# OnePath Mortgages and Income Plus funds – Additional information

31 MAY 2011

In this document, the terms 'we' and 'our' refer to OnePath Funds Management Limited (OnePath Funds Management).

This document contains important information for investors in OnePath's Mortgage and Income Plus funds. This document sets out additional information that may assist you to better understand your investment in the relevant fund. This information will be updated quarterly and will be posted in the 'Product updates' section of the ANZ website.

## OnePath Mortgage and Income Plus funds

The OnePath Mortgage and Income Plus funds invest in OnePath's Mortgage Pool ARSN 089 455 425 (Fund). Withdrawals from, and applications to, the Fund have been suspended (please see below).

The investment funds listed below have at least 50% exposure to the Fund:

| Investment fund | Constitutional name | Benchmark allocation* to Mortgage Pool |
|---|---|---|
| OnePath Mortgages | ANZ OA OnePath Mortgage Trust | 100% |
| ANZ Mortgage Fund (Series 1 and 2) | ANZ Mortgage Fund | 100% |
| OnePath Income Plus | ANZ OA OnePath Income Plus Trust | 50% |
| OnePath Original Income Plus | ANZ OA OnePath Income Plus Trust | 50% |

* These allocations may be subject to change

The funds listed in the above table are collectively referred to in this document as "**Mortgage and Income Plus Funds**". The Mortgage and Income Plus Funds gain exposure to mortgages by investing in the Fund. Given the high level of exposure to the Fund, withdrawals (including switch requests) from and applications to the Mortgage and Income Plus funds have also been suspended. Unless stated otherwise, the information in this document relates to the "**Fund**". Investors in OnePath Income Plus and OnePath Original Income Plus should note that the information provided in this document relates only to the mortgages component of their investment and not the Australian shares and property securities assets.

## Suspension of the Fund

In late 2008, and during the global financial crisis (GFC), the Fund experienced a greater volume of redemption requests and the assets could not be easily and quickly sold within the time required to meet redemption requests. A decision was made to suspend the Fund to ensure that the assets in the Fund could be managed and continue over time to produce a return to investors through the orderly realisation of assets rather than 'fire sales'. This was the preferred option rather than simply writing down these assets and realising losses in the Fund, which would not have been in the investors' best interests. This action was taken to protect investors' interest in the Fund.

## Benchmarks for Unlisted Mortgage Schemes

The Australian Securities and Investments Commission has issued *Regulatory Guide 45: Mortgage schemes – improving disclosure for retail investors* (Regulatory Guide). The Regulatory Guide sets out benchmarks for disclosure to investors to provide retail investors in mortgage schemes with the information they need to make an investment decision. We have set out below our current procedures and policies in relation to the Fund and have indicated whether or not these procedures and policies satisfy against each of the benchmarks outlined in the Regulatory Guide.

### Benchmark 1 Liquidity — Satisfied

Liquidity refers to the proportion of cash or cash equivalents within the Fund. Typically these cash assets are used to meet the Fund's short-term commitments. There are numerous factors that impact on the liquidity of the Fund, including the value of:

- investments into the Fund
- monthly interest payments by borrowers
- loans repaid by borrowers
- redemptions from the Fund
- new loans
- any undrawn loans
- market conditions.

We maintain and update cash flow estimates for the Fund on a regular basis by taking into account all of the above factors. These estimates are used to ensure the Fund has enough liquid assets to meet its projected cash needs for at least the next three months.

We have currently suspended withdrawals from (and applications into) all Mortgage and Income Plus Funds until further notice. This action has been taken to protect the best interests of all investors in the Fund

### Benchmark 2 Borrowing — Satisfied

The Fund does not borrow funds or use credit facilities for any purpose.

### Benchmark 3 Portfolio diversification — Satisfied

The Fund's portfolio of loans is well diversified across geographic region, property type, loan type and borrowers. The policies governing the lending of the Fund's assets specify limits for each of these elements, ensuring a conservative approach to lending.

The Fund has entered into a number of interest rate swaps (Derivatives) to swap fixed rate loans to variable rate loans. This section provides information on the portfolio's diversification using data as at **5 May 2011** (unless otherwise specified).

