

City Pacific First Mortgage Fund

(Formerly City Pacific Mortgage Trust)

ARSN 088 139 477

Half-Year Financial Report

31 December 2008

City Pacific First Mortgage Fund

INDEX

DIRECTORS' REPORT	2
INTERIM INCOME STATEMENT	7
INTERIM STATEMENT OF RECOGNISED INCOME AND EXPENSE	7
INTERIM BALANCE SHEET	8
INTERIM STATEMENT OF CASH FLOWS.....	9
CONDENSED NOTES TO THE INTERIM FINANCIAL STATEMENTS	10
DIRECTORS' DECLARATION	18
INDEPENDENT AUDITOR'S REVIEW REPORT	19

City Pacific First Mortgage Fund

Directors' Report

The Directors of City Pacific Limited (the "Responsible Entity" or "City Pacific") present their report together with the interim financial report of the City Pacific First Mortgage Fund (the "Fund"), for the half-year ended 31 December 2008 and the review report thereon.

Directors

The Directors of City Pacific during or since the end of the half-year are:

<i>Name</i>	<i>Period of directorship</i>
Mr Phillip Graeme Downie OAM, FCA <i>Chairman</i> <i>Independent Non-Executive Director</i>	Appointed 30 September 2008
Mr Thomas William Swan BBus, GradDipBusIP, MComLaw, DipFS(FP), FPNA, ACIS, MAICD <i>Deputy Chairman</i> <i>Independent Non-Executive Director</i>	Appointed 8 August 1997
Mr John Michael Ellis LL.B <i>Managing Director</i> <i>Chief Executive Officer</i>	Appointed 30 September 2008
Mr Stephen Anthony McCormick <i>Executive Director</i>	Appointed 20 June 2008
Mr Ian William Donaldson AM <i>Chairman</i> <i>Independent Non-Executive Director</i>	Appointed 25 May 1998 Resigned 17 December 2008
Mr Philip Keith Sullivan <i>Managing Director</i> <i>Chief Executive Officer</i>	Appointed 8 August 1997 Resigned 12 November 2008
Hon Shane L Stone AC, QC <i>Independent Non-Executive Director</i>	Appointed 16 September 2005 Resigned 28 November 2008

Principal activities

The Fund is a registered managed investment scheme with an investment strategy to invest in a portfolio of loans secured primarily by registered first mortgages over real property in Australia, with a focus on the leisure and lifestyle sector of the market in geographic locations supported by strong population growth. The Fund targets lending valuation ratios of 70%, with initial maximum lending valuation ratios of 80%, in accordance with the Fund's constitution.

The Fund did not have any employees during the half-year.

Review and results of operations

Due to the ongoing global financial crisis and its impacts on Australian property markets, the Fund's borrowers have experienced:

- An inability to repay their loans and interest as and when they are due as a result of the significant slowdown in property sales and resultant decrease in property values; and
- An inability to refinance their loans with banks or other lenders due to insufficient funding being available in the financial markets.

As a result, the repayment of loans and interest by borrowers of the Fund during the half-year was significantly less than expected. This in turn impacted the Fund's ability to repay its finance facility, pay redemption requests and pay distributions to Unitholders as outlined further in this report.

City Pacific First Mortgage Fund

Directors' Report

Review and results of operations (continued)

Despite the current and prevailing market conditions, it remains the priority of the Fund to continue to manage the Fund's mortgage loans and cash flows in order to:

- Maximise the value of the Fund's assets to ensure optimum realisation outcomes;
- Repay external debt;
- Recommence the payment of distributions to Unitholders; and
- Recommence the payment of Unitholder redemptions once the Fund has sufficient liquidity.

The Fund had total assets of \$629,845,216 as at 31 December 2008 after impairment losses (30 June 2008: \$969,422,033), which are primarily invested in registered first mortgages over real property in Australia and in bank deposits, in accordance with the Fund's constitution.

Property markets

The ongoing global financial crisis and instability is continuing to cause uncertainty and volatility in Australia's capital and property markets. With decreasing liquidity and transaction levels in property markets, there is a significant lack of clarity as to pricing levels and market drivers. As a result, the definition of market value of "a willing but not anxious buyer and seller" is being tested. The majority of transactions that are occurring involve anxious or pressured vendors and purchasers who will only buy at discounted prices. In addition, our experience has been that prices agreed during negotiations are often reduced prior to exchange of contracts as purchasers assert their greater negotiating position in the current uncertain environment. In this environment, prices and values are going through a period of heightened volatility whilst the market absorbs the various issues and reaches its conclusions.

Continued ongoing uncertainty in capital and property markets may negatively impact asset values in the future, however, these financial statements set out the financial position as at the reporting date based on available evidence and accounting estimates.

Finance facility

At 31 December 2008, the Fund's finance facility was drawn to \$90,765,000 (30 June 2008: \$129,700,000).

