Independent Auditor's Report

Independent auditor's report

To the stapled security holders of Dexus Diversified Trust

Report on the audit of the financial report

Our opinion

In our opinion:

The accompanying financial report of Dexus Diversified Trust (the Registered Scheme) and its controlled entities and stapled entities (together the Group) is in accordance with the *Corporations Act 2001*, including:

(a) giving a true and fair view of the Group's financial position as at 30 June 2018 and of its financial performance for the year then ended

(b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

What we have audited

For the purposes of consolidation accounting, Dexus Diversified Trust (DDF) is the parent entity and deemed acquirer of Dexus Industrial Trust (DIT), Dexus Office Trust (DOT) and Dexus Operations Trust (DXO). The financial report represents the consolidated results of DDF and include DDF and its controlled entities, DIT and its controlled entities, DOT and its controlled entities, and DXO and its controlled entities.

The Group financial report comprises:

- the Consolidated Statement of Financial Position as at 30 June 2018
- the Consolidated Statement of Comprehensive Income for the year then ended
- the Consolidated Statement of Changes in Equity for the year then ended
- the Consolidated Statement of Cash Flows for the year then ended
- the Notes to the Financial Statements, which include significant accounting policies
- the Directors' Declaration.

Basis for opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial report* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant

Independent Auditor's Report
continued

to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

Our audit approach

An audit is designed to provide reasonable assurance about whether the financial report is free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report.

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial report as a whole, taking into account the geographic and management structure of the Group, its accounting processes and controls and the industry in which it operates.

Materiality	*Audit scope*	*Key audit matters*
• For the purpose of our audit we used overall materiality of \$32.6 million, which represents approximately 5% of the Group's adjusted profit before tax (Funds From Operations or FFO). • We applied this threshold, together with qualitative considerations, to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements on the financial report as a whole. • We chose FFO because, in our view, it is the key performance measure of the Group. An explanation of what is included in FFO is outlined in Note 1, Operating segments. • We utilised a 5% threshold based on our professional judgement, noting it is within the range of commonly acceptable profit related thresholds.	• The Group is a stapled entity with operations in Australia. In a stapled group the securities of two or more entities are 'stapled' together and cannot be traded separately. In the case of the Group, the stapled entity includes DDF, DIT, DOT and DXO and their controlled entities. • Our audit focused on where the Group made subjective judgements; for example, significant accounting estimates involving assumptions and inherently uncertain future events. • We audited each of the individual stapled trusts that form the Group as well as the consolidation of the Group.	• Amongst other relevant topics, we communicated the following key audit matters to the Board Audit Committee: – Valuation of investment properties, including those investment properties in investments accounted for under the equity method – Carrying amount of indefinite life management rights – Carrying amount of inventory • These are further described in the *Key audit matters* section of our report.

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Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report for the current period. The key audit matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. Further, any commentary on the outcomes of a particular audit procedure is made in that context.

Key audit matter	*How our audit addressed the key audit matter*
Valuation of investment properties, including those investment properties in investments accounted for under the equity method *(Refer to Note 8 and 9)* The Group's investment property portfolio comprises: • Directly held properties included in the Consolidated Statement of Financial Position as *Investment Properties* valued at $8,242.6 million as at 30 June 2018 (2017: $7,169.1 million). • The Group's share of investment properties held through associates and joint ventures included in the Consolidated Statement of Financial Position as *Investments accounted for using the equity method* valued at $4,548.3 million as at 30 June 2018 (2017: $3,779.7 million). Investment properties are carried at fair value at reporting date using the Group's policy as described in Note 8. The valuation of investment properties is dependent on a number of assumptions and inputs including, tenant information, property age and location, expected future rental profiles, and prevailing market conditions. Amongst others, the following assumptions are key in establishing fair value: • The capitalisation rate • The adopted discount rate. We considered the valuation of investment properties to be a key audit matter due to the: • Financial significance of investment properties in the Consolidated Statement of Financial Position. • Potential for changes in the fair value of investment properties to have a significant effect on the Group's comprehensive income.	To assess the valuation of investment properties we performed the following procedures amongst others: • We considered the valuation methodology adopted by the Group and found it to be consistent with commonly accepted valuation approaches used for investment properties in the industry and the Group's valuation policy. • We obtained recent independent property market reports to develop an understanding of the prevailing market conditions in which the Group invests. We leveraged this knowledge to form independent expectations for movements in investment property values and underlying key assumptions such as capitalisation rates and discount rates. • We compared the capitalisation rates and discount rates used by the Group to ranges we determined were reasonable based on benchmark market data. Where capitalisation rates, discount rates and/or movements in individual property valuations fell outside of our anticipated ranges, we performed the following procedures, amongst others: - Met with the Group's Senior Valuation Manager and discussed the specifics of the selected individual properties including, amongst other things, any new leases entered into during the year, lease expiries, capital expenditure and vacancy rates. - Agreed significant changes in inputs to supporting documentation such as new lease agreements. We found that typically the variances related to the relative age, or size/location of the individual property in comparison to the market. In the

