana REIT (S$)	ESR-REIT (S$)	GXR	% premium over historical GXR[1]
At announcement	0.360	0.390	0.92x	1.8%
1M average	0.360	0.396	0.91x	3.3%
3M average	0.343	0.377	0.91x	3.3%
6M average	0.369	0.415	0.89x	5.8%
12M average	0.413	0.473	0.87x	7.7%
24M average	0.417	0.495	0.84x	11.6%

Note: GXR is calculated by dividing the relevant Sabana REIT unit price by the corresponding ESR-REIT unit price. For example, 1M average would be the average unit price for Sabana REIT / ESR-REIT for the 1-month period up to 15 July 2020, being the last trading day before the Joint Announcement.

(1) Calculations made using precise (i.e. not rounded) figures.

- Prior to ESR Cayman taking ownership in the Sabana Manager, an independent strategic review was conducted by the previous management team of the Sabana Manager in 2017, where the Sabana Manager had sought proposals from prospective strategic partners which would further strengthen Sabana REIT. However, there was no formal offer received by the Sabana Manager that could be presented to Sabana Unitholders as part of that strategic review.

- Since then, the Merger is the only formal offer which the Board has received for the Sabana Units or Sabana REIT's entire portfolio. The Board had followed due process to evaluate the offer and negotiate the best possible terms for the Sabana Unitholders and had, in accordance with its fiduciary duties, decided that the Merger should be put to a vote by the independent Sabana Unitholders, where ESR-REIT Manager, its concert parties as well as the common substantial Sabana Unitholders / ESR-REIT Unitholders, including ESR Cayman and its related parties are required to abstain from voting.

4. Why are Sabana Unitholders not being offered any cash?

- The Scheme Consideration was determined based on independent commercial negotiations between the Sabana Manager and the ESR-REIT Manager. Factors taken into account in arriving at the Scheme Consideration by determining the GXR include (but are not limited to):

- the prevailing and historical relative market prices of the Sabana Units and the units in ESR-REIT ("**ESR-REIT Units**");
- the NAVs of Sabana REIT and ESR-REIT, prevailing and historical prices to NAV per unit, distribution yield, market capitalization, trading liquidity, capital structure, debt costs and debt tenor of each of Sabana REIT and ESR-REIT;
- the market conditions and market value of the respective property portfolios;
- relevant precedent trust scheme transactions in Singapore; and
- the resulting pro forma financial impact of the Merger on Sabana REIT and ESR-REIT.

- In evaluating and negotiating the terms of the Merger, the Board and the management team of the Sabana Manager took into consideration various factors outlined above. Importantly, in view of the current economic environment, Sabana REIT's current debt structure and potential future AEI plans for the Enlarged REIT, it would be **prudent to have an "all-unit" merger without a cash component in order to conserve cash and preserve debt headroom, so as to retain balance sheet flexibility for the Enlarged REIT**, which Sabana Unitholders will be unitholders of upon completion of the Merger.

5. Why did Sabana REIT not consider a NAV-NAV merger?

- In evaluating and negotiating the terms of the Merger, the Board and the management team of the Sabana Manager took into consideration various factors, including DPU accretion, NAV discount, the premium of the GXR over historical exchange ratios based on unit trading prices, as well as other factors relating to the operational and business environment, especially in light of the COVID-19 pandemic.
- After careful assessment of the above factors, the Board supports the rationale of this Merger. In accordance with the Board's fiduciary duties to Sabana Unitholders, the Board and the management of Sabana REIT negotiated for the best possible terms with ESR-REIT.
- It is important to note that a NAV-NAV merger would have been both DPU and NAV dilutive for ESR-REIT Unitholders, and the Merger by way of a Scheme is ultimately required to be approved by both Sabana Unitholders and ESR-REIT Unitholders.

6. Did Sabana REIT ask the ESR-REIT Manager to raise the Scheme Consideration after some investors mentioned on 30 July 2020 that it was too low? Given that the ESR-REIT Manager said soon after, on 6 August 2020, that it did not intend to increase the Scheme Consideration, can the terms of the Merger still be modified in any way?