As a result of a delay in repayment of loans by borrowers of CPFMF as outlined above, the Fund was in breach of certain loan covenants in relation to its finance facility. During the half-year, City Pacific as Responsible Entity, renegotiated the terms of the Fund's finance facility with the financier. The amended facility required full repayment by 27 February 2009 and was intended to be met by the Fund from the scheduled repayment of first mortgage loans in the period to 27 February 2009, or a further extension was to be negotiated with the financier. Subsequent to the half-year, City Pacific renegotiated terms of this facility, with the repayment date extended to 26 February 2010.

The repayment of the facility is expected to be met by the Fund from the repayment of mortgage loans in the period to 26 February 2010.

Redemption repayment period and non-liquid Fund

Due to the high level of redemption requests received from investors, in March 2008 the Responsible Entity resolved to defer the payment of valid redemption requests received for a period of up to 180 days as allowed under the Fund's constitution. In accordance with the Fund's constitution, the Responsible Entity is able to delay payment of redemptions by up to 180 days and then a further 180 days.

During the half-year, the Responsible Entity deferred the payment of valid redemption requests for a further 180 days in accordance with the Fund's constitution. In addition, the Responsible Entity cancelled Unitholder distributions from July 2008.

Due to the ongoing global credit and liquidity crisis and its impacts on Australian property markets, the repayment of loans by borrowers of the Fund during the half-year was significantly less than expected. As a result, on 13 October 2008, the directors of City Pacific as the Responsible Entity resolved that the Fund is a "non-liquid" registered managed investment scheme in accordance with the Fund's constitution and the *Corporations Act 2001* ("the Act").

City Pacific First Mortgage Fund

Directors' Report

Review and results of operations (continued)

Redemption repayment period and non-liquid Fund (continued)

As a non-liquid registered managed investment scheme, existing redemption requests are extinguished and the process for future redemptions will operate in accordance with the Act as follows:

- The Fund will make periodic redemption offers to all Unitholders at times when there are sufficient funds available to do so. The Responsible Entity will determine the amount that constitutes "sufficient funds" for a redemption offer to be made and does not expect to make redemption offers where less than 10% of total Unitholders funds are available for each redemption offer;
- Redemption offers will be made in writing to all Unitholders and will specify the amount of funds available for that redemption offer. Unitholders wishing to redeem will be required to respond to the redemption offer stating the amount they wish to redeem (redemption request);
- In the event there is an oversubscription to the redemption offer (ie. the amount of the redemption requests exceeds the amount of the redemption offer), the redemptions will be paid on a pro-rata basis to all Unitholders who have submitted a redemption request.

Distribution payments

As a result of repayment of loans and interest by borrowers of the Fund being significantly less than expected due to the ongoing global financial crisis and its impacts on the Australian property markets, the Responsible Entity resolved to cancel Unitholder distributions from July 2008. Distributions are expected to recommence once the Fund has sufficient liquidity to do so.

Impairment losses

At 31 December 2008, as part of its normal reporting procedures, the Fund recognised net impairment losses in respect of certain assets, totalling \$338,647,103 or 35% of total assets before impairment, as outlined in notes 4 and 5.

During the period, the repayment of three mortgage loans resulted in realised impairment losses of \$2,405,476. Of this amount, impairment losses of \$1,824,210 in relation to two of the mortgage loans were recognised at 30 June 2008.

The remaining impairment losses represent estimated provisions against the Fund's assets and any impairment losses will not be realised until such time as the mortgage loans are repaid and security released. The Responsible Entity continues to work with borrowers in order to minimise potential impairment losses.

Since the 30 June 2008 annual financial report was prepared there have been a number of factors which have had a significant adverse effect on the book value of the Fund. These factors include:

- The ongoing global financial crisis and the continuing uncertainty, instability and volatility in Australian capital and property markets; and
- A number of borrowers have experienced significant financial difficulties which has resulted in the appointment of external administrators. This in turn has had the effect of significant decreases in the value of the associated underlying property securities as a result of properties not being able to be realised in the normal course of business.

This has resulted in a significant impairment loss being recognised in the 6 months ended 31 December 2008, representing approximately 35% of the Funds gross assets prior to impairment. The directors do not consider this unreasonable compared with the decline in other funds and investment asset classes. This also highlights the value and benefit of holding primarily first mortgages over real property as security for loans to the Fund's borrowers.

As a result of these and previous impairments, together with the cancelled distributions since July 2008, the net tangible asset backing of the Fund as at 31 December 2008 is \$0.61 per unit.

Commitments

As at 31 December 2008, the Fund had firm commitments for mortgage loan funding totalling \$18,464,607 (30 June 2008: \$81,809,832), being the difference between the total of mortgage loan facilities approved and total loans drawn.

These commitments are necessary in order to enable borrowers to complete their existing developments in order to then sell completed properties and repay the loans provided by the Fund, thereby protecting the value of the Fund. These commitments are expected to be met by the Fund from the repayment of mortgage loans.

City Pacific First Mortgage Fund

Directors' Report

Review and results of operations (continued)

Co-lending arrangements

The Fund has a co-lending agreement with an institutional investor. The agreement provides that the institutional investor will co-lend approximately \$100 million with the Fund in a range of first mortgages currently held by the Fund. The institutional investor acquired an interest in those mortgage loans at their book value by providing a loan facility to the borrowers. The institutional investor became a joint first mortgage lender with first priority ahead of the Fund with the proceeds of \$100 million received by the Fund by way of loan repayments. The \$100 million loan repayments were used to continue the investment objectives of the Fund.

