Letter to Shareholders

Overview

Operating results were ahead of last year. Fee related earnings grew by 50% and most of our businesses benefitted from acquisitions, growth initiatives and improved operating performance.

Fundraising continues to be strong. We completed the final close for our flagship funds, raising $27 billion in aggregate – the largest amount of capital we have closed for a series of funds. We also closed on $2 billion of capital in other funds and $5 billion of capital for co-investments and joint venture arrangements. This increased total assets under management to approximately $250 billion and fee bearing capital to $108 billion.

With the continued growth in fee bearing capital, our asset management results grew, both quarter over quarter and sequentially. Total annualized fees plus carry increased to more than $2 billion, and our run rate of annual fees to $1.2 billion. With recent fundraising, this should continue to grow in the coming years.

Brexin or Out

While the outcome of the UK vote was a surprise, our view is that the UK will thrive, but the process of getting there will not be a straight line. As long-term value investors who have seen many periods of stress in both companies and countries, we believe these situations often present opportunities to earn greater returns than might otherwise be possible. The important point to remember, though, is that one must take a long-term view and be prepared to withstand bumps along the way.

In preparation for Brexit, we increased our financial hedges on the currency to approximately 80% of our total asset values. We naturally finance our UK assets in UK pounds, so this was 50% of the "hedge." In addition to that, we sold £6 billion through financial contracts across our funds and listed partnerships to protect the rest of our assets. This ranged from 100% hedges in our private funds to 60% to 90% in our listed partnerships. We would have done more, but the size was large and the financial hedges have cash settlement requirements, so we are always wary of that risk.

Our net balance sheet exposure was roughly US$1.5 billion, in the context of balance sheet equity of $35 billion. We still have the contracts on, but as the markets settle out we will likely take many of these off.

We have 12 businesses in the UK, with approximately $25 billion of assets and 12,000 people. Some of these businesses will not likely be affected by Brexit, and some may possibly benefit. For example, we own a short stay resort business that provides vacation accommodation to those who don't own a vacation home. A big part of our competition in this business is foreign vacation travel; however, with the currency down, we will have a new competitive advantage. We also provide student housing in the UK, and with a weaker currency, the UK should be more attractive to foreign students.

The business we own that will have the most uncertainty for a while is our UK office property business. We rent space to major corporations, many of which are global. Uncertainty about the future of their business model in the UK is definitely not helpful to long term planning. The good news is that we have time, as the vast majority of our properties are fully leased on very long leases with very high quality tenants. Even our developments are mostly fully let to strong tenants. Our issue therefore isn't the next 10 years, it is the long-term business framework for London.

In this regard, our belief is that London will continue to be a very important centre of global commerce. It is centrally located, has a sound rule of law, a culture that respects capital, a free enterprise system,

English as the primary language, a favourable tax regime for foreign companies and individuals, and is a city in which people like to live. In addition, moving corporate operations is extremely disruptive and expensive, and there is no natural alternative in the European Union. This is why London was a global centre before the vote, and why we believe it will continue to be a global centre of commerce over the long term.

While we would not have chosen to have the UK in this situation, we believe they will either (1) negotiate an acceptable deal with the EU and life will go on; (2) establish itself as a large "Singapore" sitting adjacent to one of the largest three trading blocks in the world; or (3) everyone will get tired of years of negotiations and "Leave" will just fade away, with some alterations to the current situation. We believe any of these outcomes will work over the long term.

Lastly, UK interest rates recently decreased and will likely soon go even lower as a result of the above situation and pressures from EU rates. While most people predict that real estate values will go down in London, we believe that once all this settles out, due to investors' thirst for yield, quality properties with assured income may well be valued higher than they were prior to Brexit.

Negative Interest Rates

In this similar regard, there are now more than $10 trillion of bonds globally which are yielding negative returns. Many who own these bonds acquired them years ago and have therefore made excellent capital returns by riding these bond yields into negative territory. In addition, they continue to receive 1%, 2% or 3% coupons on the bonds until maturity, so many continue to hold onto these positions.