- The transaction terms have been discussed and heavily negotiated between the boards of directors and the management teams of both the Sabana Manager and the ESR-REIT Manager, with the transaction terms agreed and announced on 16 July 2020.
- As mentioned in the announcement released on 6 August 2020 by ESR-REIT, the terms of the Merger are final and binding on the parties as per the Implementation Agreement which has been entered into on 16 July 2020, and the ESR-REIT Manager has announced and it does not intend to increase the Scheme Consideration. Therefore, in accordance with Rule 20.2 of the Singapore Code on Take-overs and Mergers (the "**Code**"), the ESR-REIT Manager will not be allowed to subsequently

increase the Scheme Consideration, in any way, save that the ESR-REIT Manager may do so in a competitive situation.

7. What are the independent directors' views on the Merger?

- In accordance with its fiduciary duties, the Board is proposing the Merger by way of a Scheme for the consideration of the independent Sabana Unitholders, as it believes that independent Sabana Unitholders should have the opportunity to decide and vote on the Merger, taking into account the compelling transaction rationale, and various other factors such as the premium of the GXR over historical exchange ratios based on the respective unit trading prices, DPU accretion, NAV discount, the property portfolio of both REITs as well as the challenges of continuing as a smaller standalone REIT in comparison to a potential value uplift from being part of a larger combined REIT (4th largest industrial S-REIT by Singapore industrial GFA market share).
- The recommendation of the Board (which comprises only independent directors), along with the opinion of the IFA, will be included in the Scheme Document to be despatched or issued to the Sabana Unitholders in due course.

8. Has the Board fully evaluated its strategic options? Why did it not run a public sale process to maximise value?

- Prior to ESR Cayman taking ownership in the Sabana Manager, an independent strategic review was conducted by the previous management team of the Sabana Manager in 2017, where the Sabana Manager had sought proposals from prospective strategic partners which would further strengthen Sabana REIT. However, there was no formal offer received by the Sabana Manager that could be presented to Sabana Unitholders as part of that strategic review.
- Since then, the Merger is the only formal offer which the Board has received for Sabana Units or Sabana REIT's entire portfolio. The Board had followed due process to evaluate the offer and negotiate the best possible terms for the Sabana Unitholders and had, in accordance with its fiduciary duties, decided that the Merger should be put to a vote by the independent Sabana Unitholders, where ESR-REIT Manager, its concert parties as well as the common substantial Sabana Unitholders / ESR-REIT Unitholders, including ESR Cayman and its related parties are required to abstain from voting.
- Sabana REIT is not looking to sell all its assets. The Merger is the only offer received to date with transaction terms which have been heavily negotiated. This is a strategic merger transaction with significant long-term benefits, including size, scale and resilience, which are particularly relevant in the current challenging environment, as mentioned above.
- In addition, there are challenges to selling part of, or the entire property portfolio of Sabana REIT. Some of these challenges include the following:

  (i) Unlike other property sectors, the Singapore industrial sector is heavily regulated by JTC Corporation ("**JTC**"), with only approved buyers being able to acquire properties on JTC land. The approved buyers are qualified end-users, REITs and CMS licensed entities. There are also other assignment policies in place such as:

    (a) moratorium period for assignment / sale;

    (b) value-adding criteria whereby prospective end-buyers are subject to JTC's assessment of their proposed usage, current utilization of space, business plan and value to be generated from their business for the next five years; and

(c) other than JTC, sale of industrial properties is also subject to the approval of other authorities such as Urban Redevelopment Authority (“**URA**”), National Environment Agency (“**NEA**”) and Land Transport Authority (“**LTA**”).

Transactions involving JTC properties typically take more than six months and if approval is not granted, the whole marketing process for the property has to be repeated.

(ii) A sale of property portfolio runs the risk of better quality assets being sold, with weaker assets remaining in a sub-scale portfolio which will in turn impact Sabana REIT’s ability to grow accretively going forward; and

(iii) Execution risks of putting up material assets for sale. A delay in or failure to achieve the sale outcome due to regulations may impact ongoing and future tenancies as the tenants may be concerned with the identity and stability of their landlords.

9. If an investor presents alternative options, will Sabana REIT evaluate these options? Can Sabana REIT walk away from the Merger if the alternative options are feasible?