As at 31 December 2008, the institutional investor has co-lent \$65,586,736 with the Fund on four separate loans.

Subsequent events

Finance facility

As a result of a delay in repayment of loans by borrowers of the Fund, City Pacific, as Responsible Entity, renegotiated the terms of the Fund's finance facility with the financier. The amended facility of \$108 million is subject to certain conditions and requires full repayment by 26 February 2010 and is intended to be met by the Fund from the scheduled repayment of first mortgage loans, or a further extension be negotiated with the financier.

Independent review of mortgage loans

Subsequent to the half-year, City Pacific as Responsible Entity of the Fund engaged a professional advisory firm to undertake an independent review of the Fund's mortgage loans and provide on-going independent support in formulating and implementing optimum realisation strategies for the Fund's mortgage loans.

Unitholder meeting

On 9 March 2009, City Pacific as Responsible Entity of the Fund received correspondence from Unitholders of the Fund requesting City Pacific to call a meeting of the Fund's Unitholders to consider and vote upon certain proposed constitutional amendments primarily in relation to fees payable to the Responsible Entity by the Fund and/or borrowers of the Fund. The meeting was held on 1 May 2009.

The Board of City Pacific has resolved to amend the Fund's constitution to reduce the management fee to 2.5% of the gross asset value of the Fund following the Unitholder meeting.

Other than the items noted above, there has not arisen in the interval between the end of the half-year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the directors, to affect significantly the operations of the Fund, the results of those operations or the state of affairs of the Fund, in future financial years.

Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

The lead auditor's independence declaration is set out on page 6 and forms part of the directors' report for the half-year ended 31 December 2008.

Dated at Gold Coast this 18th day of May 2009.

Signed in accordance with a resolution of the directors:



JM Ellis
Managing Director



**LEAD AUDITOR'S INDEPENDENCE DECLARATION
UNDER SECTION 307C OF THE CORPORATIONS ACT 2001**

To: the Directors of City Pacific Limited, the Responsible Entity of City Pacific First Mortgage Fund

I declare that, to the best of my knowledge and belief, in relation to the review for the half-year ended 31 December 2008 there have been:

- (i) no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the review; and
- (ii) no contraventions of any applicable code of professional conduct in relation to the review.

A handwritten signature in blue ink that reads 'KPMG'.

KPMG

A handwritten signature in blue ink that reads 'PG Steer'.

PG Steer
Partner

18 May 2009

City Pacific First Mortgage Fund

Interim Income Statement

For the half- year ended 31 December 2008

		31 December 2008	31 December 2007
		\$	\$
	Note		
Revenue			
Interest income – mortgage loans		61,560,092	70,981,861
Distributions and interest income – other		108,439	357,090
Investment income		<u>61,668,531</u>	<u>71,338,951</u>
Expenses			
Management fees		13,194,086	16,092,647
Professional fees		703,335	-
Reversal of impairment – unrealised	4,5	(4,830,838)	-
Impairment losses – realised	4,5	581,266	1,740,656
Impairment losses – unrealised	4,5	342,896,675	-
Operating expenses before finance costs		<u>352,544,524</u>	<u>17,833,303</u>
Profit/(loss) from operating activities		<u>(290,875,993)</u>	<u>53,505,648</u>
Finance costs			
Distributions to unitholders	3	-	44,917,781
Borrowing costs incurred		6,479,726	8,587,867
Total finance costs		<u>6,479,726</u>	<u>53,505,648</u>
Net profit/(loss)		<u>(297,355,719)</u>	<u>-</u>

The income statement is to be read in conjunction with the notes to the interim financial statements.

Interim Statement of Recognised Income and Expense

For the half- year ended 31 December 2008

As the Fund has no equity, the Fund has not included any items of recognised income and expense for the current or comparative period.

The statement of recognised income and expense is to be read in conjunction with the notes to the interim financial statements.

City Pacific First Mortgage Fund

Interim Balance Sheet

as at 31 December 2008

	Note	31 December 2008 \$	30 June 2008 \$
Assets			
Cash and cash equivalents		9,041,436	3,961,506
Receivables	4	15,517,021	30,438,522
Mortgage loans receivable	5	605,286,759	935,022,005
Total assets		629,845,216	969,422,033
Liabilities			
Payables		2,324,630	1,335,688
Distributions payable	3	-	11,272,499
Interest bearing loans	6	90,720,801	129,550,099
Total liabilities (excluding net assets attributable to unitholders)		93,045,431	142,158,286
Net assets attributable to unitholders - liability	8	536,799,785	827,263,747
Net assets per unit on issue		\$0.61	\$0.94

The balance sheet is to be read in conjunction with the notes to the interim financial statements.