Information relating to the current nature of the Fund's portfolio are set out below:

### Class of activity – (property type)

| Property type | Number | $'000 | % of loan portfolio |
|---|---|---|---|
| Commercial office | 54 | 320,608 | 35% |
| Residential | 17 | 81,033 | 9% |
| Retail | 35 | 128,487 | 14% |
| Industrial | 59 | 179,668 | 20% |
| Vacant land^ | 19 | 135,724 | 15% |
| Other^ | 6 | 65,946 | 7% |
| **Total** | **190** | **911,466** | **100%** |

A full review of mortgage portfolio Key Risk Indicators (KRIs) is undertaken annually in May and current exposures within each of the above property types are within approved KRI Geographic region

^ Some loans within 'Vacant land' and 'Other' categories are marginally outside KRIs.

## Geographic region

| Geographic region | | | |
|---|---|---|---|
| **Location** | **Number** | **$'000** | **% of loan portfolio** |
| NSW | 80 | 291,447 | 32% |
| VIC | 74 | 413,774 | 45% |
| QLD | 34 | 169,104 | 19% |
| WA | 1 | 24,213 | 3% |
| ACT/NT/TAS/SA | 1 | 12,928 | 1% |
| **Total** | **190** | **911,466** | **100%** |

A full review of mortgage portfolio Key Risk Indicators (KRIs) is undertaken annually in May and current exposures within each of the above property types are within approved KRI.

## Defaults

| Borrowers* that are in material Default/Impairment | | |
|---|---|---|
| | **Number** | **$'000** |
| Default/Impaired Borrowers | 21 | 217,509 |
| **Total** | **21** | **217,509** |

*A borrower may have one or more loans but has no more than 3 loans

Default/Impaired loans represent 11% of total loans (by number) and 24% of total loans (by value).

Under the Problem Loan Guidelines an Impaired Loan is defined as either a:

- loan where payment arrears is over 30 days
- loan where review has uncovered covenant breaches of a material nature
- loan where a review has uncovered an unacceptable deterioration in the security position
- loan which is in material default (a breach of the loan contract that is substantial and may give rise to legal recovery action by the lender)

An Impaired Loans report is provided to Senior Management for each loan that is determined to be Impaired detailing the following information:

- Why the loan has become a problem loan,
- Full review of the security position including the existence of guarantees and a fixed & floating charge (if applicable),
- An assessment as to whether the Fund is likely to suffer a loss or not. The loss assessment process involves calculating the difference between the loan amount and the updated valuation amount. The need for a specific provision forms part of this process.
- A Corrective Action Plan is developed and will focus on one or more of the different loan recovery options. These options include but are not limited to seeking loan refinance, borrower's voluntarily sale of the security property or other assets, or mortgagee sale of the security property via the formal appointment of a Receiver under the mortgage.

Where the Impaired Loans report reveals a strong likelihood of loss of loan principal (based on comparison of loan balance to an up to date valuation report by a panel valuer or sale of property at an amount insufficient to repay loan), the need to raise a Specific Provision for Loss is assessed. Where provisions are made, income is set aside. These provisions are taken out of the Fund's income rather than capital and hence the returns to investors will be lower. Provisions are created over time to smooth the impact on investor returns. There is the possibility that if a large loss was incurred then the unit price could be reduced as a result.

Accounting Standard AASB 139 requires the Responsible Entity (RE) to conduct impairment tests if there is any indication that an asset may be impaired. The standard defines an impairment loss as "the amount by which the carrying amount of an asset exceeds its recoverable amount". The fair value of recoverable amount is calculated using the net present value method.

The Responsible Entity is required to consider indicators of impairment using external and internal sources of information. For the Fund, management, on behalf of the RE, has determined that the indicators of impairment may include, but not limited to, the following:

- significant decline in market value of the asset; and / or
- significant changes in market conditions

Under the impairment testing, if the recoverable amount is less than the carrying value of an asset, the carrying value of the asset must be reduced to its recoverable amount. This impairment amount is recognised immediately in the profit and loss for the mortgage pool by reducing the monthly distribution by the amount of the estimated impairment/loss.

## Security type

All loans are secured by a Registered First Mortgage over investment and owner occupied industrial, retail, commercial office, vacant land and residential property.