- The Merger is the only formal offer which the Board has received for Sabana Units or Sabana REIT’s entire portfolio. Sabana REIT has not received any other formal offer since the independent strategic review conducted in 2017 by the previous management team of the Sabana Manager.
- The Merger is considered a public takeover and is subject to the Code as well as the terms of the Implementation Agreement, which is a binding agreement between Sabana REIT and ESR-REIT. Subject to the terms of the Implementation Agreement, the Sabana Manager will not be entitled to walk away from the Merger if the alternative options are presented and the Board will be obliged to propose the Merger to the independent Sabana Unitholders for their consideration.
- If, however, the Sabana Manager receives an unsolicited proposal from an investor during the offer period, the Board will be entitled under the Implementation Agreement to perform all acts that may be necessary to comply with and discharge their fiduciary duties and/or statutory, regulatory and/or legal obligations under all applicable laws and regulations. This includes announcing the receipt of any such proposal in compliance with applicable laws or regulations, reviewing and evaluating such proposal, and making recommendations to the Sabana Unitholders as may be required under applicable laws and regulations.

10. How did this transaction come about? What was ESR Cayman’s role during the negotiations?

- The Sabana Manager reviews its portfolio on an ongoing basis and constantly seeks measures to strengthen and improve the resilience and performance of its portfolio so as to create long-term value for Sabana Unitholders. This includes evaluating the potential merits of a merger for the Sabana Unitholders.
- In May 2020, Sabana REIT received a letter of interest from ESR-REIT proposing a merger between Sabana REIT and ESR-REIT, subsequent to which Sabana REIT undertook a detailed deal assessment, which involved lengthy and careful deliberations and evaluations, and financial advisors were engaged to evaluate the commercial terms of the offer.
- The Board is completely independent, and there were no ESR Cayman representatives at any of its meetings.
- The Sabana Manager and the Board, aided by their financial advisors, conducted the transaction assessments and commercial negotiations.

C. Execution of growth strategy by Sabana REIT

11. Has Sabana REIT looked closely at past suggestions from investors to grow earnings organically? How have these suggestions been evaluated?

- The Sabana Manager reviews its portfolio on an ongoing basis and constantly seeks measures to strengthen and improve the resilience and performance of its portfolio so as to create long-term value for Sabana Unitholders.
- The Sabana Manager has evaluated the following suggestions from Sabana Unitholders, but notes that these suggestions do not take into consideration the practical challenges that an industrial REIT manager faces in the Singapore industrial market:

(i) It was suggested that Sabana REIT is inefficiently under-geared with substantial debt headroom to acquire new assets or pursue unit buybacks.

The Sabana Manager wishes to highlight the following:

- As at 30 June 2020, 93.8% of the Sabana portfolio is secured against its borrowings of S$284.4 million. That leaves only 6.2% of the portfolio, representing two assets valued at S$51.7 million, which may be encumbered for any additional secured financing (including for AEIs and working capital purposes). This is more reflective of the actual debt headroom available for Sabana REIT.
  - In addition, applying the typical approximate 50% LTV ratio that banks have historically lent to Sabana REIT on a secured basis, given its portfolio size and asset quality, means that with only two assets valued at S$51.7 million unencumbered, Sabana REIT would only be able to potentially obtain additional amount of approximately S$25.9 million in loans.
  - As Sabana REIT's debt financing is mostly on a secured basis, the actual debt headroom is limited to the number of properties left to be secured for financing and the LTV on the valuation of the secured properties.
- If Sabana REIT continues to operate on a standalone basis, Sabana REIT, as the smallest industrial REIT in Singapore listed on the SGX-ST, will continue to be less competitive in the REITs market. On the contrary, as an Enlarged REIT following the Merger, Sabana REIT would be better positioned to compete for a larger piece of the overall Singapore industrial property market, with a larger debt headroom, greater financial flexibility and more competitive cost of funding on an enlarged basis.
- Furthermore, with respect to the unit buybacks, the Sabana Manager considers Sabana REIT's capital structure / management holistically along with the overall strategy and operating environment to create long-term value for Sabana Unitholders. Given the operating cash flow requirements, there is limited debt headroom for the Sabana Manager to pursue unit buybacks.

- Finally, as Sabana REIT continues to weather the COVID-19 pandemic, it is crucial to maintain fiscal discipline and prudence. As such, the immediate focus is on managing Sabana REIT's existing operations and having ample liquidity while maintaining a stable balance sheet and cash position.

(ii) It was suggested that there are opportunities for further upside given untapped GFA.