City Pacific First Mortgage Fund

Interim Statement of Cash Flows

For the half-year ended 31 December 2008

	31 December 2008	31 December 2007
	\$	\$
Cash flows from operating activities		
Interest received – mortgage loans	9,815,732	68,888,149
Distributions and interest received - other	113,277	264,618
Responsible entity fees and other costs paid	(12,916,716)	(22,245,940)
Distributions paid	(4,380,742)	(24,849,611)
Borrowing costs paid	(6,365,786)	(8,871,536)
	(13,734,235)	13,185,680
Net cash flows from/(used in) operating activities		
Cash flows from investing activities		
Mortgage loan funds advanced	(49,134,970)	(431,824,422)
Mortgage loan funds repaid	106,884,135	515,289,163
	57,749,165	83,464,741
Net cash flows from/(used in) investing activities		
Cash flows from financing activities		
Proceeds from borrowings	-	216,300,000
Repayment of borrowings	(38,935,000)	(173,300,000)
Proceeds from issue of redeemable units	-	230,911,700
Payments on redemption of redeemable units	-	(346,135,170)
	(38,935,000)	(72,223,470)
Net cash flows from/(used in) financing activities		
Net increase/(decrease) in cash and cash equivalents	5,079,930	24,426,951
Cash and cash equivalents at 1 July	3,961,506	22,462,033
Cash and cash equivalents at 31 December	9,041,436	46,888,984

The statement of cash flows is to be read in conjunction with the notes to the interim financial statements

City Pacific First Mortgage Fund

Condensed notes to the interim financial statements

For the half-year ended 31 December 2008

1. Reporting entity

The City Pacific First Mortgage Fund (“Fund”) is a registered managed investment scheme under the Corporations Act 2001. The Fund was constituted on 23 June 1998 and will terminate on 23 June 2078 unless terminated in accordance with the Constitution. The interim financial report of the Fund is for the six months ended 31 December 2008.

(a) Statement of compliance

The interim financial report is a general purpose financial report which has been prepared in accordance with AASB 134 *Interim Financial Reporting* and the Corporations Act 2001.

The interim financial report does not include all of the information required for a full annual financial report, and should be read in conjunction with the most recent annual financial report.

The interim financial report was authorised for issue by the directors of the Responsible Entity on 18 May 2009.

(b) Use of estimates and judgements

The preparation of half-year financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future period affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have most significant effect on the amount recognised in:

- Note 1(d) Going concern
- Notes 4 and 5 Impairment of receivables and mortgage loans
- Note 10 First mortgage loans secured by property located at Martha Cove, Victoria

(c) Significant accounting policies

The accounting policies applied by the Fund in this interim financial report are the same as those applied by the Fund in its financial report as at and for the year ended 30 June 2008.

(d) Going Concern

The interim financial statements have been prepared on a going concern basis, which contemplates the continuation of normal business operations and the realisation of assets and settlement of liabilities in the normal course of business.

During the half-year ended 31 December 2008:

- As a result of the ongoing global credit and liquidity crisis and its impact on the Australian property markets, certain parties who had borrowed from the Fund were unable to repay or refinance existing mortgage loans due for repayment in the 6 months to 31 December 2008, resulting in expected cash inflows to the Fund not being received as anticipated;
- As disclosed in note 6, the Fund amended the terms of its finance facilities;
- As disclosed in note 3, the Fund cancelled distributions to Unitholders;
- As disclosed in notes 4 and 5, the Fund recognised net impairment losses of approximately \$338.6 million;
- City Pacific as Responsible Entity of the Fund was in breach of the net tangible asset condition of its Australian Financial Services Licence; and
- The Responsible Entity resolved that the Fund is a “non-liquid” registered managed investment scheme in accordance with the Fund’s constitution and the *Corporations Act 2001* (“the Act”).

City Pacific First Mortgage Fund
Condensed notes to the interim financial statements
For the half-year ended 31 December 2008

1. Significant accounting policies (continued)

(d) Going Concern (continued)

Subsequent to year end, as disclosed in note 11, the Responsible Entity of the Fund has:

- Renegotiated the terms of the Fund's finance facility with the financier. The agreement requires the repayment of the facility in full by 26 February 2010, subject to the achievement of certain significant repayment milestones in the period to 26 February 2010, and is expected to be repaid by the Fund from the repayment of mortgage loans.

The directors of the Responsible Entity have prepared the interim financial statements on the going concern basis, as it is their intention to:

- Repay the bank facility of \$91 million from scheduled loan repayments in the period to 26 February 2010;
- Recommence the payment of distributions to Unitholders once the Fund has sufficient liquidity;
- Make periodic redemption offers to all Unitholders at times when there are sufficient funds available to do so, in accordance with the Act;
- Continue to fund loan drawdown requests on approved mortgage loan facilities in order to enable borrowers to complete their existing developments and facilitate the sale of completed properties and repayment of loans; and
- Seek additional investment from sources such as sophisticated or institutional investors.

The Responsible Entity has prepared cashflow projections that support the Fund's ability to meet debt repayments and fund loan draw down commitments on approved mortgage loan facilities.