Over the next number of years, as most of these bonds mature, institutions will be forced to look for new options for much of this $10 trillion of cash, as few will invest the proceeds into new bonds with negative yields. There are only four places in the world for most of this capital to go: (1) U.S. treasuries; (2) corporate and asset backed bonds; (3) equities; and (4) real assets.

As many of the institutions that own these negative yield bonds have requirements to hold government rated securities, it is likely that a significant portion of this capital will be utilized to buy U.S. treasuries. As a result, there should continue to be a robust bid for U.S. Treasuries for a long time. This should result in the 5 to 10-year treasury yield curve being flatter than would otherwise ever been imagined, even if the Federal Reserve begins to increase short rates.

For illustrative purposes, it is possible that 50%, or a further $5 trillion, could recirculate out of negative yield European and Japanese bonds into U.S. Treasuries. The treasury market, while very large and liquid, is approximately $15 trillion in size. This will therefore have a significant impact for years unless negative bond yields reverse in the EU and Japan.

The balance of this cash will have to go to corporate and asset backed credit, equities – and increasingly, real assets. Despite the large size of these sectors globally, a further $5 trillion is a great deal of capital. Real assets, predominantly real estate and infrastructure, are among the safest long duration investments for earning decent returns in the context of the above. As a result, we believe we will continue to see substantial capital flow into real assets, which should further enhance the overall positive environment for our business.

Price versus Value

Value investing is, in essence, the arbitrage between "Price" and "Value." The goal of a value investor is to arbitrage price differentials between the Price put on assets, whether that be in the public or private market, and the Value of those assets. Unlike classic arbitrage, however, value investing is not risk free, and profits are not instantaneous or certain. And while simple to understand, it takes years to develop the discipline, patience and judgment required to successfully implement a value investing strategy.

We are great believers that over the longer term, the Price of a security will equal its Value. However, in the short term, for many reasons, Price often does not equal Value. Investors in the stock market, of

course, have a daily mechanism to determine the Price of assets which are quoted. For private investments, the Price is not quoted daily, but is influenced heavily by the supply and demand of capital.

Price is more difficult to ascertain in the private markets – particularly during periods of market volatility, and it can be higher or lower than long-term values. This is usually dependent on supply and demand of capital, which is in turn influenced by investor attitudes. In robust markets, there is generally more capital than there are assets. This forces the Price higher, even to the point where it exceeds Value. In stressed markets, if a sale is necessary, the Price can be much lower than Value. The 20% post-Brexit mark-downs offered to retail investors in UK property funds for liquidity is an example of this.

Inversely, we are often asked how it is that we are able sell assets above our IFRS values. The answer usually lies in the fact that we only try to sell assets in robust capital environments, catching the window where Price is greater than our view of Value.

In summary, Price is merely a function of the supply and demand characteristics for capital that is looking to be invested in a sector of the market, or in a specific asset or stock. Price is often influenced by topical news of the day, market sentiment, availability of capital, and other factors that may or may not have any relevance to the Value of a specific security.

Value, on the other hand, is the net present value of the future cash flows of a business or asset, based on assumptions for future growth and discounted at the appropriate risk rate for that particular investment strategy. The difficulty in ascertaining Value is that there is no absolute value for anything, so there will always be a wide range of views over an asset's growth profile and the appropriate discount rate. The experience and discipline we have in determining these factors for real assets is one of the key attributes of our franchise.

Utilizing our Competitive Advantages

Often transactions don't work out exactly the way we think they will. Sometimes they work out better, sometimes worse. When they work out worse, we usually need to work a lot harder and utilize our competitive advantages to turn around situations that otherwise might impair an investment.

As an example, in 2007 we acquired a mezzanine loan backed by a group of hotels in Germany. The senior loan was €470 million and the mezzanine loan was €170 million. The loans were senior to the €150 million of equity invested.

Fast forward to 2009. Our borrower defaulted on the loans and chose to walk from the investment. We made the decision to stay with it, and worked through German insolvency courts to ensure we could retain our investment and take over management of the portfolio. We committed to buy out other bondholders and converted our original mezzanine loan and €50 million of further cash into a 50% equity interest in the hotels. We then raised a €325 million first mortgage on the properties to complete the buyout of the other investors.