The Sabana Manager wishes to highlight the following:

- The concept of "untapped GFA" being equivalent to "land" as mentioned by certain investors is misleading. For most of Sabana REIT's properties, there is not much "excess" land (capable of independent development) for Sabana REIT to develop the second or third property. In order to make use of the "untapped GFA", it will first need to tear down the existing property in order to redevelop to a bigger property. Construction for the bigger property usually takes approximately 18 to 24 months, during which the owner (or landlord) will not be able to collect any rent while still having to pay for all expenses.

- By way of illustration, the average gross revenue contribution per asset (based on 17 properties, excluding 1 Tuas Avenue 4 which is currently vacant), is approximately 6%. The tearing down and redevelopment of an asset will immediately see a 6% drop in DPU across the development period of approximately 18 to 24 months while still incurring all other property expenses and additional funding costs for the AEI. The consideration to redevelop also depends on (i) whether the property is tenanted and if the REIT is able to pre-terminate the tenancies to carry out such redevelopment works; (ii) availability of funds; (iii) limitations of the development limit under the Property Fund Guidelines; (iv) approvals by various government agencies such as JTC or LTA; and (v) visibility on tenancy.

- Feasibility of "adding" GFA without affecting the existing structure so as to minimise the impact on existing tenancies and DPU are also explored but such methods can be very costly, may cause disturbance to existing occupiers and only works for smaller scale AEI where the specifications and integrity of the structure will not be adversely affected.

- As a standalone REIT, it would be more challenging and would take a significantly longer time for Sabana REIT to maximise its untapped GFA. However, following the Merger, the Enlarged REIT may potentially benefit from optimising its untapped GFA given that: (1) the closing down of assets may not adversely impact DPU as much or may potentially be negligible, given that each asset contributes a much smaller proportion of the portfolio; (2) more flexible leasing arrangements may be made with existing tenants who still have leases running (e.g., relocating existing tenants to other assets within the portfolio) as the portfolio is larger with alternative assets which may suit tenant requirements; (3) the cost of funding these redevelopments can be cheaper, resulting in higher returns; and (4) the Enlarged REIT will have an increased development headroom under the Property Funds Appendix, given the larger portfolio.

(iii) It was suggested that Sabana REIT should grow earnings by exploring a sale of assets.

The Sabana Manager wishes to highlight the following:

- Sabana Manager has consistently explored divestments of selected assets, which were deemed to be non-core.
- When the new management of Sabana REIT came onboard in 2018 following its strategic review, it announced and implemented its refreshed strategy ("**Refreshed Strategy**"). Some key initiatives pursuant to the Refreshed Strategy included:
    - divestment of non-performing and matured assets. The Sabana Manager completed the sale of 6 Woodlands Loop in early 2018 and 9 Tai Seng Drive in early 2019; and
    - the Sabana Manager was also pursuing the divestment of 1 Tuas Avenue 4, which was eventually aborted as the buyer was not granted approval by JTC. As explained by the Sabana Manager in relation to question 8 above, the approval requirement from JTC represents one of the key challenges to asset transactions in the Singapore industrial market. The Sabana Manager was open to exploring the sale of some other assets but there has been little interest, especially given the current softer economic environment.
- However, a sale of assets may not necessarily be at a compelling price. This is evident in a recent factory sale along Tuas Avenue 4 (with a 28-year lease), which was sold for S$3.7 million, being 32% lower than the S$5 million guide price (Business Times article on 27 July 2020 titled "Distressed properties sold via private treaty as auctions remain no-go").
- Post the streamlining of its portfolio, the management of the Sabana Manager is now focused on delivering Phase 2 of its Refreshed Strategy, where the focus will be on enhancing portfolio returns through AEIs. As explained in relation to question 11(ii) above, being part of the Enlarged REIT post-Merger with access to lower cost of funding will in turn reduce overall execution risks and enhance returns.

(iv) It was suggested that Sabana REIT should pay management fees in units.

The Sabana Manager wishes to highlight the following:

- The issue price of the new Sabana Units to settle the payment of management fees is based on a 10business day volume-weighted average price ("**VWAP**"). As Sabana REIT has typically traded below its NAV per unit, the issuance of new units for fee settlement at issue prices below NAV per unit would be NAV dilutive to Sabana Unitholders. Moreover, the additional new units issued would increase the total number of outstanding Sabana Units (total unit base), leading to DPU dilution in the following semi-annual distributions.