To continue as a going concern, it will be necessary for the Fund to:

- Continue the existing finance arrangements with its financier;
- Realise sufficient cash funds from the repayment, refinancing or sale of mortgage loans to:
 - repay the bank facility of \$91 million by 26 February 2010 or obtain an extension from its financier;
 - fund all loan drawdown commitments on approved mortgage loan facilities;
 - fund all other costs associated with the operation of the Fund; and
- Raise additional investment funds to continue normal business operations.

In the event that the Fund cannot continue as a going concern, it may not realise its assets or settle its liabilities in the normal course of operations and at the amounts stated in the interim financial report.

2. Segment information

The Fund operates as a first mortgage fund and the Fund's operations and customers are located predominantly within Australia. The Fund provides first mortgage finance to borrowers.

3. Distributions

Due to the ongoing global financial crisis and its impacts on Australian property markets, the Fund's borrowers have experienced:

- An inability to repay their loans and interest as and when they are due as a result of the significant slowdown in property sales and resultant decrease in property values; and
- An inability to refinance their loans with banks or other lenders due to insufficient funding being available in the financial markets.

As a result, the repayment of loans and interest by borrowers of the Fund during the half-year was significantly less than expected. This in turn impacted the Fund's ability to pay distributions to Unitholders, with the Responsible Entity necessarily cancelling distributions from July 2008. Accordingly, the Fund did not pay any distributions in relation to the half-year ended 31 December 2008 (2007: \$44,917,781).

City Pacific First Mortgage Fund

Condensed notes to the interim financial statements

For the half-year ended 31 December 2008

	31 December 2008	30 June 2008
4. Receivables	\$	\$
Interest receivable – mortgage loans	89,129,255	50,101,346
Net impairment losses	(73,636,993)	(19,692,422)
	15,492,262	30,408,924
Distributions and interest receivable – other	24,759	29,598
	15,517,021	30,438,522

Impairment losses

At 31 December 2008, as part of its normal review procedures and in response to the ongoing global financial crisis and its impacts on the Australian property markets, the Responsible Entity recorded net realised and unrealised impairment losses in respect of interest receivable of \$54,450,622 (2007: \$1,740,656) for the half-year.

During the period, the repayment of three mortgage loans resulted in realised impairment losses of \$506,050 in respect of interest receivable. Of this amount, interest receivable impairment losses of \$211,530 in relation to two of the mortgage loans were recorded at 30 June 2008.

During the period, the Fund recorded an impairment loss reversal of interest receivable of \$2,443,017 in respect of one mortgage loan as the amount is now considered recoverable in accordance with a recent independent valuation.

In assessing whether interest receivable may be impaired, the Responsible Entity considerations included but were not limited to:

- Valuations of security properties completed by registered valuers;
- Appraisals from real estate agents;
- Actual sale prices realised on completed projects;
- Recent offers to purchase security properties arising out of marketing campaigns;
- Current and forecast market conditions;
- Status of individual loans; and
- Estimated time to realise mortgage loans.

These impairment losses represent estimates of losses that may be incurred based on a number of assumptions including amounts that may be received upon repayment or sale of the security property and the period until funds are returned. In the current economic conditions there is uncertainty as to the amount that could be realised on the sale of security properties, and the time it may take to achieve a sale. Accordingly, actual impairment losses incurred may differ significantly from these estimates.

The Responsible Entity considers that, based on evidence available at 31 December 2008, all interest on remaining mortgage loans should be recovered in full and accordingly no further impairment losses have been recorded.

Property markets

The ongoing global financial crisis and instability is continuing to cause uncertainty and volatility in Australia's capital and property markets. With decreasing liquidity and transaction levels in property markets, there is a significant lack of clarity as to pricing levels and market drivers. As a result, the definition of market value of "a willing but not anxious buyer and seller" is being tested. The majority of transactions that are occurring involve anxious or pressured vendors and purchasers who will only buy at discounted prices. In addition, our experience has been that prices agreed during negotiations are often reduced prior to exchange of contracts as purchasers assert their greater negotiating position in the current uncertain environment. In this environment, prices and values are going through a period of heightened volatility whilst the market absorbs the various issues and reaches its conclusions.

Continued ongoing uncertainty in Australian capital and property markets may negatively impact asset values in the future, however, these financial statements set out the financial position as at the reporting date based on available evidence and accounting estimates.

City Pacific First Mortgage Fund
Condensed notes to the interim financial statements
For the half-year ended 31 December 2008

	31 December 2008	30 June 2008
	\$	\$
5. Mortgage loans		
Held directly:		
Mortgage loans	920,911,018	968,349,208
Net impairment losses	<u>(315,624,259)</u>	<u>(33,327,203)</u>
	<u>605,286,759</u>	<u>935,022,005</u>

Impairment losses

At 31 December 2008, as part of its normal review procedures and in response to the ongoing global financial crisis and its impacts on the Australian property markets, the Responsible Entity recorded net realised and unrealised impairment losses in respect of mortgage loans of \$284,196,481 (2007: nil) for the half-year.

During the period, the repayment of three mortgage loans resulted in realised impairment losses of \$1,899,425 in respect of mortgage loans. Of this amount, mortgage loan impairment losses of \$1,612,680 in relation to two of the mortgage loans were recorded at 30 June 2008.

