Q&A Session at Explanatory Meeting for Investors and Analysts
For the 29th Fiscal Period Ended January 31, 2018
Held on March 16, 2018 (Summary)

【Q&A】

<Questioner A>

(Question A-1) Is there still room for decrease in cap rate with regard to real estate appraisal? Also, is there room for increase in appraised rent in real estate appraisal?

(Answer A-1) As for the period-end estimated price in continuous appraisal, it is said that it is about time for the cap rate to stop decreasing. However, it decreased by approximately 10bps in more than half of the properties this fiscal period. This is considered to reflect the recent transaction cases. Accordingly, we believe that the decrease in cap rate has stopped in many properties but there is still a possibility that it will continue to decrease in some properties.
In addition, rent level is used as the assumption of real estate appraisal but future rent revision for each property is not taken into consideration as future cash flow is calculated based on the most recent rent in appraisal reports. There are still tenants with a positive gap as indicated in the rent gap on page 13 and 14 in the presentation material. Furthermore, there is room for gradual increase of rent when rent revision is conducted in the future as there are cases of upward rent revision among tenants with a negative gap.

(Question A-2) The lease agreement for QFRONT will expire in 2019 and we believe that much room for rent increase will remain. Please tell us the current status of negotiation and the future policy.

(Answer A-2) As for QFRONT, the current lease agreement will expire in December 2019. The contract type is a regular lease agreement and measures such as tenant replacement and rent revision upon termination of lease period will be dependent on the negotiation. Negotiations with each tenant in December 2019 and onward have just started and we will proceed with negotiations by helping them understand the neighboring market environment.

(Question A-3) TOKYU REIT acquired a property in the fiscal period ended January 2018

(29th fiscal period) but the investment unit price was low compared to NAV and we believe that there was also an option to acquire treasury investment units. We think that this was also attributable to insufficient cash on hand but we would like to know your thoughts on the acquisition of treasury investment units.

(Answer A-3) We recognize that the acquisition of treasury investment units is an option that should be considered as a measure that contributes to the enhancement of unitholder value. However, it is difficult to secure funds for the acquisition of treasury investment units at this point in time as we have used cash on hand for the repayment of interest-bearing liabilities and acquisition of Maison Peony Toritsudaigaku. In addition, it is necessary to avoid insider trading when acquiring treasury investment units. We recognize that it is difficult for us to acquire treasury investment units as we are currently having an informal discussion with Tokyu Corporation concerning the future pipeline support given the next mid-term management plan of Tokyu Corporation, the sponsor, and that it is difficult to avoid insider trading.

<Questioner B>

(Question B-1) There are descriptions on hotels on page 15 in the presentation material and we would like to know your thoughts on acquisition of hotels alone or acquisition of complex properties including hotels.

(Answer B-1) The possible use is indicated in the Image of Complex A on page 15 in the presentation material. Specifically, properties developed by Tokyu Corporation, the sponsor, are assumed and complex properties including hotels and residences are also included in such properties. (hotels alone cannot be acquired).

Therefore, we changed the use of investment properties as well as the management guideline at the general meeting of unitholders held last April by judging that there is a possibility that we will acquire properties with such use in the future.

(Question B-2) Area of tenant turnover are indicated on page 10 in the presentation material and move-ins and move-outs were both on an upward trend until the fiscal period ended January 2018 (29th fiscal period). Which tenants are actually moving in and out?

(Answer B-2) As explained in the financial results overview, the increase in move-ins and move-outs were due to continuous move-outs of large tenants. There were move-outs of large tenants at Setagaya Business Square in May 2016 and at Tokyu Toranomon Building in the fiscal period ended January 2018 (29th fiscal period) but vacancies were all refilled and the occupied area also increased.

At Setagaya Business Square, a domestic subsidiary of a foreign corporation that was occupying the building moved out in May 2016 and the occupancy rate dropped to 80%. After that, vacancies were refilled over about two fiscal periods and the building was occupied not by large tenants but by small tenants.

At Tokyu Toranomon Building, a tenant that leased 4 out of 9 floors moved to a newly constructed building for floor area expansion. The four floors were occupied with no downtime but were included in both the occupied and vacated areas.

(Question B-3) The forecasted occupied and vacated areas for the next two fiscal periods indicated on page 10 in the presentation material are small compared to the actual areas, and large move-ins and move-outs in recent periods are temporary. Do you think such move-ins and move-outs will gradually decrease in the future?

(Answer B-3) We believe that the possibility of move-outs of large tenants that are currently not factored in by the fiscal period ending January 2019 (31st fiscal period) is low as notice of cancellation of lease agreements were made also by tenants who were believed to have a high risk of cancellation in addition to tenants who already made notice of cancellation of lease agreements.

<Questioner C>

(Question C-1) The level of DPU reached 2,650 yen without the reversal of reduction entry but are you going to set the next target in the level of DPU?

(Answer C-1) We would like to explain the level of DPU based on the assumption that there are no special negative factors indicated in “Variable Factors of Distribution per Unit” on page 6 in the presentation material.

The first special factor for the fiscal period ending January 2019 (31st fiscal period) is the move-out of tenants for two floors at TOKYU REIT Kiba Building.

The floors were assumed to be vacant for the full period in the business forecast and a decrease of 36 yen will become a positive factor in the next period with the occupancy of tenants after that.