Independent Auditor's Report
continued

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Key audit matter	*How our audit addressed the key audit matter*
• Inherently subjective nature of investment property valuations arising from the use of assumptions in the valuation methodology. • Sensitivity of valuations to key input assumptions, including capitalisation rates, and discount rates.	context of the specific properties identified, we found the reasons for variances appropriate. • As the Group engaged external experts to determine the fair value of investment properties, we considered the independence, experience and competency of the Group's independent experts as well as the results of their procedures.
Carrying amount of indefinite life management rights *(Refer to Note 19)* At 30 June 2018 indefinite life management rights (management rights) amounting to $286.0 million (2017: $286.0 million) were recognised by the Group (included in the intangible assets balance). In accordance with the requirements of Australian Accounting Standards, indefinite life management rights are not amortised and are tested at least annually for impairment. The Group performed impairment testing of the management rights by comparing the recoverable amount of the management rights to their carrying amount. The Group concluded that management rights were not impaired. We considered the carrying amount of management rights a key audit matter given the: • Financial significance of the balance in the Consolidated Statement of Financial Position • Significant judgement required by the Group in estimating the recoverable amount of management rights • Sensitivity of the Group's assessment to changes in key assumptions such as growth rates, discount rates, and future cash flows.	To assess the impairment model used to determine the recoverable amount, we performed the following audit procedures, amongst others: • Assessed whether the division of the Group's management rights into cash generating units (CGU), was in line with the Australian Accounting Standards and consistent with our knowledge of the Group's operations and internal Group reporting. • Tested the mathematical accuracy of each impairment model's calculations. • Evaluated the Group's methodology and selected inputs and assumptions in the impairment model, such as discount rate, revenue and expense growth rates by comparing to observable market expectations. • Tested that forecast cash flows used in the impairment model were consistent with the most up-to-date budgets approved by the Board. For cash flows beyond year three that were not covered by formal budgets, we assessed the growth rates applied by comparing to observable market expectations. • Evaluated the Group's historical ability to forecast future cash flows by comparing budgets to reported actual results. • Considered the Group's sensitivity analysis on key assumptions used in the impairment model to assess under which assumptions an impairment would occur and whether this was reasonably possible. • Together with PwC valuation experts we considered whether the discount rate applied was consistent with observable market expectations.

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Key audit matter	*How our audit addressed the key audit matter*
Carrying amount of inventory *(Refer to Note 10)* The Group develops a portfolio of office and industrial sites for future sale, which are classified as inventory. At 30 June 2018 the carrying amount of the Group's inventory was $544.7 million (2017: $211.3 million). The Group's inventories are held at the lower of the cost or net realisable value for each inventory asset. The cost of inventory is calculated using actual acquisition costs, construction costs, development related costs and interest capitalised for eligible projects. Net realisable value is determined by using the valuation techniques referred to in the key audit matter: *Valuation of investment properties, including those properties in investments accounted for under the equity method* to determine the estimated future selling price, and adjusted for the estimated cost to complete and transaction costs. We considered the carrying amount of inventory to be a key audit matter given the: • Judgement required in determining the fair value of properties transferred from investment properties to inventory at the date of transfer. Refer to key audit matter: *Valuation of investment properties, including those properties in investments accounted for under the equity method* for key judgements in determining the fair value. • Judgements required by the Group in determining the estimated future selling prices, costs to complete and transaction costs. • Financial significance of the inventory balance in the Consolidated Statement of Financial Position. • The subsequent impact to FFO from the disposal of inventory where cost is determined by the fair value at the date of transfer.	To assess the carrying amount of inventory we performed the following procedures amongst others: • We used a risk based approach to select a sample of inventory assets on which to perform net realisable value testing. For the selected assets we: - Discussed with management the life cycle of the project, key project risks, changes to project strategy, current and future estimated sales prices, construction progress and costs and any new and previous impairments. - Selected a sample of costs capitalised to inventory to test that the cost had been capitalised in accordance with the Group's policy/methodology and the requirements of Australian Accounting Standards. - Compared the market capitalisation rates and net market income used by the Group to calculate net realisable value to market capitalisation rates and rental rates published by external independent valuation experts. - Compared the carrying amount of inventory against the Group's estimate of net realisable value as at 30 June 2018. • For properties transferred from investment property to inventory, we: - Performed the procedures outlined in the key audit matter: *Investment Properties for Valuation of investment properties, including those properties in investments accounted for under the equity method* in assessing the appropriateness of the fair value at the date of transfer. - Inspected the investment committee paper and board approval to ensure that the transfer was executed in accordance with the approved terms.

Independent Auditor's Report
continued

Other information

The Directors of the responsible entity of the Group, Dexus Funds Management Limited (the Directors), are responsible for the other information. The other information comprises the information included in the annual report for the year ended 30 June 2018, including Overview, Performance, Positive Momentum, Governance, Directors' Report and Investor Information, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and we do not and will not express an opinion or any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the financial report

The Directors are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the Directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the Directors are responsible for assessing the ability of the Group to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report.

A further description of our responsibilities for the audit of the financial report is located at the Auditing and Assurance Standards Board website at: http://www.auasb.gov.au/auditors_responsibilities/ar1.pdf. This description forms part of our auditor's report.

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Report on the remuneration report

Our opinion on the remuneration report

We have audited the remuneration report included in pages 24 to 42 of the Directors' Report for the year ended 30 June 2018.

In our opinion, the remuneration report of Dexus Diversified Trust for the year ended 30 June 2018 complies with section 300A of the *Corporations Act 2001*.

Responsibilities

The directors are responsible for the preparation and presentation of the remuneration report in accordance with section 300A of *the Corporations Act 2001*. Our responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with Australian Auditing Standards.

PricewaterhouseCoopers

PricewaterhouseCoopers

Matthew Lunn
Partner

Sydney
14 August 2018