During the period, the Fund recorded an impairment loss reversal of \$2,387,821 in respect one mortgage loan as the amount is now considered recoverable in accordance with a recent independent valuation.

In assessing whether mortgage loans may be impaired, the Responsible Entity considerations included but were not limited to:

- Valuations of security properties completed by registered valuers;
- Appraisals from real estate agents;
- Actual sale prices realised on completed projects;
- Recent offers to purchase security properties arising out of marketing campaigns;
- Current and forecast market conditions;
- Status of individual loans; and
- Estimated time to realise mortgage loans.

These impairment losses represent estimates of losses that may be incurred based on a number of assumptions including amounts that may be received upon repayment or sale of the security property and the period until funds are returned. In the current economic conditions there is uncertainty as to the amount that could be realised on the sale of security properties, and the time it may take to achieve a sale. Accordingly, actual impairment losses incurred may differ significantly from these estimates.

The Responsible Entity considers that, based on evidence available at 31 December 2008, all principal on remaining mortgage loans should be recovered in full and accordingly no further impairment losses have been recorded.

Co-lending arrangements

The Fund has a co-lending agreement with an institutional investor. The agreement provides that the institutional investor will co-lend approximately \$100 million with the Fund in a range of first mortgages currently held by the Fund. The institutional investor acquired an interest in those mortgage loans at their book value by providing a loan facility to the borrowers. The institutional investor became a joint first mortgage lender with first priority ahead of the Fund with the proceeds of \$100 million received by the Fund by way of loan repayments. The \$100 million loan repayments were used to continue the investment objectives of the Fund.

As at 31 December 2008, the institutional investor has co-lent \$65,586,736 with the Fund on four separate loans.

City Pacific First Mortgage Fund
Condensed notes to the interim financial statements
For the half-year ended 31 December 2008

5. Mortgage loans (continued)

Property markets

The ongoing global financial crisis and instability is continuing to cause uncertainty and volatility in Australia's capital and property markets. With decreasing liquidity and transaction levels in property markets, there is a significant lack of clarity as to pricing levels and market drivers. As a result, the definition of market value of "a willing but not anxious buyer and seller" is being tested. The majority of transactions that are occurring involve anxious or pressured vendors and purchasers who will only buy at discounted prices. In addition, our experience has been that prices agreed during negotiations are often reduced prior to exchange of contracts as purchasers assert their greater negotiating position in the current uncertain environment. In this environment, prices and values are going through a period of heightened volatility whilst the market absorbs the various issues and reaches its conclusions.

Continued ongoing uncertainty in Australian capital and property markets may negatively impact asset values in the future, however, these financial statements set out the financial position as at the reporting date based on available evidence and accounting estimates.

	31 December 2008	30 June 2008
	\$	\$
6. Interest bearing loans		
Borrowings	90,765,000	129,700,000
Prepaid borrowing costs	(44,199)	(149,901)
	90,720,801	129,550,099

The Responsible Entity has established a finance facility for the Fund which is secured by a fixed and floating charge over the assets of the Fund, providing the funder with first priority over the assets of the Fund.

As a result of a delay in repayment of loans by borrowers of CPFMF and other factors, the Fund was in breach of certain loan covenants in relation to its finance facility during and subsequent to the half-year ended 31 December 2008. During the half-year, City Pacific as Responsible Entity, renegotiated the terms of the Fund's finance facility with the financier. The amended facility required full repayment by 27 February 2009 and was intended to be met by the Fund from the scheduled repayment of first mortgage loans in the period to 27 February 2009, or a further extension was to be negotiated with the financier. Subsequent to the half-year, City Pacific renegotiated terms of this facility, with the repayment date extended to 26 February 2010, subject to the achievement of certain significant repayment milestones in the period to 26 February 2010. The repayment of the facility is expected to be met by the Fund from the repayment of mortgage loans in the period to 26 February 2010.

7. Commitments

As at 31 December 2008, the Fund had firm commitments for additional mortgage loan funding totalling \$18,464,607 (30 June 2008: \$81,809,832), being the difference between the total of mortgage loan facilities approved and total loans drawn.

These commitments are necessary in order to enable borrowers to complete their existing developments in order to then sell completed properties and repay the loans provided by the Fund, thereby protecting the value of the Fund. These commitments are expected to be met by the Fund from the repayment of mortgage loans.

City Pacific First Mortgage Fund
Condensed notes to the interim financial statements
For the half-year ended 31 December 2008

8. Unitholders' funds – classified as liability

	31 December 2008		30 June 2008	
	No. of units	\$	No. of units	\$
Units on issue:				
Opening balance	880,283,372	827,263,747	1,034,937,114	1,034,937,114
Applications	-	-	288,232,514	288,232,514
Redemptions	-	-	(483,348,743)	(483,348,743)
Reinvestments	6,891,757	6,891,757	40,462,487	40,462,487
	<u>887,175,129</u>	<u>834,155,504</u>	<u>880,283,372</u>	<u>880,283,372</u>
Profit/(loss) for the period	-	(297,355,719)	-	(53,019,625)
Closing balance	<u>887,175,129</u>	<u>536,799,785</u>	<u>880,283,372</u>	<u>827,263,747</u>

All units in the Fund are of the same class and carry equal rights. Under the Fund constitution, each unit represents a right to an individual share in the Fund and does not extend to a right to the underlying assets of the Fund.