Joint and several guarantees are generally required from all shareholders/ directors of the borrowing entity and any corporate shareholders of the borrowing entity. Guarantees may be required from other corporate entities controlled by the borrower or any guarantor, if the income from those entities is to be relied upon for loan servicing

## Borrower concentration – Largest borrower and largest group exposure as a percentage of mortgages under management

| Borrower concentration | |
|---|---|
| | % |
| Largest borrower | 10.63 |
| Ten largest borrowers | 48.48 |
| Largest group exposure | 10.63 |

## Undrawn loan commitments – the amount that can be drawn down under approved limits

| Undrawn loan commitments | | | |
|---|---|---|---|
| | Number | $'000 | % of loan portfolio |
| Approved limits | 4 | 29,870 | 3% |
| Undrawn portion of approved limits | | 4,896 | 0.5% |

## Maturity profile

| Maturity profile | | | |
|---|---|---|---|
| Maturity in months | Number | $'000 | % of loan portfolio |
| Matured | 40 | 216,892 | 24% |
| 0 – 3 months | 30 | 127,069 | 14% |
| 3 – 6 months | 18 | 65,593 | 7% |
| 6 – 12 months | 20 | 187,650 | 21% |
| 1 – 2 years | 42 | 202,639 | 22% |
| 2 – 3 years | 29 | 76,635 | 8% |

| | | | |
|---|---|---|---|
| 3 – 4 years | 11 | 34,988 | 4% |
| 4 – 5 years | 0 | 0 | 0% |
| **Total** | **190** | **911,466** | **100%** |

## Loan to security valuation ratios

| **Loan Valuation ratios** | | | |
|---|---|---|---|
| **Loan to value ratio** | **Number** | **$'000** | **% of loan portfolio** |
| 0.00% – 50.00% | 54 | 155,492 | 17% |
| 50.01% – 60.00% | 35 | 196,420 | 22% |
| 60.01% – 66.00% | 37 | 253,914 | 28% |
| 66.01 – 70.00% | 33 | 91,473 | 10% |
| 70.01% – 75.00% | 2 | 20,155 | 2% |
| 75.01% + | 29 | 194,012 | 21% |
| **Total** | **190** | **911,466** | **100%** |

## Loans by Interest rates

| **Interest rates** | | | |
|---|---|---|---|
| **Interest rate mix** | **Number** | **$'000** | **% of loan portfolio** |
| 0.00% – 5.99% | 2 | 19,000 | 2% |
| 6.00% – 6.49% | 43 | 240,042 | 26% |
| 6.50% – 6.99% | 30 | 47,198 | 5% |
| 7.00% – 7.49% | 27 | 184,264 | 20% |
| 7.50% – 7.99% | 22 | 113,368 | 13% |
| 8.00% – 8.49% | 19 | 42,581 | 5% |
| 8.50% – 8.99% | 8 | 32,253 | 4% |
| 9.00% – 9.49% | 16 | 84,199 | 9% |
| 9.50% + | 23 | 148,561 | 16% |
| **Total** | **190** | **911,466** | **100%** |

### Loans by Interest capitalisation – Loans where interest is capitalised within the approved limits

| Capitalisation | | |
|---|---|---|
| **Loans capitalised** | **Number** | **$'000** |
| Approved limits | 0 | 0 |
| Undrawn portion of approved limits | 0 | 0 |

### Non-loan assets of the scheme including the value of such assets

| Non-loan assets of the scheme including the value of such assets | | |
|---|---|---|
| | **Value ($'000s)** | **% of scheme** |
| Mortgages | 911,466 | 81% |
| Fixed Interest | 31,548 | 3% |
| Cash | 183,060 | 16% |
| **Total** | **1,126,074** | **100%** |

### General Lending Principles

OnePath limits the loan amount for any one borrower or borrower group to 5% of funds under management (total mortgage loans plus non-loan assets such as cash and fixed interest investments). For borrowers and borrower groups who exhibit superior financial strength and where the security is multiple properties exhibiting strong lettability and saleability profiles, the loan limit is 6.5% of funds under management.