12. Why did Sabana REIT register such low occupancy rates / a slowdown in occupancy rates despite the change in Sponsor? Can you clarify the impact of master leases on this?

- In 1H2020, the overall portfolio occupancy stood at 77.3%, which is an improvement over the FY2019 overall portfolio occupancy of 75.4%.
- Excluding 1 Tuas Avenue 4 (which is vacant due to being slated for divestment), the occupancy in 1H2020 was actually at 80.2%.
- The dip in occupancy rates in 3Q2019 and 4Q2019 was mainly due to the conversion of 10 Changi South Street 2 ("**10CSS2**") and 3A Joo Koon Circle ("**3AJKC**") from master-leased to multi-tenanted properties. 10CSS2 was a termination event as a result of default by then master-tenant while 3AJKC was a non-renewal due to tenant's expansion plan which 3AJKC could not accommodate; however, Sabana REIT has since secured tenants for approximately 95% of 3AJKC (of which approximately 40% is on short-term lease). It is worth noting that short-term leases of less than one year are not included in the overall occupancy rate computation.
- These two assets contributed to approximately 12.4% of the portfolio occupancy, magnified by the small portfolio size, due to Sabana REIT being the smallest industrial S-REIT in terms of asset size.
- The default / non-renewal of the two master tenants were neither within the Sabana Manager's nor ESR Cayman's controls.
- Following the Merger with ESR-REIT, Sabana Unitholders will be able to benefit from an Enlarged REIT that will be larger, stronger, more diversified and resilient with significantly more favorable debt terms, diversifying portfolio risks, and increasing execution capabilities while maintaining a stable DPU profile and potentially enhancing returns from the AEIs.

13. What are the challenges of Sabana REIT as a standalone smaller REIT?

In summary, the following are some of the challenges which Sabana REIT faces as one of the smallest S-REITs in the S-REIT industry:

- There are limited financing resources to fund the growth of Sabana REIT as all the loan funding in Sabana REIT are on a secured basis. Currently, approximately 93.8% of its portfolio are encumbered, notwithstanding that Sabana REIT has a low aggregate leverage ratio. Only two assets valued at S$51.7 million as at 30 June 2020 are unencumbered. Assuming a loan-to-value ("**LTV**") ratio of 50%, the available debt headroom is S$25.9 million.
- Higher cost of funds due to higher credit and portfolio risk as a standalone REIT, compared to the Enlarged REIT, makes Sabana REIT less competitive in obtaining financing for its initiatives.
- Lower development limit (based on 10% of total deposited property value of Sabana REIT) to undertake frequent and larger size AEIs and / or redevelopments to keep its portfolio contemporary to improve its occupancy and DPU within a short period of time.
- Vacancy rate and financial impact from loss of revenue due to downtime from AEIs and/or redevelopments of portfolio are magnified due to a smaller asset base.
- Overseas expansion is difficult as a growth strategy for a small REIT with no networks, visible and sustainable pipelines and scalability, etc.
- Limited risk diversification on smaller portfolio.

Sabana REIT can survive as a standalone REIT but will face more difficulties and constraints due to its small asset base as a small REIT as highlighted in our clarifications to questions 11 and 12 above. If the COVID-19 situation is prolonged, it will present Sabana REIT with continuing and more uncertainties because of its size.

Therefore, a better option is to consider the only offer proposed to Sabana REIT – to merge with ESR-REIT to create a more sizeable, more liquid and more resilient platform with long-term synergies in order to improve the position of Sabana Unitholders and come out of the COVID-19 pandemic stronger.

D. General questions relating to Sabana REIT

14. Why has Sabana REIT not removed its Shari'ah compliance despite earlier calls from investors? Were you timing it for the Merger?

- The new management team of the Sabana Manager came onboard in 2018, and had to prioritise key issues within the group, from high and unsustainable leverage, to divesting non-core assets, and improving asset returns. The Sabana Manager actively reviews its strategies and positioning on an ongoing basis in view of creating long-term value for Sabana Unitholders, including but not limited to assessing the continued relevance of maintaining the Shari'ah compliance status.
- In relation to the Merger, ESR-REIT, as the Enlarged REIT post the Merger, is the entity which will remain listed on the SGX-ST. Since ESR-REIT is not a Shari'ah compliant REIT and all the Sabana REIT's existing loans will be refinanced with conventional bank loans and debts on an unsecured basis which are non-Shari'ah compliant in nature by ESR-REIT post-Merger, the current Shari'ah compliant status of Sabana REIT will not be retained post-Merger.