Our original underwriting was correct, and these hotels performed extremely well despite the crisis. We reworked some of the properties and prepared redevelopments for the future. We also were fortunate that quantitative easing in the Eurozone drove cap rates down and values up.

Recently we completed the sale of the portfolio for more than €800 million. After repayment of the senior mortgage, net proceeds for our half was $265 million. Our new money earned 3 times capital, or a 100% IRR since commitment. All told, this was 2.1 times our original loan with a compound IRR since the original capital outlay eight years ago of 13%.

Overall, we were only able to turn this investment around because: (1) we had capital and the conviction to commit when few others did; (2) we had people who understood the situation and were able to work through the insolvency court; and (3) we had an operating business to rework the portfolio. In the end we turned a tough situation into a positive outcome, but only because of our significant management and financial resources.

Transaction Sourcing

We often acquire assets through "off-market" means. This enables us to find transactions that are not generally available to most others, and allows us to avoid auctions much of the time. This usually means that over the longer term we can be disciplined with our capital and are also able to earn returns in accordance with our goals.

Off-market to us means the following: (1) we have significant capital to deploy in the sectors we operate in and as a result, when a seller considers who might buy their large asset, we are usually at the top of the list because as transactions get larger, that list gets shorter; (2) we operate in many markets with a global footprint, and when markets are out of favour we are usually there with a bid; and (3) we have operating capabilities and a reputation that often enable us to bring more to a deal than just capital; this allows us to underwrite with speed and certainty, and find additional value from an asset.

As an example, during the first quarter we acquired 50% of a development site in Washington, D.C. with a developer who had done a fantastic job assembling the site, preparing it for development and finding a very high quality tenant for most of the space. The developer felt it would benefit from our scale and experience in completing large scale developments of this nature. With our backing, the tenant signed its lease, the lenders financed the project and we are under construction today. We should earn excellent returns on our capital, which again is possible because of our reputation, our operating capabilities and our financial strength.

As a second example, we have been working to acquire a natural gas pipeline business in southern Brazil from Petrobras. This transaction, if completed, will involve a very large commitment of capital and a sophisticated operating business in a country that is under considerable stress. We have exclusivity to complete this transaction and are thrilled to be involved with this asset. We have this opportunity because we have the capital, deep knowledge of Brazil, and expertise to diligence and operate a natural gas pipeline. As a result, we believe odds favour good long-term returns.

Our business is based on utilizing our competitive advantages to source transactions, followed by working the assets we acquire to enhance the returns over those that might otherwise result without our resources. In total, these advantages should enable us to earn greater returns, and as these enhanced returns compound over time, they can meaningfully add value to those we invest on behalf of.

Performance Across Our Business

Asset Management

Assets under management in the quarter grew to approximately $250 billion. Fee bearing capital increased by 15% to $108 billion. Combined, base fees and target carry now generate an annualized run-rate of over $2.0 billion. Along with the larger scale of our operations, our profitability as a manager continues to increase due to the relatively fixed base of costs we have. In this regard, fee related earnings grew by 50% to $191 million in the quarter and we continue to also generate carried interest on capital deployed in our funds.

As at and for the twelve months ended June 30 (millions)	Q2'12	Q2'13	Q2'14	Q2'15	Q2'16	CAGR
Total assets under management	$158,280	$183,498	$191,803	$217,948	$243,479	11%
Fee bearing capital	56,001	78,270	81,233	93,955	108,312	18%
Annual run rate of fees plus target carry	610	997	1,119	1,430	2,011	35%
Fee related earnings (LTM)	132	240	341	440	660	50%

We completed several milestones during the last year, establishing the next phase of growth across our portfolio. Fundraising was closed for our most recent series of flagship private funds, including our infrastructure fund at $14 billion, our real estate fund at $9 billion and our private equity fund at $4 billion. All three of these funds surpassed their fundraising targets and are double or more the size of their predecessor funds. We are thrilled to welcome approximately 150 new investors into our franchise, who

contributed more than $9 billion of capital, and greatly value our existing investors who committed a further $11 billion of capital.