9. Related parties

Responsible entity

City Pacific, as Responsible Entity, receives management fees from the Fund. Management fees paid to City Pacific include the costs it incurs in operating the Fund, including salaries and wages of investor relations, loans management, administration and management staff, investor communication costs, custodian fees, compliance costs, audit fees, legal fees, advertising, brokerage, insurance, occupancy costs and operating overheads. Certain costs are also being met directly by the Fund.

Management fees paid or payable to City Pacific during the half-year were \$13,194,086 (2007: \$16,092,647), representing 2.8% per annum of average gross assets of the Fund for the period, prior to impairment. The Board of City Pacific has resolved to amend the Fund's constitution to reduce the management fee to 2.5% of the gross asset value of the Fund following the Unitholder held on 1 May 2009.

Related party loans

As at 31 December 2008 the Fund was due the following loans from entities associated with the Responsible Entity or its associates, prior to impairment losses:

	Responsible Entity Ownership Interest	Loan balance at 31 December	Funds advanced during the period	Repayments made during the period	Interest paid/ payable	Interest rate at 31 December
Marina Cove Pty Ltd	30.6%	75,879,022	1,358,977	1,700,972	7,387,259	13.0%
Lake Views Estates Pty Ltd	15.3%	51,805,742	12,318	2,895,151	4,057,982	13.0%
MP Pacific Investments Unit Trust	15.3%	15,000,000	-	600,000	2,256,985	13.0%
SP Marina Pty Ltd	50.0%	16,675,113	4,915,113	-	1,190,277	13.0%
Sunrise Waters Unit Trust	50.0%	23,573,772	4,477	-	2,561,916	13.0%
Grande Pacific Syndicate 1	50.0%	56,561,338	19,075,397	10,952,726	1,208,272	12.5%
Grande Pacific Syndicate 2	50.0%	24,703,302	12,439	-	1,939,516	13.0%
		<u>264,198,289</u>	<u>25,378,721</u>	<u>16,148,849</u>	<u>20,602,207</u>	

City Pacific First Mortgage Fund
Condensed notes to the interim financial statements
For the half-year ended 31 December 2008

9. Related parties (continued)

Related party loans (continued)

These loans are secured by registered first mortgage and are on normal commercial terms and conditions. The Fund recorded net impairment losses of \$50,176,452 in respect of mortgage loans and interest receivable owing from Lake Views Estates Pty Ltd, Sunrise Waters Unit Trust and Grande Pacific Syndicates 1 and 2 (2007: nil) during the half-year ended 31 December 2008.

During the period, the Fund recorded an impairment loss reversal of mortgage loans of \$2,387,821 and interest receivable of \$2,443,017 in respect of mortgage loans owing from Marina Cove Pty Ltd as the amounts are now considered recoverable in accordance with a recent independent valuation.

10. First mortgage loans secured by property located at Martha Cove, Victoria

As at 31 December 2008, the Fund had the following mortgage loans and interest receivable, after impairment losses, secured by registered first and second mortgages over land situated at Martha Cove, Victoria. The recoverability of these loans are supported by independent valuations of the security property on an orderly realisation basis.

	\$
Owing by Marina Cove Pty Ltd	83,266,281
Owing by other related parties	7,263,995
Owing by other unrelated parties	82,049,159
	172,579,435
	172,579,435

The Fund recorded net impairment losses of \$18,327,785 and \$3,087,704 in respect of mortgage loans and interest receivable secured by registered first and second mortgages over land situated at Martha Cove, Victoria, as outlined in notes 4 and 5.

During the period, the Fund recorded an impairment loss reversal of mortgage loans of \$2,387,821 and interest receivable of \$2,443,017 in respect of mortgage loans owing from Marina Cove Pty Ltd as the amounts are now considered recoverable in accordance with a recent independent valuation.

Marina Cove Pty Ltd is a 100% owned controlled entity of the CP1 Limited Group and the owner of a property development at Martha Cove, Victoria, which is the mortgage security for the loans and interest receivable noted above.

CP1 Limited and Marina Cove Pty Ltd are in breach of certain finance facilities. To continue as a going concern it will be necessary for them to:

- Come to appropriate arrangements with their financiers; and
- Realise sufficient funds from the sale of assets to repay outstanding debt obligations.

There is uncertainty whether CP1 Limited and Marina Cove Pty Ltd will be able to continue as going concerns.

If CP1 Limited and Marina Cove Pty Ltd cannot continue as going concerns, the realisable value of the security property securing loans and interest receivable totalling \$172,579,435 may be significantly reduced.