15. Would removing Sabana REIT's Shari'ah compliance requirement have increased DPU significantly?

- In the past three years, the Sabana Manager has only encountered one or two prospective tenants with small footprint requirements who had activities that do not comply with the Shari'ah compliance requirement. As such, these prospective tenants would not have made any significant impact on the occupancy or rental revenue contribution to Sabana REIT.
- As part of the delisting of Sabana REIT post the Merger, ESR-REIT has obtained conventional bank loans to fully refinance Sabana REIT's Shari'ah compliant debt.
- The suggestion that the removal of Shari'ah compliance of Sabana REIT would drastically reduce financing costs is a misconception because the borrower's credit risk determines LTV quantum and loan pricing for financing of properties. Lenders assess the credit risk of a REIT by the size, quality, portfolio diversity, stability of cashflows, percentage of secured versus unsecured assets, debt expiry profile, debt tenor and track record of sponsor's backing (i.e. credit factors) in determining the LTV and pricing terms for Sabana REIT's debt. Removing the Shari'ah compliance does not change the credit risk profile of a REIT. This is evident by the fact that three of the four lending banks lending to ESR-REIT for the Proposed Merger are existing lending banks of Sabana REIT, and are currently lending to Sabana REIT at an interest rate of 3.8% per annum and on a secured basis, whereas the Enlarged REIT is able to refinance this debt at <u>a lower interest rate of 2.5% per annum with a longer tenor on an unsecured basis, against the same Sabana portfolio</u>. As a standalone entity currently, it would remain challenging for Sabana REIT to obtain similar debt terms, with or without its Shari'ah compliance status, due to its credit risk as a small REIT.

16. Can you disclose the provisions and allowances for impairments that you have made?

- In light of the still-evolving COVID-19 situation and uncertainties, Sabana REIT has made a one-time provision for rental waivers and allowances for impairment losses on trade receivables for certain tenants across the portfolio out of prudence and practicality:
    - Provision for impairments of accounts receivables of S$992k as a provision for bad debt;
    - Provision for rental rebates of S$806k to support SMEs as required by the Fortitude Budget;
    - Sabana REIT has an SME tenant exposure of approximately 50%, which increases the risk of the portfolio given that they would have been more significantly affected by the COVID-19 pandemic and thus providing a need for greater prudence in conserving cash;
    - Changes and variations in government policies and legislations with regards to landlords' obligations to tenants further add to potential cashflow uncertainties, e.g. COVID-19 (Temporary Measures) Act 2020.
- These provisions were required by Sabana REIT through the uncertain times of COVID-19 pandemic, and were made on a basis that is appropriate and according to the relevant accounting standards as audited by the auditors.

17. Can you please clarify the contribution of the retail component from the New Tech Park AEI?

- Contrary to the claim that the retail component has been conveniently absent in the pro forma DPU calculations, the preparation of the pro forma financial effects follows strict accounting guidelines which only allows adjustments directly related to the Merger to be made. The financial effects are also prepared in accordance with the financial reporting standards, as reviewed by the Reporting Accountant. As disclosed in the 1H2020 results presentation, the retail component is envisaged to be completed in 1Q2021 and cannot be directly attributed to the Merger.
- In addition, some investors may have alluded to the retail component potentially generating a net property income ("**NPI**") of S$4.4 million in FY2021 that would yield more than 10% growth in DPU. This would imply a rental rate of approximately S$13.10 psf/month on 100% occupancy and 100% of its GFA, assuming a typical 65% NPI margin. However, in reality, retail units are leased on NLA (and not on GFA) basis, excluding common areas and facilities which are non-revenue generating. For example, the new retail mall in New Tech Park will have a NLA of approximately 35,000 sqft out of the 43,000 sqft GFA.
- Further, according to URA's Retail Space Vacancy data, the vacancy rate for 2Q 2020 has increased to 9.6% from 8.0% in 1Q 2020. Asking rentals in CommercialGuru[2] for similar type retail malls in Business 1 development range from S$5.00 to S$10.00 psf/month and are lower than the rental rate of S$13.10 psf/month which has been implied. Hence, even assuming 100% occupancy at S$10.00psf/month on a NLA of 35,000 sqft, based on a full year projection (notwithstanding that the new mall will likely start collecting rental only from 2Q 2021, after provisions for rent-free fitting out period), the NPI that could potentially be generated is only approximately S$2.7 million instead of S$4.4 million for FY2021. Furthermore, the NPI of S$2.7 million is before the deduction of other costs such as interest costs, management and trustee fees, etc. If additional costs were taken into

[2] Source: www.commercialguru.com.sg

consideration, the potential growth in DPU would likely be considerably lower than the 10% estimation.