We completed the launch of Brookfield Business Partners (BBU) during the quarter, providing you a special distribution, which in turn enabled us to establish the publicly traded equity base of this entity. The spin-off of BBU completes the fourth pillar of our strategy and provides investors with the ability to invest more directly in the businesses within our private equity group. We are confident that we can grow BBU and provide enhanced returns for our shareholders, both through their holdings of BBU and the additional fees that we will earn for managing the business over time.

The continued build out of our four listed partnerships, as well as our flagship private funds, provides us with access to significant capital and puts us in a position to complete transactions that each of these entities might not otherwise be able to do on their own. We believe this is key to our success as an asset manager, and has laid the foundation for us to expand our investment capabilities to match the increased demand for real assets.

Brookfield Property Group

Our property group generated company FFO of $362 million, of which our share was $275 million. FFO continues to benefit from the contribution of new investments made over the past twelve months and additional income from recently signed leases in our core office portfolio.

The majority of our investment markets are strong. New York has continued to display favourable real estate fundamentals and activity has been healthy. Toronto has improved significantly over the last year. Our Berlin portfolio has attracted several new tenants and we increased the office occupancy by more than 20% in less than a year. Sydney continues to attract investment capital from both domestic and offshore buyers, and while London was extremely strong prior to Brexit, it is still too early to tell what the short-term effects will be.

Our U.S. mall portfolio continues to perform well and we are positioned to realize high single-digit FFO growth for the next few years. We remain focused on redeveloping properties, primarily converting department stores that paid nominal rents into rent paying “inline” stores. Strong retailers are continuing to integrate e-commerce into their businesses and occupancy in our malls is over 96%.

We continue to take advantage of strong demand for high quality real estate through capital recycling, selling core assets at attractive values and redeploying this capital into new investments. In the second quarter we sold core office assets across the U.S., Europe and Australia, raising net proceeds of over $1 billion, bringing our total to $1.5 billion for the year. We also commenced a similar strategy in our core retail business, selling a partial interest in Fashion Show mall in Las Vegas for net proceeds of approximately $0.8 billion.

We deployed capital in opportunistic strategies, including approximately $600 million on the privatization of a U.S. regional mall business in early July. We have begun integrating this business within the broader scope of the organization and believe there is significant opportunity to unlock value that was not possible for it as a standalone public company. We acquired a large residential rental communities business in the U.S. investing nearly $600 million of equity. Although this sector has consistently achieved above-average earnings growth, it has been a fragmented industry with a lack of well-capitalized institutional owners. We also made further investments in the self-storage, student housing, the hospitality sectors and an office portfolio with equity investments of nearly $600 million.

Brookfield Renewable Group

Our renewable power business generated FFO of $80 million, of which our share was $37 million. After experiencing strong generation in the first three months of the year, the second quarter brought continued improvement in hydrology in Brazil, but lower inflows across several of our North American watersheds. New assets helped offset this impact, but we still fell short of levels expected. The good news, though, is

that most of our reservoirs are now near expected levels and are well positioned to capture premium summer pricing.

We acquired an additional interest in our 3,000 megawatt Colombian hydroelectric portfolio during the quarter, increasing our interest in the company to 84%. We expect to complete the acquisition of the remaining interest in this $2.7 billion business later in the summer. We also completed the acquisition of a 296 megawatt hydroelectric portfolio in Pennsylvania, which complements our existing hydro fleet in the northeastern U.S.

These acquisitions build upon our recent growth of almost 1,500 megawatts of high quality hydro in the northeastern U.S., for an aggregate equity investment of nearly $2 billion. These assets have been acquired during a historically low power price environment, and provide stable cash flows today with significant potential upside if we can eventually sign long-term contracts at prices approximating those required to incentivize continued investment in utility-scale power generation.