City Pacific First Mortgage Fund
Condensed notes to the interim financial statements
For the half-year ended 31 December 2008

11. Subsequent events

Finance facility

As a result of a delay in repayment of loans by borrowers of the Fund, City Pacific, as Responsible Entity, renegotiated the terms of the Fund's finance facility with the financier. The amended facility of \$108 million is subject to certain conditions and requires full repayment by 26 February 2010 and is intended to be met by the Fund from the scheduled repayment of first mortgage loans, or a further extension be negotiated with the financier.

The repayment of the facility is expected to be met by the Fund from the repayment of mortgage loans in the period to 26 February 2010.

Independent review of mortgage loans

Subsequent to the half-year, City Pacific as Responsible Entity of the Fund engaged a professional advisory firm to undertake an independent review of the Fund's mortgage loans and provide on-going independent support in formulating and implementing optimum realisation strategies for the Fund's mortgage loans.

Unitholder meeting

On 9 March 2009, City Pacific as Responsible Entity of the Fund received correspondence from Unitholders of the Fund requesting City Pacific to call a meeting of the Fund's Unitholders to consider and vote upon certain proposed constitutional amendments primarily in relation to fees payable to the Responsible Entity by the Fund and/or borrowers of the Fund. The meeting was held on 1 May 2009.

The Board of City Pacific has resolved to amend the Fund's constitution to reduce the management fee to 2.5% of the gross asset value of the Fund following the Unitholder meeting.

City Pacific First Mortgage Fund

Directors' declaration

In the opinion of the directors of City Pacific Limited, the Responsible Entity of City Pacific First Mortgage Fund:

- 1 the financial statements and notes, set out on pages 7 to 17, are in accordance with the Corporations Act 2001, including:
 - (a) giving a true and fair view of the financial position of the Fund as at 31 December 2008 and of its performance for the half-year ended on that date; and
 - (b) complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the Corporations Regulations 2001;
- 2 there are reasonable grounds to believe that the Fund will be able to pay its debts as and when they become due and payable.

Dated at Gold Coast this 18th day of May 2009.

Signed in accordance with a resolution of the directors of City Pacific Limited:



JM Ellis
Managing Director



Independent auditor's review report to the unitholders of City Pacific First Mortgage Fund

We have reviewed the accompanying half-year financial report of City Pacific First Mortgage Fund ("the Fund"), which comprises the interim balance sheet as at 31 December 2008, income statement, statement of recognised income and expense and statement of cash flows for the half-year ended on that date, a statement of accounting policies, other explanatory notes and the directors' declaration set out on pages 7 to 18.

Directors' Responsibility for the Financial Report

The directors of City Pacific Limited (the "Responsible Entity") are responsible for the preparation and fair presentation of the half-year financial report in accordance with Australian Accounting Standards (including Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal control relevant to the preparation and fair presentation of the half-year financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of Interim and Other Financial Reports Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the half-year financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the Fund's financial position as at 31 December 2008 and its performance for the half-year ended on that date; and complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As auditor of City Pacific First Mortgage Fund, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Independence

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*.

Conclusion

Whilst we draw your attention to the material uncertainties referred to below, based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of City Pacific First Mortgage Fund is not in accordance with the *Corporations Act 2001*, including:

- (a) giving a true and fair view of the Fund's financial position as at 31 December 2008 and of its performance for the half-year ended on that date; and
- (b) complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*.

Material uncertainty regarding continuation as a going concern

Without qualification of the above conclusion, we draw attention to note 1(d) to the interim financial report. This note indicates that the ability of the Fund to continue as a going concern is dependent upon the Fund realising sufficient cash from the repayment, refinancing or sale of existing mortgage loans, and the raising of additional investment funds, to repay short term debt funding, provide funding for the ongoing business operation including meeting all loan drawdown commitments, recommence the payment of distributions and make an offer for redemptions to investors. Due to the matters set out in note 1(d), a material uncertainty exists which casts significant doubt about the Fund's ability to continue as a going concern.

**Independent auditor's review report to the unitholders of City Pacific First Mortgage Fund**

Material uncertainty regarding the carrying value of assets secured by property located at Martha Cove, Victoria

Without qualification of the above conclusion, we draw attention to note 10 to the financial report. The recoverability of the Fund's mortgage loans and interest receivable which is secured by registered first and second mortgages over property located at a property development being completed by Marina Cove Pty Ltd at Martha Cove, Victoria is dependent upon Marina Cove Pty Ltd, and its parent entity, CP1 Limited continuing as a going concern.

To continue as a going concern CP1 Limited and Marina Cove Pty Ltd must come to appropriate arrangements with their financiers and realise sufficient funds from the sale of assets including the Martha Cove property development to meet their debt obligations, including amounts payable to the Fund. If CP1 Limited and Marina Cove Pty Ltd cannot continue as going concerns, the realisable value of the security property may be significantly reduced.

The existence of these material uncertainties casts significant doubt about the full recoverability of the Fund's assets secured by property located at Martha Cove, Victoria, which total \$172,579,435 at 31 December 2008.

A handwritten signature in blue ink that reads 'KPMG'.

KPMG

A handwritten signature in blue ink that reads 'PG Steer'.

PG Steer
Partner