The decrease in revenue at Setegaya Business Square, which is the second point, is dependent on the impact of free rent and is considered to make profit contribution with the termination of free rent period in the next period. As for Setagaya Business Square, the recent free rent period is five to six months.

In addition, the third point is the decrease in revenue by 20 million yen for Tokyu Bancho Building and by 16 million yen for Tokyu Ginza 2-chome Building due to rent holiday for the fiscal period ending January 2019 (31st fiscal period) as indicated on page 12 in the presentation material and such portion will be eliminated in the next fiscal period. A DPU of 2,800 yen will be the next target by assuming that the above three factors will occur again in the next period and onwards.

(Question C-2) With regard to the change in investment policy, we believe that acquiring properties under favorable conditions is difficult as there will be more rivals that will become the candidate for buyers of small-scale properties. Was it a good idea to acquire small-scale properties at this point in time by actually investing in such properties?

(Answer C-2) The investment amount for Maison Peony Toritsudaigaku acquired this time was 1.2 billion yen and there are almost no properties located near stations in the Tokyu area and exceeding 4 billion yen, which is the minimum investment amount. Furthermore, we have once lowered the investment standard last April as an investment amount of 1 to 2 billion yen is realistic when assuming retail properties near stations in the Tokyu area and complex properties composed of retail stores and residences.

In addition, property information is obtained through a channel different from those of other developers by utilizing Tokyu Group’s unique information network in the Tokyu area. The information obtained this time was received from Tokyu Livable. There are many potential candidate buyers but we believe that the point of being able to conduct price negotiation with sellers at an earlier timing is an advantage of the group in the Tokyu area.

(Question C-3) At Setagaya Business Square, TOKYU REIT Shinjuku Building, KALEIDO

Shibuya Miyamasuzaka and Tokyu Toranomon Building, how much did rent increase after the move-outs of tenants compared to before their move-ins?

(Answer C-3) As to Setagaya Business Square, the tenant moved in with a rent of a little less than 20,000 yen/tsubo per month, which is the level equivalent to the market rent. Because the successor moved in with a rent at the market rent level whereas the previous large tenant who moved out had over-the-market-rent rent, the rent has decreased by roughly 1,000 yen/tsubo per month. Since the rent of the tenant who moved in to Setagaya Business Square is reflected in market rent as an actual lease case, the market rent of the area has been on the upward trend.

As for TOKYU REIT Shinjuku Building, which has a market rent of around 24,000 to 25,000 yen/tsubo per month, we were able to conclude an agreement at a higher-than-the-market-rent level due to Shinjuku area having a low vacancy rate. The new rent is up more than 20% from that of the previous tenant and is around 10% higher than the market rent. We feel that the area has a potential to see the market rent grow a little further.

KALEIDO Shibuya Miyamasuzaka is mostly occupied by restaurants, and since it stands on a side street of Meiji-Dori Street, the rent level is slightly lower than buildings on Meiji-Dori Street. The tenant which moved in this time is a café where customers can relax while experiencing virtual reality (VR), a business category we have never had as a tenant. Having a different rent level from market rent for restaurants and also having contributed to alleviating the concentration of restaurants, the tenant has led to revitalization of the building. Although the rent level of KALEIDO Shibuya Miyamasuzaka has been set lower compared with other properties in Shibuya area, we were able to conclude a lease agreement which is likely to improve the rent level this time. The new rent is up more than 20% from that of the previous tenant and is 10%-20% higher than the market rent.

As for Tokyu Toranomon Building, the new tenant's rent is slightly higher than the that of the previous tenant and is almost equal to the market rent. However, a change was made in the lease type, from a regular lease agreement to a fixed-term lease agreement.

＜Questioner D＞

(Question D-1) Concerning the "Rent Revision Trends" on page 11 in the presentation material, while upward rent revision accounted for 56% in the previous fiscal period, such has decreased to 37% in the fiscal period ended January 2018 (29th fiscal period). How do you view the figure will change going forward?

(Answer D-1) The figure on this page shows the percentage of tenants who agreed with upward rent revision among those facing rent revision. Future figures will depend on the ratio of tenants that face rent revision and the status of rent gap.

As shown on page 14 in the presentation material, for office, 36.1% of tenants which become subject to rent revision in the fiscal period ending July 2018 (30th fiscal period) and 69.8% of tenants which become subject to rent revision in the fiscal period ending January 2019 (31st fiscal period) are with positive gap. Therefore, we think there is room for upward rent revision to the level of the market rent, but it depends on the negotiation with individual tenants.

(Question D-2) How do you intend to fill the gap between the current rent and the market rent? I believe shortening the average rent revision term for retail properties now at 5.59 years and changing contracts to fixed term lease agreements will enhance positive evaluation of the unit investment price. What are your thoughts on this?

(Answer D-2) If possible, we would like to change to fixed-term lease agreements with shorter terms. However, particularly with retail properties, since the tenants often invest in interior assets, it is rather difficult to conclude short-term agreements from the standpoint of investment recovery.

Furthermore, the reason for the continuation of positive gap for retail properties is that tenants with a long rent revision term are concentrated in an area where market rent has risen, and the largest factor for the positive gap for retail properties is QFRONT. We have successfully revised rents upward to surpass the market rents for retail properties other than QFRONT. Since QFRONT will be subject to renewal of its lease agreement in December 2019, we will negotiate to revise the rent as close as to the market rent.