We continue to advance the construction of 127 megawatts of hydroelectric and biomass development projects in Brazil, as well as 29 megawatts of wind projects in Ireland. These projects are expected to generate over 700 gigawatts annually, with commissioning anticipated between 2016 and 2018.

Finally, we continue to expand on our energy marketing strategy to position our hydro portfolio as an attractive and significant source of clean power complementing wind and solar development. We are pursuing contracting opportunities in a number of markets and expanding our outreach to corporate buyers who are becoming a more influential market for the procurement of renewable power.

Brookfield Infrastructure Group

Our infrastructure group generated FFO of $279 million in the quarter, of which our share was $111 million. Results were strong and reflected contributions from an increased interest in our U.S. pipeline operations. FFO on a ‘same-store’ constant currency basis increased by 11%, driven by the growth of new in-place connections and newly installed smart meters in our UK regulated distribution business.

We continue to grow our infrastructure business through internal growth projects and acquisitions. We have a strong pipeline of projects, with almost $2 billion in the queue that we expect to be deployed within the next 36 months.

During the second quarter, we acquired an interest in a portfolio of urban toll roads in Peru and increased our stake in our Brazilian toll road business, investing over $500 million of capital. In addition, we recently progressed two transactions that will significantly expand our utilities operating group.

As mentioned earlier, we are progressing the acquisition of a controlling stake in Brazil’s critical natural gas transmission infrastructure. Separately, we were recently awarded a portfolio of greenfield transmission lines and are now in discussions with several sellers to acquire operating assets to establish a business with substantial scale in the country. These are long-life, 30-year concession assets that earn cash flows under a stable, availability-based regulatory framework. With approximately 2,800 km of greenfield projects underway in Brazil and 10,000 km of transmission lines in Chile, we are an industry leader in the South American transmission sector.

In addition to these ongoing investment initiatives, we recently completed the previously announced acquisition of a large gas storage business, investing $440 million. We are also very close to completing the acquisition of an Australian logistics company, having recently cleared all regulatory and shareholder approvals and are on track to completing this transaction in the coming weeks.

Brookfield Private Equity Group

Our private equity operations generated FFO of $97 million in the quarter. These results were generated by our wholly owned operations. Going forward the results will be both from our wholly owned operations, and from Brookfield Business Partners, which is now 79% owned by us.

Our building products operations have shown continued strong performance, both from higher OSB prices and shipment volumes compared to this time last year. Our U.S. land and housing development operations had a good spring selling season, while Canada was relatively stable due to strong results in the east, offset by weakness in Alberta due to reduced activity in the oil and gas sector. In Brazil, we believe we have seen the bottom of the market in condominium sales and have recently started new launches of projects in our operations. With our financial capacity, we believe we can emerge as one of the leaders in the years ahead.

We continue to make progress in our business services operations and recorded strong results. Our construction business achieved significant year-over-year growth and we have a record backlog of projects. As part of our growth strategy within our facilities management operations, we signed agreements to acquire two businesses, adding over 50 million square feet of facilities under management. We marked key milestones, entering the large U.S. market and obtaining expertise to manage data centres which, given cloud storage, should continue to be a growth market for a long time.

While the current commodity environment is causing some challenges for certain of our existing operations, we are redoubling our efforts to position our operations to flourish as commodity markets recover. Our energy business in Western Australia was a bright spot and has continued to generate meaningful cash flow as we substantially contracted our oil and gas production when we acquired the business.

We are focused on investing our private equity fund as well as looking for exceptional long-term businesses to combine into Brookfield Business Partners. We believe we can offer management teams a home for their businesses, and this should be a compelling proposition to many.

Closing

We remain committed to being a world-class alternative asset manager, and investing capital for you and our investment partners in high-quality, simple to understand assets which earn a solid cash return on equity, while emphasizing downside protection for the capital employed.

The primary objective of the company continues to be generating increased cash flows on a per share basis, and as a result, higher intrinsic value per share over the longer term.

Please do not hesitate to contact any of us, should you have suggestions, questions, comments, or ideas you wish to share with us.

J. Bruce Flatt
Chief Executive Officer

August 12, 2016