- With the Merger, it is important for Sabana Unitholders to note that even after the Merger, Sabana Unitholders will still be able to benefit from the additional NPI from the retail component after its completion, as part of the Enlarged REIT, and this is in addition to the 12.9% pro forma DPU accretion from the Merger. Sabana Unitholders should, however, be aware that there may be some degree of uncertainty due to current economic environment.

18. Can you disclose what adjustments or assumptions have been made in determining the Merger's pro forma DPU? How reasonable and realistic are such adjustments and assumptions?

- Please refer to Schedule 4 of the Joint Announcement ("Pro forma financial effects of the Merger") for the details of the pro forma 1H2020 DPU calculations and adjustments.
- The preparation of the pro forma financial effects follows strict accounting guidelines which only allows for adjustments directly related to the Merger to be made. The pro forma financial effects were also prepared in accordance with the financial reporting standards, as reviewed by the Reporting Accountant.

By Order of the Board

Sabana Real Estate Investment Management Pte. Ltd.
(Company registration number 201005493K, Capital markets services licence no: CMS100169)
As Manager of Sabana Shari'ah Compliant Industrial Real Estate Investment Trust

Han Yong Lee
Chief Executive Officer
28 August 2020

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Sabana REIT

Sabana REIT was listed on the SGX-ST on 26 November 2010. It was established principally to invest in income-producing real estate used for industrial purposes, as well as real estate-related assets, in line with Shari'ah investment principles. As at 30 June 2020, Sabana REIT has a diversified portfolio of 18 properties in Singapore, in the high-tech industrial, warehouse and logistics, chemical warehouse and logistics, as well as general industrial sectors. The total assets of the Group amount to approximately S$0.9 billion as at 30 June 2020.

Sabana REIT is listed in several indices within the SGX S-REIT Index, Morgan Stanley Capital International, Inc (MSCI) Index and FTSE index. Sabana REIT is one of the constituents of the FTSE ST Singapore Shariah Index.

Sabana REIT is managed by Sabana Real Estate Investment Management Pte. Ltd. (in its capacity as the Manager of Sabana REIT) in accordance with the terms of the trust deed dated 29 October 2010 (as amended). Sabana REIT is a real estate investment trust constituted on 29 October 2010 under the laws of Singapore.

For further information on Sabana REIT, please visit www.sabana-reit.com.

Directors' Responsibility Statement

The directors of the Manager (including those who may have delegated detailed supervision of this announcement) have taken all reasonable care to ensure that the facts stated and opinions expressed in this announcement (other than those relating to ESR-REIT and/or the ESR-REIT Manager) are fair and accurate and that there are no other material facts not contained in this announcement, the omission of which would make any statement in this announcement misleading. The directors of the Manager jointly and severally accept responsibility accordingly.

Where any information has been extracted or reproduced from published or otherwise publicly available sources or obtained from a named source (including ESR-REIT and the ESR-REIT Manager), the sole responsibility of the directors of the Manager has been to ensure through reasonable enquiries that such information is accurately extracted from such sources or, as the case may be, reflected or reproduced in this announcement. The directors of the Manager do not accept any responsibility for any information relating to ESR-REIT and/or the ESR-REIT Manager.

Important Notice

The value of units in Sabana REIT ("**Units**") and the income derived from them may fall as well as rise. Units are not obligations of, deposits in, or guaranteed by, the Manager, HSBC Institutional Trust Services (Singapore) Limited, as trustee of Sabana REIT, or any of their respective affiliates.

An investment in Units is subject to investment risks, including the possible loss of the principal amount invested. Investors have no right to request that the Manager redeem or purchase their Units while the Units are listed. It is intended that Sabana Unitholders may only deal in their Units through trading on the SGX-ST. Listing of the Units on the SGX-ST does not guarantee a liquid market for the Units.