Japan Metropolitan Fund Investment Corporation

August 2022 (41st) Period Q&A Session

Q&A Session Summary

Date: Thursday, October 20, 2022

In the Q&A Session, seven participants put forward a total of thirteen questions. The questions and answers have been grouped under the titles “External Growth”, “Internal Growth” and “Financial Forecasts”, based on the details of the questions.

【External Growth】

Q1.： As the synergy effects with the new sponsor KKR, the changes realized, including an increase in the number of large portfolio deals under consideration and acquisition of projects resulting from joint participation with KKR in portfolio deals are described. Was the partnership with KKR the key to this as these changes were difficult to attain independently by JMF?

A1.： These changes are the fruit of the synergy effects of KKR participation as the new sponsor. First, the volume of pipeline information increased dramatically by 43% year-on-year, and information concerning large portfolio deal projects, which have been difficult for JMF as a single entity to consider, increased. Secondly, JMF and KKR are jointly considering a large portfolio deal project. Portfolio deals comprising a mixture of properties that can be handled under the REIT scheme and those that cannot be handled under the scheme have previously been difficult for JMF to consider by itself. This time, however, properties that cannot be handled under the REIT scheme can be considered on the basis of the private fund scheme of KKR, which has enabled us to participate jointly in the project. As a result, we successfully acquired preferential negotiating rights for the project. JMF has the right for one property and the rest have been granted to the KKR private fund.

Q2.： It was mentioned that M&A is one future option for raising unitholder value. Is an M&A deal going to be realized in the short term? Or is it just envisioned as a mid- to long-term forecast?

A2.： We cannot tell you exactly when an M&A deal will be realized because it depends on negotiations with the seller. At present, we are staring concrete action concerning M&A.

Q3.： I understand that KKR and JMF bid jointly on a portfolio project to acquire residential properties. Are there any differences in the criteria for residential properties between KKR and JMF? Please explain the property prioritization rules to be employed in considering portfolio projects. I would also like to know JMF’s approach to acquiring properties through portfolio deal projects.

A3.： Rules on how to prioritize properties to acquire during consideration have been clearly defined between JMF and the KKR private fund. JMF has priority in considering property information that has been obtained by it, and property information that JMF decides not to consider is considered with second priority by the private fund. JMF invests in properties in urban areas with high traffic in Japan, for all uses. Specifically, JMF seeks properties located in areas within a 10-minute walk from the closest station which can be reached from business districts in Tokyo and Osaka in 30 to 40 minutes by train. On the other hand, the KKR private fund will consider each property in light of the level of potential yield and will also look at investment target uses in the same way as JMF. Although JMF shifted to a diversified REIT about a year ago, the share of residential properties remains less than 1% of the overall portfolio. We are intending to further increase this figure to improve the portfolio balance. We will actively purchase residential properties that fit our criteria, focusing on those with mid- and long-term competitiveness in light of the aim of keeping the portfolio stable. Furthermore, only properties that are deemed to provide yields at the level of our strategic targets are to be candidates. Our current main strategy is asset replacement. In order to secure higher yields from properties we are acquiring than from those we sell, we will proceed with replacements focusing on yields. The residential properties disclosed today have been acquired with yield levels of 4% amid fierce competition.

Q4.： Page 9 of the investor presentation refers to “collaboration with KKR to create real estate carve-out opportunities from corporates.” Is such collaboration ongoing or planned for the future?

A4.： I would like to refrain from commenting on that at present.

Q5.： Page 9 of the investor presentation refers to “increased pipeline information.” What types of information have JMF obtained? Please explain any features of the information such as property use or scale, etc.

A5.： Pipeline information on the mixed-use type properties that JMF has been targeting the most has been increasing. We have informed KKR that we have high interest in buying mixed-use type properties, which are, in general, difficult to operate. We have also equally received pipeline information concerning offices and residences.

Q6.： It was explained that there are some mixed-use properties among the portfolio deal projects under consideration and JMF is willing to actively purchase them in addition to residences. Will the acquisition of mixed-use properties that meet JMF’s criteria through portfolio deals increase from now on?

A6.： One of our approaches is to firmly buy mixed-use properties that are offered as single projects. Although the volume of information on portfolio deals has increased after joining the KKR group, information on residential properties accounts for the largest share among the information. Nevertheless, mixed-use type properties or those that can be converted to mixed-use type are included in the portfolio deal projects. JMF may buy, in partnership with KKR, mixed-use type properties through portfolio acquisitions.