Borrower's capacity to service loans is assessed from two perspectives namely (i) income from the property is considered in determining "property only" interest cover and (ii) all sources of the borrower(s) and guarantor(s) are considered in determining "all sources /all commitments " interest cover. For loans secured by investment property, interest cover must be a minimum 1.5 times from property only income; and a minimum 1.5 times interest cover from "all sources/ all commitments". Lower "all sources/all commitments" interest cover of a minimum 1.25 times may be acceptable with lower LVR (below 65%). For loans secured by owner occupied property a minimum 1.75 times interest cover from "all sources/ all commitments" is required. Loan interest cover is required to be available from a combination of sustainable sources, i.e. property income generated by the security property as evidenced by lease contracts and / or consistent demonstrable historical servicing ability from business or other operations over the most recent two year period, as evidenced by tax returns or other financial statements.

At the time of loan rollover, it is OnePath's policy to require that an updated valuation of the security property be undertaken. However by exception and based on OnePath's verification of the current rental income from the property or estimated market rental, a waiver of obtaining a new valuation may be permitted provided the security property is visited by OnePath mortgage team personnel or a panel valuer.

### Benchmark 4 Related party transactions — Satisfied

The Fund does not lend any assets to related parties.

A portion of the Fund's non-loan assets are invested with the Australia and New Zealand Banking Group Limited (ANZ). These investments are made on commercial terms into ANZ's banking products.

### Benchmark 5 Valuations — Satisfied

Valuations on properties (excluding development properties) are based on their current state ('as is'). For development properties, valuations are based on 'as is' and 'on completion' basis.

Valuations are obtained prior to loan approval and properties are revalued after three years if applicable. Valuations may be no more than 90 days old on the date of settlement.

Valuations for the Fund are conducted by valuers selected from a panel of registered valuers (qualified/registered/licenced in the particular state or territory of operation) and must comply with industry standards and codes. One valuer cannot conduct more than 1/3 of valuations for the Fund by dollar value.

OnePath maintains a panel of external valuers (formally reviewed by OnePath every six months) that are used to value security properties. The panel comprises mainly large independent firms with a national presence, as well as more specialist valuers selected on their known level of experience in the type of property being valued. All valuations must be conducted pursuant to OnePath's Valuation Policy, under OnePath's instructions and must be counter-signed by a director if the valuer is not a director.  Valuations may be no more than 90 days old on the date of loan settlement. There can be no more than two consecutive valuations that may be conducted by the same valuation firm or the individual valuer on the same security property. Vacant possession value is adopted where security property is substantially owner occupied. For loan rollovers, valuation may be waived in some circumstances provided an up to date rental income schedule is provided and verified by OnePath and security property is re-inspected by an OnePath Mortgage Investment team member or a panel valuer.

OnePath limits the loan amount for any one borrower or borrower group that is secured by a single security property, to 5% of funds under management (total mortgage loans plus non-loan assets such as cash and fixed interest investments). Due to falling funds under management, one loan that is due to mature in December 2012, currently exceeds the 5% limit.

### Benchmark 6 Lending principles — Not Satisfied^

A loan-to-valuation ratio (LVR) is determined by dividing the loan amount by the property's value. The higher the LVR, the greater the risk that the Fund will not be able to fully recover the loan amount if property values reduce. The maximum LVR at approval on the Fund's loans is 75%, with the standard LVR being 70%.

For construction loans (where the property is being developed for future use or sale) the maximum LVR is limited to the lesser of 80% of total development costs or 70% of the 'as if complete' or net realisable value.

The initial advance should not exceed 65% of the site value, including reasonable value attributed to the development application or permit by the OnePath Australia Panel Valuer. This is provided that pre-sales/pre-lease requirements are satisfied at the time of the initial advance otherwise the maximum initial advance is limited to 60%.

These loans stipulate that monies are only released on a cost to complete basis as certified by OnePath Australia's appointed Panel Quantity Surveyor.

^ In terms of the overall portfolio the weighted average LVR of the loan portfolio is 68%.However as at 5 May 2011, there were a portion of the impaired loans where the LVR on these loans exceeded 80% based on the most recent valuation. The LVRs have arisen due to a fall in the valuation of the underlying security properties. It is for this reason that our portfolio does not satisfy the benchmark as set out in the Regulatory Guide.

### Benchmark 7 Distributions — Satisfied

Monthly distributions from the Fund are provided to investors based solely on the level of income earned in the month. This income is derived from the monthly interest paid on the Fund's loans, as well as interest and movements in capital value of the Fund's cash and fixed interest assets.  It is intended that all future distributions will be solely from earnings of the Fund.