【Internal Growth】

Q7.： As for the successes with office leasing in refilling of large blocks in a short period, please explain the key factors and leasing methods.

A7.： In the past six months, rent increases and vacancy decreases have progressed. One reason we successfully refilled large blocks in a short period is prompt renewals of physical structures such as entrances to make them appealing in new lease contract negotiations. Another action that contributed to the successes is the introduction of rent-free periods for properties located in areas where occupancy rates are declining, which enabled us to secure tenants at an early time.

Q8.： What will the occupancy rate be, taking into account the rent-free periods, at the end of the August 2023 (43rd) period?

A8.： The occupancy rate of office and mixed-use type properties at the end of the August 2023 period is forecast to be 94.3% on the basis of the contracted area occupied in the total leasable area of each property. This figure includes the occupancy rate of office properties under the rent-free period, which accounts for around 1.5% of the total. Accordingly, the occupancy rate after deducting the occupancy rate of office properties under the rent-free periods will be approximately 93%.

Q9.： The rent revision effort seems to be progressing smoothly, as indicated by the increase by 84 million yen during the period described in Page 4 of the investor presentation. Which property uses have contributed to such rent increases? Has KKR’s knowledge contributed to the rent increases?

A9.： As summarized in Page 12 of the investor presentation, retail, office, and residential property rents were revised upward by 3.3%, 1.6%, and 2.6%, respectively, at the lease renewal times during the past six months. In total, we achieved rent increases of 84 million yen in the period. We consider that these results are the outcome of JMF’s efforts to utilize its asset management capacity developed over more than 20 years. The in-house structure enabling leasing businesses and renewals has been established since the days of JMF’s predecessors, Japan Retail Fund Investment Corporation, which specialized in retail properties, and MCUBS MidCity Investment Corporation, which focused on office properties. We believe that the achievements attained in each period are derived from our efforts to build up tenant relationships by leasing and renewing leases on our own, without outsourcing those operations.

Q10.： In the investor presentation, year-on-year sales increases by 135% to 150% among flagship properties such as GYRE, La Porte Aoyama, and MARINE & WALK YOKOHAMA are listed as factors indicating that further increases in the revenue-based rent can be expected. How are these increases in sales contributing to the increase in the revenue-based rent? What are the forecast levels of revenue-based rent for the next period and beyond.

A10.： As shown in Page 13 of the investor presentation, the increase in the revenue-based rent is increasing with the increases in retail sales. The revenue-based rent of the August 2022 (41st) period increased by approximately 3% from the previous period. The revenue-based rent ratio is especially high with mozo wonder city and KAWASAKI Le FRONT, described in the table on the left of Page 13. The sales of mozo wonder city have been increasing since a renewal last spring, which indicates a possible increase in the revenue-based rent in the next and following periods.

【Financial Forecasts】

Q11.： What points were conservatively considered in forecasting DPU and EPU for the August 2023 (43rd) period? Are there any potential risks?

A11.： Considering the recent surge in electricity rates, utility costs were estimated conservatively. Specifically, we presumed that utility costs revenue as operating revenue cannot be increased much for tenants. On the other hand, it was assumed that the utility costs, which account for a portion of our operating costs, will increase further. As for the refilling of office properties, among others, while vacancies where advance notice of leaving has been submitted to us are reflected in the forecast, the outlook for refilling is not included at all in the forecast.

Q12.： Please explain the factors that are estimated to decrease the Other Rental Revenues from the February 2023 (42nd) period to the August 2023 (43rd) period.

A12.： This is due to the removal of a one-time payment of approximately 1 billion yen from large tenants to cover restoration costs.

Q13.： What is the background of reserving gains on disposal till the February 2026 (48th) period?

A13.： We intend to allocate gains on disposal to several periods, not putting the whole of the gains into a certain period. One reason behind this is to firm up the EPU and DPU bottom lines. Another reason is to push EPU and DPU further upward with the gains on disposal, taking advantage of the increased profitability of our portfolio at present, as shown by the advancement of refilling of large office blocks and the increased revenue-based rent of retail properties. Firming up the EPU and DPU bottom lines will also function as a countermeasure against the surging utility costs.