Distributions from the investment funds that invest in the Fund are made from income they receive from the Fund. For OnePath Income Plus and OnePath Original Income Plus, monthly distributions also take into account an estimate of income earned by share and property assets, as well as any capital gains within the funds. The fund suspension does not affect regular income payments.

The Fund does not promote a return on the investment

### Benchmark 8 Withdrawals — Satisfied

The constitution sets out your ability and OnePath Funds Management's obligations in relation to withdrawing from the Mortgage and Income Plus Funds. When the Mortgage and Income Plus Funds are liquid, OnePath Funds Management is required to pay a withdrawal request within the time prescribed by the constitution. That time period is different for each fund and OnePath Funds Management may have the power, in certain circumstances, to extend that timeframe to a further period as authorised by the relevant constitution.

| Investment fund | Constitutional name | When the fund is liquid, period when a redemption request must be paid |
|---|---|---|
| OnePath Mortgages* | ANZ OA OnePath Mortgage Trust | Within 30 days. |
| ANZ Mortgage Fund (Series 1 and 2)* | ANZ Mortgage Fund | Within 90 days. |
| OnePath Income Plus | ANZ OA OnePath Income Plus Trust | Within 30 days.<br><br>We have the power to extend that time by an additional 28 days under certain circumstances. |
| OnePath Original Income Plus | ANZ OA OnePath Income Plus Trust | Within 30 days.<br><br>We have the power to extend that time by an additional 28 days under certain circumstances. |

*These funds do not promote a fixed unit price, however, the unit price for applications and withdrawals in these funds have traditionally been $1.00.

Investments in the Fund do not have fixed terms or maturity dates, and therefore, rollovers do not apply.

### Return of Capital process from March 2011

Following the Fund's suspension, we offered investors opportunities to withdraw from the Mortgage and Income Plus Funds by opening withdrawal windows quarterly.

To ensure that all investors do not miss out on opportunities to withdraw from the Mortgage and Income Plus Funds and to remove the administration burden for investors, we have recently changed our withdrawal process. As of March 2011 we will no longer offer withdrawal windows. Instead, we will return available liquidity in the form of a capital repayment to all investors on a pro rata quarterly basis. Investors do not need to submit a form - they will automatically receive this payment. For investors who are in a unit trust, a return of capital will reduce the cost base of the unit. What this means is that the unit price of the relevant unit price will fall by exactly the value of the capital payment. The number of units will not change. It is important to note that notwithstanding best efforts some assets may be realised at a discount and as such you may not receive your full capital back. We will continue to actively manage the Fund to minimise any further impairments. Please refer to Benchmark 3 for further information on impairments.

This change does not affect the way we process applications for financial hardship. Claims will continue to be processed in accordance with current procedures. If you think that you are eligible for a payment under financial hardship please visit www.anz.com > personal > investments-advice > resources> fund suspensions.

At this stage the Funds remain suspended however they are not being terminated. OnePath is still considering the long term approach in relation to the Funds. If this status changes we will inform investors.

OnePath Funds Management Limited (ABN 21 003 002 800 AFSL 238342) is the issuer of this information.

The issuer is a wholly owned subsidiary of Australia and New Zealand Banking Group Limited (ABN 11 005 357 522) (ANZ). ANZ is an authorised deposit taking institution (Bank) under the Banking Act 1959 (Cth). Although the issuer is owned by ANZ it is not a Bank. Except as described in the relevant Product Disclosure Statement (PDS), an investment with the issuer is not a deposit or other liability of ANZ or its related group companies and none of them stands behind or guarantees the issuer or the capital or performance of your investment. Your investment is subject to investment risk, including possible repayment delays and loss of income and principal invested.

This information is current as at 31 May 2011 but may be subject to change. The information is of a general nature and does not take into account your personal needs, financial circumstances or objectives. Before acting on this information, you should consider the appropriateness of the information, having regard to your needs, financial circumstances and objectives. You should read the relevant PDS and Product Updates available at www.anz.com or by calling Customer Service for a free copy on 13 38 63, and consider whether a particular product is right for you before making a decision to acquire, continue to hold or dispose of the product.